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CHAPTER-1

ACCOUNTING STANDARDS

AS-4 Contingencies and Events Occurring after Balance Sheet Date

Q-1 While preparing its final accounts for the year ended 31st March, 2016, a company made provision for bad debts @ 5% of its total debtors. In the last week of February, 2016 a debtor for Rs. 20 lakhs had suffered heavy loss due to an earthquake; the loss was not covered by any insurance policy. In April, 2016 the debtor became a bankrupt. Can the company provide for the full loss arising out of insolvency of the debtor in the final accounts for the year ended 31st March, 2016?

Commentwith reference to relevant Accounting Standard.

Ans : As per AS 4 'Contingencies and Events Occurring After the Balance Sheet Date', adjustment to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the Balance Sheet date.

A debtor for Rs. 20,00,000 suffered heavy loss due to earthquake in the last week of February, 2016 which was not covered by insurance. Thisinformation with its implicationswas already known to the company. Thefact that he became bankrupt in April, 2016 (after the balance sheet date) is only an additional information related to the condition existing on the balance sheet date.

Accordingly, full provision for bad debts amounting Rs. 20,00,000 should be made, to cover the loss arising due to the insolvency of a debtor, in the final accounts for the year ended 31st March 2016. Since the company has already made 5% provision of its total debtors, additional provision amounting Rs. 19,00,000 shall be made (20,00,000 x95%).

Q-2 The Board of Directors of New Graphics Ltd. in its Board Meeting held on 18th April, 2017, considered and approved the Audited Financial results along with Auditors Report for the Financial Year ended 31st March, 2017 and recommended a dividend of Rs. 2 per equity share (on 2 crore fully paid up equity shares of Rs. 10 each) for the year ended 31st March, 2017 and if approved by the members at the forthcoming Annual General Meeting of the company on 18th June, 2017, the same will be paid to all the eligible shareholders.

Discuss on the accounting treatment and presentation of the said proposed dividend in the annual accounts of the company for the year ended 31st March, 2017 as per the applicable Accounting Standard and other Statutory Requirements.

Ans : As per the amendment in AS 4 "Contingencies and Events Occurring After the Balance Sheet Date" vide Companies (Accounting Standards) Amendments Rules, 2016 dated 30th March, 2016, the events which take place after the balance sheet date, are sometimes reflected in the financial statements because of statutory requirements or because of their special nature.

However, dividends declared after the balance sheet date but before approval of financial statements are not recognized as a liability at the balance sheet date because no statutory obligation exists at that time. Hence such dividends are disclosed in the notes to financial statements.

Provision for proposed dividends is not required to be made as per the amendment in AS 4. Such proposed dividends are to be disclosed in the notes to financial statements. Accordingly, the dividend of Rs.4 crores recommended by New Graphics Ltd. in its Board meeting on 18th April, 2017 shall not be accounted for in the books for the year 2016-17 irrespective of the fact that it pertains to the year 2016-17 and will be paid after approval in the Annual General Meeting of the members/shareholders.

Q-3 The accounting year of Dee Limited ended on 31st March, 2018 but the accounts were approved on 30th April, 2018. On 15th April, 2018 a fire occurred in the factory and office premises. The loss by fire is of such a magnitude that it was not possible to expect the enterprise Dee Limited to start operation again.

State with reasons, whether the loss due to fire is an adjusting or non- adjusting event and how the fact of loss is to be disclosed by the company in the context of the provisions of AS-4 (Revised).

Ans : As per AS 4 (Revised) "Contingencies and Events occurring after the Balance Sheet Date", an event occurring after the balance sheet date should be an adjusting event even if it does not reflect any condition existing on the balance sheet date, if the event is such as to indicate that the fundamental accounting assumption of going concern is no longer appropriate.

The fire occurred in the factory and office premises of an enterprise after 31 March, 2018 but before approval of financial statement of 30.4.18. The loss by fire is of such a magnitude that it is not reasonable to expect the Dee Ltd. to start operations again, i.e., the going concern assumption is not valid. Since the fire occurred after 31/03/18, the loss on fire is not a result of any condition existing on 31/03/18. But the loss due to fire is an adjusting event the entire accounts need to be prepared on a liquidation basis with adequate disclosures by the company by way of note in its financial statements in the following manner:

"Major fire occurred in the factory and office premises on 15th April, 2018 which has made impossible for the enterprise to start operations again. Therefore, the financial statements have been prepared on liquidation basis."

Q-4 An earthquake destroyed a major warehouse of PQR Ltd. on 30.4.2019. The accounting year of the company ended on 31.3.2019. The accounts were approved on 30.6.2019. The loss from earthquake is estimated at ₹ 25 lakhs. State with reasons, whether the loss due to earthquake is an adjusting or non-adjusting event and how the fact of loss is to be disclosed by the company.

Ans : Para 8.3 of AS 4 “Contingencies and Events Occurring after the Balance Sheet Date”, states that adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. The destruction of warehouse due to earthquake did not exist on the balance sheet date i.e. 31.3.2019. Therefore, loss occurred due to earthquake is not to be recognized in the financial year 2018-2019.

However, according to para 8.6 of the standard, unusual changes affecting the existence or substratum of the enterprise after the balance sheet date may indicate a need to consider the use of fundamental accounting assumption of going concern in the preparation of the financial statements. As per the information given in the question, the earthquake has caused major destruction; therefore, fundamental accounting assumption of going concern is called upon.

Hence, the fact of earthquake together with an estimated loss of ₹ 25 lakhs should be disclosed in the Report of the Directors for the financial year 2018-2019.

Q-5 With reference to AS 4 "Contingencies and events occurring after the balance sheet date", state whether the following events will be treated as contingencies, adjusting events or non-adjusting events occurring after balance sheet date in case of a company which follows April to March as its financial year.

(i) A major fire has damaged the assets in a factory on 5th April, 5 days after the year end. However, the assets are fully insured and the books have not been approved by the Directors.

(ii) A suit against the company's advertisement was filed by a party on 10th April, 10 days after the year end claiming dama ges of ₹ 20 lakhs.

Ans. According to AS 4 on `Contingencies and Events Occurring after the Balance Sheet Date', adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date.

However, adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. "Contingencies" used in the Standard is restricted to conditions or situations at the balance sheet date, the financial effect of which is to be determined by future events which may or may not occur.

(i) Fire has occurred after the balance sheet date and also the loss is totally insured. Therefore, the event becomes immaterial and the event is non -adjusting in nature.

(ii) The contingency is restricted to conditions existing at the balance sheet date.
However, in the given case, suit was filed against the company's advertisement by a party on 10th April for amount of ₹ 20 lakhs. Therefore, it does not fit into the definition of a contingency and hence is a non -adjusting event.

Q-6 The financial statements of PQ Ltd. for the year 2017-18 approved by the Board of Directors on 15th July, 2018. The following information was provided :

(i) A suit against the company's advertisement was filed by a party on 20th April, 2018, claiming damages of ₹ 25 lakhs.

(ii) The terms and conditions for acquisition of business of another company have been decided by March, 2018. But the financial resources were arranged in April, 2018 and amount invested was ₹ 50 lakhs.

(iii) Theft of cash of ₹ 5 lakhs by the cashier on 31st March, 2018 but was detected on 16th July, 2018.

(iv) Company sent a proposal to sell an immovable property for ₹ 40 lakhs in March, 2018. The book value of the property was ₹ 30 lakhs on 31st March, 2018. However, the deed was registered on 15th April, 2018.

(v) A, major fire has damaged the assets in a factory on 5th April, 2018. However, the assets are fully insured.

With reference to AS-4 "Contingencies and events occurring after the balance sheet date", state whether the above mentioned events will be treated as contingencies, adjusting events or non-adjusting events occurring after the balance sheet date.

Ans.

(i) Suit filed against the company is a contingent liability but it was not existing as on balance sheet date as the suit was filed on 20th April after the balance Sheet date. As per AS 4, 'Contingencies' used in the Standard is restricted to conditions or situations at the balance sheet date, the financial effect of which is to be determined by future events which may or may not occur. Hence, it will have no effect on financial statements and will be a non-adjusting event.

(ii) In the given case, terms and conditions for acquisition of business were finalised and carried out before the closure of the books of accounts but transaction for payment of financial resources was effected in April, 2018. This is clearly an event occuring after the balance sheet date. Hence, necessary adjustment to assets and liabilities for acquisition of business is necessary in the financial statements for the year ended 31st March 2018.

(iii) Only those significant events which occur between the balance sheet date and the date on which the financial statements are approved, may indicate the need for adjustment to assets and liabilities existing on the balance sheet date or may require disclosure. In the given case, theft of cash was detected on 16th July, 18 after approval of financial statements by the Board of Directors, hence no treatment is required.

(iv) Adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. In the given case, sale of immovable property was under proposal stage (negotiations also not started) on the balance sheet date. Therefore, no adjustment to assets for sale of immovable property is required in the financial statements for the year ended 31st March, 2018.

(v) The condition of fire occurrence was not existing on the balance sheet date. Only the disclosure regarding event of fire and loss being completely insured may be given in the report of approving authority.

Q-7 With reference to AS 4 "Contingencies and events occurring after the balance sheet date", state whether the following events will be treated as contingencies, adjusting events or non-adjusting events occurring after balance sheet date in case of a company which follows April to March as its financial year.

(i) A major fire has damaged the assets in a factory on 5th April, 5 days after the year end. However, the assets are fully insured and the books have not been approved by the Directors.

(ii) A suit against the company's advertisement was filed by a party on 10th April, 10 days after the year end claiming damages of ₹ 20 lakhs.

Ans. According to AS 4 on `Contingencies and Events Occurring after the Balance Sheet Date', adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date. However, adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. "Contingencies" used in the Standard is restricted to conditions or situations at the balance sheet date, the financial effect of which is to be determined by future events which may or may not occur.

(i) Fire has occurred after the balance sheet date and also the loss is totally insured. Therefore, the event becomes immaterial and the event is non-adjusting in nature.

(ii) The contingency is restricted to conditions existing at the balance sheet date. However, in the given case, suit was filed against the company's advertisement by a party on 10th April for amount of ₹ 20 lakhs. Therefore, it does not fit into the definition of a contingency and hence is a non-adjusting event.

Q-8 A fire, on 2nd April, 2020, completely destroyed a manufacturing plant of Omega Ltd. whose financial year ended on 31st March, 2020, the financial statements were approved by their approving authority on 15th June, 2020. It was expected that the loss of ₹ 10 million would be fully covered by the insurance company. How will you disclose it in the financial statements of Omega Ltd. for the year ended 31st March, 2020.

Ans. The event is a non-adjusting event since it occurred after the year-end and does not relate to the conditions existing at the year-end. However, it is necessary to consider the validity of the going concern assumption having regard to the extent of insurance cover. Also, since it is said that the loss would be fully recovered by the insurance company, the fact should be disclosed by way of a note to the financial statements.

Q-9 The Board of Directors of New Graphics Ltd. in its Board Meeting held on 18th April, 2017, considered and approved the Audited Financial results along with Auditors Report for the Financial Year ended 31st March, 2017 and recommended a dividend of Rs.2 per equity share (on 2 crore fully paid up equity shares of Rs.10 each) for the year ended31st March, 2017 and if approved by the members at the forthcoming Annual General Meeting of the companyon 18th June, 2017, the same will be paid to all the eligible shareholders.

Discuss on the accounting treatment and presentation of the said proposed dividend in the annual accounts of the company for the year ended 31st March, 2017 as per the applicable Accounting Standard and other Statutory Requirements.

Ans. As per the amendment in AS 4 "Contingencies and Events Occurring After the Balance Sheet Date" vide Companies (Accounting Standards) Amendments Rules, 2016 dated 30th March, 2016, the events which take place after the balance sheet date, are sometimes reflected in the financial statements because of statutory requirements or because of their special nature.

However, dividends declared after the balance sheet date but before approval of financial statements are not recognized as a liability at the balance sheet date because no statutory obligation exists at that time. Hence such dividends are disclosed in the notes to financial statements.

No, provision for proposed dividends is not required to be made. Such proposed dividends are to be disclosed in the notes to financial statements. Accordingly, the dividend of ? 4 crores recommended by New Graphics Ltd. in its Board meeting on 18th April, 2017 shall not be accounted for in the books for the year 2016-17 irrespective of the fact that it pertains to the year 2016-17 and will be paid after approval in the Annual General Meeting of the members/shareholders.

Q-10 While preparing its final accounts for the year ended 31st March, 2017, a company made provision for bad debts @ 5% of its total debtors. In the last week of February, 2017 a debtor for Rs.20 lakhs had suffered heavy loss due to an earthquake; the loss was not covered by any insurance policy. In April, 2017 the debtor became a bankrupt. Can the company provide for the full loss arising out of insolvency of the debtor in the final accounts for the year ended 31st March, 2017? You are required to advise the company in line with AS 4.

Ans. As per AS 4 'Contingencies and Events Occurring After the Balance Sheet Date', adjustment to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the Balance Sheet date.

A debtor for Rs 20,00,000 suffered heavy loss due to earthquake in the last week of February, 2017 which was not covered by insurance. This information with its implications was already known to the company. The fact that he became bankrupt in April, 2017 (after the balance sheet date) is only an additional information related to the condition existing on the balance sheet date.

Accordingly, full provision for bad debts amounting Rs. 20,00,000 should be made, to cover the loss arising due to the insolvency of a debtor, in the final accounts for the year ended 31st March 2017. Since the company has already made 5% provision of its total debtors, additional provision amounting Rs. 19,00,000 shall be made (20,00,000 x 95%) for the year ended 31st March, 2017.

Q-11 An earthquake destroyed a major warehouse of PQR Ltd. on 30.4.2019. The accounting year of the company ended on 31.3.2019. The accounts were approved on 30.6.2019. The loss from earthquake is estimated at ₹ 25 lakhs. State with reasons, whether the loss due to earthquake is an adjusting or non-adjusting event and how the fact of loss is to be disclosed by the company.

Ans. Para 8.3 of AS 4 “Contingencies and Events Occurring after the Balance Sheet Date”, states that adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. The destruction of warehouse due to earthquake did not exist on the balance sheet date i.e. 31.3.2019. Therefore, loss occurred due to earthquake is not to be recognized in the financial year 2018-2019.

However, according to para 8.6 of the standard, unusual changes affecting the existence or substratum of the enterprise after the balance sheet date may indicate a need to consider the use of fundamental accounting assumption of going concern in the preparation of the financial statements. As per the information given in the question, the earthquake has caused major destruction; therefore, fundamental accounting assumption of going concern is called upon.

Hence, the fact of earthquake together with an estimated loss of ₹ 25 lakhs should be disclosed in the Report of the Directors for the financial year 2018-2019.

Q-12 With reference to AS 4 "Contingencies and events occurring after the balance sheet date", ***identify*** whether the following events will be treated as contingencies, adjusting events or non-adjusting events occurring after balance sheet date in case of a company which follows April to March as its financial year.

(i) A major fire has damaged the assets in a factory on 5th April, 5 days after the year end. However, the assets are fully insured and the books have not been approved by the Directors.

(ii) A suit against the company's advertisement was filed by a party on 10th April, 10 days after the year end claiming damages of Rs.20 lakhs.

Ans. According to AS 4 on 'Contingencies and Events Occurring after the Balance Sheet Date', adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date. However, adjustments to assets and liabi lilies are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. "Contingencies" used in the Standard is restricted to conditions or situations at the balance sheet date, the financial effect of which is to be determined by future events which may or may not occur.

(i) Fire has occurred after the balance sheet date and also the loss is totally insured. Therefore, the event becomes immaterial and the event is **non-adjusting** in nature.

(ii) The contingency is restricted to conditions existing at the balance sheet date. However, in the given case, suit was filed against the company's advertisement by a party on 10th April for amount of Rs. 20 lakhs. Therefore, it does not fit into the definition of a contingency and hence is a **non-adjusting event**.

Q-13 An earthquake destroyed a major warehouse of PQR Ltd. on 30.4.2021. The accounting year of the company ended on 31.3.2021. The accounts were approved on 30.6.2021. The loss from earthquake is estimated at ₹ 25 lakhs. State with reasons, whether the loss due to earthquake is an adjusting or non-adjusting event and how the fact of loss is to be disclosed by the company.

Ans. AS 4 “Contingencies and Events Occurring after the Balance Sheet Date”, states that adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. The destruction of warehouse due to earthquake did not exist on the balance sheet date i.e. 31.3.2021. Therefore, loss occurred due to earthquake is not to be recognized in the financial year 2020-2021.

However, according the standard, unusual changes affecting the existence or substratum of the enterprise after the balance sheet date may indicate a need to consider the use of fundamental accounting assumption of going concern in the preparation of the financial statements. As per the information given in the question, the earthquake has caused major destruction; therefore, fundamental accounting assumption of going concern is called upon.

Hence, the fact of earthquake together with an estimated loss of ₹ 25 lakhs should be disclosed in the Report of the Directors for the financial year 2020-2021.

Q-14 Tee Ltd. closes its books of accounts every year on 31st March. The financial statements for the year ended 31 March 2020 are to be approved by the approving authority on 30 June 2020. During the first quarter of 2020-2021, the following events / transactions has taken place. The accountant of the company seeks your guidance for the following:

(i) Tee Ltd. has an inventory of 50 stitching machines costing at ₹ 5,500 per machine as on 31 March 2020. On 31 March 2020 the company is expecting a heavy decline in the demand in next year. The inventories are valued at cost or net realisable value, whichever is lower. During the month of April 2020, due to fall in demand, the prices have gone down drastically. The company has sold 5 machines during this month at a price of ₹ 4,000 per machine.

(ii) A fire has broken out in the company's godown on 15 April 2020. The company has estimated a loss of ₹ 25 lakhs of which 75% is recoverable from the Insurance company.

(iii) The company has entered into a sale agreement on 30 March 2020 to sell a property for a consideration of ₹ 7,50,000 which is being carried in the books at ₹ 5,50,000 at the year end. The transfer of risk and reward and sale is complete in the month of May 2020 when conveyance and possession get completed.

(iv) The company has received, during the year 2018-2019, a government grant of ₹ 15 lakhs for purchase of a machine. The company has received a notice for refund of the said grant on 15 June, 2020 due to violation of some of the conditions of grant during the year 2019-2020.

You are required to state with reasons, how the above transactions will be dealt with in the financial statement for the year ended 31st March 2020.

Ans. Events occurring after the balance sheet date are those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of Directors in the case of a company, and by the corresponding approving authority in the case of any other entity.

Assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date or that indicate that the fundamental accounting assumption of going concern is not appropriate.

In the given case, financial statements are approved by the approving authority on 30 June 2020.

On the basis of above principles, following will be the accounting treatment in the financial statements for the year ended at 31 March 2020:

(i) Since on 31 March 2020, Tee Ltd. was expecting a heavy decline in the demand of the stitching machine. Therefore, decline in the value during April, 2020 will be considered as an adjusting event. Hence, Tee Ltd. needs to adjust the amounts recognized in its financial statements w.r.t. net realisable value at the end of the reporting period. Accordingly, inventory should be written down to ₹ 4,000 per machine. Total value of inventory in the books will be 50 machines x ₹ 4,000 = ₹ 2,00,000.

(ii) A fire took place after the balance sheet date i.e. during 2020-2021 financial year. Hence, corresponding financials of 2019-2020 financial year should not be adjusted for loss occurred due to fire. However, in this circumstance, the going concern assumption will be evaluated. In case the going concern assumption is considered to be appropriate even after the occurrence of fire, no disclosure of the same is required in the financial statements. Otherwise, disclosure be given.

(iii) Since the transfer of risk and reward and sale was complete in the month of May, 2020 when conveyance and possession got complete, no revenue should be recognised with respect to it in the financial statements of 2019-2020. However, a disclosure for the same should be given by the entity.

(iv) Since the notice has been received after 31 March but before 30 June 2020 (approval date), the said grant shall be adjusted in the financial statements for financial year 2019-2020 because the violation of the conditions took place in the financial year 2019-2020 and the company must be aware of it.

Q-15 Surya Limited follows the financial year from April to March. It has provided the following information.

(i) A suit against the Company's Advertisement was filed by a party on 5th April, 2021, claiming damages of ₹ 5 lakhs.

(ii) Company sends a proposal to sell an immovable property for ₹ 45 lakhs in March 2021. The book value of the property is ₹ 30 lakhs as on year end date. However, the Deed was registered on 15th April, 2021.

(iii) The terms and conditions for acquisition of business of another company have been decided by the end of March 2021, but the financial resources were arranged in April 2021. The amount invested was ₹ 50 lakhs.

(iv) Theft of cash amounting to f4 lakhs was done by the Cashier in the month of March 2021 but was detected on the next day after the Financial Statements have been approved by the Directors.

Keeping in view the provisions of AS-4, you are required to state with reasons whether the above events are to be treated as Contingencies, Adjusting Events or Non-Adjusting Events occurring after Balance Sheet date.

Ans.

(i) Suit filed against the company is a contingent liability but it was not existing as on date of balance sheetdate as the suit was filed on 5th April after the balance sheet date. As per AS 4, `Contingencies' is restrictedto conditions or situations at the balance sheet date, the financial effect of which is to be determined byfuture events which may or may not occur. However, it may be disclosed with the nature of contingency, being a contingent liability.

This event does not pertain to conditions on the balance sheet date. Hence, it will have no effect on financial statements and will be a non-adjusting event.

(ii) In this case, no adjustment to assets and liabilities is required as the event does not affect the determination and the condition of the amounts stated in the financial statements for the year ended 31st March, 2021. There was just a proposal before 31st March, 2021 and hence sale cannot be shown in the financial statements for the year ended 31st March, 2021.

Sale of immovable property is an event occurring after the balance sheet date and is a non-adjusting event.

(iii) In the given case, terms and conditions for acquisition of business were finalized before the balance sheet date and carried out before the closure of the books of accounts but transaction for payment of financial resources was effected in April, 2021.

Hence, it is an adjusting event and necessary adjustment to assets and liabilities for acquisition of business is necessary in the financial statements for the year ended 31st March 2021.

(iv) Only those events which occur between the balance sheet date and the date on which the financial statements are approved, may indicate the need for adjustments to assets and liabilities as at the balance sheet date or may require disclosure.

In the given case, as the theft of cash was detected after approval of financial statements, no adjustment is required. Hence it is non-adjusting event.

Q-16 A case is going on between ABC Ltd. and Tax department on claiming the exemption for certain items, for the year 2019-2020. The court has issued the order on 15th April and rejected the claim of the company. Accordingly, company is liable to pay the additional tax. The financial statements were approved on 31st May, 2020. Shall company account for such tax in the year 2019-2020 or shall it account for in the year 2020-2021?

Ans. To decide whether, the event is adjusting or not adjusting two conditions need to be satisfied,

(a) There has to be evidence

(b) The event must have been related to period ending on reporting date.

Here both the conditions are satisfied. Court order is a conclusive evidence which has been received before approval of the financial statements since the liability is related to earlier year. The event will be considered as an adjusting event and accordingly the amount will be adjusted in accounts of 2019 2020.

Q-17 XYZ Ltd. operates its business into various segments. Its financial year ended on 31st March, 2020 and the financial statements were approved by their approving authority on 15th June, 2020. The following material events took place:

a. A major property was sold (it was included in the balance sheet at ₹ 25,00,000) for which contracts had been exchanged on 15th March, 2020. The sale was completed on 15th May, 2020 at a price of ₹ 26,50,000.

b. On 2nd April, 2020, a fire completely destroyed a manufacturing plant of the entity. It was expected that the loss of ₹ 10 million would be fully covered by the insurance company.

c. A claim for damage amounting to ₹ 8 million for breach of patent had been received by the entity prior to the year-end. It is the director's opinion, backed by legal advice that the claim will ultimately prove to be baseless. But it is still estimated that it would involve a considerable expenditure on legal fees.

You are required to state with reasons, how each of the above items should be dealt with in the financial statements of XYZ Ltd. for the year ended 31st March, 2020.

Ans. **Treatment as per AS 4 `Contingencies and Events Occurring After the Balance Sheet Date'**

(a) The sale of property should be treated as an adjusting event since contracts had been exchanged prior to the year-end. The effect of the sale should be reflected in the financial statements ended on 31.3.2020 and the profit on sale of property ₹ 1,50,000 would be considered.

(b) The event is a non-adjusting event since it occurred after the year-end and does not relate to the conditions existing at the year-end. However, it is necessary to consider the validity of the going concern assumption having regard to the extent of insurance cover. Also, since it is said that the loss would be fully recovered by the insurance company, the fact should be disclosed by way of a note to the financial statements.

(c) On the basis of evidence provided, the claim against the company will not succeed. Thus, ₹ 8 million should not be provided in the account, but should be disclosed by means of a contingent liability with full details of the facts. Provision should be made for legal fee expected to be incurred to the extent that they are not expected to be recovered.

Q-18 Tee Ltd. closes its books of accounts every year on 31st March. The financial statements for the year ended 31st March 2020 are to be approved by the approving authority on 30th June 2020. During the first quarter of 2020-2021, the following events / transactions has taken place. The accountant of the company seeks your guidance for the following:

(i) Tee Ltd. has an inventory of 50 stitching machines costing at ₹ 5,500 per machine as on 31st March 2020. The company is expecting a heavy decline in the demand in next year. The inventories are valued at cost or net realizable value, whichever is lower. During the month of April 2020, due to fall in demand, the prices have gone down drastically. The company has sold 5 machines during April, 2020 at a price of ₹ 4,000 per machine.

(ii) A fire has broken out in the company's godown on 15th April 2020. The company has estimated a loss of ₹ 25 lakhs of which 75% is recoverable from the Insurance company.

(iii) A suit against the company's advertisement was filed by a party on 10th April, 2020 10 days after the year end claiming damages of ₹ 20 lakhs.

You are required to state with reasons, how the above transactions will be dealt with in the financial statements for the year ended 31 March 2020.

Ans. Events occurring after the balance sheet date are those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of Directors in the case of a company, and, by the corresponding approving authority in the case of any other entity. Assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date or that indicate that the fundamental accounting assumption of going concern is not appropriate. In the given case, financial statements are approved

by the approving authority on 30 June 2020. On the basis of above principles, following will be the accounting treatment in the financial statements for the year ended at 31 March 2020:

(i) Since on 31 March 2020, Tee Ltd. was expecting a heavy decline in the demand of the stitching machine. Therefore, decline in the value during April, 2020 will be considered as an adjusting event. Hence, Tee Ltd. needs to adjust the amounts recognized in its financial statements w.r.t. net realizable value at the end of the reporting period. Accordingly, inventory should be written down to ₹ 4,000 per machine. Total value of inventory in the books will be 50 machines x ₹ 4,000 = ₹ 2,00,000.

(ii) A fire took place after the balance sheet date i.e. during 2020-2021 financial year. Hence, the financial statements for the year 2019-2020 should not be adjusted for loss occurred due to fire. However, in this circumstance, the going concern assumption will be evaluated. In case the going concern assumption is considered to be appropriate even after the occurrence of fire, no disclosure of the same is required in the financial statements.

(iii) The contingency is restricted to conditions existing at the balance sheet date. However, in the given case, suit was filed against the company's advertisement by a party on 10th April for amount of ₹ 20 lakhs. Therefore, it does not fit into the definition of a contingency and hence is a non-adjusting event.

Q-19 As per the provision of AS 4, you are required to state with reason whether the following transactions are adjusting event or non-adjusting event for the year ended 31.03.2021 in the books of NEW Ltd. (accounts of the company were approved by board of directors on 10.07.2021):

1. Equity Dividend for the year 2020-21 was declared at the rate of 7% on 15.05.2021.
2. On 05.03.2021, ₹ 53,000 cash was collected from a customer but not deposited by the cashier. This fraud was detected on 22.06.2021.
3. One building got damaged due to occurrence of fire on 23.05.221. Loss was estimated to be ₹ 81,00,000.

Ans.

(i) If dividends are declared after the balance sheet date but before the financial statements are approved, the dividends are not recognized as a liability at the balance sheet date because no obligation exists at that time unless a statute requires otherwise. Such dividends are disclosed in the notes. Thus, no liability for dividends needs to be recognized in financial statements for financial year ended 31st March, 2021 and declaration of dividend is non-adjusting event.

(ii) As per AS 4 'Contingencies and Events occurring after the Balance Sheet Date' an event occurring after the balance sheet date may require adjustment to the reported values of assets, liabilities, expenses or incomes if such events relate to conditions existing at the balance sheet date. In the given case, fraud of the accounting period is detected after the balance sheet date but before approval of the financial statements, it is necessary to recognize the loss. Thus loss amounting ₹ 53,000 should be adjusted in the accounts of the company for the year ended 31st March, 2021 as it is adjusting event.

(iii) AS 4 states that adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. The damage of one building due to fire did not exist on the balance sheet date i.e. 31.3.2021. Therefore, loss occurred due to fire is not to be recognized in the financial year 2020-2021 as it is non-adjusting event.

However, according to the standard, unusual changes affecting the existence or substratum of the enterprise after the balance sheet date may indicate a need to consider the use of fundamental accounting assumption of going concern in the preparation of the financial statements. As per the information given in the question, the fire has caused major destruction; therefore, fundamental

accounting assumption of going concern would have to be evaluated. Considering that the going concern assumption is still valid, the fact of fire together with an estimated loss of ‘ 81 lakhs should be disclosed in the report of the approving authority for financial year 2020-21 to enable users of financial statements to make proper evaluations and decisions.

Q-20 The financial statements of Alpha Ltd. for the year 2019-2020 were approved by the Board of Directors on 15th July, 2020. The following information was provided:

(i) A suit against the company’s advertisement was filed by a party on 20th April, 2020 claiming damages of ₹ 25 lakhs.

(ii) The terms and conditions for acquisition of business of another company had been decided by March, 2020. But the financial resources were arranged in April, 2020 and amount invested was ‘ 50 lakhs.

(iii) Theft of cash of ₹ 5 lakhs by the cashier on 31st March, 2020, was detected on 16th July, 2020.

(iv) The company started a negotiation with a party to sell an immovable property for ₹ 40 lakhs in March, 2020. The book value of the property is ₹ 30 lakh on 31st March, 2020. However, the deed was registered on 15th April, 2020.

(v) A major fire had damaged the assets in a factory on 5th April, 2020. However, the assets were fully insured.

With reference to AS 4, state whether the above mentioned events will be treated as contingencies, adjusting events or non-adjusting events occurring after the balance sheet date.

Ans.

(i) **Non-adjusting event:** Suit filed against the company is a contingent liability but it was not existing as on date of balance sheet date as the suit was filed on 20th April after the balance sheet date. As per AS 4, ‘Contingencies’ is restricted to conditions or situations at the balance sheet date, the financial effect of which is to be determined by future events which may or may not occur. Hence, it will have no effect on financial statement and will be a non-adjusting event.

(ii) **Adjusting event:** In the given case, terms and conditions for acquisition of business were finalised before the balance sheet date and carried out before the closure of the books of accounts but transaction for payment of financial resources was effected in April, 2020.

Hence, necessary adjustment to assets and liabilities for acquisition of business is necessary in the financial statements for the year ended 31st March 2020.

(iii) **Non-adjusting event:** Only those events which occur between the balance sheet date and the date on which the financial statements are approved, may indicate the need for adjustments to assets and liabilities as at the balance sheet date or may require disclosure.

In the given case, as the theft of cash was detected on 16th July, 2020 ie after approval of financial statements, no adjustment is required.

(iv) **Non-adjusting event:** Adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. In the given case, sale of immovable property was under proposal stage (negotiations only started) on the balance sheet date, and was not finalized. Therefore, adjustment to assets for sale of immovable property is not necessary in the financial statements for the year ended 31st March, 2020. Disclosure may be given in Report of approving Authority.

(v) **Non-adjusting event:** Adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. The condition of fire occurrence was not existing on the balance sheet date. Only the disclosure regarding fire and loss, being completely insured may be given in the report of approving authority.

AS-5 Net Profit or Loss for the Period, Prior Period Items and Change in Accounting Policies

Q-1 Explain whether the following will constitute a change in accounting policy or not as per AS 5.

(i) Introduction of a formal retirement g ratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement.

(ii) Management decided to pay pension to those employees who have retired after completing 5 years of service in the organization. Such employees will get pension of ₹20,000 per month. Earlier there was no such scheme of pension in the organization .

Ans. As per AS 5 Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy.

(i) Accordingly, introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex -gratia payments to employees on retirement is not a change in an accounting policy.

(ii) Similarly, the adoption of a new accounting policy for events or transactions which did not occur previously or that were immaterial will not be treated as a change in an accounting policy.

Q-2 The Accountant of Mobile Limited has sought your opinion with relevant reasons, whether the following transactions will be treated as change in Accounting Policy or not for the year ended 31st March, 2019. Please advise him in the following situations in accordance with the provisions of relevant Accounting Standard;

(i) Provision for doubtful debts was created @ 2% till 31st March, 2018. From the Financial year 2018-2019, the rate of provision has been changed to 3%.

(ii) During the year ended 31st March, 2019, the management has introduced a formal gratuity scheme in place of ad-hoc ex-gratia payments to employees on retirement.

(iii) Till the previous year the furniture was depreciated on straight line basis over a period of 5 years. From current year, the useful life of furniture has been changed to 3 years.

(iv) Management decided to pay pension to those employees who have retired after completing 5 years of service in the organization. Such employees will get pension of Rs. 20,000 per month. Earlier there was no such scheme of pension in the organization.

(v) During the year ended 31st March, 2019, there was change in cost formula in measuring the cost of inventories.

Ans. In the given case, Mobile limited created 2% provision for doubtful debts till 31st March, 2018. Subsequently in 2018-19, the company revised the estimates based on the changed circumstances and wants to create 3% provision. Thus change in rate of provision of doubtful debt is change in estimate and is not change in accounting policy. This change will affect only current year.

(ii) As per AS 5, the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy. Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is a transaction which is substantially different from the previous policy, will not be treated as change in an accounting policy.

(iii) Change in useful life of furniture from 5 years to 3 years is a change in estimate and is not a change in accounting policy.

(iv) Adoption of a new accounting policy for events or transactions which did not occur previously should not be treated as a change in an accounting policy. Hence the introduction of new pension

scheme is not a change in accounting policy.

(v) Change in cost formula used in measurement of cost of inventories is a change in accounting policy.

Q-3 Explain in brief, the alternative measurement bases, for determining the value at which an element can be recognized in the Balance Sheet or Statement of Profit and Loss.

Ans : The Framework for Recognition and Presentation of Financial statements recognises four alternative measurement bases for the purpose of determining the value at which an element can be recognized in the balance sheet or statement of profit and loss. These bases are: (i)Historical Cost; (ii)Current cost (iii) Realisable (Settlement) Value and (iv) Present Value.

A brief explanation of each measurement basis is as follows :

1. **Historical Cost**: Historical cost means acquisition price. According to this, assets are recorded at an amount of cash or cash equivalent paid or the fair value of the asset at the time of acquisition. Liabilities are generally recorded at the amount of proceeds received in exchange for the obligation.
2. **Current Cost**: Current cost gives an alternative measurement basis. Assets are carried out at the amount of cash or cash equivalent that would have to be paid if the same or an equivalent asset was acquired currently. Liabilities are carried at the undiscounted amount of cash or cash equivalents that would be required to settle the obligation currently.
3. **Realisable (Settlement) Value**: As per realisable value, assets are carried at the amount of cash or cash equivalents that could currently be obtained by selling the assets in an orderly disposal. Liabilities are carried at their settlement values; i.e. the undiscounted amount of cash or cash equivalents paid to satisfy the liabilities in the normal course of business.
4. **Present Value**: Under present value convention, assets are carried at present value of future net cash flows generated by the concerned assets in the normal course of business. Liabilities under this convention are carried at present value of future net cash flows that are expected to be required to settle the liability in the normal course of business.

Q-4 PQR Ltd. is in the process of finalizing its accounts for the year ended 31st March, 2018. The company seeks your advice on the following:

(i) Goods worth of 5,00,000 were destroyed due to flood in September, 2015. A claim was lodged with insurance company. But no entry was passed in the books for insurance claim in the financial year 2015-16. In March, 2018, the claim was passed and the company received a payment of f 3,50,000 against the claim. Explain the treatment of such receipt in final account for the year ended 31st March, 2018.

(ii) Company created a provision for bad and doubtful debts at 2.5% on debtors in preparing the financial statements for the year 2017-18.

Subsequently, on a review of the credit period allowed and financial capacity of the customers, the company decides to increase the provision to 8% on debtors as on 31.03.2018. The accounts were not approved by the Board of Directors till the date of decision. While applying the relevant accounting standard, can this revision be considered as an extra ordinary item or prior period item?

Ans :

(i) As per the provisions of AS 5 "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies", prior period items are income or expenses, which arise, in the current period as a result of error or omissions in the preparation of financial statements of one or more prior periods. Further, the nature and amount of prior period items should be separately disclosed in the statement of profit and loss in a manner that their impact on current profit or loss can be perceived.

In the given instance, it is clearly a case of error/omission in preparation of financial statements for the year 2015-16. Hence, claim received in the financial year 2017-18 is a prior period item and should be separately disclosed in the statement of Profit and Loss.

(ii) In the given case, a limited company created 2.5% provision for doubtful debts for the year 2017-2018. Subsequently, the company revised the estimates based on the changed circumstances and wants to create 8% provision.

As per AS 5, the revision in rate of provision for doubtful debts will be considered as change in estimate and is neither a prior period item nor an extraordinary item.

The effect of such change should be shown in the profit and loss account for the year ending 31st March, 2018.

Q-5 Bela Ltd. has a vacant land measuring 20,000 sq. mts, which it had no intention to use in the future. The Company decided to sell the land to tide over its liquidity problems and made a profit of Rs.10 Lakhs by selling the said land. Moreover, there was a fire in the factory and a part of the unused factory shed valued at Rs.8 Lakhs was destroyed. The loss from fire was set off against the profit from sale of land and profit of Rs.2 lakhs was disclosed as net profit from sale of assets.

You are required to examine the treatment and disclosure done by the company and advise the company in line with AS 5.

Ans. As per AS 5 "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies" Extraordinary items should be disclosed in the statement of profit and loss as a part of net profit or loss for the period. The nature and the amount of each extraordinary item should be separately disclosed in the statement of profit and loss in a manner that its impact on current profit or loss can be perceived.

In the given case the selling of land to tide over liquidation problems as well as fire in the Factory does not constitute ordinary activities of the Company. These items are distinct from the ordinary activities of the business. Both the events are material in nature and expected not to recur frequently or regularly. Thus, these are Extraordinary Items.

Therefore, in the given case, disclosing net profits by setting off fire losses against profit from sale of land is not correct. The profit on sale of land, and loss due to fire should be disclosed separately in the statement of profit and loss.

Q-6 State whether the following statements are 'True' or 'False'. Also give reason for your answer.

(1) As per the provisions of AS-5, extraordinary items should not be disclosed in the statement of profit and loss as a part of net profit or loss for the period.

(2) As per the provisions of AS-12, government grants in the nature of promoters' contribution which become refundable should be reduced from the capital reserve.

(3) As per the provisions of AS-2, inventories should be valued at the lower of cost and selling price.

(4) As per the provisions of AS-13, a current investment is an investment, that by its nature, is readily realisable and is intended to be held for not more than six months from the date on which such investment is made.

(5) As per the provisions of AS-4, a contingency is a condition or situation, the ultimate outcome of which (gain or loss) will be known or determined only on the occurrence of one or more uncertain future events.

Ans.

(1) **False :** The nature and the amount of each extraordinary item should be separately disclosed in the statement of profit and loss in a manner that its impact on current profit or loss can be perceived.

(2) **True:** When grants in the nature of promoters' contribution becomes refundable, in part or in full to the government on non-fulfillment of some specified conditions, the relevant amount refundable to the government is reduced from the capital reserve.

(3) **False:** Inventories should be valued at the lower of cost and net realizable value (not selling price) as per AS 2.

(4) **False:** A current investment is an investment that is by its nature readily realizable and is intended to be held for not more than one year from the date on which such investment is made.

(5) **False:** A contingency is a condition or situation, the ultimate outcome of which, gain or loss, will be known or determined only on the occurrence, or non-occurrence, of one or more uncertain future events.

Q-7 Explain whether the following will constitute a change in accounting policy or not as per AS 5.

(i) Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement.

(ii) Management decided to pay pension to those employees who have retired after completing 5 years of service in the organization. Such employees will get pension of ₹ 20,000 per month. Earlier there was no such scheme of pension in the organization.

Ans. As per AS 5 `Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy.

(i) Accordingly, introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is not a change in an accounting policy.

(ii) Similarly, the adoption of a new accounting policy for events or transactions which did not occur previously or that were immaterial will not be treated as a change in an accounting policy.

Q-8 The Accountant of Virush Limited has sought your opinion, whether the following transactions will be treated as change in Accounting Policy or not for the year ended 31st March, 2020. Please advise him in the following situations in accordance with the provisions of relevant Accounting Standard;

(i) Till the previous year the machinery was depreciated on straight line basis over a period of 5 years. From current year, the useful life of furniture has been changed to 3 years.

(ii) Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement.

Ans.

(i) Change in useful life of machinery from 5 years to 3 years is a change in estimate and is not a change in accounting policy.

(ii) Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is not a change in an accounting policy.

Q-9 Goods of Rs.5,00,000 were destroyed due to flood in September, 2015. A claim was lodged with insurance company, but no entry was passed in the books for insurance claim.

In March, 2018, the claim was passed and the company received a payment of Rs.3,50,000 against the claim. Explain the treatment of such receipt in final accounts for the year ended 31st March, 2018.

Ans. As per the provisions of AS 5 "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies", prior period items are income or expenses, which arise, in the current period as a result of error or omissions in the preparation of financial statements of one or more prior periods. Further, the nature and amount of prior period items should be separately disclosed in the statement of profit and loss in a manner that their impact on current profit or loss can be perceived.

In the given instance, it is clearly a case of error in preparation of financial statements for the year 2015-16. Hence, claim received in the financial year 2017-18 is a prior period item and should be separately disclosed in the statement of Profit and Loss.

Q-10 The Accountant of Mobile Limited has sought your opinion with relevant reasons, whether the following transactions will be treated as change in Accounting Policy or not for the year ended 31st March, 2017. You are required to advise him in the following situations in accordance with the provisions of AS 5

(i) Provision for doubtful debts was created @ 2% till 31st March, 2016. From the Financial year 2016-2017, the rate of provision has been changed to 3%.

(ii) During the year ended 31st March, 2017, the management has introduced a formal gratuity scheme in place of ad-hoc ex-gratia payments to employees on retirement.

(iii) Till the previous year the furniture was depreciated on straight line basis over a period of 5 years. From current year, the useful life of furniture has been changed to 3 years.

(iv) Management decided to pay pension to those employees who have retired after completing 5 years of service in the organization. Such employees will get pension of Rs.20,000 per month. Earlier there was no such scheme of pension in the organization.

(v) During the year ended 31st March, 2017, there was change in cost formula in measuring the cost of inventories.

Ans. **(i)** In the given case, Mobile limited created 2% provision for doubtful debts till 31st March, 2016. Subsequently in 2016-17, the company revised the estimates based on the changed circumstances and wants to create 3% provision. Thus change in rate of provision of doubtful debt is change in estimate and is not change in accounting policy. This change will affect only current year.

(ii) As per AS 5, the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy. Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is a transaction which is substantially different from the previous policy, will not be treated as change in an accounting policy.

(iii) Change in useful life of furniture from 5 years to 3 years is a change in estimate and is not a change in accounting policy.

(iv) Adoption of a new accounting policy for events or transactions which did not occur previously should not be treated as a change in an accounting policy. Hence the introduction of new pension scheme is not a change in accounting policy.

(v) Change in cost formula used in measurement of cost of inventories is a change in accounting policy.

Q-11 The Accountant of Mobile Limited has sought your opinion with relevant reasons, whether the following transactions will be treated as change in Accounting Policy or not for the year ended 31st March, 2019. Please advise him in the following situations in accordance with the provisions of relevant Accounting Standard;

(i) Provision for doubtful debts was created @ 2% till 31st March, 2018. From the Financial year 2018-2019, the rate of provision has been changed to 3%.

(ii) During the year ended 31st March, 2019, the management has introduced a formal gratuity scheme in place of ad-hoc ex-gratia payments to employees on retirement.

(iii) Till the previous year the furniture was depreciated on straight line basis over a period of 5 years. From current year, the useful life of furniture has been changed to 3 years.

(iv) Management decided to pay pension to those employees who have retired after completing 5 years of service in the organization. Such employees will get pension of ₹ 20,000 per month. Earlier there was no such scheme of pension in the organization.

(v) During the year ended 31st March, 2019, there was change in cost formula in measuring the cost of inventories.

Ans.(i) In the given case, Mobile limited created 2% provision for doubtful debts till 31st March, 2018. Subsequently in 2018-19, the company revised the estimates based on the changed circumstances and wants to create 3% provision. Thus change in rate of provision of doubtful debt is change in estimate and is not change in accounting policy. This change will affect only current year.

(ii) As per AS 5, the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy. Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is a transaction which is substantially different from the previous policy, will not be treated as change in an accounting policy.

(iii) Change in useful life of furniture from 5 years to 3 years is a change in estimate and is not a change in accounting policy.

(iv) Adoption of a new accounting policy for events or transactions which did not occur previously should not be treated as a change in an accounting policy. Hence the introduction of new pension scheme is not a change in accounting policy.

(v) Change in cost formula used in measurement of cost of inventories is a change in accounting policy.

Q-12 Bela Ltd. has a vacant land measuring 20,000 sq. mts, which it had no intention to use in the future. The Company decided to sell the land to tide over its liquidity problems and made a profit of Rs.10 Lakhs by selling the said land. Moreover, there was a fire in the factory and a part of the unused factory shed valued at Rs.8 Lakhs was destroyed. The loss from fire was set off against the profit from sale of land and profit of Rs.2 lakhs was disclosed as net profit from sale of assets.

*You are required to **examine** the treatment and disclosure done by the company and advise the company in line with AS 5.*

Ans. As per AS 5 "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies" Extraordinary items should be disclosed in the statement of profit and loss as a part of net profit or loss for the period. The nature and the amount of each extraordinary item should be separately disclosed in the statement of profit and loss in a manner that its impact on current profit or loss can be perceived.

In the given case the selling of land to tide over liquidation problems as well as fire in the Factory does not constitute ordinary activities of the Company. These items are distinct from the ordinary activities of the business. Both the events are material in nature and expected not to recur frequently or regularly. Thus, these are Extraordinary Items.

Therefore, in the given case, disclosing net profits by setting off fire losses against profit from sale of land is not correct. The profit on sale of land, and loss due to fire should be disclosed separately in the statement of profit and loss.

Q-13 State whether the following items are examples of change in Accounting Policy / Change in Accounting Estimates / Extraordinary items / Prior period items / Ordinary Activity:

(i) Actual bad debts turning out to be more than provisions.

(ii) Change from Cost model to Revaluation model for measurement of carrying amount of PPE.

(iii) Government grant receivable as compensation for expenses incurred in previous accounting period.

(iv) Treating operating lease as finance lease.

(v) Capitalization of borrowing cost on working capital.

(vi) Legislative changes having long term retrospective application.

(vii) Change in the method of depreciation from straight line to WDV.

(viii) Government grant becoming refundable.

(ix) Applying 10% depreciation instead of 15% on furniture.

(x) Change in useful life of fixed assets.

Ans. Classification of given items is as follows:

Sr. No.	Particulars	Remarks
(i)	Actual bad debts turning out to be more than provisions	Change in Accounting Estimates
(ii)	Change from Cost model to Revaluation model for measurement of carrying amount of PPE	Change in Accounting Policy
(iii)	Government grant receivable as compensation for expenses incurred in previous accounting period	Extra -ordinary Items
(iv)	Treating operating lease as finance lease.	Prior- period Items
(v)	Capitalization of borrowing cost on working capital	Prior-period Items (as interest on working capital loans is not eligible for capitalization)
(vi)	Legislative changes having long term retrospective application	Ordinary Activity
(vii)	Change in the method of depreciation from straight line to WDV	Change in Accounting Estimates
(viii)	Government grant becoming refundable	Extra -ordinary Items
(ix)	Applying 10% depreciation instead of 15% on furniture	Prior- period Items
(x)	Change in useful life of fixed assets	Change in Accounting Estimates

Q-14 XYZ Ltd. is in the process of finalizing its account for the year ended 31st March, 2020. The company seeks your advice on the following:

The company's tax assessment for assessment year 2017-18 has been completed on 14th February, 2020 with a demand of ₹ 5.40 crore. The company paid the entire due under protest without prejudice to its right of appeal. The company files its appeal before the appellate authority wherein the grounds of appeal cover tax on additions made in the assessment order for a sum of ₹ 3.70 crore.

Ans. Since the company is not appealing against the addition of ₹ 1.70 crore (₹ 5.40 crore less ₹ 3.70 crore), therefore, the same should be provided/ expensed off in its accounts for the year ended on 31st March, 2020. However, the amount paid under protest can be kept under the heading `Long-term Loans & Advances / Short-term Loans and Advances' as the case may be alongwith disclosure as contingen t liability of ₹ 3.70 crore.

Q-15 There was a major theft of stores valued at ₹ 10 lakhs in the preceding year which was detected only during current financial year (2020-2021). How will you deal with this information in preparing the financial statements of R Ltd. for the year ended 31st March, 2021.

Ans. Due to major theft of stores in the preceding year (2019-2020) which was detected only during the current financial year (2020–2021), there was overstatement of closing inventory of stores in the preceding year. This must have also resulted in the overstatement of profits of previous year, brought forward to the current year. The adjustments are required to be made in the current year as `Prior

Period Items' as per AS 5 (Revised) on Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies. Accordingly, the adjustments relating to both opening inventory of the current year and profit brought forward from the previous year should be separately disclosed in the statement of profit and loss together with their nature and amount in a manner that their impact on the current profit or loss can be perceived. Alternatively, it may be assumed that in the preceding year, the value of inventory of stores as found out by physical verification of inventories was considered in the preparation of financial statements of the preceding year. In such a case, only the disclosure as to the theft and the resulting loss is required in the notes to the accounts for the current year i.e, year ended 31st March, 2021.

Q-16 Management decided to pay pension to those employees who have retired after completing 5 years of service in the organisation. Such employees will get pension of ₹ 20,000 per month. Earlier there was no such scheme of pension in the organization. Explain whether this will constitute a change in accounting policy or not as per AS 5.

Ans. As per AS 5 `Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy. Accordingly, the adoption of a new accounting policy of paying pension to retired employees is a policy for events or transactions which did not occur previously. Hence, it will not be treated as a change in an accounting policy.

Q-17 The Accountant of Mobile Limited has sought your opinion with relevant reasons, whether the following transactions will be treated as change in Accounting Policy or not for the year ended 31st March, 2021. Please advise him in the following situations in accordance with the provisions of relevant Accounting Standard;

(i) Provision for doubtful debts was created @ 2% till 31st March, 2020. From theFinancial year 2020-2021, the rate of provision has been changed to 3%.

(ii) During the year ended 31st March, 2021, the management has introduced a formal gratuity scheme in place of ad-hoc ex-gratia payments to employees on retirement.

(iii) Till the previous year the furniture was depreciated on straight line basis over a period of 5 years. From current year, the useful life of furniture has been changed to 3 years.

(iv) Management decided to pay pension to those employees who have retired after completing 5 years of service in the organization. Such employees will get pension of ₹ 20,000 per month. Earlier there was no such scheme of pension in the organization.

(v) During the year ended 31st March, 2021, there was change in cost formula inmeasuring the cost of inventories.

Ans.

(i) In the given case, Mobile limited created 2% provision for doubtful debts till 31st March, 2020. Subsequently in 2020-21, the company revised the estimates based on the changed circumstances and wants to create 3% provision. Thus change in rate of provision of doubtful debt is change in accounting estimate and is not a change in accounting policy. This change will affect only current year.

(ii) As per AS 5, the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy. Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is a transaction which is substantially different from the previous policy, will not be treated as change in accounting policy.

(iii) Change in useful life of furniture from 5 years to 3 years is a change in accounting estimate and is not a change in accounting policy.

(iv) Adoption of a new accounting policy for events or transactions which did not occur previously should not be treated as a change in an accounting policy.

Hence the introduction of new pension scheme is not a change in accounting policy.

(v) Change in cost formula used in measurement of cost of inventories is a changein accounting policy.

Q-18 A company created a provision of ₹ 7,50,000 for staff welfare while preparing the financial statements for the year 2021-22. On 31st March 2022, in a meeting with staff welfare association, it was decided to increase the amount of provision for staff welfare to ₹ 10,00,000. The accounts were approved by Board of Directors on 15th April, 2022.

You are required to explain the treatment of such revision in financial statements for the year ended 31st March 2022 in line with the provisions of AS 5?

Ans. As per AS 5 "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies", the change in amount of staff welfare provision amounting ₹ 2,50,000 is neither a prior period item nor an extraordinary item. It is a change in estimate, which has been occurred in the year 2021-22.

As per the provisions of the standard, normally, all items of income and expense which are recognized in a period are included in the determination of the net profit or loss for the period. This includes extraordinary items and the effects of changes in accounting estimates. However, the effect of such change in accounting estimate should be classified using the same classification in the statement of profit and loss, as was used previously, for the estimate.

AS-7 CONSTRUCTION CONTRACTS

Q-1 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	9,000
Variation in Revenue (+)	-	200	200
Contracts costs incurred up to the reporting date	2,093	6,168*	8,100**
Estimated profit for whole contract	950	1,000	1,000

*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 Stat ement of Profit and Loss as per AS -7 (revised).

Ans. The amounts of revenue, expenses and profit recognized in the statement of profit and loss in three years are computed below:

(Amount in ₹ lakhs)

	Up to the reporting date	Recognized in previous years	Recognized in current year
Year 1			
Revenue (9,000 x 26%)	2,340	-	2,340
Expenses (8,050 x 26%)	2,093	-	2,093
Profit	**247**	-	**247**
Year 2			
Revenue (9,200 x 74%)	6,808	2,340	4,468
Expenses (8,200 x 74%)	6,068	2,093	3,975
Profit	**740**	**247**	**493**
Year 3			
Revenue (9,200 x 100%)	9,200	6,808	2,392
Expenses (8,200 x 100%)	8,200	6,068	2,132
Profit	**1,000**	**740**	**260**
Working Note:			
	Year 1	**Year 2**	**Year 3**
Revenue after considering variations	9,000	9,200	9,200
Less: Estimated profit for whole contract	950	1,000	1,000
Estimated total cost of the contract (A)	8,050	8,200	8,200
Actual cost incurred upto the reporting date (B)	2,093	6,068 (6,168 -100)	8,200 (8,100+100)
Degree of completion (B/A)	26%	74%	100%

Q-2 X Ltd. negotiates with Bharat Petroleum Corporation Ltd (BPCL), for construction of "Franchise Retail Petrol Outlet Stations". Based on proposals submitted to different Zonal offices of BPCL, the final approval for one outlet each in Zone A, Zone B, Zone C, Zone D, is awarded to X Ltd. Agreement (in single document) is entered into with BPCL for Rs. 490 lakhs. The agreement lays down values for each of the four outlets (Rs. 88 + 132 + 160 + 110 lakhs) in addition to individual completion time. You are required to examine and comment whether X Ltd., will treat it as a single contract or four separate contracts.

Ans. As per AS 7 on `Construction Contracts', when a contract covers a number of assets, the construction of each asset should be treated as a separate construction contract when:

(a) separate proposals have been submitted for each asset;

(b) each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and

(c) the costs and revenues of each asset can be identified.

In the given case, each outlet is submitted as a separate proposal to different Zonal Office, which can be separately negotiated, and costs and revenues thereof can be separately identified. Hence, each asset will be treated as a "single contract" even if there is one document of contract. Therefore, four separate contract accounts have to be recorded and maintained in the books of X Ltd. For each contract, principles of revenue and cost recognition have to be applied separately and net income will be determined for each asset as per AS 7.

Q-3 M/s Highway Constructions undertook the construction of a highway on 01.04.2016. The contract was to be completed in 2 years. The contract price was estimated at Rs.150 crores. Up to 31.03.2017 the company incurred Rs. 120 crores on the construction. The engineers involved in the project estimated that a further Rs. 45 crores would be incurred for completing the work.

What amount should be charged to profit and loss statement for the year 2016 -17 as per the provisions of Accounting Standard 7 "Construction Contracts"?

Ans. **Statement showing amount to be charged to Profit and Loss Statement as per AS 7**

	Rs. in crores
Cost of construction incurred upto 31.03.2017	120
Add: Estimated future cost	45
Total estimated cost of construction	165
Degree of completion (120/165 x 100)	72.73%
Revenue recognized (72.73% of 150)	109 (approx)
Total foreseeable loss (165 – 150)	15
Less: Loss for the current year (120 – 109)	11
Loss to be provided for in the P&L statement	4

Q-4 On 1st December, 2018, "Sampath" Construction Company Limited undertook a contract to construct a building for ₹ 108 lakhs. On 31st March, 2019 the company found that it had already spent ₹ 83.99 lakhs on the construction. A prudent estimate of additional cost for completion was ₹ 36.01 lakhs.

You are required to compute the amount of provision for foreseeable loss, which must be made in the Final Accounts for the year ended 31st March, 2019 based on AS 7 "Accounting for Construction Contracts."

Ans : **Calculation of foreseeable loss for the year ended 31st March, 2019**

(as per AS 7 "Construction Contracts")

	(₹ in lakhs)
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	12.00

According to para 35 of AS 7 (Revised 2002) "Construction Contracts", when it is probable that total contract costs will exceed 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.

Q-5 GTI Ltd. negotiates with Bharat Oil Corporation Ltd. (BOCL), for construction of "Retail Petrol & Diesel Outlet Stations". Based on proposals submitted to different Regional Offices of BOCL, the final approval for one outlet each in Region X, Region Y, Region Z is awarded to GTI Ltd. A single agreement is entered into between two. The agreement lays down values for each of the three outlets i.e. ₹ 102 lacs, ₹ 150 lacs,₹ 130 lacs for Region X, Region Y, Region Z respectively. Agreement also lays down completion time for each Region.

Comment whether GTI Ltd. will treat it as single contract or three separate contracts with reference to AS-7?

Ans : As per AS 7 `Construction Contracts', when a contract covers number of assets, the construction of each asset should be treated as a separate construction contract when:

(a) separate proposals have been submitted for each asset;

(b) each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and

(c) the costs and revenues of each asset can be identified.

In the given case, each outlet is submitted as a separate proposal to different Zonal Offices, which can be separately negotiated, and costs and revenues thereof can be separately identified. Hence, each asset will be treated as a "single contract" even if there is one single agreement for contracts.

Therefore, three separate contract accounts must be recorded and maintained in the books of GTI Ltd. For each contract, principles of revenue and cost recognition must be applied separately and net income will be determined for each asset as per AS 7.

Q-6 Uday Constructions undertake to construct a·bridge for the Government of Uttar Pradesh. The construction commenced during the financial year ending 31.03.2018 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. You are given the following information for the year ended 31.03.2018:

Cost incurred upto 31.03.2018 ₹ 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 ascertain the state of completion and compute the amount of revenue and profit to be recognized for the year as per AS-7.

Ans.

	₹ in crore
Cost of construction of bridge incurred upto 31.3.18	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) x 100 = 40%

Revenue and Profit to be recognized for the year ended 31st March, 2018 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, 2018 = ₹ 5.04 crore less ₹ 4 crore = 1.04 crore.

Q-7 (i) AP Ltd., a construction contractor, undertakes the construction of commercial complex for Kay Ltd. AP Ltd. submitted separate proposals for each of 3 units of commercial complex. A single agreement is entered into between the two parties. The agreement lays down the value of each of the 3 units, i.e. ₹ 50 Lakh ₹ 60 Lakh and ₹ 75 Lakh respectively. Agreement also lays down the completion time for each unit.

Comment, with reference to AS- 7, whether AP Ltd., should treat it as a single contract or three separate contracts.

(ii) On 1st December, 2017, GR Construction Co. Ltd. undertook a contract to construct a building for ₹ 45 lakhs. On 31st March, 2018, the company found that it had already spent ₹ 32.50 lakhs on the construction. Additional cost of completion is estimated at ₹ 15.10 lakhs. What amount should be charged to revenue in the final accounts for the year ended 31st March, 2018 as per provisions of AS-7?

Ans.

(i) As per AS 7 `Construction Contracts', when a contract covers a number of assets, the construction of each asset should be treated as a separate construction contract when:

(a) separate proposals have been submitted for each asset;

(b) each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and

(c) the costs and revenues of each asset can be identified.

Therefore, Mr. AP Ltd. is required to treat construction of each unit as a separate construction contract as the above-mentioned conditions of AS 7 are fulfilled in the given case.

(ii)

	₹ in lakhs
Cost of construction incurred till date	32.50
Add: Estimated future cost	15.10
Total estimated cost of construction	47.60

Percentage of completion till date to total estimated cost of construction

= (32.50/47.60) x 100 = 68.28%

Proportion of total contract value recognised as revenue for the year ended 31st March, 2018 per AS 7 (Revised)

= Contract price x percentage of completion

= ₹ 45 lakh x 68.28% = ₹ 30.73 lakhs.

	(₹ in lakhs)
Total cost of construction	47.60
Less: Total contract price	(45.00)
Total foreseeable loss to be recognized as expense	2.60

According to of AS 7, when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately.

Q-8 Sarita Construction Co. obtained a contract for construction of a dam. The following detailsare available in records of company for the year ended 31st March, 2018:

	₹ 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.

Ans.

(i)

Loss for the year ended, 31st March, 2018	**(₹ 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 ₹ 4,250 will be recognized.

(ii)

Contract work-in-progress as on 31.3.18	**(₹ in lakhs)**
Contract work-in-progress i.e. cost incurred to date are ₹ 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 x 100) of total costs ofconstruction.

Proportion of total contract value recognised as revenue:

46.15% of ₹ 12,000 lakhs = ₹ 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) ₹ in lakhs

= [3,250 – 7,000] ₹ in lakhs

Amount due to customers = ₹ 3,750 lakhs.

Q-9 Uday Constructions undertake to construct a·bridge for the Government of Uttar Pradesh.

The construction commenced during the financial year ending 31.03.2019 and is likely to be completed by the next financial year. The contract is for a fixed price of ₹ 12 crore with an escalation clause. You are given the following information for the year ended 31.03.2019:

Cost incurred upto 31.03.2019	₹ 4 crore
Further cost estimated to complete the contract	₹ 6 crore

Escalation in cost was by 5%. Hence, the contract price is also increased by 5%.

You are required to ascertain the stage of completion and compute the amount of revenue and profit to be recognized for the year as per AS 7.

Ans.

	₹ in crore
Cost of construction of bridge incurred upto 31.3.2019	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) x 100 = 40%

Revenue and Profit to be recognized for the year ended 31st March, 2019 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, 2019 = ₹ 5.04 crore – ₹ 4 crore = 1.04 crore.

Q-10 Akar Ltd. signed on 01/04/19, a construction contract for ₹ 1,50,00,000. Following particulars are extracted in respect of contract, for the period ending 31/03/20.

- Materials used ₹ 71,00,000
- Labour charges paid ₹ 36,00,000
- Hire charges of plant ₹ 10,00,000
- Other contract cost incurred ₹ 15,00,000
- Labour charges of ₹ 2,00,000 are still outstanding on 31.3.20.
- It is estimated that by spending further ₹ 33,50,000 the work can be completed in all respect.

You are required to compute profit/loss for the year to be taken to Profit & Loss Account and additional provision for foreseeable loss to be recognized as per AS 7.

Ans. Statement showing the amount of profit/loss to be taken to Profit and Loss Account and additional provision for the foreseeable loss as per AS 7.

	Cost of Construction	₹	₹
	Material used		71,00,000
	Labour Charges paid	36,00,000	
Add:	Outstanding on 31.03.2020	2,00,000	38,00,000
	Hire Charges of Plant		10,00,000
	Other Contract cost incurred		15,00,000
	Cost incurred upto 31.03.2020		1,34,00,000
Add:	Estimated future cost		33,50,000
	Total Estimated cost of construction		1,67,50,000
	Degree of completion (1,34,00,000/1,67,50,000 x 100)		80%
	Revenue recognized (80% of 1,50,00,000)		1,20,00,000
	Total foreseeable loss (1,67,50,000 - 1,50,00,000)		17,50,000
Less:	Loss for the current year (1,34,00,000 - 1,20,00,000)		14,00,000
	Loss to be provided for		3,50,000

Q-11 A contractor firm obtained a contract for construction of bridge. The following details are available in the records kept for the year ended March 31, 2021:

	in Crore)
Total Contract Price	500
Work Certified	250
Work not Certified	80
Estimated further Cost to Completion	220
Progress Payment Received	200
Payment to be Received	70

You are required to calculate :

(i) The amount of revenue to be recognized.

(ii) The amount of profit or loss to be recognized.

(iii) The amount due from/ to customers.

Also present relevant disclosures as per AS-7 (Revised).

Ans. (a)

(i) **Proportion of total contract value recognized as revenue**

Percentage of completion of contract to total estimated cost of construction

$= [(250 + 80) / (250 + 80 + 220)] \times 100 = 60\%$

Revenue to be recognized till date = 60% of ₹ 500 crore = ₹ 300 crore.

(ii) **Calculation of profit/ loss for the year ended 31st March, 2021** **(₹ in crore)**

Total estimated cost of construction		
Work certified	250	
Work not certified	80	
Estimated further cost to completion	220	550
Less: Total contract price		(500)
Total foreseeable loss to be recognized as expense		50

According to AS 7 "Construction Contracts", when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately.

(iii) **Amount due from / to customers** = Contract costs incurred till date + Recognised profits – Recognised losses – (Progress payments received + Progress payments to be received)

= ₹ [(250 + 80) + Nil – 50 – (200 + 70)] crore

= ₹ [330 – 50 – 270] crore

Amount due from customers (shown as an asset) = ₹ 10 crore.

(iv) **The relevant disclosures under AS 7 (Revised) are given below:**

	₹ in crores
Contract revenue till 31st March, 2021	300
Contract expenses till 31st March, 2021	330
Recognized losses for the year 31st March, 2021	50
Progress billings f (200+ 70)	270
Progress (billed but not received from contractee)	70
Gross amount due from customers	10

Q-12 PRZ & Sons Ltd. are Heavy Engineering contractors specializing in construction of dams. From the records of the company, the following data is available pertaining to year ended 31st March, 2021:

	(₹ crore)
Total Contract Price	2,400
Work Certified	1,250
Work pending certification	250
Estimated further cost to completion	1,750
Stage wise payments received	1,100
Progress payments in pipe line	300

Using the given data and applying the relevant Accounting Standard you are required to:

(i) Compute the amount of profit/loss for the year ended 31st March, 2021.

(ii) Arrive at the contract work in progress as at the end of financial year 2020-21.

(iii) Determine the amount of revenue to be recognized out of the total contract value.

(iv) Work out the amount due from/to customers as at year end.

Ans.

(i)

Calculation of profit/ loss for the year ended 31st March, 2021	**(₹ in crores)**
Total estimated cost of construction (1,250 + 250 + 1,750)	3,250
Less: Total contract price	(2,400)
Total foreseeable loss to be recognized as expense	850

According to AS 7 (Revised 2002) "Construction Contracts", when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately.

(ii)

Contract work-in-progress i.e. cost incurred to date	(₹ in crores)
Work certified	1,250
Work not certified	250
	1,500

(iii) Proportion of total contract value recognised as revenue

Percentage of completion of contract to total estimated cost of construction

= (1,500 / 3,250)„e100 = 46.15%

Revenue to be recognized till date = 46.15% of ₹ 2,400 crores = ₹ 1,107.60 crores.

(iv) Amount due from / to customers = Contract costs + Recognised profits – Recognised losses – (Progress payments received + Progress payments to be received)

= ₹ [1,500 + Nil – 850 – (1100 + 300)] crores

= ₹ [1,500 – 850 – 1,400] crores

Amount due to customers (shown as liability) = ₹ 750 crores.

Q-13 The following data is provided for M/s. Raj Construction Co.

(i) Contract Price - ₹ 85 lakhs

(ii) Materials issued - ₹ 21 Lakhs out of which Materials costing ₹ 4 Lakhs is still lying unused at the end of the period.

(iii) Labor Expenses for workers engaged at site - ₹ 16 Lakhs (out of which ₹ 1 Lakh is still unpaid)

(iv) Specific Contract Costs - ₹ 5 Lakhs

(v) Sub-Contract Costs for work executed - ₹ 7 Lakhs, Advances paid to sub-contractors - ₹ 4 Lakhs

(vi) Further Cost estimated to be incurred to complete the contract - ₹ 35 Lakhs

You are required to compute the Percentage of Completion, the Contract Revenue and Cost to be recognized as per AS-7.

Ans. Computation of contract cost

	₹ Lakh	₹ Lakh
Material cost incurred on the contract (net of closing stock)	21-4	17
Add: Labor cost incurred on the contract (including outstanding amount)		16
Specified contract cost	given	5
Sub-contract cost (advances should not be considered)		7
Cost incurred (till date)		45
Add: further cost to be incurred		35
Total contract cost		80

Percentage of completion = Cost incurred till date/Estimated total cost

= ₹ 45,00,000/₹ 80,00,000

= 56.25%

Contract revenue and costs to be recognized

Contract revenue (₹ 85,00,000 x 56.25%) = ₹ 47,81,250

Contract costs = 45,00,000

Q-14 Rajendra undertook a contract ₹ 20,00,000 on an arrangement that 80% of the value of work done, as certified by the architect of the contractee should be paid immediately and that the remaining 20% be retained until the Contract was completed.

In Year 1, the amounts expended were ₹ 8,60,000, the work was certified for ₹ 8,00,000 and 80% of this was paid as agreed. It was estimated that future expenditure to complete the Contract would be ₹ 10,00,000.

In Year 2, the amounts expended were ₹ 4,75,000. Three-fourth of the work under contract was certified as done by December 31st and 80% of this was received accordingly. It was estimated that future expenditure to complete the Contract would be ₹ 4,00,000.

In Year 3, the amounts expended were ₹ 3,10,000 and on June 30th, the whole Contract was completed.

Show how Contract revenue would be recognized in the P & L A/c of Mr. Rajendra each year.

Ans. **Year 1**

Actual expenditure	₹8,60,000
Future estimated expenditure	10,00,000
Total Expenditure	18,60,000

$$\text{\% of work completed} = \frac{8,60,000}{18,60,000} \times 100 = 46.24\% \text{ (rounded off)}$$

Revenue to be recognized = 20,00,000 x 46.24%

= ₹ 9,24,800

Year 2

Actual expenditure	4,75,000
Future Expenditure	4,00,000
Expenditure incurred in Year 1	8,60,000
	17,35,000

$$\text{\% of work completed} = \frac{4,75,000\ 8,60,000}{17,35,000} = 76.95\% \text{ (rounded off)}$$

Revenue to be recognized (cumulative) = 20,00,000 x 76.95%

= 15,39,000

Less: revenue recognized in Year 1 =	(9,24,800)
Revenue to be recognized in Year 2 =	₹ 6,14,200

Year 3

Whole contract got completed therefore total contract value less revenue recognized up to year 2 will be amount of revenue to be recognized in year 3 i.e. 20,00,000 – 15,39,000 (9,24,800 + 6,14,200) = ₹ 4,61,000.

Note: Calendar year has been considered as accounting year

Q-15 Sky Limited belongs to Heavy Engineering Contractors specializing in construction of Flyovers. The company just entered into a contract with a local municipal corporation for building a flyover. No activity has started on this contract.

As per the terms of the contract, Sky Limited will receive an additional ₹ 50 lakhs if the construction of the flyover were to be finished within a period of two years from the commencement of the contract.

The Accountant of the entity wants to recognize this revenue since in the past the company has been able to meet similar targets very easily. Give your opinion on this treatment.

Ans. **(a)** According to AS 7 'Construction Contracts', incentive payments are additional amounts payable to the contractor if specified performance standards are met or exceeded. For example, a contract may allow for an incentive payment to the contractor for early completion of the contract. Incentive payments are included in contract revenue when both the conditions are met:

(i) the contract is sufficiently advanced that it is probable that the specified performance standards will be met or exceeded; and

(ii) the amount of the incentive payment can be measured reliably.

In the given problem, the contract has not even begun and hence the contractor (Sky Limited) should not recognize any revenue of this contract. Therefore, the accountant's contention for recognizing ₹50 lakhs as revenue is not correct.

Q-16 ABC Ltd., a construction contractor, undertakes the construction of commercial complex for XYZ Ltd. ABC Ltd. submitted separate proposals for each of 3 units of commercial complex. A single agreement is entered into between the two parties. The agreement lays down the value of each of the 3 units i .e. ₹ 50 lakh, ₹ 60 lakh and ₹ 75 lakh respectively. Agreement also lays down the completion time for each unit.

Comment, with reference to AS 7, whether ABC Ltd., should treat it as a single contract or three separate contracts.

Ans. As per AS 7 ₹Construction Contracts', when a contract covers a number of assets, the construction of each asset should be treated as a separate construction contract when:

(a) separate proposals have been submitted for each asset;

(b) each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and

(c) the costs and revenues of each asset can be identified.

ABC Ltd. has submitted separate proposals for each of the 3 units of commercial complex. Also the revenue and completion time has been laid down for each unit separately which implies separate negotiation for them.

Therefore, ABC Ltd. is required to treat construction of each unit as a separate construction contract as the above-mentioned conditions of AS 7 are fulfilled in the given case.

Q-17 In the case of a fixed price contract, the outcome of a construction contract can be estimated reliably only when certain conditions prescribed under AS 7 are satisfied. You are required to describe these conditions mentioned in the standard.

Ans. **(a)** In the case of a fixed price contract, the outcome of a construction contract c an be estimated reliably when all the following conditions are satisfied:

(i) total contract revenue can be measured reliably;

(ii) it is probable that the economic benefits associated with the contract will flow to the enterprise;

(iii) both the contract costs to complete the contract and the stage of contract completion at the reporting date can be measured reliably; and

(iv) the contract costs attributable to the contract can be clearly identified and measured reliably so that actual contract costs incurred can be compared with prior estimates.

(b) Mr. `X' as a contractor has just entered into a contract with a local municipal body for building a flyover. As per the contract terms, `X' will receive an additional ₹ 2 crore if the construction of the flyover were to be finished within a period of two years of the commencement of the contract. Mr. X wants to recognize this revenue since in the past he has been able to meet similar targets very easily. Is X correct in his proposal? Discuss.

(b) According to AS 7 (Revised) `Construction Contracts', incentive payments are additional amounts payable to the contractor if specified performance standards are met or exceeded. For example, a contract may allow for an incentive payment to the contractor for early completion of the contract. Incentive payments are included in contract revenue when: (i) the contract is sufficiently advanced that it is probable thatthe specified performance standards will be met or exceeded; and (ii) the amount of the incentive payment can be measured reliably. In the given problem, the contract has not even begun and hence the contractor (Mr. X) should not recognize any revenue of this contract.

Q-18 B Ltd. undertook a construction contract for ₹ 50 crores in April, 2020. The cost of construction was initially estimated at ₹ 35 crores. The contract is to be completed in 3 years. While executing the contract, the company estimated that the cost of completion of the contract would be ₹ 53 crores.

Can the company provide for the expected loss in the financial Statements for the year ended 31st March, 2021? Explain.

Ans.(b) As per para 35 of AS 7 "Construction Contracts", when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately. Therefore, the foreseeable loss of ₹3 crores (' 53 crores less ₹ 50 crores) should be recognized as an expense immediately in the year ended 31st March, 2021. The amount of loss is determined irrespective of

(i) Whether or not work has commenced on the contract;

(ii) Stage of completion of contract activity; or

(iii) The amount of profits expected to arise on other contracts which are not treated as a single construction contract in accordance provisions of AS 7.

Q-19 Bricks Ltd. signed on 01/04/21, a construction contract for ₹ 1,50,00,000. Following particulars are extracted in respect of contract, for the period ending 31/03/22:

- Materials issued ₹ 75,00,000
- Labour charges paid ₹ 36,00,000
- Hire charges of plant ₹ 10,00,000
- Other contract cost incurred ₹ 15,00,000
- Out of material issued, material lying unused at the end of period is ₹ 4,00,000
- Labour charges of ₹ 2,00,000 are still outstanding on 31.3.22.
- It is estimated that by spending further ₹ 33,50,000 (including material unused ₹4,00,000), the work can be completed in all respect.

You are required to compute profit/loss to be taken to Profit & Loss Account and additional provision for foreseeable loss as per AS 7.

Ans. **Statement showing the amount of profit/loss to be taken to Profit and Loss Account and additional provision for the foreseeable loss as per AS 7**

	Cost of Construction	₹	₹
	Material Issued	75,00,000	
Less:	Unused Material at the end of period	4,00,000	71,00,000
	Labour Charges paid	36,00,000	
Add:	Outstanding on 31.03.2022	2,00,000	38,00,000
	Hire Charges of Plant		10,00,000

	Other Contract cost incurred	15,00,000
	Cost incurred upto 31.03.2022	1,34,00,000
Add:	Estimated future cost	33,50,000
	Total Estimated cost of construction	1,67,50,000
	Degree of completion (1,34,00,000/1,67,50,000 x 100)	80%
	Revenue recognized (80% of 1,50,00,000)	1,20,00,000
	Total foreseeable loss (1,67,50,000 - 1,50,00,000)	17,50,000
Less:	Loss for the current year (1,34,00,000 - 1,20,00,000)	14,00,000
	Loss to be provided for	3,50,000

Q-20 Sarita Construction Co. obtained a contract for construction of a dam. The following details a re available in records of company for the year ended 31st March, 2021:

	₹ **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, 2021.

(ii) Contract work in progress as at end of financial year 2020-21.

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

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

Ans.

(i) Loss for the year ended, 31st March, 2021 (₹ 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, 2021 amounting ₹ 4,250 will be recognized.

(ii) Contract work-in-progress as on 31.3.21 (₹ in lakhs)

Contract work-in-progress i.e. cost incurred to date are ₹ 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 31.3.21 is 46.15% (7,500/16,250 x 100) of total costs of construction.

Proportion of total contract value recognised as revenue:

46.15% of ₹ 12,000 lakhs = ₹ 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)] ₹ in lakhs = [3,250 – 7,000] ₹ in lakhs

Amount due to customers = ₹ 3,750 lakhs

Q-21 Sudesh Ltd. acquired a patent at a cost of ₹ 2,40,00,000 for a period of 5 years and the product life-cycle was also 5 years. The company capitalized the cost and started amortizing the asset at ₹ 48,00,000 per annum. After two years it was found that the product life-cycle may continue for another 5 years from then. The net cash flows from the product during these 5 years were expected to be ₹ 36,00,000, ` 46,00,000, ₹ 44,00,000, ₹ 40,00,000 and ₹ 34,00,000. Find out the amortization cost of the patent for each of the years if the patent was renewable and Sudesh Ltd. got it renewed after expiry of five years.

Ans. The entity amortised ₹ 48,00,000 per annum for the first two years i.e. ₹96,00,000. The remaining carrying cost can be amortized during next 5 years on the basis of net cash flows arising from the sale of the product. The amortisation may be found as follows:

Year	Net cash flows (₹)	Amortization Ratio	Amortization Amount (₹)
I	-	0.20	48,00,000
II	-	0.20	48,00,000
III	36,00,000	0.180	25,92,000
IV	46,00,000	0.230	33,12,000
V	44,00,000	0.220	31,68,000
VI	40,00,000	0.200	28,80,000
VII	34,00,000	0.170	24,48,000
Total	2,00,00,000	1.000	2,40,00,000

It may be seen from above that from third year onwards, the balance of carrying amount ₹ 1,44,00,000 has been amortized in the ratio of net cash flows arising from the product .

AS-9 REVENUE RECOGNITION

Q-1 The following information of Meghna Ltd. is provided:

(i) Goods of ₹ 60,000 were sold on 20-3-2019 but at the request of the buyer these were delivered on 10-4-2019.

(ii) On 15-1-2019 goods of ₹ 1,50,000 were sent on consignment basis of which 20% of the goods unsold are lying with the consignee as on 31 -3-2019.

(iii) ₹ 1,20,000 worth of goods were sold on approval basis on 1 -12-2018. The period of approval was 3 months after wh ich they were considered sold. Buyer sent approval for 75% goods up to 31 -1-2019 and no approval or disapproval received for the remaining goods till 31 -3-2019.

(iv) Apart from the above, the company has made cash sales of ₹ 7,80,000 (gross).
Trade discount of 5% was allowed on the cash sales.

You are required to advise the accountant of Meghna Ltd., with valid reasons, the amount to be recognized as revenue in above cases in the context of AS -9.

Ans. As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should

be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i) The sale is complete but delivery has been postponed at buyer 's request. M/s Paper Products Ltd. should recognize the entire sale of ₹ 60,000 for the year ended 31st March, 2019.

Case (ii) 20% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 1,20,000 (80% of ₹ 1,50,000). In case of consignment sale revenue should not be recognized u ntil the goods are sold to a third party.

Case (iii) In case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time perio d for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting ₹ 1,20,000 as the time period for rejecting

the goods had expired.

Case (iv) Trade discounts given should be deducted in determining revenue. Thus ₹ 39,000 should be deducted from the amount of turnover of ₹ 7,80,000 for the purpose of recognition of revenue. Thus, revenue should be ₹ 7,41,000.

Q-2 Fashion Limited is engaged in manufacturing of readymade garments. They provide you the following information on 31st March, 2019:

(i) On 15th January, 2019 garments worth Rs. 4,00,000 were sent to Anand on consignment basisof which 25% garments unsold were lying with Anand as on 31st March, 2019.

(ii) Garments worth Rs. 1,95,000 were sold to Shine boutique on 25th March, 2019 but at therequest of Shine Boutique, these were delivered on 15th April, 2019.

(iii) On 1st November, 2018 garments worth Rs. 2,50,000 were sold on approval basis. The period of approval was 4 months after which they were considered sold. Buyer sent approval for 75% goods up to 31st December, 2018 and no approval or disapproval received for the remaining goods till 31st March, 2019.

You are required to advise the accountant of Fashion Limited, the amount to be recognised as revenue in above cases in the context of AS 9.

Ans. As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derivedfrom the sale of the goods.

Case (i): 25% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for Rs. 3,00,000 (75% of Rs. 4,00,000) for the year ended on 31.3.19. In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Case (ii): The sale is complete but delivery has been postponed at buyer's request. Fashion Ltd. should recognize the entire sale of Rs.1,95,000 for the year ended 31st March, 2019.

Case (iii): In case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting Rs. 2,50,000 as the time period for rejecting the goods had expired.

Thus total revenue amounting Rs. 7,45,000 (3,00,000+1,95,000+2,50,000) will be recognized for the year ended 31st March, 2019 in the books of Fashion Ltd.

Q-3 Ruby Ltd. sold goods through its agent. As per terms of sales, consideration is payable within one month. In the event of delay in payment, interest is chargeable @ 10% p.a. from the agent. The company has not realized interest from the agent in the past. For the year ended 31st March, 2017 interest due from agent (because of delay in payment) amounts to ₹ 5 lakhs. The accountant of Ruby Ltd. booked Rs. 5 lakhs as interest income in the year ended 31st March, 2017.

Examine and discuss the contention of the accountant with reference to AS 9 "Revenue Recognition".

Ans. As per AS 9 "Revenue Recognition", "where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, the revenue recognition is postponed to the extent of uncertainty involved. In such cases, the revenue is recognized only when it is reasonably certain that the ultimate collection will be made". In this case, the company never realized interest for the delayed payments made by the agent. Hence, based on the past experience, the realization of interest for the delayed payments by the agent is very much uncertain. The interest should be recognized only if the ultimate collection is certain. Therefore, the interest income of ₹ 5 lakhs should not be recognized in the books for the year ended 31st March, 2017. Thus the contention of accountant is incorrect. However, if the agents have agreed to pay the amount of interest and there is an element of certainty associated with these receipts, the accountant is correct regarding booking of ₹ 5 lakhs as interest amount.

Q-4 The Board of Directors decided on 31.3.2019 to increase the sale price of certain items retrospectively from 1st January, 2019. In view of this price revision with effect from 1st January 2019, the company has to receive ₹ 15 lakhs from its customers in respect of sales made from 1st January, 2019 to 31st March, 2019. Accountant cannot make up his mind whether to include ₹ 15 lakhs in the sales for 2018-2019. Advise.

Ans. Price revision was effected during the current accounting period 2018-2019. As a result, the company stands to receive ₹ 15 lakhs from its customers in respect of sales made from 1st January, 2019 to 31st March, 2019. If the company is able to assess the ultimate collection with reasonable certainty, then additional revenue arising out of the said price revision may be recognised in 2018-2019 vide para 10 of AS 9.

Q-5 Raj Ltd. entered into an agreement with Heena Ltd. to dispatch goods valuing ₹ 5,00,000 every month for next 6 months on receipt of entire payment. Heena Ltd. accordingly made the entire payment of ₹ 30,00,000 and Raj Ltd. started dispatching the goods. In fourth month, due to fire in premise of Heena Ltd., Heena Ltd. requested to Raj Ltd. not to dispatch goods worth ₹15,00,000 ready for dispatch. Raj Ltd. accounted ₹ 15,00,000 as sales and transferred the balance to Advance received against Sales account.

Comment upon the above treatment by Raj Ltd. with reference to the provision of AS-9.

Ans. As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

In the given case, transfer of property in goods results in or coincides with the transfer of significant risks and rewards of ownership to the buyer. Also, the sale price has been recovered by the seller.

Hence, the sale is complete but delivery has been postponed at buyer's request. Raj Ltd. should recognize the entire sale of ₹ 30,00,000 (₹ 5,00,000 x 6) and no part of the same is to be treated as Advance Received against Sales.

Q-6 A manufacturing company has the following stages of production and sale in manufacturing fine paper rolls:

Date	Activity	Cost to Date(₹)	Net Realizable Value(₹)
15.1.16	Raw Material	1,00,000	80,000
20.1.16	Pulp (WIP 1)	1,20,000	1,20,000
27.1.16	Rough & thick paper (WIP 2)	1,50,000	1,80,000
15.2.16	Fine Paper Rolls	1,80,000	3,50,000
20.2.16	Ready for sale	1,80,000	3,50,000
15.3.16	Sale agreed and invoice raised	2,00,000	3,50,000
02.4.16	Delivered and paid for	2,00,000	3,50,000

Explain the stage on which you think revenue will be generated and calculate how much would be net profit for year ending 31.3.16 on this product as per AS 9.

Ans. According to AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration thatwill be derived from the sale of the goods.

Thus, sales will be recognized only when following two conditions are satisfied:

(i) The sale value is fixed and determinable.

(ii) Property of the goods is transferred to the customer.

Both these conditions are satisfied only on 15.3.2016 when sales are agreed upon at a price and goods are allocated for delivery purpose through invoice. The amount of net profit ₹ 1,50,000 (3,50,000 – 2,00,000) would be recognized in the books for the year ending 31st March, 2016.

Q-7 Given below are the following informations of B.S. Ltd.

(i) Goods of ₹ 50,000 were sold on 18-03-2018 but at the request of the buyer thesewere delivered on 15-04-2018.

(ii) On 13-01-2018 goods of ₹ 1,25,000 are sent on consignment basis of which 20% ofthe goods unsold are lying with the consignee as on 31-03-2018.

(iii) ₹ 1,00,000 worth of goods were sold on approval basis on 01-12-2017. The period of approval was 3 months after which they were considered sold. Buyer sent approval for 75% goods up to 31-01-2018 and no approval or disapproval received for the remaining goods till 31-03-2018.

You are required to advise the accountant of B.S. Ltd., with valid reasons, the amount to be recognized as revenue for the year ended 31st March, 2018 in above cases in the context of AS-9.

Ans. As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will bederived from the sale of the goods.

Case (i) : The sale is complete but delivery has been postponed at buyer's request. B.S. Ltd. should recognize the entire sale of ₹ 50,000 for the year ended 31st March, 2018.

Case (ii) : In case of consignment sale revenue should not be recognized until the goods are sold to a third party.20% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 1,00,000 (80% of ₹ 1,25,000).

Case (iii) : In case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting ₹ 1,00,000 as the time period for rejecting the goods had expired.

Thus total revenue amounting ₹ 2,50,000 (50,000 + 1,00,000+ 1,00,000) will be recognized for the year ended 31st March, 2018 in the books of B.S. Ltd.

Q-8 Indicate in each case whether revenue can be recognized and when it will be recognized as per As -9.

(1) Trade discount and colume received.

(2) Whwether goods are sold to distrivutor or others for resale.

(3) Whether seller consurrently agrees to repurchase the same goods at a late date.

(4) Insurance agency commission for rendering services.

(5) On 11-3-2019 cloths worth ₹50,000 were sold to X mart,but due to refurbishing of their showroom being underway,on their request cloths were delivered on 12-04-2019.

Ans. (1) Trade discounts and volume rebates received are not encompassed within the definition of revenue, since they represent a reduction of cost. Trade discounts and volume rebates given should be deducted in determining revenue.

(2) When goods are sold to distributor or others, revenue from such sales can generally be recognized if significant risks of ownership have passed; however, in some situations the buyer may in substance be an agent and in such cases the sale should be treated as a consignment sale.

(3) For transactions, where seller concurrently agrees to repurchase the same goods at a later date that are in substance a financing agreement, the resulting cash inflow is not revenue as defined and should not be recognized as revenue.

(4) Insurance agency commissions should be recognized on the effective commencement or renewal dates of the related policies.

(5) On 11.03.2019, if X mart takes title and accepts billing for the goods then it is implied that the sale is complete and all risk and reward on ownership has been transferred to the buyers.

Revenue should be recognized for year ended 31st March, 2019 notwithstanding that physical delivery has not been completed so long as there is every expectation that delivery will be made and items were ready for delivery to the buyer at the time.

Q-9 The following information of Meghna Ltd. is provided:

(i) Goods of ₹ 60,000 were sold on 20-3-2019 but at the request of the buyer these were delivered on 10-4-2019.

(ii) On 15-1-2019 goods of ₹ 1,50,000 were sent on consignment basis of which 20% of the goods unsold are lying with the consignee as on 31-3-2019.

(iii) ₹ 1,20,000 worth of goods were sold on approval basis on 1-12-2018. The period of approval was 3 months after which they were considered sold. Buyer sent approval for 75% goods up to 31-1-2019 and no approval or disapproval received for the remaining goods till 31-3-2019.

(iv) Apart from the above, the company has made cash sales of ₹ 7,80,000 (gross). Trade discount of 5% was allowed on the cash sales.

You are required to advise the accountant of Meghna Ltd., with valid reasons, the amount to be recognized as revenue in above cases in the context of AS-9.

Ans. As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i) The sale is complete but delivery has been postponed at buyer's request. M/s Paper Products Ltd. should recognize the entire sale of ₹ 60,000 for the year ended 31st March, 2019.

Case (ii) 20% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 1,20,000 (80% of ₹ 1,50,000). In case of consignment sale revenue should not be recognized until the goods are sold to a **third party.**

Case (iii) In case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting ₹ 1,20,000 as the time period for rejecting the goods had expired.

Case (iv) Trade discounts given should be deducted in determining revenue. Thus ₹ 39,000 should be deducted from the amount of turnover of ₹ 7,80,000 for the purpose of recognition of revenue. Thus, revenue should be ₹ 7,41,000.

Q-10 Fashion Limited is engaged in manufacturing of readymade garments. They provide you the following information on 31st March, 2019:

(i) On 15th January, 2019 garments worth ₹ 4,00,000 were sent to Anand on consignment basis of which 25% garments unsold were lying with Anand as on 31st March, 2019.

(ii) Garments worth ₹ 1,95,000 were sold to Shine boutique on 25th March, 2019 but at the request of Shine Boutique, these were delivered on 15th April, 2019.

You are required to advise the accountant of Fashion Limited, the amount to be recognised as revenue in above cases in the context of AS 9.

Ans. As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i): 25% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 3,00,000 (75% of ₹ 4,00,000) for the year ended on 31.3.19. In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Case (ii): The sale is complete but delivery has been postponed at buyer's request.

Fashion Ltd. should recognize the entire sale of ₹1,95,000 for the year ended 31st March, 2019.

Q-11 New Era Publications publishes a monthly magazine on 15th of every month. It sells advertising space in the magazine to advertisers on the terms of 80% sale value payable in advance and the balance within 30 days of the release of the publication. The sale of space for the March 2020 issue was made in February 2020. The magazine was published on its scheduled date. It received ₹ 2,40,000 on 10.3.2020 and ₹ 60,000 on 10.4.2020 for the March, 2020 issue.

Discuss in the context of AS 9 the amount of revenue to be recognized and the treatment of the amount received from advertisers for the year ending 31.3.2020. What will be the treatment if the publication is delayed till 2.4.2020?

Ans. As per AS 9 'Revenue Recognition', in a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method as the service is performed, whichever relates the revenue to the work accomplished. In the given case, income accrues when the related advertisement appears before public. The advertisement service would be considered as performed on the day the advertisement is published and hence revenue is recognized on that date. In this case, 15.03.2020 is the date of publication of the magazine. Hence, ₹ 3,00,000 (₹ 2,40,000 + ₹ 60,000) is recognized as income in March, 2020. The terms of payment are not relevant for considering the date on which revenue is to be recognized. Since, the revenue of ₹ 3,00,000 will be recognised in the March, 2020, ₹ 60,000 will be treated as amount due from advertisers as on 31.03.2020 and ₹ 2,40,000 will be treated as payment received against the sale. However, if the publication is delayed till 02.04.2020 revenue recognition will also be delayed till the advertisements get published in the magazine. In that case revenue of ₹ 3,00,000 will be recognized in the year ended 31.03.2020 after the magazine is published on 02.04.2020**.** The amount received from sale of advertising space on 10.03.2020 of ₹ 2,40,000 will be considered as an advance from advertisers as on 31.03.2020.

Q-12 Fashion Limited is engaged in manufacturing of readymade garments. They provide you the following information on 31st March, 2021:

(i) On 15th January, 2021 garments worth ₹ 4,00,000 were sent to Anand on consignment basis of which 25% garments unsold were lying with Anand as on 31st March, 2021.

(ii) Garments worth ₹ 1,95,000 were sold to Shine boutique on 25th March, 2021 but at the request of Shine Boutique, these were delivered on 15th April, 2021.

(iii) On 1st November, 2020 garments worth ₹ 2,50,000 were sold on approval basis. The period of approval was 4 months after which they were considered sold. Buyer sent approval for 75% goods up to 31st December, 2020 and no approval or disapproval received for the remaining goods till 31st March, 2021.

You are required to advise the accountant of Fashion Limited, the amount to be recognised as revenue in above cases in the context of AS 9.

Ans. As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i): 25% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 3,00,000 (75% of Rs. 4,00,000) for the year ended on 31.3.21. In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Case (ii): The sale is complete but delivery has been postponed at buyer's request. Fashion Ltd. should recognize the entire sale of Rs.1,95,000 for the year ended 31st March, 2021.

Case (iii): In case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting Rs. 2,50,000 as the time period for rejecting the goods had expired.

Thus total revenue amounting Rs. 7,45,000 (3,00,000+1,95,000+2,50,000) will be recognized for the year ended 31st March, 2021 in the books of Fashion Ltd.

Q-13 Old Era Publication Publishes a popular monthly magazine on 15th of every month. The publication sells the advertising space on terms of 90% payable in advance and the balance 10% payable within 30 days of release of the publication. The space for March 2020 issue of the magazine was sold in the month of February, 2020. The magazine was published as per schedule on 15th of the month. The amount of ₹ 2,70,000 has been received upto 31st March, 2020 and ₹ 30,000 was received on 10th April, 2020 for advertisement published in the March issue of the publication.

Please advise the accountant the amount of revenue to be recognized in the context of the provisions of AS 9 'Revenue Recognition' during the year ending on 31st March, 2020.

Ans. **Definition:** As per AS 9 'Revenue Recognition', in a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method, whichever relates the revenue to the work accomplished.

Analysis of given case: In the given case, income accrues when the related advertisement appears before public. The advertisement service would be considered as performed on the day the advertisement is appeared for public and hence revenue is recognized on that date. In this case, it is 15.03.2020, the date of publication of the magazine.

Accounting treatment for given situation: Hence, ₹ 3,00,000 (₹ 2,70,000 + ₹ 30,000) is recognized as income in March, 2020. The terms of payment are not relevant for considering the date on which revenue is to be recognized. ₹ 30,000 is treated as amount due from advertisers as on 31.03.2020 and ₹ 2,70,000 will be treated as payment received against the sale.

Q-14 Tonk Tanners is engaged in manufacturing of leather shoes. They provide you the following information for the year ended 31st March,2020:

(i) On 31st December, 2019 shoes worth ₹ 3,20,000 were sent to Mohan Shoes for sale on consignment basis of which 25% shoes were unsold and lying with Mohan Shoes as on 31st March, 2020.

(ii) On 10th January, 2020, Tonk Tanner supplied shoes worth ₹ 4,50,000 to Shani Shoes and concurrently agrees to re-purchase the same goods on 11th April. 2020.

(iii) On 21st March, 2020 shoes worth ₹ 1,60,000 were sold to Shoe Shine but due to refurbishing of their showroom being underway, on their request, shoes were delivered on 12th April, 2020.

You are required to advise the accountant of Tonk Tanners, when amount is to be recognised as revenue in 2019 -20 in above cases in the context of AS 9.

Ans.

(i) Shoes sent to Mohan Shoes (consignee) for consignment sale

In case goods are sent for consignment sale, revenue is recognized when significant risks of ownership have passed from seller to the buyer.

In the given case, Mohan Shoes is the consignee i.e. an agent of Tonk Tanners and not the buyer.

Therefore, the risk and reward is considered to vest with Tonk Tanners only till the time the sale is made to the third party by Mohan Shoes; although the goods are held by Mohan Shoes. Hence, in the year 2019- 2020, the sale will be recognized for the amount of goods sold by Mohan Shoes to the third party i.e. for ₹ 3,20,000 x 75% = ₹ 2,40,000.

(ii) Sale/repurchase agreements i.e. where seller concurrently agrees to repurchase the same goods at a later date

For such transactions that are in substance a financing agreement, the resulting cash inflow is not revenue and should not be recognised as revenue in the year 2019-2020. Hence, sale of ₹ 4,50,000 to Shani Shoes should not be recognized as revenue.

(iii) Delivery is delayed at buyer's request

On 21st March, 2020, if Shoe Shine takes title and accepts billing for the goods then it is implied that the sale is complete and all the risk and rewards of ownership has been transferred to the buyer. In case no significant uncertainty exists regarding the amount of consideration for sale, revenue shall be recognized in the year 2019-2020 irrespective of the fact that the delivery is delayed on the request of Shoe Shine.

Q-15 How will you recognize revenue in the following cases:

1. Installation Fees;
2. Advertising and insurance agency commissions;
3. Subscriptions for publications.

Ans. **Installation Fees**: In cases where installation fees are other than incidental to the sale of a product, they should be recognized as revenue only when the equipment is installed and accepted by the customer.

Advertising and insurance agency commissions: Revenue should be recognized when the service is completed. For advertising agencies, media commissions will normally be recognized when the related advertisement or commercial appears before the public and the necessary intimation is received by the agency, as opposed to production commission, which will be recognized when the project is completed. Insurance agency commissions should be recognized on the effective commencement or renewal dates of the related policies.

Subscription for publications: Revenue received or billed should be deferred and recognized either on a straight-line basis over time or, where the items delivered vary in value from period to period, revenue should be based on the sales value of the item delivered in relation to the total sales value of all items covered by the subscription.

Q-16 Shipra Ltd., has been successful jewellers for the past 100 years and sales are against cash only (returns are negligible). The company also diversified into apparels. A young senior executive was put in charge of Apparels business and sales increased 5 times. One of the conditions for sales is that dealers can return the unsold stocks within one month of the end of season. Sales return for the year was 25% of sales. Suggest a suitable Revenue Recognition Policy, with reference to AS 9.

Ans. As per AS 9 "Revenue recognition", revenue recognition is mainly concerned with the timing of recognition of revenue in statement of profit and loss of an enterprise. The amount of revenue arising on a transaction is usually determined by the agreement between the parties involved in the transaction. When uncertainties exist regarding the determination of the amount, or its associated costs, these uncertainties may influence the timing of revenue recognition.

Effect of Uncertainty- In the case of the jewellery business the company is selling for cash and returns are negligible. Hence, revenue can be recognized on sales. On the other hand, in Apparels Industry, the dealers have a right to return the unsold goods within one month of the end of the season. In this case, the company is bearing the risk of sales return and therefore, the company should not recognize the revenue to the extent of 25% of its sales. The company may disclose suitable revenue recognition policy in its financial statements separately for both Jewellery and Apparels business.

Q-17 An infrastructure company has constructed a mall and entered into agreement with tenants towards license fee (monthly rental) and variable license fee, a percentage on the turnover of the tenant (on an annual basis). Chief Financial Officer of the company wants to account/recognize license fee as income for 12 months during current year and variable license fee as income during next year, since invoice is raised in the subsequent year. Comment whether the treatment desired by the CFO is correct or not.

Ans. (a) AS 9 on Revenue Recognition, is mainly concerned with the timing of recognition of revenue in the Statement of Profit and Loss of an enterprise. The amount of revenue arising on a transaction is usually determined by agreement between the parties involved in the transaction. However, when uncertainties exist regarding the determination of the amount, or its associated costs, these uncertainties may influence the timing of revenue recognition. Further, as per accrual concept, revenue should be recognized as and when it is accrued i.e. recorded in the financial statements of the periods to which they relate. In the present case, monthly rental towards license fee and variable license fee as a percentage on the turnover of the tenant (though on annual basis) is the income related to common financial year.

Therefore, recognizing the fee as revenue cannot be deferred simply because the invoice is raised in subsequent period. Hence it should be recognized in the financial year of accrual. Therefore, the contention of the Chief Financial Officer is not in accordance with AS 9.

Q-18 Indicate in each case whether revenue can be recognized and when it will berecognized as per AS 9.

(1) Trade discount and volume rebate received.

(2) Where goods are sold to distributors or others for resale.

(3) Where seller concurrently agrees to repurchase the same goods at a later date.

(4) Insurance agency commission for rendering services.

Ans. (b)

(1) Trade discounts and volume rebates received are not encompassed within the definition of revenue, since they represent a reduction of cost. Trade discounts and volume rebates given should be deducted in determining revenue.

(2) When goods are sold to distributor or others, revenue from such sales can be recognized if significant risks of ownership have passed; however, in some situations the buyer may in substance be an agent and in such cases the sale should be treated as a consignment sale.

(3) For transactions, where seller concurrently agrees to repurchase the same goods at a later date that are in substance a financing agreement, the resulting cash inflow is not revenue as defined and should not be recognized as revenue.

(4) Insurance agency commissions should be recognized on the effective commencement or renewal dates of the related policies.

Q-19 Given the following information of Rainbow Ltd.

(i) On 15th November, goods worth ₹ 5,00,000 were sold on approval basis. The period of approval was 4 months after which they were considered sold. Buyer sent approval for 75% goods sold upto 31st January and no approval or disapproval received for the remaining goods till 31st March.

(ii) On 31st March, goods worth ₹ 2,40,000 were sold to Bright Ltd. but due to refurnishing of their show-room being underway, on their request, goods were delivered on 10th April.

(iii) Rainbow Ltd. supplied goods worth ₹ 6,00,000 to Shyam Ltd. and concurrently agrees to re-purchase the same goods on 14th April.

(iv) Dew Ltd, used certain assets of Rainbow Ltd. Rainbow Ltd. received ₹ 7.5 lakhs and ₹ 12 as interest and royalties respectively from Dew Ltd. during the year 2020-21.

(v) On 25th December, goods of ₹ 4,00,000 were sent on consignment basis of which 40% of the goods unsold are lying with the consignee at the year-end on 31st March.

In each of the above cases, you are required to advise, with valid reasons, the amount to be recognized as revenue under the provisions of AS-9.

Ans. (i) As per AS 9 "Revenue Recognition", in case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed.

Therefore, revenue should be recognized for the total sales amounting ₹ 5,00,000 as the time period for rejecting the goods had expired.

(ii) The sale is complete but delivery has been postponed at buyer's request. The entity should recognize the entire sale of ₹ 2,40,000 for the year ended 31st March.

(iii) Sale/repurchase agreements i.e. where seller concurrently agrees to repurchase the same goods at a later date, such transactions that are in substance a financing agreement, the resulting cash inflow is not revenue as defined and should not be recognized as revenue. Hence no revenue to be recognized in the given case.

(iv) Revenue arising from the use by others of enterprise resources yielding interest and royalty should be recognized when no significant uncertainty as to measurability or collectability exists. The interest should be recognized on time proportion basis taking into account the amount outstanding and rate applicable. The royalty should be recognized on accrual basis in accordance with the terms of relevant agreement.

(v) 40% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹2,40,000 (60% of ₹4,00,000). In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Q-20 New Era Publications publishes a monthly magazine on 15th of every month. It sells advertising space in the magazine to advertisers on the terms of 80% sale value payable in advance and the balance within 30 days of the release of the publication. The sale of space for the March 2020 issue was made in February 2020. The magazine was published on its scheduled date. It received ₹ 2,40,000 on 10.3.2020 and ₹ 60,000 on 10.4.2020 for the March, 2020 issue.

Discuss in the context of AS 9 the amount of revenue to be recognized and the treatment of the amount received from advertisers for the year ending 31.3.2020. What will be the treatment if the publication is delayed till 2.4.2020?

Ans. As per AS 9 'Revenue Recognition', in a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method as the service is performed, whichever relates the revenue to the work accomplished. In the given case, income accrues when the related advertisement appears before public. The advertisement service would be considered as performed on the day the advertisement is published and hence revenue is recognized on that date. In this case, 15.03.2020 is the date of publication of the magazine. Hence, ₹ 3,00,000 (₹ 2,40,000 + ₹ 60,000) is recognized as income in March, 2020. The terms of payment are not relevant for considering the date on which revenue is to be recognized.

Since, the revenue of ₹ 3,00,000 will be recognised in the March, 2020, ₹60,000 will be treated as amount due from advertisers as on 31.03.2020 and ₹ 2,40,000 will be treated as payment received against the sale. However, if the publication is delayed till 02.04.2020 revenue recognition will also be delayed till the advertisements get published in the magazine. In that case revenue of ₹ 3,00,000 will be recognized in the year ended 31.03.2020 after the magazine is published on 02.04.2020**.** The amount received from sale of advertising space on 10.03.2020 of ₹ 2,40,000 will be considered as an advance from advertisers as on 31.03.2020.

AS-14 ACCOUNTING FOR AMALGAMATION

Q-1 Som Ltd. agreed to takeover Dove Ltd. on 1st April, 2020. The terms and conditions of takeover were as follows:

(i) Som Ltd. issued 56,000 equity shares of ₹100 each at a premium of ₹10 per share to the equity shareholders of Dove Ltd.

(ii) Cash payment of ₹ 1,00,000 was made to equity shareholders of Dove Ltd.

(iii) 20,000 fully paid preference shares of ₹ 70 each issued at par to discharge the preference shareholders of Dove Ltd.

You are required to calculate the amount of purchase consideration as per the provisions of AS 14.

Ans. As per AS 14, `Accounting for Amalgamations' consideration for the amalgamation means the aggregate of shares and other securities issued and payment made in form of cash or other assets by the transferee company to the shareholders of the transferor company.

(i) Computation of Purchase Consideration:

		₹
(a)	Preference Shares:	
	20,000 Preference shares in Som Ltd. @ ₹ 70 per share	14,00,000
(b)	Cash	1,00,000
(c)	Equity shares: 56,000 equity shares in Som Ltd. @ ₹ 110 per share	61,60,000
		76,60,000

Q-2 List the conditions to be fulfilled as per AS-14 (Revised) for an amalgamation to be in the nature of merger.

Ans. Amalgamation in the nature of merger is an amalgamation which satisfies all the following conditions:

(i) All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.

(ii) Shareholders holding not less than 90% of the face value of the equity shares of the transferor company (other than the equity shares already held therein, immediately before the amalgamation, by the transferee company or its subsidiaries or their nominees) become equity shareholders of the transferee company by virtue of the amalgamation.

(iii) The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.

(iv) The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company.

(v) No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies.

Q-3 Astha Ltd. is absorbed by Nistha Ltd.; the consideration being the takeover of liabilities, the payment of cost of absorption not exceeding ₹ 10,000 (actual cost ₹ 9,000); the payment of the 9% debentures of ₹ 50,000 at a premium of 20% through 8% debentures issued at a premium of 25% of face value and the payment of ₹ 15 per share in cash and allotment of three 11% preference shares of ₹ 10 each and four equity shares of ₹ 10 each at a premium of 20% fully paid for every five shares in Astha Ltd.

The number of shares of the vendor company are 1,50,000 of ₹ 10 each fully paid. Calculate purchase consideration as per AS 14.

Ans. As per AS 14 `Accounting for Amalgamations', the term `consideration' has been defined as the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company.

The payment made by transferee company to discharge the Debenture holders and outside liabilities and cost of winding up of transferor company shall not be considered as part of purchase consideration.

Computation of Purchase Consideration

	₹
Cash payment ₹15 x 1,50,000	22,50,000
11% Preference Shares of ₹ 10 each [(1,50,000 x 3/5) x ₹ 10]	9,00,000
Equity shares of ₹ 10 each @ 20% premium	
[(1,50,000 x 4/5) x ₹ 12]	14,40,000
Total Purchase consideration	45,90,000

Q-4 Moon Limited is absorbed by Sun Limited; the consideration, being the takeover of liabilities, the payment of cost of absorption not exceeding ₹ 10,000 (actual cost ` 9000); the payment of 9% Debentures of ₹ 50,000 at a premium of 20% through 8% debentures issued at a premium of 25% of face value; the payment of ₹ 18 per share in cash; allotment of two 11% preference shares of ₹10/- each and one equity share of ₹ 10/- each at a premium of 30% fully paid for every three shares in Moon Limited respectively.

The number of shares of the vendor company is 1,50,000 of ₹ 10/- each fully paid.

Calculate purchase consideration as per AS-14.

Ans. As per AS 14 "Accounting for Amalgamations", the term consideration has been defined as the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company.

Purchase consideration will be:

	₹	Form
Equity shareholders:		
1,50,000 × ₹ 18	27,00,000	Cash
1,50,000 × 2/3 × ₹ 10	10,00,000	11% Pref. shares
1,50,000 × 1/3 × ₹ 13	6,50,000	Equity shares
43,50,000		

Note:

1. According to AS 14, 'consideration' excludes the any amount payable to debenture - holders. The liability in respect of debentures of vendor company will be taken by transferee company, which will then be settled by issuing new debentures.
2. Liquidation expenses will also not form part of purchase consideration.

Q-5 List the conditions to be fulfilled as per AS 14 (Revised) for an amalgamation to be in the nature of merger, in the case of companies.

Ans. Amalgamation in the nature of merger is an amalgamation which satisfies all the following conditions.

(i) All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company and the business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company

(ii) Shareholders holding not less than 90% of the face value of the equity shares of the transferor company (other than the equity shares already held therein, immediately before the amalgamation, by the transferee company or its subsidiaries or their nominees) become equity shareholders of the transferee company by virtue of the amalgamation.

(iii) The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.

(iv) No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies.

AS-17 SEGMENT REPORTING

Q-1 The Chief Accountant of Cotton Garments Limited gives the following data regarding its five segments:

(₹ in Crore)

Particulars	A	B	C	D	E	Total
Segment Assets	40	15	10	10	5	80
Segment Results	(95)	5	5	(5)	15	(75)
Segment Revenue	310	40	30	40	30	450

The Chief Accountant is of the opinion that segment "A" alone should be reported. Is he justified in his view? Examine his opinion in the light of provisions of AS 17 'Segment Reporting'.

Ans. As per AS 17 `Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

(i) Its revenue from sales to external customers and from other transactions with other segments is 10% or more of the total revenue - external and internal of all segments; or

(ii) Its segment result whether profit or loss is 10% or more of:

(1) The combined result of all segments in profit; or

(2) The combined result of all segments in loss,

whichever is greater in absolute amount; or

(iii) Its segment assets are 10% or more of the total assets of all segments.

Further, if the total external revenue attributable to reportable segments constitutes less than 75% of total enterprise revenue, additional segments should be identified as reportable segments even if they do not meet the 10% thresholds until at least 75% of total enterprise revenue is included in reportable segments.

Accordingly,

(a) On the basis of revenue from sales criteria, segment A is a reportable segment.

(b) On the basis of the result criteria, segments A & E are reportable segments

(since their results in absolute amount is 10% or more of ₹100 crore).

(c) On the basis of asset criteria, all segments except E are reportable segments.

Since all the segments are covered in atleast one of the above criteria, all segments have to be reported upon in accordance with AS 17.

Hence, the opinion of chief accountant that only segment `A' is reportable is wrong.

Q-2 M/s Nathan Limited has three segments namely P, Q and R. The assets of the company are ₹ 15 crores. Segment P has 4 crores, Segment Q has 6 crores and Segment R has 5 crores. Deferred tax assets included in the assets of each segment are P - ₹ 1 crore, Q - Rs.0.90 crores and R - Rs.0.80 crores. The accountant contends all these three segments are reportable segments. Comment.

Ans : According to AS 17 "Segment Reporting", segment Assets do not include income tax assets.

Therefore, the revised total assets are 12.3 crores [Rs.15 - (Rs. 1 + 0.9 + 0.8).

<u>Details of Segment wise assets</u>

Segment P holds total assets of Rs 3 crores (Rs 4 crores - Rs 1 crores);

Segment Q holds Rs. 5.1 crores (Rs 6 crores - 0.9 crores);

Segment R holds Rs 4.2 crores (Rs 5 crores - Rs 0.8 crores).

Thus, all the three segments hold more than 10% of the total assets, all segments are reportable segments.

Hence, the contention of the Accountant that all three segments are reportable segments is correct.

Q-3 A Company has an inter-segment transfer pricing policy of charging at cost less 5%. The market prices are generally 20% above cost.

You are required to examine whether the policy adopted by the company is correct or not?

Ans : AS 17 `Segment Reporting' requires that inter-segment transfers should be measured on the basis that the enterprise actually used to price these transfers. The basis of pricing inter-segment transfers and any change therein should be disclosed in the financial statements. Hence, the enterprise can have its own policy for pricing inter-segment transfers and hence, inter-segment transfers may be based on cost, below cost or market price. However, whichever policy is followed, the same should be disclosed and applied consistently. Therefore, in the given case inter-segment transfer pricing policy adopted by the company is correct if followed consistently.

Q-4 PK Ltd. has identified business segment as its primary reporting format. It has identified India, USA and UK as three geographical segments. It sells its products in the Indian market, which constitutes 70 percent of the Company's sales. 25 per cent is sold in USA and the balance is sold in UK. Is PK Ltd. as part of its geographical secondary segment information, required to disclose segment revenue from export sales, where such sales are not significant?

Ans : As per AS 17 if primary format of an enterprise for reporting segment information is business segments, it should also report segment revenue from external customers by geographical area based on the geographical location of its customers, for each geographical segment whose revenue from sales to external customers is 10 per cent or more of enterprise revenue. Accordingly, for the purposes of disclosing secondary segment information, PK Ltd. is not required to disclose segment revenue from export sales to UK, since that segment does not meet the 10 per center more of enterprise revenue threshold. However, other secondary segment information as per AS 17 should be disclosed in respect of this segment if the thresholds prescribed in the AS 17 are met.

Q-5 Calculate the segment results of a manufacturing organization from the following information:

Segments	A	B	C	Total
Directly attributed revenue	5,00,000	3,00,000	1,00,000	9,00,000
Enterprise revenue (allocated in 5 : 4 : 2 basis)				1,10,000
Revenue from transactions with other segments				
Transaction from B	1,00,000		50,000	1,50,000
Transaction from C	10,000	50,000		60,000
Transaction from A		25,000	1,00,000	1,25,000
Operating expenses	3,00,000	1,50,000	75,000	5,25,000
Enterprise expenses (allocated in 5 : 4 : 2 basis)				77,000
Expenses on transactions with other segments				
Transaction from B	75,000		30,000	
Transaction from C	6,000	40,000		
Transaction from A		18,000	82,000	

Ans. Calculation of segment result

Segments	A	B	C	Total
Directly attributed revenue	5,00,000	3,00,000	1,00,000	9,00,000
Enterprise revenue (allocated in 5 : 4 : 2 basis)	50,000	40,000	20,000	1,10,000
Revenue from transactions with other segments				
Transaction from B	1,00,000		50,000	1,50,000
Transaction from C	10,000	50,000		60,000
Transaction from A		25,000	1,00,000	1,25,000
Total segment revenue as per AS 17 (A)	6,60,000	4,15,000	2,70,000	13,45,000
Operating expenses	3,00,000	1,50,000	75,000	5,25,000
Enterprise expenses (allocated in 5 : 4 : 2 basis)	35,000	28,000	14,000	77,000
Expenses on transactions with other segments				
Transaction from B	75,000		30,000	1,05,000
Transaction from C	6,000	40,000		46,000
Transaction from A		18,000	82,000	1,00,000
Total segment expenses as per AS 17 (B)	4,16,000	2,36,000	2,01,000	8,53,00
Segment result (A-B)	2,44,000	1,79,000	69,000	4,92,000

Q-6 The Chief Accountant of Cotton Garments Limited gives the following data regarding its five segments:

(₹ in Crore)

Particulars	A	B	C	D	E	Total
Segment Assets	40	15	10	10	5	80
Segment Results	(95)	5	5	(5)	15	(75)
Segment Revenue	310	40	30	40	30	450

The Chief Accountant is of the opinion that segment "A" alone should be reported. Is he justified in his view? Examine his opinion in the light of provisions of AS 17 `Segment Reporting'.

Ans. As per AS 17 `Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

(i) Its **revenue** from sales to external customers and from other transactions with other segments is 10% or more of the total revenue- external and internal of all segments; or

(ii) Its segment **result** whether profit or loss is 10% or more of:

(1) The combined result of all segments in profit; or

(2) The combined result of all segments in loss,

whichever is greater in absolute amount; or

(iii) Its segment **assets** are 10% or more of the total assets of all segments.

Further, if the total external revenue attributable to reportable segments constitutes less than 75% of total enterprise revenue, additional segments should be identified as reportable segments even if they do not meet the 10% thresholds until at least 75% of total enterprise revenue is included in reportable segments.

Accordingly,

(a) On the basis of **revenue from sales** criteria, segment A is a reportable segment.

(b) On the basis of the **result** criteria, segments A & E are reportable segments (since their results in absolute amount is 10% or more of ₹ 100 crore).

(c) On the basis of **asset** criteria, all segments except E are reportable segments.

Since all the segments are covered in atleast one of the above criteria, all segments have to be reported upon in accordance with AS 17.

Hence, the opinion of chief accountant that only segment `A' is reportable is wrong.

Q-7 A Company has an inter-segment transfer pricing policy of charging at cost less 5%.

The market prices are generally 20% above cost. You are required to examine whether the policy adopted by the company for pricing inter-segment transfers at reduced prices is correct or not in line with the provisions of AS 17?

Ans. AS 17 ₹Segment Reporting' requires that inter-segment transfers should be measured on the basis that the enterprise actually used to price these transfers. The basis of pricing inter-segment transfers and any change therein should be disclosed in the financial statements. Hence, the enterprise can have its own policy for pricing inter - segment transfers and hence, inter-segment transfers may be based on cost, below cost or market price. However, whichever policy is followed, the same should be disclosed and applied consistently. Therefore, in the given case inter -segment transfer pricing policy adopted by the company is correct if followed consistently.

Q-8 PK Ltd. has identified business segment as its primary reporting format. It has identified India, USA and UK as three geographical segments. It sells its products in the Indian market, which constitutes 70 percent of the Company's sales. 25 per cent is sold in USA and the balance is sold in UK. Is PK Ltd. as part of its geographical secondary segment information, required to disclose segment revenue from export sales, where such sales are not significant?

Ans. As per AS 17 if primary format of an enterprise for reporting segment information is business segments, it should also report segment revenue from external customers by geographical area based on the geographical location of its customers, for each geographical segment whose revenue from sales to external customers is 10 per cent or more of enterprise revenue. Accordingly, for the purposes of disclosing secondary segment information, PK Ltd. is not required to disclose segment revenue from export sales to UK, since that segment does not meet the 10 per center more of enterprise revenue threshold. However, other secondary segment information as per AS 17 should be disclosed in respect of this segment if the thresholds prescribed in the AS 17 are met.

Q-9 In May, 2018, Capacity Ltd. took a bank loan to be used specifically for the construction of a new factory building. The construction was completed in January, 2019 and the building was put to its use immediately thereafter. Interest on the actual amount used for construction of the building till its completion was ₹ 18 lakhs, whereas the total interest payable to the bank on the loan for the period till 31st March, 2019 amounted to ₹ 25 lakhs.

Can ₹ 25 lakhs be treated as part of the cost of factory building and thus be capitalized on the plea that the loan was specifically taken for the construction of factory building? Explain the treatment in line with the provisions of AS 16. AS 17 Segment Reporting.

Ans. AS 16 clearly states that capitalization of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use are completed. Therefore, interest on the amount that has been used for the construction of the building up to the date of completion (January, 2019) i.e. ₹ 18 lakhs alone can be capitalized. It cannot be extended to ₹ 25 lakhs.

Q-10 A Company has an inter-segment transfer pricing policy of charging at cost less 5%. The market prices are generally 20% above cost.

You are required to examine whether the policy adopted by the company is correct or not?

Ans. AS 17 `Segment Reporting' requires that inter-segment transfers should be measured on the basis that the enterprise actually used to price these transfers. The basis of pricing inter-segment transfers and any change therein should be disclosed in the financial statements. Hence, the enterprise can have its own policy for pricing inter-segment transfers and hence, inter-segment transfers may be based on cost, below cost or market price. However, whichever policy is followed, the same should be disclosed and applied consistently. Therefore, in the given case inter-segment transfer pricing policy adopted by the company is correct if followed consistently.

Q-11 A Company has an inter-segment transfer pricing policy of charging at cost less 5%. The market prices are generally 20% above cost.

You are required to examine whether the policy adopted by the company is correct or not?

Ans. AS 17 'Segment Reporting' requires that inter-segment transfers should be measured on the basis that the enterprise actually used to price these transfers. The basis of pricing inter-segment transfers and any change therein should be disclosed in the financial statements. Hence, the enterprise can have its own policy for pricing intersegment transfers and hence, inter-segment transfers may be based on cost, below cost or market price. However, whichever policy is followed, the same should be disclosed and applied consistently. Therefore, in the given case inter-segment transfer pricing policy adopted by the company is correct if followed consistently.

Q-12 The Senior Accountant of AMF Ltd. gives the following data regarding its five segments:

(₹ in lakhs)

Particulars	**P (₹)**	**Q (₹)**	**R (₹)**	**S (₹)**	**T (₹)**	**Total (₹)**
Segment Assets	80	30	20	20	10	160
Segment Results	(190)	10	10	(10)	30	(150)
Segment Revenue	620	80	60	80	60	900

The Senior Accountant is of the opinion that segment "P" alone should be reported. Is he justified in his view? Examine his opinion in the light of provision of AS-17 'Segment Reporting'.

Ans. As per AS 17 'Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

(i) Its revenue from sales to external customers and from other transactions with other segments is 10% or more of the total revenue- external and internal of all segments; or

(ii) Its segment result whether profit or loss is 10% or more of:

(1) The combined result of all segments in profit; or

(2) The combined result of all segments in loss, whichever is greater in absolute amount; or

(iii) Its segment assets are 10% or more of the total assets of all segments.

Accordingly,

(a) On the basis of revenue from sales criteria, segment P is a reportable segment.

(b) On the basis of the result criteria, segments P & T are reportable segments (since their results in absolute amount is 10% or more of ₹ 200 Lakhs).

(c) On the basis of asset criteria, all segments except T are reportable segments.

Since all the segments are covered in at least one of the above criteria, all segments have to be reported upon in accordance with AS 17. Hence, the opinion of chief accountant that only segment `P' is reportable is wrong.

Q-13 The accountant of Parag Limited has furnished you with the following data related to its Business Divisions:

(₹ in Lacs)

Division	A	B	C	D	Total
Segment Revenue	100	300	200	400	1,000
Segment Result	45	-70	80	-10	45
Segment Assets	39	51	48	12	150

You are requested to identify the reportable segments in accordance with the criteria laid down in AS 17.

Ans. As per AS 17 `Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

Its revenue from sales to external customers and from other transactions with other segments is 10% or more of the total revenue- external and internal of all segments; or

Its segment result whether profit or loss is 10% or more of:

- The combined result of all segments in profit; or
- The combined result of all segments in loss,

whichever is greater in absolute amount; or

Its segment assets are 10% or more of the total assets of all segments.

On the basis of revenue criteria, segments A, B, C and D - all are reportable segments.

On the basis of the result criteria, segments A, B and C are reportable segments (since their results in absolute amount is 10% or more of 125 Lakhs).

On the basis of asset criteria, all segments except D are reportable segments.

Since all the segments are covered in at least one of the above criteria, all segments have to be reported upon in accordance with Accounting Standard (AS) 17.

Q-14 A Company has an inter-segment transfer pricing policy of charging at cost less 5%.

The market prices are generally 20% above cost.

You are required to examine whether the policy adopted by the company is correct or not?

Ans. AS 17 `Segment Reporting' requires that inter-segment transfers should be measured on the basis that the enterprise actually used to price these transfers. The basis of pricing inter-segment transfers and any change therein should be disclosed in the financial statements. Hence, the enterprise can have its own policy for pricing intersegment transfers and hence, inter-segment transfers may be based on cost, below cost or market price. However, whichever policy is followed, the same should be disclosed and applied consistently. Therefore, in the given case inter -segment transfer pricing policy adopted by the company is correct if followed consistently.

Q-15 Company A is engaged in the manufacture of chemicals. The company manufactures five types of chemicals that have different applications. Can this company include more than one type of chemical in a single business segment? Comment.

Ans. As per AS 17, "A business segment is a distinguishable component of an enterprise that is engaged in providing an individual product or service or a group of related products of services and that is subject to risks and returns that are different from those of other business segments. Factors that should be considered in determining whether products or services are related include:

(a) the nature of the products of services;

(b) the nature of the productions processes;

(c) the type of class of customers for the products or services;

(d) the methods use to distribute the products or provide the services; and

(e) if applicable, the nature of the regulatory environment, for example, banking, insurance, or public utilities."

As per provisions of the standard, a single business segment does not include products and services with significantly differing risks and returns. Products and services included in a single business segment may be dissimilar with respect to one or several factors listed above but are expected to be similar with respect to majority of the factors.

In the present case, the Company should consider whether the chemicals with different applications, have similar risks end returns. For this purpose, the Company should ascertain whether one or more types of chemicals are related keeping in view the relevant factors including those given in the definition of business segment. Chemicals having different applications can be included in a single business segment if majority of the relevant factors including those listed above are similar. This would ensure that the chemicals having significantly different risks and returns are not included in a single business segment.

Q-16 Is an enterprise required to disclose changes in the basis of allocation of revenue and expenses to segments? Explain.

Ans. effect on segment information should be disclosed. Such disclosure should include a description of the nature of the change, and the financial effect of the change if it is reasonably determinable." It also states that "some changes in accounting policies relate specifically to segment reporting. Examples include changes in identification of segments and changes in the basis for allocating revenues and expenses to segments. Such changes can have a signif icant impact on the segment information reported but will not change aggregate financial information reported for the enterprise. To enable users to understand and impact of such changes, this Statement requires the disclosure of the nature of change and the financial effect of the change, if reasonably determinable".

In view of the above, a change in the basis of allocation of revenue and expenses to segments is a change in the accounting policy adopted for segment reporting. Accordingly, if the change has a material financial effect on the segment information, a description of the nature of the change, and the financial effect of the change, if it is reasonably determinable, should be disclosed.

Q-17 Company A is engaged in the manufacture and sale of products, which constitute two distinct business segments. The products of the Company are sold in the domestic market only. The management information system of the Company is organized to reflect operating information by two broad market segments, rural and urban. Besides the two business segments, how should Company A identify geographical segments?

Do geographical segments exist within the same country? Explain in line with the provisions of AS 17.

Ans. AS 17 explains that, "a single geographical segment does not include operations in economic environments with significantly differing risks and returns. A geographical segment may be a single country, a group of two or more countries, or a region within a country". Accordingly, to identity geographical segments, Company A needs to evaluate whether the segments reflected in the management information system function in environments that are subject to significantly differing risks and returns irrespective of the fact whether they are within the same country.

The Standard recognizes that, "Determining the composition of a business or geographical segment involves a certain amount of judgement…". Accordingly, while the management information system of the Company provides segment information for rural and urban geographical segments for the purpose of internal reporting, judgement is required to determine whether these segments are subject to significantly differing risks and returns based on the definition of geographical segment. In making such a judgement, aspect like different pricing and other policies, e.g., credit policies, deployment of resources between different regions etc., may be considered for the purpose identifying 'urban and 'rural' as separate geographical segment.

Company A, in making judgment for identifying geographical segments, should also consider the relevance, reliability and comparability over time of segment information that will be reported. The Standard, explains that, "In making that judgement,enterprise management takes into account the objective of reporting financial information by segment as set forth in the standard and the qualitative characteristics of financial statements. The qualitative characteristics include the relevance, reliability and comparability over time of financial information that is reported about the different groups of products and services of an enterprise and about its operations in particular geographical areas, and the usefulness of that information for assessing the risks and returns of the enterprise."

Q-18 A Company has an inter-segment transfer pricing policy of charging at cost less 10%.

The market prices are generally 20% above cost. You are required to examine whether the policy adopted by the company is correct or not?

Ans. AS 17 'Segment Reporting' requires that inter-segment transfers should be measured on the basis that the enterprise actually used to price these transfers. The basis of pricing inter-segment transfers and any change therein should be disclosed in the financial statements. Hence, the enterprise can have its own policy for pricing intersegment transfers and hence, inter-segment transfers may be based on cost, below cost or market price. However, whichever policy is followed, the same should be disclosed and applied consistently. Therefore, in the given case inter-segment transfer pricing policy adopted by the company is correct if followed consistently.

AS-18 RELATED PARTY TRANSACTIONS

Q-1 Arohi Ltd. sold goods for ₹ 90 lakhs to Anya Ltd. during financial year ended 31-3-2019. The Managing Director of Arohi Ltd. own 100% of Anya Ltd. The sales were made to Anya Ltd. at normal selling prices followed by Arohi Ltd. The Chief accountant of Arohi Ltd contends that these sales need not requir e a different treatment from the other sales made by the company and hence no disclosure is necessary as per the accounting standard. Is the Chief Accountant correct?

Comment in accordance with AS 18.

Ans. As per AS 18 `Related Party Disclosures', Enterprises over which the key management personnel is able to exercise significant influence are related parties.

This includes enterprises owned by directors or major shareholders of the reporting enterprise that have a member of key management in common with the reporting enterprise. In the given case, Arohi Ltd. and Anya Ltd. are related parties and hence disclosure of transaction between them is re quired irrespective of whether the transaction was done at normal selling price. Hence the contention of Chief Accountant of Arohi Ltd. is wrong.

Q-2 SP hotels Limited enters into an agreement with Mr. A for running its hotel for a fixed return payable to the later every year. The contract involves the day-to-day management of the hotel, while all financial and operating policy decisions are taken by the Board of Directors of the company. Mr. A does not own any voting power in SP Hotels Limited. Would he be considered as a related party of SP Hotels Limited"?

Ans. Mr. A will not be considered as a related party of SP Hotels Limited in view of paragraph 3(c) of AS 18 which states, "individuals owning, directly or indirectly, an interest in the voting power of the reporting enterprise that gives them control or significant influence over the enterprise, and relatives of any such individual". In the given case, in the absence of share ownership, Mr. A would not be considered to exercise significant influence on SP Hotels Limited, even though there is an agreement giving him the power to manage the company. Further, the fact that Mr. A does not have the ability to direct or instruct the board of directors does not qualify him as a key management personnel.

Q-3 Sun Ltd. sold goods for ₹ 50 lakhs to Moon Ltd. during financial year ended 31st March 2017 at normal selling price followed by Sun Ltd. The Managing Director of Sun Ltd. holds 75% shares of Moon Ltd. The Chief accountant of Sun Ltd contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per the accounting standard. You are required to examine and advise whether the contention of the Chief Accountant is correct?

Ans. As per AS 18 `Related Party Disclosures', Enterprises over which a key management personnel is able to exercise significant influence are related parties. This includes enterprises owned by directors or major shareholders of the reporting enterprise and enterprise that have a member of key management in common with the reporting enterprise.

In the given case, Sun Ltd. and Moon Ltd are related parties and hence disclosure of transaction between them is required irrespective of whether the transaction was done at normal selling price.

Hence the contention of Chief Accountant of Sun Ltd is wrong.

Q-4 Is remuneration paid to Board of Directors a related party transaction? Explain. AS 19 Leases

Ans. In case of a Company, the Managing Director, whole time director, manager and any person in accordance with whose directions or instructions the board of directors of the company is accustomed to act, are usually considered Key Managerial Personnel (KMP).

Persons who do not have the authority and responsibility for planning, directing and controlling the activities of the enterprise would not be KMP. Conversely, persons without any formal titles may be considered to be KMP, if they plan, direct and control the activities of the enterprise.

Further, as per Sec 2(76) of Companies Act, 2013, a related party includes a director or his relative. Sec 2(34) defines a director as a director appointed to the Board of a Company.

Hence, remuneration paid to Board of Directors will be considered as related party transaction.

Q-5 Identify the related parties in the following cases as per AS-18

(i) Maya Ltd. holds 61 % shares of Sheetal Ltd.

Sheetal Ltd. holds 51 % shares of Fair Ltd.

Care Ltd. holds 49% shares of Fair Ltd.

(Give your answer - Reporting Entity wise for Maya Ltd., Sheetal Ltd., Care Ltd. and Fair Ltd.)

(ii) Mr. Subhash Kumar is Managing Director of A Ltd. and also holds 72% capital of B Ltd.

Ans. **(i)**

(a) Reporting entity- Maya Ltd.

- Sheetal Ltd. (subsidiary) is a related party
- Fair Ltd.(subsidiary) is a related party

(b) Reporting entity- Sheetal Ltd.

- Maya Ltd. (holding company) is a related party
- Fair Ltd. (subsidiary) is a related party

(c) Reporting entity- Fair Ltd.

- Maya Ltd. (holding company) is a related party
- Sheetal Ltd. (holding company) is a related party
- Care Ltd. (investor/ investing party) is a related party

(d) Reporting entity- Care Ltd.

- Fair Ltd. (associate) is a related party

(ii) Mr. Subhash Kumar is Key management personnel as he has the authority for planning, directing and controlling the activities of A Ltd. He also holds substantial interest in B Ltd. as he holds 72% capital of B Ltd. Thus, Mr. Subhash is related party for both A Ltd. and B Ltd. Moreover, as per the definition of related party relationship described in para 3 of AS 18, enterprises over which Subhash is able to exercise significant influence are also related parties. Thus, a Ltd. and B Ltd. will also be construed as related to each other.

Q-6 Following transactions are disclosed as on 31st March, 2018:

(i) Mr. Sumit, a relative of Managing Director, received remuneration of ₹ 2,10,000 for his services in the company for the period from 1st April, 2017 to 30th June, 2017. He left the service on 1st July, 2017.

Should the relative be identified as a related party as on closing date i.e. on 31-3-2018 for the purpose of AS-18.

(ii) Goods sold amounting to ₹ 50 lakhs to associate company during the 1st quarter ended on 30th June, 2017. After that related party relationship ceased to exist. However, goods were supplied as was supplied to any other ordinary customer.Decide whether transactions of the entire year have to be disclosed as related party transaction.

Ans. **(i)** According to AS 18 `Related Party Disclosures', parties are considered to be related if at any time during the reporting period, one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Hence, Mr. Sumit a relative of key management personnel should be identified as related party as at the closing date i.e. on 31.3.2018 as he received remuneration forhis services in the company from1st April,2017 to 30th June, 2017and this period comes under the reporting period.

(ii) As per provision of AS 18, the transactions only for the period in which related party relationships exist need to be reported.

Hence, transactions of the entity with its associate company for the first quarter ending 30.06.2017 only are required to be disclosed as related party transactions. Transactions of the entire year need not be disclosed as related party transactions and transactions for the period (after 1st July) in which related party relationship did not exist need not be reported.

Hence transaction of sale of goods with the associate company for first quarter ending 30th June, 2017 for ₹ 50 Lakhs only are required to be disclosed as related party transaction on 31.3.18.

Q-7 Arohi Ltd. sold goods for ₹ 90 lakhs to Anya Ltd. during financial year ended 31-3-2019. The Managing Director of Arohi Ltd. own 100% of Anya Ltd. The sales were made to Anya Ltd. at normal selling prices followed by Arohi Ltd. The Chief accountant of Arohi Ltd contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per the accounting standard. Is the Chief Accountant correct? Comment in accordance with AS 18.

Ans. As per AS 18 'Related Party Disclosures', Enterprises over which the key management personnel is able to exercise significant influence are related parties. This includes enterprises owned by directors or major shareholders of the reporting enterprise that have a member of key management in common with the reporting enterprise. In the given case, Arohi Ltd. and Anya Ltd. are related parties and hence disclosure of transaction between them is required irrespective of whether the transaction was done at normal selling price. Hence the contention of Chief Accountant of Arohi Ltd. is wrong.

Q-8 On the basis of provisions of AS 18 'Related Party Disclosures':

(i) Identify the related parties in the following cases:

X Limited holds 60% shares of Y Limited

Y Limited holds 55% shares of W Limited

Z Limited holds 35% shares of W Limited

(ii) Himalaya Limited sold goods for ₹ 40 Lakhs to Aravalli Limited during financial year ended on March 31, 2019. The Managing Director of Himalaya Limited owns 80% shares of Aravalli Limited. The sales were made to Aravalli Limited at normal selling prices followed by Himalaya Limited. The chief accountant of Himalaya Limited contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per AS 18. You are required to comment on this.

Ans.

(i) X Ltd., Y Ltd. & W Ltd. are related to each other. Z Ltd. & W Ltd. are related to each other by virtue of associate relationship. However, neither X Ltd. nor Y Ltd. is related to Z Ltd. and vice versa since neither control nor significant influence exists between them.

(ii) Himalaya Ltd. and Aravalli Ltd are related parties since key management personnel of Himalaya Ltd. ie. its managing director holds 80% in Aravalli Ltd. and hence disclosure of transaction between them is required irrespective of whether the transaction was done at normal selling price. Hence the contention of Chief Accountant of Himalaya Ltd that these sales require no disclosure under related party transactions, is wrong.

Q-9 Mr. Arnav a relative of key management personnel received remuneration of ₹ 3,00,000 for his services in the company for the period April 1, 2019 to June 30, 2019. On July 1, 2019 he left the job.

Should Mr. Arnav be identified as Related Party at the closing date i.e. March 31, 2020 for the purposes of AS 18?

Ans. According to AS 18 'Related Party Disclosures', parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Hence**,** Mr. Arnav a relative of key management personnel should be identified as related party as at the closing date i.e. on 31.3.2020.

Q-10 A limited company sold goods to its associate company for the 1st quarter ending June 30, 2020. After that, the related party relationship ceased to exist. However, goods were supplied continuously even after June 30, 2020 as was supplied to another ordinary customer. Does this require disclosure as related party transaction for the entire financial year?

Ans. As per AS 18, transactions of company with its associate company for the first quarter ending 30.06.2020 only are required to be disclosed as related party transactions. The transactions for the period in which related party relationship did not exist need not be reported.

Q-11

(i) Khushi Limited enter into an agreement with Mr. Happy for running a business for a fixed amount payableto the later every year. The contract states that the day-to-day management of the business will behandled by Mr. Happy, while all financial and operating policy decisions are taken by the Board of Directors of the Company. Mr. Happy does not own any voting power in Khushi Limited.

(ii) Shri Bhanu a relative of key management personnel received remuneration of ₹ 3,50,000 for his services in the company for the period from 1st April, 2020 to 30th June, 2020. On 1st July, 2020, he left the service.

You are required to suggest how the above transactions will be treated as at the closing date i.e. on 31st March, 2021 for the purposes of AS 18- Related Party Disclosures.

Ans. (i) Mr. Happy will not be considered as a related party of Khushi Limited in view of provisions of AS 18 "Related Party Disclosures" which states, "individuals owning, directly or indirectly, an interest in the voting power of the reporting enterprise that gives them control or significant influence over the enterprise, and relatives of any such individual are related parties".

In the given case, in the absence of share ownership, Mr. Happy would not be considered to exercise significant influence on Khushi Limited, even though there is an agreement giving him the power to manage the company. Further, the fact that Mr. Happy does not have the ability to direct or instruct the board of directors does not qualify him as a key management personnel.

(ii) According to AS 18 on `Related Party Disclosures', parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Hence, Shri Bhanu, a relative of key management personnel should be identified as related party for disclosure in the financial statements for the year ended 31.3.2021 as he received remuneration for his services in the company for the period from 1st April,2020 to 30th June,2020.

Q-12 R Ltd. has 60% voting right in S Ltd. S Ltd. has 15% voting right in T Ltd. R Ltd. directly enjoys voting right of 10% in T Ltd. T Ltd. is a listed company and regularly supplies goods to R Ltd. The management of T Ltd. has not disclosed its relationship with R Ltd. You are required to assess the situation from the view point of AS 18 on Related Party Disclosures.

Ans. AS 18 `Related Party Disclosures', defines related party as one that has at any time during the reporting period, the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Definition for Control

Here, control is defined as ownership directly or indirectly of more than one -half of the voting power of an enterprise; and Significant Influence is def ined as participation in the financial and/or operating policy decisions of an enterprise but not control of those policies.

Nature of Relationship

R Ltd. has direct economic interest in T Ltd. to the extent of 10%, and through S Ltd. in which it is the majority shareholders, it has further control of 9% in T Ltd. (60% of S Ltd.'s 15%). These two taken together (10% + 9%) make the total control of 19%.

Conclusion

In the present case, control of R Ltd. in T Ltd. directly and through S Ltd., is only 19%. Significant influence may also not be exercised as an investing party (R Ltd.) holds, directly or indirectly through intermediaries only 19% of the voting power of the T Ltd. Accordingly, R Ltd. and T Ltd. are not related parties. Hence related party disclosure, as per AS 18, is not required.

Q-13 Omega Bank Limited holds 25 per cent of the voting power of B Limited. Omega Bank Limited also provides finance by way of a loan to B Limited at market rates of interest, on account of which, Omega Bank Limited would have the power to nominate one person to the board of directors of B Limited. Any major transactions proposed to be entered into by B Limited would need the consent of Omega Bank Limited. Would Omega Bank Limited be considered as related party for B Ltd. (reporting enterprise)?

Ans. Omega Bank Limited would be a related party of B Limited. As per AS 18 "associates and joint ventures of the reporting enterprise and the investing party of venture in respect of which the reporting enterprise is an associate or a joint venture r" are related party relationship. Further, an associate has been defined as "an enterprise in which an investing reporting party has significant influence and which is neither a subsidiary nor a joint venture of the party". Significant influence has been defined to be "participation in the financial and /or operating policy decisions of an enterprise, but not control of those policies". Further, it is given in the standard that significant influence may be gained by share ownership, agreement or statute. As regards share ownership, there is a presumption that ownership of 20 per cent or more of the voting power enables the enterprise to exercise significant influence, unless it could be clearly demonstrated otherwise. In the given example, Omega Bank Limited exercises significant influence over B Limited by virtue of ownership of 25 per cent of the voting power. Omega Bank Limited is also a provider of finance for B Limited (as it has provided a loan to B Limited), and as per the standard, a provider of finance is deemed not to be a related party during its normal dealings with the enterprise by virtue only of those dealing. However, in this case, the exemption would not be available to Omega Bank Limited as the exercise of significant influence of Omega Bank Limited over B Limited has been demonstrated on account of ownership of more than 20 per cent of voting power. Accordingly, Omega Bank Limited would be construed to be a related party in the financial statements of B Limited and consequently, the latter would be required to disclose the transactions with Omega Bank Limited in its financial statements.

Q-14 A Limited has two Associates, B Limited and C Limited, and owns 25 per cent of the voting power of B Limited and 30 per cent of the voting power of C Limited. Would B Limited be considered a related party for the purpose of financial statements of C Limited?

Ans. Both B Limited and C Limited are `associates' of A Limited. Follow-associates cannot be regarded as a related parties only by virtue of the relationship. AS 18 states that "enterprise that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise" are related parties. Further, it is given that "associates and joint ventures of the reporting enterprise and the investing party or venture in respect of which the reporting enterprise is an associate or a joint venturer" are also related parties. As B Limited is not an associate of C Limited, nor is it being controlled, directly or indirectly, by C Limited or is not so controlling C Limited, it is not a related party of C Limited.

Q-15 In respect of a key supplier who is dependent on the company for its existence and the company enjoys influence over the prices of this supplier (which may not be formally demonstrable), can the supplier and the company be considered as related parties?

Ans. The supplier and the company cannot be considered to be related parties merely because the latter is able to influence the transaction price between the parties.

Paragraph 3 of AS 18 states that "enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise" are considered to be related party relationships.

However, the conditions which define the existence of control, as follows, are not satisfied in the given example.

- 'ownership, directly or indirectly, of more than one-half of the voting power of an enterprise, or
- Control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise, or
- a substantial interest in voting power and the power to direct, by statue or agreement, the financial and/or operating policies of the enterprise".

Paragraph 10 of the standard defines significant influence as "participation in the financial and/or operating policy decisions of an enterprise, but not control of those policies". In the given example, although the supplier and the company have entered into a commercial transaction, the terms of which are influenced by the latter because of its better bargaining power in the specific market for such goods, it cannot be concluded that there is participation in the financial and/or operating policy decisions.

Therefore, as the conditions specified by the Standard for being classified as a related party are not satisfied in the given example, the company cannot be said to be related to the supplier. This view is supported by paragraph 4 (b) of the Standard which states that "a single customer, supplier, franchiser, distributor, or general agent with whom an enterprise transacts a significant volume of business merely by virtue of the resulting economic dependence" would not be deemed to be related parties.

Q-16 Define "Key management personnel" in the context of AS 18.

Ans. In context of AS 18, "Key management personnel" are those persons who have the authority and responsibility for planning, directing and controlling the activities of the reporting enterprise. For example, in the case of a company, the managing director(s), whole time director(s), manager and any person in accordance with whose directions or instructions the board of directors of the company is accustomed to act,are usually considered key management personnel.

Q-17 (i) Mr. Arnav a relative of key management personnel received remuneration of ₹ 3,00,000 for his services in the company for the period April 1, 2019 to June 30, 2019. On July 1, 2019 he left the job.

Should Mr. Arnav be identified as Related Party at the closing date i.e. March 31, 2020 for the purposes of AS 18?

(ii) A limited company sold goods to its associate company for the 1st quarter ending June 30, 2020. After that, the related party relationship ceased to exist. However, goods were supplied continuously even after June 30, 2020 as was supplied to another ordinary customer. Does this require disclosure as related party transaction for the entire financial year?

Ans. (i) According to AS 18 'Related Party Disclosures', parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Hence**,** Mr. Arnav a relative of key management personnel should be identified as related party as at the closing date i.e. on 31.3.2020.

(ii) As per AS 18, transactions of company with its associate company for the first quarter ending 30.06.2020 only are required to be disclosed as related party transactions. The transactions for the period in which related party relationship did not exist need not be reported.

AS-19 LEASES

Q-1 ABC Ltd. took a machine on lease from XYZ Ltd., the fair value being ₹ 10,00,000.

The economic life of the machine as well as the lease term is 4 years. At the end of each year, ABC Ltd. pays ₹ 3,50,000. The lessee has guaranteed a residual value of ₹ 50,000 on expiry of the lease to the lessor. However, XYZ Ltd. estimates that the residential value of the machinery will be ₹ 35,000 only. The implicit rate of return is 16% and PV factors at 16% for year 1, year 2, year 3 and year 4 are 0.8621, 0.7432, 0.6407 and 0.5523 respectively. You a re required to calculate the value of machinery to be considered by ABC Ltd. and the finance charges for each year.

Ans. As per AS 19 "Leases", the lessee should recognize the lease as an asset and a liability at the ince ption of a finance lease. Such recognition should be at an amount equal to the fair value of the leased asset at the inception of lease. However, if the fair value of the leased asset exceeds the present value of minimum lease payment from the standpoint o f the lessee, the amount recorded as an asset and liability should be the present value of minimum lease payments from the standpoint of the lessee.

Value of machinery

In the given case, fair value of the machinery is ₹ 10, 00,000 and the net present value of minimum lease payments is ₹ 10, 07,020 (Refer working Note). As the present value of the machine is more than the fair value of the machine, the machine and the corresponding liability will be recorded at value of ₹10,00,000.

Calculation of finance charges for each year

Year	Finance charge (₹)	Payment (₹)	Reduction in outstanding liability (₹)	Outstanding liability (₹)
1st year beginning	-	-	-	10,00,000
End of 1st year	1,60,000	3,50,000	1,90,000	8,10,000
End of 2nd year	1,29,600	3,50,000	2,20,400	5,89,600
End of 3rd year	94,336	3,50,000	2,55,664	3,33,936
End of 4th year	53,430	3,50,000	2,96,570	37,366

Working Note:

Present value of minimum lease payments

Annual lease rental x PV factor

₹ 3,50,000 x (0.8621 + 0.7432 + 0.6407+ 0.5523)	₹ 9,79 ,405
Present value of guaranteed residual value ₹ 50,000 x (0.5523)	₹ 27,615
	₹ 10,07,020

Q-2 A Ltd. sold machinery having WDV of ₹ 40 lakhs to B Ltd. for ₹ 50 lakhs and the same machinery was leased back by B Ltd. to A Ltd. The lease back is operating lease. Explain the accounting treatment as per AS 19 in the following cases:

(i) Sale price of ₹ 50 lakhs is equal to fair value.

(ii) Fair value is ₹ 45 lakhs and sale price is ₹ 38 lakhs.

(iii) Fair value is ₹ 40 lakhs and sale price is ₹ 50 lakhs.

(iv) Fair value is ₹ 46 lakhs and sale price is ₹ 50 lakhs

(v) Fair value is ₹ 35 lakhs and sale price is ₹ 39 lakhs.

Ans. Following will be the treatment in the given cases:

(i) When sale price of ₹ 24 lakhs is equal to fair value, A Ltd. should immediatelyrecognise the profit of ₹ 4 lakhs (i.e. 24 – 20) in its books.

(ii) When fair value is ₹ 20 lakhs & sale price is ₹ 24 lakhs then profit of ₹ 4 lakhs is tobe deferred and amortised over the lease period.

(iii) When fair value is ₹ 22 lakhs & sale price is ₹ 25 lakhs, profit of ₹ 2 lakhs (22 - 20) to be immediately recognised in its books and balance profit of ₹ 3 lakhs (25-22) is to be amortised/deferred over lease period.

(iv) When fair value of leased machinery is ₹ 25 lakhs & sale price is ₹ 18 lakhs, then loss of ₹ 2 lakhs (20 – 18) to be immediately recognised by A Ltd. in its books provided loss is not compensated by future lease payment.

(v) When fair value is ₹ 18 lakhs & sale price is ₹ 19 lakhs, then the loss of ₹ 2 lakhs (20-18) to be immediately recognised by A Ltd. in its books and profit of ₹ 1 lakhs (19-18) should be amortised/ deferred over lease period.

Q-3 Sun Limited wishes to obtain a machine costing ₹ 30 lakhs by way of lease. The effective life of the machine is 14 years, but the company requires it only for the first 5 years. It enters into an agreement with Star Ltd., for a lease rental for ₹ 3 lakhs p.a. payable in arrears and the implicit rate of interest is 15%. The chief accountant of Sun Limited is not sure about the treatment of these lease rentals and seeks your advise. You are required to explain the necessary accounting treatment in line with AS 19. (use annuity factor at @ 15% for 3 years as 3.36)

Ans. As per AS 19 `leases', a lease will be classified as finance lease if at the inception of the lease, the present value of minimum lease payment amounts to at least substantially all of the fair value of leased asset. In the given case, the implicit rate of interest is given at 15%. The present value of minimum lease payments at 15% using PV- Annuity Factor can be computed as:

Annuity Factor (Year 1 to Year 5)	3.36 (approx.)
Present Value of minimum lease payments (₹ 3 lakhs each year)	₹ 10.08 lakhs (approx.)

Thus present value of minimum lease payments is ₹ 10.08 lakhs and the fair value of the machine is Rs. 30 lakhs. In a finance lease, lease term should be for the major part of the economic life of the asset even if title is not transferred. However, in the given case, the effective useful life of the machine is 14 years while the lease is only for five years. Therefore, lease agreement is an operating lease. Lease payments under an operating lease should be recognized as an expense in the statement of profit and loss on a straight line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

Q-4 Aksat International Limited has given a machinery on lease for 36 months, and its useful life is 60 months. Cost & fair market value of the machinery is ₹ 5,00,000. The amount will be paid in 3 equal annual installments and the lessee will return the machinery to lessor at termination of lease. The unguaranteed residual value at the end of 3 years is ₹ 50,000. IRR of investment is 10% and present value of annuity factor of ₹ 1 due at the end of 3 years at 10% IRR is 2.4868 and present value of ₹ 1 due at the end of 3rd year at 10% IRR is 0.7513.

You are required to comment with reason whether the lease constitute finance lease or operating lease. If it is finance lease, calculate unearned finance income.

Ans : **Determination of Nature of Lease**

Present value of unguaranteed residual value at the end of 3rd year

= ₹ 50,000 x 0.7513

= ₹ 37,565

Present value of lease payments = ₹ 5,00,000 – ₹ 37,565
= ₹ 4,62,435
The percentage of present value of lease payments to fair value of the equipment is
(₹ 4,62,435/ ₹ 5,00,000) x 100 = 92.487%.
Since, lease payments substantially covers the major portion of the fair value; the lease constitutes a finance lease.

Calculation of Unearned Finance Income

Annual lease payment = ₹ 4,62,435/ 2.4868 = ₹ 1,85,956 (approx.)
Gross investment in the lease = Total minimum lease payments + unguaranteed residual value
= (₹ 1,85,956 × 3) + ₹ 50,000
= ₹ 5,57,868 + ₹ 50,000 = ₹ 6,07,868

Unearned finance income

= Gross investment - Present value of minimum lease payments and unguaranteed residual value
= ₹ 6,07,868 – ₹ 5,00,000 = ₹ 1,07,868.

Q-5 ABC Ltd. took a machine on lease from XYZ Ltd., the fair value being ₹ 10,00,000. The economic life of the machine as well as the lease term is 4 years. At the end of each year, ABC Ltd. pays ₹ 3,50,000. The lessee has guaranteed a residual value of ₹ 40,000 on expiry of the lease to the lessor. However, XYZ Ltd. estimates that the residential value of the machinery will be ₹ 35,000 only. The implicit rate of return is 16% and PV factors at 16% for year 1, year 2, year 3 and year 4 are 0.8621, 0.7432, 0.6407 and 0.5523 respectively. You are required to calculate the value of machinery to be considered by ABC Ltd. and the finance charges for each year.

Ans : As per AS 19 "Leases", the lessee should recognize the lease as an asset and a liability at the inception of a finance lease. Such recognition should be at an amount equal to the fair value of the leased asset at the inception of lease. However, if the fair value of the leased asset exceeds the present value of minimum lease payment from the standpoint of the lessee, the amount recorded as an asset and liability should be the present value of minimum lease payments from the standpoint of the lessee.

Value of machinery : In the given case, fair value of the machinery is ₹ 10, 00,000 and the net present value of minimum lease payments is ₹ 10,01,497 (Refer working Note). As the present value of the machine is more than the fair value of the machine, the machine and the corresponding liability will be recorded at fair value of ₹ 10,00,000.

Calculation of finance charges for each year

Year	Finance charge (₹)	Payment(₹)	Reduction in outstanding liability (₹)	Outstanding liability (₹)
1st year beginning	-	-	-	10,00,000
End of 1st year	1,60,000	3,50,000	1,90,000	8,10,000
End of 2nd year	1,29,600	3,50,000	2,20,400	5,89,600
End of 3rd year	94,336	3,50,000	2,55,664	3,33,936
End of 4th year	53,430	3,50,000	2,96,570	37,366

Working Note:

Present value of minimum lease payments

Annual lease rental x PV factor ₹ 3,50,000 x (0.8621 + 0.7432 + 0.6407+ 0.5523)	₹ 9,79 ,405
Present value of guaranteed residual value ₹ 40,000 x (0.5523)	₹ 22,092
	₹ 10,01,497

Q-6 WIN Ltd. has entered into a three year lease arrangement with Tanya sports club in respect of Fitness Equipments costing ₹ 16,99,999.50. The annual lease payments to be made at the end of each year are structured in such a way that the sum of the Present Values of the lease payments and that of the residual value together equal the cost of the equipments leased out. The unguaranteed residual value of the equipment at the expiry of the lease is estimated to be ₹ 1,33,500. The assets would revert to the lessor at the end of the lease. Given that the implicit rate of interest is 10%.

You are required to calculate the amount of the annual lease payment and the unearned finance income. Discounting Factor at 10% for years 1, 2 and 3 are 0.909, 0.826 and 0.751 respectively.

Ans. (i) Computation of annual lease payment to the lessor

	₹
Cost of equipment	16,99,999.50
Unguaranteed residual value	1,33,500.00
Present value of residual value after third year @ 10%(₹ 1,33,500 × 0.751)	1,00,258.50
Fair value to be recovered from lease payments(₹ 16,99,999.5– ₹ 1,00,258.5)	15,99,741.00
Present value of annuity for three years is 2.486	
Annual lease payment = ₹ 15,99,741/ 2.486	6,43,500.00

(ii) Computation of Unearned Finance Income

	₹
Total lease payments (₹ 6,43,500 x 3)	19,30,500
Add: Unguaranteed residual value	1,33,500
Gross investment in the lease	20,64,000.00
Less: Present value of investment (lease payments andresidual value) (₹ 1,00,258.5+ ₹ 15,99,741)	(16,99,999.50)
Unearned finance income	3,64,000.50

Q-7 Jaya Ltd. took a machine on lease from Deluxe Ltd., the fair value being ₹ 11,50,000. Economic life of the machine as well as lease term is 4 years. At the end of each year,lessee pays ₹ 3,50,000 to lessor. Jaya Ltd. has guaranteed a residual value of ₹ 70,000 on expiry of the lease to Deluxe Ltd., however Deluxe Ltd. estimates that residual value will be only ₹ 25,000. The implicit rate of return is 10% p.a. and present value factors at 10% are : 0.909, 0.826, 0.751 and 0.683 at the end of 1st, 2nd, 3rd and 4th year respectively.

Calculate the value of machinery to be considered by Jaya Ltd. and the value of the lease liability as per AS-19.

Ans. According to para 11 of AS 19 "Leases", the lessee should recognise the lease as an asset and a liability at an amount equal to the fair value of the leased asset at the inception of the finance lease. However, if the fair value of the leased asset exceeds the present value of the minimum lease payments from the standpoint of the lessee, the amount recorded as an asset and a liability should be the present value of the minimum lease payments from the standpoint of the lessee**.**

In calculating the present value of the minimum lease payments the discount rate is the interest rate implicit in the lease. Present value of minimum lease payments will be calculated as follows:

Year	**Minimum Lease Payment** ₹	**Internal rate of return (Discount rate @10%)**	**Present value** ₹
1	3,50,000	0.909	3,18,150
2	3,50,000	0.826	2,89,100
3	3,50,000	0.751	2,62,850
4	4,20,000*	0.683	2,86,860
Total	14,70,000		11,56,960

Present value of minimum lease payments ₹ 11,56,960 is more than fair value at the inception of lease i.e. ₹ 11,50,000, therefore, the lease liability and machinery should be recognized in the books at ₹ 11,50,000 as per AS 19.

Q-8 A Ltd. sold JCB having WDV of ₹ 20 lakhs to B Ltd. for ₹ 24 lakhs and the same JCB was leased back by B Ltd. to A Ltd. The lease is operating lease. In context of Accounting Standard 19 "Leases" explain the accounting treatment of profit or loss in the books of A Ltd. if

(i) Sale price of ₹ 24 lakhs is equal to fair value.

(ii) Fair value is ₹ 20 lakhs and sale price is ₹ 24 lakhs.

(iii) Fair value is ₹22 lakhs and sale price is ₹ 25 lakhs.

(v) Fair value is ₹ 25 lakhs and sale price is ₹ 18 lakhs.

(v) Fair value is ₹ 18 lakhs and sale price is ₹ 19 lakhs.

Ans. Following will be the treatment in the given cases:

(i) When sale price of ₹ 24 lakhs is equal to fair value, A Ltd. should immediatelyrecognise the profit of ₹ 4 lakhs (i.e. 24 – 20) in its books.

(ii) When fair value is ₹ 20 lakhs & sale price is ₹ 24 lakhs then profit of ₹ 4 lakhs is tobe deferred and amortised over the lease period.

(iii) When fair value is ₹ 22 lakhs & sale price is ₹ 25 lakhs, profit of ₹ 2 lakhs (22 - 20) to be immediately recognised in its books and balance profit of ₹ 3 lakhs (25-22) is to be amortised/deferred over lease period.

(iv) When fair value of leased machinery is ₹ 25 lakhs & sale price is ₹ 18 lakhs, then loss of ₹ 2 lakhs (20 – 18) to be immediately recognised by A Ltd. in its books provided loss is not compensated by future lease payment.

(v) When fair value is ₹ 18 lakhs & sale price is ₹ 19 lakhs, then the loss of ₹ 2 lakhs (20-18) to be immediately recognised by A Ltd. in its books and profit of ₹ 1 lakhs (19-18) should be amortised/ deferred over lease period.

Q-9 Classify the following into either operating lease or finance lease with reason:

(1) Economic life of asset is 10 years, lease term is 9 years, but asset is not acquired at the end of lease term.

(2) Lessee has option to purchase the asset at lower than fair value at the end of lease term.

(3) Lease payments should be recognized as an expense in the statement of Profit & Loss of a lessee.

(4) Present Value (PV) of Minimum Lease Payment (MLP) = "X" Fair value of the asset is "Y" And X = Y.

(5) Economics life of the asset is 5 years, lease term is 2 years, but the asset is of special nature and has been procured only for use of the lessee.

Q-10 ABC Ltd. took a machine on lease from XYZ Ltd., the fair value being ₹ 10,00,000. The economic life of the machine as well as the lease term is 4 years. At the end of each year, ABC Ltd. pays ₹ 3,50,000. The lessee has guaranteed a residual value of ₹ 50,000 on expiry of the lease to the lessor. However, XYZ Ltd. estimates that the residential value of the machinery will be ₹ 35,000 only. The implicit rate of return is 16% and PV factors at 16% for year 1, year 2, year 3 and year 4 are 0.8621, 0.7432, 0.6407 and 0.5523 respectively. You are required to calculate the value of machinery to be considered by ABC Ltd. and the finance charges for each year.

Ans. As per AS 19 "Leases", the lessee should recognize the lease as an asset and a liability at the inception of a finance lease. Such recognition should be at an amount equal to the fair value of the leased asset at the inception of lease. However, if the fair value of the leased asset exceeds the present value of

minimum lease payment from the standpoint of the lessee, the amount recorded as an asset and liability should be the present value of minimum lease payments from the standpoint of the lessee.

Value of machinery

In the given case, fair value of the machinery is ₹ 10, 00,000 and the net present value of minimum lease payments is ₹ 10, 07,020 (Refer working Note). As the present value of the machine is more than the fair value of the machine, the machine and the corresponding liability will be recorded at value of ₹10,00,000.

Calculation of finance charges for each year

Year	Finance charge (₹)	Payment (₹)	Reduction in outstanding liability (₹)	Outstanding liability (₹)
1st year beginning	-	-	-	10,00,000
End of 1st year	1,60,000	3,50,000	1,90,000	8,10,000
End of 2nd year	1,29,600	3,50,000	2,20,400	5,89,600
End of 3rd year	94,336	3,50,000	2,55,664	3,33,936
End of 4th year	53,430	3,50,000	2,96,570	37,366

Working Note:

Present value of minimum lease payments

Annual lease rental x PV factor ₹ 3,50,000 x (0.8621 + 0.7432 + 0.6407+ 0.5523)	₹ 9,79 ,405
Present value of guaranteed residual value ₹ 50,000 x (0.5523)	₹ 27,615
	₹ 10,07,020

Q-11 Classify the following into either operating or finance lease:

(i) If Present value (PV) of Minimum lease payment (MLP) = "X" ; Fair value of the asset is "Y" and X=Y.

(ii) Economic life of the asset is 7 years, lease term is 6.5 years, but asset is not acquired at the end of the lease term;

(iii) Economic life of the asset is 6 years, lease term is 2 years, but the asset is of special nature and has been procured only for use of the lessee.

Ans.

(i) The lease is a finance lease if X = Y, or if X substantially equals Y.

(ii) The lease will be classified as a finance lease, since a substantial portion of the life of the asset is covered by the lease term.

(iii) Since the asset is procured only for the use of lessee, it is a finance lease.

Q-12 Viral Ltd. sold machinery having WDV of ₹ 40 lakhs to Saral Ltd. for ₹ 50 lakhs and the same machinery was leased back by Saral Ltd. to Viral Ltd. The lease back is in nature of operating lease. You are required to explain the treatment in the given cases –

(i) Fair value is ₹ 45 lakhs and sale price is ₹ 38 lakhs.

(ii) Fair value is ₹ 40 lakhs and sale price is ₹ 50 lakhs.

(iii) Fair value is ₹ 46 lakhs and sale price is ₹ 50 lakhs

Ans. As per AS 19, where sale and leaseback results in operating lease, then the accounting treatment in different situations is as follows:

Situation 1: **Sale price = Fair Value**

Profit or loss should be recognized immediately.

Situation 2: **Sale Price < Fair Value**

Profit should be recognized immediately. The loss should also be recognized immediately except that, if the loss is compensated by future lease payments at below market price, it should be deferred and amortized in proportion to the lease payments over the period for which the asset is expected to be used.

Situation 3: **Sale Price > Fair Value**

The excess over fair value should be deferred and amortized over the period for which the asset is expected to be used.

Following will be the treatment in the situations given in the question:

(i) When fair value of leased machinery is ₹ 45 lakhs & sales price is ₹ 38 lakhs, then loss of ₹ 2 lakhs (40 – 38) to be immediately recognized by Viral Ltd. in its books provided loss is not compensated by future lease payment.

(ii) When fair value is ₹ 40 lakhs & sales price is ₹ 50 lakhs then, profit of ₹ 10 lakhs is to be deferred and amortized over the lease period.

(iii) When fair value is ₹ 46 lakhs & sales price is ₹ 50 lakhs, profit of ₹ 6 lakhs (46 less 40) to be immediately recognized in its books and balance profit of ₹4 lakhs (50-46) is to be amortized/ deferred over lease period.

Q-13 S. Square Private Limited has taken machinery on finance lease from S.K. Ltd. The information is as under: Lease term = 4 years

Fair value at inception of lease = ₹ 20,00,000

Lease rent = ₹ 6,25,000 p.a. at the end of year

Guaranteed residual value = ₹ 1,25,000

Expected residual value = ₹ 3,75,000

Implicit interest rate = 15%

Discounted rates for 1st year, 2nd year, 3rd year and 4th year are 0.8696, 0.7561, 0.6575 and 0.5718 respectively.

You are required to calculate the value of the lease liability as per AS-19 and also disclose impact of this on Balance sheet and Profit & loss account at the end of year 1.

Ans. According to AS 19 "Leases", the lessee should recognise the lease as an asset and a liability at an amount equal to the lower of the fair value of the leased asset at the inception of the finance lease and the present value of the minimum lease payments from the standpoint of the lessee.

In calculating the present value of the minimum lease payments the discount rate is the interest rate implicit in the lease. Present value of minimum lease payments will be calculated as follows:

Year	Minimum Lease Payment	Implicit interest rate (Discount rate @15%)	Present value
1	6,25,000	0.8696	5,43,500
2	6,25,000	0.7561	4,72,563
3	6,25,000	0.6575	4,10,937
4	7,50,000*	0.5718	4,28,850
Total	26,25,000		18,55,850

Present value of minimum lease payments ₹ 18,55,850 is less than fair value at the inception of lease i.e. ₹ 20,00,000, therefore, the asset and corresponding lease liability should be recognised at ₹ 18,55,850 as per AS 19.

Q-14 Monu Ltd. sold machinery having WDV of ₹ 400 lakhs to Sonu Ltd. for ₹ 500 lakhs and the same machinery was leased back by Sonu Ltd. to Monu Ltd. The lease back was in nature of operating lease.

Explain the accounting treatment as per AS 19 in the following cases:

(i) Sale price of ₹ 500 lakhs is equal to fair value.

(ii) Fair value is ₹ 450 lakhs and sale price is ₹ 380 lakhs.

(iii) Fair value is ₹ 400 lakhs and sale price is ₹ 500 lakhs.

(iv) Fair value is ₹ 460 lakhs and sale price is ₹ 500 lakhs

Ans. Following will be the treatment in the given cases:

(i) When sales price of ₹ 500 lakhs is equal to fair value, Monu Ltd. should immediately recognise the profit of ₹ 100 lakhs (i.e. 500 – 400) in its books.

(ii) When fair value of leased machinery is ₹ 450 lakhs & sales price is ₹ 380 lakhs, then loss of ₹ 20 lakhs (400 – 380) to be immediately recognised by Monu Ltd. in its books provided loss is not compensated by future lease payment.

(iii) When fair value is ₹ 400 lakhs & sales price is ₹ 500 lakhs then, profit of ₹ 100 lakhs is to be deferred and amortised over the lease period.

(iv) When fair value is ₹ 460 lakhs & sales price is ₹ 500 lakhs, profit of ₹ 60 lakhs (460-400) to be immediately recognised in its books and balance profit of ₹ 40 lakhs (500-460) is to be amortised/ deferred over lease period.

Q-15 X Ltd. sold machinery having WDV of ₹ 300 lakhs to Y Ltd. for ₹ 400 lakhs and the same machinery was leased back by Y Ltd. to X Ltd. The lease back arrangement is operating lease. Give your comments in the following situations:

(i) Sale price of ₹ 400 lakhs is equal to fair value.

(ii) Fair value is ₹ 450 lakhs.

(iii) Fair value is ₹ 350 lakhs and the sale price is ₹ 250 lakhs.

(iv) Fair value is ₹ 300 lakhs and sale price is ₹ 400 lakhs.

(v) Fair value is ₹ 250 lakhs and sale price is ₹ 290 lakhs.

Ans. Following will be the treatment in the given cases:

(i) When sale price of ₹ 400 lakhs is equal to fair value, X Ltd. should immediately recognize the profit of ₹ 100 lakhs (i.e. 400 - 300) in its books.

(ii) When fair value is ₹ 450 lakhs then also profit of ₹ 100 lakhs should be immediately recognized by X Ltd.

(iii) When fair value of leased machinery is ₹ 350 lakhs & sales price is ₹ 250 lakhs, then loss of ₹ 50 lakhs (300 - 250) to be immediately recognized by X Ltd. in its books provided loss is not compensated by future lease payment.

(iv) When fair value is ₹ 300 lakhs & sales price is ₹ 400 lakhs then, profit of ₹ 100 lakhs is to be deferred and amortized over the lease period.

(v) When fair value is ₹ 250 lakhs & sales price is ₹ 290 lakhs, then the loss of ₹ 50 lakhs (300-250) to be immediately recognized by X Ltd. in its books and profit of ₹ 40 lakhs (290-250) should be amortized/deferred over lease period.

Q-16 Sooraj Limited wishes to obtain a machine costing ₹ 30 lakhs by way of lease. The effective life of the machine is 14 years, but the company requires it only for the first 3 years. It enters into an agreement with Star Ltd., for a lease rental for ₹ 3 lakhs p.a. payable in arrears and the implicit rate of interest is 15%. The chief accountant of Sooraj Limited is not sure about the treatment of these lease rentals and seeks your advice. (use annuity factor at @ 15% for 3 years as 3.36)

Ans. As per AS 19 `leases', a lease will be classified as finance lease if at the inception of the lease, the present value of minimum lease payment amounts to at least substantially all of the fair value of leased asset. In the given case, the implicit rate of interest is given at 15%. The present value of minimum lease payments at 15% using PV- Annuity Factor can be computed as:

Annuity Factor (Year 1 to Year 3)	3.36
Present Value of minimum lease payments (₹ 3 lakhs each year)	₹ 10.08 lakhs

Thus present value of minimum lease payments is ₹10.08 lakhs and the fair value of the machine is ₹ 30 lakhs. In a finance lease, lease term should be for the major part of the economic life of the asset even if title is not transferred. However, in the given case, the effective useful life of the machine is 14 years while the lease is only for three years. Therefore, lease agreement is an operating lease. Lease payments under an operating lease should be recognized as an expense in the statement of profit and loss on a straight line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

In calculating the present value of the of minimum lease payments, the discount rate is the interest rate implicit in the lease.

Q-17 Classify the following into either operating or finance lease:

(i) If Present value (PV) of Minimum lease payment (MLP) = "X"; Fair value of theasset is "Y" and X=Y.

(ii) Economic life of the asset is 7 years, lease term is 6.5 years, but asset is notacquired at the end of the lease term;

(iii) Economic life of the asset is 6 years, lease term is 2 years, but the asset is of special nature and has been procured only for use of the lessee.

Ans.(i) The lease is a finance lease if X = Y, or if X substantially equals Y.

(ii) The lease will be classified as a finance lease, since a substantial portion of the life of the asset is covered by the lease term.

(iii) Since the asset is procured only for the use of lessee, it is a finance lease.

Q-18 Viral Ltd. sold machinery having WDV of ₹ 40 lakhs to Saral Ltd. for ' 50 lakhs and the same machinery was leased back by Saral Ltd. to Viral Ltd. The lease back is in nature of operating lease. You are required to explain the treatment in the given cases –

(i) Fair value is ₹ 45 lakhs and sale price is ₹ 39 lakhs.

(ii) Fair value is ₹ 40 lakhs and sale price is ₹ 49 lakhs.

(iii) Fair value is ₹ 46 lakhs and sale price is ₹ 50 lakhs

Ans. As per AS 19, where sale and leaseback results in operating lease, then the accounting treatment in different situations is as follows:

Situation 1: **Sale price = Fair Value**

Profit or loss should be recognized immediately.

Situation 2: **Sale Price < Fair Value**

Profit should be recognized immediately. The loss should also be recognized immediately except that, if the loss is compensated by future lease payments at below market price, it should be deferred and amortized in proportion to the lease payments over the period for which the asset is expected to be used.

Situation 3: Sale Price > Fair Value

The excess over fair value should be deferred and amortized over the period for which the asset is expected to be used.

Following will be the treatment in the situations given in the question:

(i) When fair value of leased machinery is ₹ 45 lakhs & sale price is ₹ 39 lakhs, then loss of ₹ 1 lakh (40 – 39) to be immediately recognized by Viral Ltd. in its books provided loss is not compensated by future lease payment.

(ii) When fair value is ₹ 40 lakhs & sale price is ₹ 49 lakhs then, profit of ₹ 9 lakhs is to be deferred and amortized over the lease period.

(iii) When fair value is ₹ 46 lakhs & sale price is ₹ 50 lakhs, profit of ₹ 6 lakhs (46 less 40) to be immediately recognized in its books and balance profit of ₹ 4 lakhs (50-46) is to be amortized/ deferred over lease period.

Q-19 You are required to give the necessary journal entry at the inception of lease to record the asset taken on finance lease in books of lessee from the following information:

Lease period	=	5 years;
Annual lease rents	=	₹ 50,000 at the end of each year.
Guaranteed residual value	=	₹ 25,000
Fair Value at the inception (beginning) of lease	=	₹ 2,00,000

Interest rate implicit on lease is = 12.6% (Discounted rates for year 1 to 5 are .890, .790, .700, .622 and .552 respectively).

Ans. Present value of minimum lease payment is computed below:

Year	MLP	DF (12.6%)	PV
	₹		₹
1	50,000	0.890	44,500
2	50,000	0.790	39,500
3	50,000	0.700	35,000
4	50,000	0.622	31,100
5	50,000	0.552	27,600
5	25,000	0.552	13,800
			1,91,500

Present value of minimum lease payment = ₹ 1,91,500

Fair value of leased asset = ₹ 2,00,000

As per AS 19, on the date of inception of Lease, Lessee should show it as an asset and corresponding liability at lower of Fair value of leased asset at the inception of the lease and present value of minimum lease payments from the standpoint of the lessee. The accounting entry at the inception of lease to record the asset taken on finance lease in books of lessee is suggested below:

	₹	₹
Asset A/c Dr.	1,91,500	
To Lessor (Lease Liability) A/c		1,91,500

(Being recognition of finance lease as asset and liability)

AS-20 EARNING PER SHARE

Q-1 From the following information, you are required to compute Basic and Diluted Earnings Per Share (EPS) of M/s. XYZ Limited for the year ended 31st March, 2019 :

Net Profit for the year after tax:	₹ 75,00,000
Number of Equity Shares of ₹ 10 each outstanding:	₹ 10,00,000

1,00,000, 8% Convertible Debentures of ₹ 100 each were issued by the Company at the beginning of the year. 1,10,000 Equity Shares were supposed to be issued on conversion. Consider rate of Income Tax as 30%.

Ans. **Computation of basic earnings per share**

Net profit for the current year / Weighted average number of equity shares outstanding during the year

₹ 75,00,000 / 10,00,000 = ₹ 7.50 per share

Computation of diluted earnings per share $\frac{\text{Adjusted net profit for the current year}}{\text{Weighted average number of equity shares}}$

Adjusted net profit for the current year

	₹
Net profit for the current year	75,00,000
Add: Interest expense for the current year	8,00,000
Less: Tax relating to interest expense (30% of ₹ 8,00,000)	(2,40,000)
Adjusted net profit for the current year	80,60,000

Number of equity shares resulting from conversion of debentures

= 1,10,000 Equity shares (given in the question)

Weighted average number of equity shares used to compute diluted earnings per share

= 11,10,000 shares (10,00,000 + 1,10,000)

Diluted earnings per share

= ₹ 80,60,000/ 11,10,000

= ₹ 7.26 per share

Note: Conversion of convertible debentures into Equity Share will be dilutive potential equity shares. Hence, to compute the adjusted profit the interest paid on such debentures will be added back as the same would not be payable in case these are converted into equity shares.

Q-2 From the following information, you are required to compute the basic and adjusted Earnings per share:

Net profit for 2015-16	11 lakh
Net profit for 2016-17	15 lakh
No. of shares issued before rights issue	5 lakhs
Right issue	One for every 5 held
Right issue price	15 per share
Last date of exercising right option	1-06-2016
Fair value of shares before right issue	21 per share

Ans. **Computation of theoretical ex-rights fair value per share**

$$\frac{\text{Fair value of all outstanding shares immediately prior to exercise of rights + Total amount received from exercise of rights}}{\text{Number of shares outstanding prior to exercise + number of shares issued in the exercise}}$$

$$\frac{(₹\ 21.00 \times 5,00,000 \text{ shares}) + (₹\ 15.00 \times 1,00,000 \text{ shares})}{5,00,000 \text{ shares} + 1,00,000 \text{ shares}}$$

Theoretical ex-rights fair value per share = ₹ 20.00

(a) **Computation of adjustment factor**

(b) $$\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex-rights value per share}} = \frac{₹(21.00)}{₹(20.00)} = 1.05$$

Computation of earnings per share

	Year 2015-16	**Year 2016-17**
EPS for the year 2015-16 as originally reported:		
(₹ 11,00,000/5,00,000 shares)	₹ 2.20	
EPS for the year 2015-16 restated for rights issue:		
[₹ 11,00,000/ (5,00,000 shares x 1.05)]	₹ 2.10	
EPS for the year 2016-17 including effects of rights issue		
$\frac{₹15,00,000}{(5,00,000 \times 1.05 \times 2/12) + (6,00,000 \times 10/12)}$		₹ 2.55

Q-3 The following information relates to M/s. XYZ Limited for the year ended 31st March, 2019:

Net Profit for the year after tax: ₹ 37,50,000

Number of Equity Shares of ₹ 10 each outstanding: ₹ 5,00,000

Convertible Debentures Issued by the Company (at the beginning of the year)

Particulars	**Nos.**
8% Convertible Debentures of ₹ 100 each	50,000
Equity Shares to be issued on conversion	55,000

The Rate of Income Tax: 30%.

You are required to calculate Basic and Diluted Earnings Per Share (EPS).

Ans. **Computation of basic earnings per share**

Net profit for the current year / Weighted average number of equity shares outstanding during the year

₹ 37,50,000 / 5,00,000 = ₹ 7.50 per share

Computation of diluted earnings per share $\frac{\text{Adjusted net profit for the current year}}{\text{Weighted average number of equity shares}}$

Adjusted net profit for the current year

	₹
Net profit for the current year	37,50,000
Add: Interest expense for the current year	4,00,000
Less: Tax relating to interest expense (30% of ₹ 4,00,000)	(1,20,000)
Adjusted net profit for the current year	40,30,000

Number of equity shares resulting from conversion of debentures

= 55,000 Equity shares (given in the question)

Weighted average number of equity shares used to compute diluted earnings per share

= 5,55,000 shares (5,00,000 + 55,000)

Diluted earnings per share

= 40,30,000/ 5,55,000 = ₹ 7.26 per share

Note: Conversion of convertible debentures into Equity Share will be dilutive potential equity shares. Hence, to compute the adjusted profit the interest paid on such debentures will be added back as the same would not be payable in case these are converted into equity shares.

Q-4 "While calculating diluted EPS, effect is given to all dilutive potential equity shares that were outstanding during the period." Explain this statement in the light of relevant AS.

Also calculate the diluted EPS from the following information:

Net Profit for the current year (After Tax)	₹ 1,00,00,000
No. of Equity shares outstanding	10,00,000
No. of 10% Fully Convertible Debentures of ₹ 100 each (Each Debenture is compulsorily & fully convertible into 10 equity shares issued at the mid of the year)	1,00,000
Debenture interest expense for the current year	₹ 5,00,000

Assume applicable Income Tax rate @ 30%

Ans. As per AS 20 `Earnings per Share', the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding during the period should be adjusted for the effects of all dilutive potential equity shares for calculation of diluted earnings per share. Hence, "in calculating diluted earnings per share, effect is given to all dilutive potential equity shares that were outstanding during the period."

$$\text{Computation of diluted earnings per share} = \frac{\text{Adjusted net profit for the current year}}{\text{Weighted average number of equity shares}}$$

Adjusted net profit for the current year

	₹
Net profit for the current year (after tax)	1,00,00,000
Add: Interest expense for the current year	5,00,000
Less: Tax relating to interest expense (30% of ₹ 5,00,000)	(1,50,000)
Adjusted net profit for the current year	1,03,50,000

Weighted average number of equity shares

Number of equity shares resulting from conversion of debentures

$= \frac{1,00,000 \times 100}{10}$ = 10,00,000 Equity shares

Weighted average number of equity shares used to compute diluted earnings per share

= [(10,00,000 x 12) + (10,00,000 x 6)]/12 = 15,00,000 equity shares

Diluted earnings per share = ₹ 1,03,50,000 / 15,00,000 shares = ₹ 6.90 per share

Q-5 The following information is available for TON Ltd. for the accounting year 2015-16 and 2016-17:

	Net profit for	**₹**
Year	2015-16	35,00,000
Year	2016-17	45,00,000

No of shares outstanding prior to right issue 15,00,000 shares.

Right issue : One new share for each 3 shares outstanding i.e. 5,00,000 shares.

: Right Issue price ₹ 25

: Last date to exercise rights 31st July, 2016

Fair value of one equity share immediately prior to exercise of rights on 31.07.2016 is ₹ 35.

You are required to compute:

(i) Basic earnings per share for the year 2015-16.

(ii) Restated basic earnings per share for the year 2015-16 for right issue.

(iii) Basic earnings per share for the year 2016-17.

Ans. **Computation of Basic Earnings per Share**

		Year 2015-16(₹)	**Year 2016-17(₹)**
(i)	EPS for the year 2015-16 as originally reported = Net profit for the year attributable to equity shareholder / weighted average number of equity share soutstanding during the year ₹ 35,00,000/ 15,00,000 shares	2.33	
(ii)	EPS for the year 2015-16 restated for the right issue ₹ 35,00,000/15,00,0000 shares x 1.08	2.16	
(iii)	EPS for the year 2016-17 (including effect of rightissue) ₹ 45,00,000 / [(15,00,000x1.08 x 4/12) +(20,00,000x8/12)]		2.40

Working Notes :

1. Computation of theoretical ex-rights fair value per share =

$$\frac{\text{Fair value of all outstanding shares immediately prior to exercise of rights + total amount received from exercise}}{\text{Number of shares outstanding prior to exercise + number of shares issued in the exercise}}$$

[(₹ 35 x15,00,000) + (₹ 25 x 5,00,000)] / (15,00,000 + 5,00,000) = ₹ 32.5

2. Computation of adjustment factor

$$\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex - rights value per share}} = ₹\ 35 / 32.50 = 1.08 \text{ (approx.)}$$

Q-6 From the following information given by Sampark Ltd., Calculate Basis EPS and Diluted EPS as per AS 20 :

	₹
Net Profit for the current year	2,50,00,000
No. of Equity Shares Outstanding	50,00,000
No. of 12% convertible debentures of ₹ 100 each	50,000
Each debenture is convertible into 8 Equity Shares	
Interest expense for the current year	6,00,000
Tax saving relating to interest expense (30%)	1,80,000

Ans. **Calculation of Basic Earning Per Share**

$$\text{Basic EPS} = \frac{\text{Net Profit for the current year}}{\text{No. of Equity Shares}} = \frac{₹2,50,00,000}{50,00,000}$$

Basic EPS per share = ₹ 5

Calculation of Diluted Earning Per Share

$$\textbf{Diluted EPS} = \frac{\text{Adjusted net profit for the current year}}{\text{Weighted average no. of Equity Shares}}$$

Adjusted net profit for the current year	₹
Net profit for the current year	2,50,00,000
Add: Interest expenses for the current year	6,00,000
Less: Tax saving relating to Tax Expenses	(1,80,000)
	2,54,20,000

No. of equity shares resulting from conversion of debentures: 4,00,000 Shares

Weighted average no. of equity shares used to compute diluted EPS: (50,00,000 + 4,00,000) = 54,00,000 Equity Shares

Diluted earnings per share: (2,54,20,000/54,00,000) = ₹ 4.71 (Approx.)

Q-7 As at 1st April, 2016 a company had 6,00,000 equity shares of ₹ 10 each (₹ 5 paid up by all shareholders). On 1st September, 2016 the remaining ₹ 5 was called up and paid by all shareholders except one shareholder having 60,000 equity shares. The net profit for the year ended 31st March, 2017 was ₹ 21,96,000 after considering dividend on preference shares and dividend distribution tax on such dividend totalling to ₹ 3,40,000.

Compute Basic EPS for the year ended 31st March, 2017 as per Accounting Standard 20 "Earnings Per Share".

Ans. **Basic Earnings per share (EPS) =** $\dfrac{\text{Net profit attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$

$$= \frac{21,96,000}{4,57,500 \text{ Shares} \left(\text{as per working note}\right)} = ₹\ 4.80 \text{ per share}$$

Working Note :

Calculation of weighted average number of equity shares

As per AS 20 `Earnings Per Share', partly paid equity shares are treated as a fraction of equity share to the extent that they were entitled to participate in dividend relative to a fully paid equity share during the reporting period. Assuming that the partly paid shares are entitled to participate in the dividend to the extent of amount paid, weighted average number of shares will be calculated as follows:

Date	No. of equity shares	Amount paid per share	Weighted average no. of equity shares
	₹	₹	₹
1.4.2016	6,00,000	5	6,00,000 E 5/10 E 5/12 = 1,25,000
1.9.2016	5,40,000	10	5,40,000 E 7/12 = 3,15,000
1.9.2016	60,000	5	60,000 E 5/10 E 7/12 = 17,500
Total weighted average equity shares			4,57,500

Q-8 Following information is supplied by K Ltd.

Number of shares outstanding prior to right issue - 2,50,000 shares.

Right issue price - ₹ 98

Last date of exercising rights-30-06-2018.

Fair value of one equity share immediately prior to exercise of right on 30-06-2018 is ₹ 102.

Net Profit to equity shareholders:

2017-2018 - ₹ 50,00,000

2018 - 2019 - ₹ 75,00,000

You are required to calculate the basic earnings per share as per AS - 20 Earning per Share.

Ans.

$$\frac{\text{Fair value of shares immediately prior to exercise of rights} + \text{Total amount received from exercise}}{\text{Number of shares outstanding prior to exercise} + \text{Number of shares issued in the exercise}}$$

$$\frac{102 \times 2,50,000 \text{ Shares} + ₹\ 98 \times 1,00,000 \text{ shares}}{3,50,000 \text{ shares}}$$

Theoretical ex-rights fair value per share = ₹ 100.86

Computation of adjustment factor:

$$\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex - rights value per share}} = 102/100.86 = 1.01$$

Computation of earnings per share:

EPS for the year 2017-18 as originally reported: ₹ 50,00,000/2,50,000 shares = ₹ 20

EPS for the year 2017-18 restated for rights issue: = ₹ 50,00,000/ (2,50,000 shares x 1.01)

= ₹ 19.80

EPS for the year 2018-19 including effects of rights issue:

EPS = 75,00,000/3,25,625* = ₹ 23.03

* [(2,50,000 x 1.01 x 3/12) + (3,50,000 x 9/12)] =63,125 + 2,62,500 = 3,25,625 shares

Note: Financial year (ended 31st March) is considered as accounting year while giving the above answer.

Q-9 From the following information, you are required to compute Basic and Diluted Earnings Per Share (EPS) of M/s. XYZ Limited for the year ended 31st March, 2019 :

Net Profit for the year after tax: ₹75,00,000

Number of Equity Shares of ₹ 10 each outstanding: ₹ 10,00,000

1,00,000, 8% Convertible Debentures of ₹ 100 each were issued by the Company at the beginning of the year. 1,10,000 Equity Shares were supposed to be issued on conversion. Consider rate of Income Tax as 30%.

Ans. **Computation of basic earnings per share**

Net profit for the current year / Weighted average number of equity shares outstanding during the year

₹ 75,00,000 / 10,00,000 = ₹ 7.50 per share

$$\text{Computation of diluted earnings per share} \frac{\text{Adjusted net profit for the current year}}{\text{Weighted average number of equity shares}}$$

Adjusted net profit for the current year

	₹
Net profit for the current year	75,00,000
Add: Interest expense for the current year	8,00,000
Less: Tax relating to interest expense (30% of ₹ 8,00,000)	(2,40,000)
Adjusted net profit for the current year	80,60,000

Number of equity shares resulting from conversion of debentures

= 1,10,000 Equity shares (given in the question)

Weighted average number of equity shares used to compute diluted earnings per share

= 11,10,000 shares (10,00,000 + 1,10,000)

Diluted earnings per share

= ₹ 80,60,000/ 11,10,000

= ₹7.26 per share

Note: Conversion of convertible debentures into Equity Share will be dilutive potential equity shares. Hence, to compute the adjusted profit the interest paid on such debentures will be added back as the same would not be payable in case these are converted into equity shares.

Q-10 A-One Limited supplied the following information. You are required to compute the earnings per share as per AS 20:

Net profit attributable to equity shareholders — Year 2017-18: ₹ 1,00,00,000

Year 2018-19 : ₹ 1,50,00,000

Number of shares outstanding prior to Right Issue 50,00,000 shares

Right Issue: One new share for each four outstanding shares i.e., 12,50,000 shares

Right Issue Price - ₹ 96

Last date of exercising rights - 30-06-2018

Fair value of one equity share immediately prior to exercise of rights on 30-06-2018 was ₹ 101.

Ans. **Computation of earnings per share**

	2017-18	2018-19
	₹	₹
EPS for the year 2017-18 as originally reported:	2.00	
(₹ 1,00,00,000 / 50,00,000 shares)		
EPS for the year 2017-18 restated for rights issue:	1.98	
₹1,00,00,000 / (50,00,000 shares x 1.01) *		
EPS for the year 2018-19 including effects of rights issue		
Rs. 1,50,00,000		
(50,00,000 x 1.01 x 3/12)+ (62,50,000 x 9/12)		2.52

**Computation of earnings per share in case of Rights Issue requires computation of adjustment factor which is given as working note*.

Working Notes:

1. Computation of theoretical ex-rights fair value per share

$$\frac{\text{Fair value of all outstanding shares immediately prior to exercise of rights+total amount received from exercise}}{\text{Number of shares outstanding prior to exercise + Number of shares issued in the exercise}}$$

$$\frac{(₹\ 101 \times 50,00,000 \text{ shares}) + (₹\ 96 \times 12,50,000 \text{ shares})}{50,00,000 \text{ shares} + 12,50,000 \text{ shares}}$$

= ₹ 62,50,00,000 / 62,50,000 = ₹100

Therefore, theoretical ex-rights fair value per share is = ₹ 100

2. Computation of adjustment factor

$$\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex-rights value per share}}$$

$$= \frac{₹(101)}{₹(100)} = 1.01$$

Q-11 The following information relates to XYZ Limited for the year ended 31st March, 2021:

Net Profit for the year after tax:	₹ 37,50,000
Number of Equity Shares of ₹ 10 each outstanding:	₹ 5,00,000

Convertible Debentures Issued by the Company (at the beginning of the year)

Particulars	**No.**
8% Convertible Debentures of ₹ 100 each	50,000
Equity Shares to be issued on conversion	55,000

The Rate of Income Tax: 30%.

You are required to calculate Basic and Diluted Earnings Per Share (EPS).

Ans. **Computation of basic earnings per share**

Net profit for the current year / Weighted average number of equity shares outstanding during the year ₹ 37,50,000 / 5,00,000 = ₹ 7.50 per share

Computation of diluted earnings per share $\frac{\text{Adjusted net profit for the current year}}{\text{Weighted average number of equity shares}}$

Adjusted net profit for the current year

	₹
Net profit for the current year	37,50,000
Add: Interest expense for the current year	4,00,000
Less: Tax relating to interest expense (30% of ₹ 4,00,000)	(1,20,000)
Adjusted net profit for the current year	40,30,000

Number of equity shares resulting from conversion of debentures

= 55,000 Equity shares (given in the question)

Weighted average number of equity shares used to compute diluted earnings per share

= 5,55,000 shares (5,00,000 + 55,000)

Diluted earnings per share

= 40,30,000/ 5,55,000 = ₹ 7.26 per share

Note: Conversion of convertible debentures into Equity Share will be dilutive potential equity shares. Hence, to compute the adjusted profit the interest paid on such debentures will be added back as the same would not be payable in case these are converted into equity shares.

Q-12 On 1st April, 2019 a company had 6,00,000 equity shares of ₹ 10 each (₹ 5 paid up by all shareholders). On 1st September, 2019 the remaining ₹ 5 was called up and paid by all shareholders except one shareholder having 60,000 equity shares. The net profit for the year ended 31st March, 2020 was ₹ 21,96,000 after considering dividend ₹ 3,40,000 on preference shares.

You are required to compute Basic EPS for the year ended 31st March, 2020 as per Accounting Standard 20 "Earnings Per Share".

Ans. Basic Earnings per share (EPS) =

$$\frac{\text{Net profit attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$$

$$\frac{21,96,000}{4,57,500 \text{ Shares (as per working note)}} = ₹\ 4.80 \text{ per share}$$

Working Note:

Calculation of weighted average number of equity shares

As per AS 20 ₹Earnings Per Share', partly paid equity shares are treated as a fraction of equity share to the extent that they were entitled to participate in dividend relative to a fully paid equity share during the reporting period. Assuming that the partly paid shares are entitled to participate in the dividend to the extent of amount paid, weighted average number of shares will be calculated as follows:

Date	No. of equity shares	Amount paid per share	Weighted average no. of equity shares
	₹	₹	₹
1.4.2020	6,00,000	**5**	6,00,000 x 5/10 x 5/12 = 1,25,000
1.9.2020	5,40,000	**10**	5,40,000 x 7/12 = 3,15,000
1.9.2020	60,000	**5**	60,000 x 5/10 x 7/12 = 17,500
Total weighted average equity shares			4,57,500

Q-13 In the following list of shares issued, for the purpose of calculation of weighted average number of shares, from which date, weight is to be considered:

(i) Equity Shares issued in exchange of cash,
(ii) Equity Shares issued as a result of conversion of a debt instrument,
(iii) Equity Shares issued in exchange for the settlement of a liability of the enterprise,
(iv) Equity Shares issued for rendering of services to the enterprise,
(v) Equity Shares issued in lieu of interest and/or principal of an other financial instrument,
(vi) Equity Shares issued as consideration for the acquisition of an asset other than in cash.

Ans. The following dates should be considered for consideration of weights for the purpose of calculation of weighted average number of shares in the given situations:

(i) Date of Cash receivable
(ii) Date of conversion
(iii) Date on which settlement becomes effective
(iv) When the services are rendered
(v) Date when interest ceases to accrue
(vi) Date on which the acquisition is recognised.

Q-14 AB Limited is a company engaged in manufacturing industrial packaging equipment. As per the terms of an agreement entered with its debenture holders, the company is required to appropriate adequate portion of its profits to a specific reserve over the period of maturity of the debentures such that, at the redemption date, the reserve constitutes at least half the value of such debentures. As such appropriations are not available for distribution to the equity shareholders, AB Limited has excluded this from the numerator in the computation of Basic EPS. Is this treatment correct as per provisions of AS 20?

Ans. The appropriation made to such a mandatory reserve created for the redemption of debentures would be included in the net profit attributable to equity shareholders for the computation of Basic EPS. AS 20 states that "For the purpose of calculating basic earnings per share, the net profit or loss for the period attributable to equity shareholders should be the net profit or loss for the period after deducting preference dividends and any attributable tax thereto for the period". With an emphasis on the phrase attributable to equity shareholders, it may be construed that such amounts appropriated to mandatory reserves, though not available for distribution as dividend, are still attributable to equity shareholders. Accordingly, these amounts should be included in the computation of Basic EPS. In view of this, the treatment made by the company is not correct.

Q-15 "The rights of a shares of a particular class, once issued, can be varied or altered." Comment on this statement in line with the provisions of the Companies Act.

Ans. The rights of shares of a particular class, once issued, can be varied or altered :

(a) If provision with respect to such variation is contained in the memorandum or articles of the company; or
(b) In the absence of any such provision in the memorandum or articles, if such variation is not prohibited by the terms of issue of the shares of that class.

However, it would require consent in writing of the holders of not less than three-fourths of the issued shares of that class or by means of a special resolution passed at a separate meeting of the holders of the issued shares of that class. Hence, if equity shareholders series A require a change in their right, of a particular nature, either a special resolution of a specially convened meeting of this class of shareholders will suffice, or otherwise more than 75% shareholders can give their consent in writing. It must be understood that a company having equity shares with voting rights cannot convert them into equity shares with differential voting rights, or vice-versa. However, the variation in their rights should not affect the rights of any other class, say Equity shares 'B' class or Preference shares. In such situation,

if variation by one class of shareholders affects the rights of any other class of shareholders, the consent of three-fourths of such other class of shareholders shall also be obtained and the provisions of the Companies Act section shall apply to such variation.

Q-16 Stock options have been granted by AB Limited to its employees and they vest equally over 5 years, i.e., 20 per cent at the end of each year from the date of grant. The options will vest only if the employee is still employed with the company at the end of the year. If the employee leaves the company during the vesting period, the options that have vested can be exercised, while the others would lapse. Currently, AB Limited includes only the vested options for calculating Diluted EPS. Should only completely vested options be included for computation of Diluted EPS? Is this in accordance with the provisions of AS 20? Explain.

Ans. The current method of calculating Diluted EPS adopted by AB limited is not in accordance with AS 20. The calculation of Diluted EPS should include all potential equity shares, i.e., all the stock options granted at the balance sheet date, which are dilutive in nature, irrespective of the vesting pattern. The options that have lapsed during the year should be included for the portion of the period the same were outstanding, pursuant to the requirement of the standard.

AS 20 states that "A potential equity share is a financial instrument or other contract that entitles, or may entitle, its holder to equity shares". Options including employee stock option plans under which employees of an enterprise are entitled to receive equity shares as part of their remuneration and other similar plans are examples of potential equity shares. Further, for the purpose of calculating diluted earnings per share, the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding during the period should be adjusted for the effects of all dilutive potential equity shares.

Q-17 X Limited, as at March 31, 2021, has income from continuing ordinary operations of ₹ 2,40,000, a loss from discontinuing operations of ₹ 3,60,000 and accordingly a net loss of ₹ 1,20,000. The Company has 1,000 equity shares and 200 potential equity shares outstanding as at March 31, 2021. You are required to compute Basic and Diluted EPS?

Ans. As per AS 20 "Potential equity shares should be treated as dilutive when, and only when, their conversion to equity shares would decrease net profit per share from continuing ordinary operations". As income from continuing ordinary operations, ₹2,40,000 would be considered and not ₹ (1,20,000), for ascertaining whether 200 potential equity shares are dilutive or anti-dilutive. Accordingly, 200 potential equity shares would be dilutive potential equity shares since their inclusion would decrease the net profit per share from continuing ordinary operations from ₹ 240 to ₹ 200. Thus the basic E.P.S would be ₹ (120) and diluted E.P.S. would be ₹ (100).

Q-18 "At the time calculating diluted earnings per share, effect is given to all dilutive potential equity shares that are outstanding during the period". Comment and also calculate the basic and diluted earnings per share for the year 2020-21 from the following information:

(i)	Net profit after tax for the year	₹ 64,12,500
(ii)	No. of equity shares outstanding	15,00,000
(iii)	No. of 9% convertible debentures of ₹ 100 issued on 1st July,2020	75,000
(iv)	Each debenture is convertible into 8 Equity Shares	
(v)	Tax relating to interest expenses	35%

Ans. In calculating diluted earnings per share, effect is given to all dilutive potential equity shares that were outstanding during the period." As per AS 2 0 'Earnings per Share', the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstandingfx during the period should be adjusted for the effects of all dilutive potential equity shares for the purpose of calculation of diluted earnings per share.

Basic EPS for the year 2020-21= 64,12,500/15,00,000 = ₹ 4.275 or ₹ 4.28

Computation of diluted earnings per share for year 2020-21

Adjusted net profit for the current year

Weighted average number of equity shares

Adjusted net profit for the current year will be (64,12,500 + 5,06,250 – 1,77,188) = ₹ 67,41,562

No. of equity shares resulting from conversion of debentures:

6,00,000 Shares (75,000 × 8)

Weighted average no. of equity shares used to compute diluted EPS:

(15,00,000 X12/12+ 6,00,000X9/12)

= 19,50,000 Shares

Diluted earnings per share: (67,41,562/19,50,000) = ₹ 3.46

Working Note:

Interest expense for 9 months = 75,00,000×9%×9/12 =₹ 5,06,250

Tax expense 35 % on interest is ₹ 1,77,188 (5,06,250 x 35%)

Q-19 Explain the concept of 'weighted average number of equity shares outstanding during the period'. Also compute, based on AS 20, the weighted average number of equity shares in the following case:

		No. of shares
1st April, 2021	Balance of equity shares	7,20,000
31st August, 2021	Equity shares issued for cash	2,40,000
1st February, 2022	Equity shares bought back	1,20,000
31st March, 2022	Balance of equity shares	8,40,000

Ans. As per AS 20, "Earnings Per Share", the weighted average number of equity shares outstanding during the period reflects the fact that the amount of shareholders' capital may have varied during the period as a result of a larger or less number of shares outstanding at any time. For the purpose of calculating basic earnings per share, the number of equity shares should be the weighted average number of equity shares outstanding during the period.

Weighted average number of equity shares:

7,20,000 X 5/12	= 3,00,000 shares
9,60,000 X 5/12	= 4,00,000 shares
8,40,000 X 2/12	= 1,40,000 shares
	8,40,000 shares

Q-20 On 1st April, 2019 a company had 6,00,000 equity shares of ₹ 10 each (₹ 5 paid up by all shareholders). On 1st September, 2019 the remaining ₹ 5 was called up and paid by all shareholders except one shareholder having 60,000 equity shares. The net profit for the year ended 31st March, 2020 was ₹ 21,96,000 after considering dividend on preference shares and dividend distribution tax on such dividend totalling to ₹ 3,40,000.

You are required to compute Basic EPS for the year ended 31st March, 2020 as per Accounting Standard 20 "Earnings Per Share".

Ans. Basic Earnings per share (EPS) =

$$\frac{\text{Net profit attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$$

$$= \frac{21,96,000}{4,57,500 \text{ Shares} \left(\text{as per working note}\right)} = ₹\ 4.80 \text{ per share}$$

Working Note:

Calculation of weighted average number of equity shares

As per AS 20 'Earnings Per Share', partly paid equity shares are treated as a fraction of equity share to the extent that they were entitled to participate in dividend relative to a fully paid equity share during the reporting period. Assuming that the partly paid shares are entitled to participate in the dividend to the extent of amount paid, weighted average number of shares will be calculated as follows:

Date	No. of equity shares ₹	Amount paid per share ₹	Weighted average no. of equity shares ₹
1.4.2019	6,00,000	5	6,00,000 E 5/10 E 5/12 = 1,25,000
1.9.2019	5,40,000	10	5,40,000 E 7/12 = 3,15,000
1.9.2019	60,000	5	60,000 E 5/10 E 7/12 = 17,500

Total weighted average equity shares 4,57,500

AS-22 ACCOUNTING FOR TAXES ON INCOME

Q-1 The following particulars are stated in the Balance Sheet of PQR Ltd. as on 31.03.2018:

	(₹ in lakh)
Deferred Tax Liability (Cr.)	30.00
Deferred Tax Assets (Dr.)	15.00

The following transactions were reported during the year 2018 -2019:

i.	Tax Rate	30%
		(₹ in lakh)
ii.	Depreciation as per books	80.00
	Depreciation for tax purposes	70.00
iii.	Items disallowed in 2017 - 2018 and allowed for tax purposes in 2018- 2019.	10.00
iv.	Donations to Private Trust made in 2018 -2019.	10.00

There were no additions to Fixed Assets during the year.

You are required to show the impact of various items on Deferred Tax Assets and Deferred Tax Liability as on 31.03.2019.

Ans. Impact of various items in terms of AS 22 deferred tax liability/deferred tax asset

Transactions	**Analysis**	**Nature of difference**	**Effect**	**Amount**
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	₹ (80- 70) lakh x 30% = ₹ 3 lakh

	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	₹ 10 lakh x 30% = ₹ 3 lakh
Donation to private trusts	Not an allowable expenditure under IT Act.	Permanent difference	Not applicable	Not applicable

Q-2 Beta Ltd. is a full tax free enterprise for the first ten years of its existence and is in the second year of its operation. Depreciation timing difference resulting in a tax liability in year 1 and 2 is Rs. 1,000 lakhs and Rs. 2,000 lakhs respectively. From the third year it is expected that the timing difference would reverse each year by Rs. 50 lakhs. Assuming tax rate of 40%, find out the deferred tax liability at the end of the second year and any charge to the Profit and Loss account.

Ans : As per para 13 of Accounting Standard (AS) 22, Accounting for Taxes on Income", deferred tax in respect of timing differences which originate during the tax holiday period and reverse during the tax holiday period, should not be recognized to the extent deduction from the total income of an enterprise is allowed during the tax holiday period as per the provisions of sections 10A and 10B of the Income-tax Act. Deferred tax in respect of timing differences which originate during the tax holiday period but reverse after the tax holiday period should be recognized in the year in which the timing differences originate. However, recognition of deferred tax assets should be subject to the consideration of prudence. For this purpose, the timing differences which originate first should be considered to reverse first.

Out of Rs. 1,000 lakhs depreciation, timing difference amounting Rs. 400 lakhs (Rs. 50 lakhs x 8 years) will reverse in the tax holiday period and therefore, should not be recognized. However, for Rs. 600 lakhs (Rs. 1,000 lakhs . Rs. 400 lakhs), deferred tax liability will be recognized for Rs. 240 lakhs (40% of Rs. 600 lakhs) in first year. In the second year, the entire amount of timing difference of Rs. 2,000 lakhs will reverse only after tax holiday period and hence, will be recognized in full. Deferred tax liability amounting Rs. 800 lakhs (40% of Rs. 2,000 lakhs) will be created by charging it to profit and loss account and the total balance of deferred tax liability account at the end of second year will be Rs. 1,040 lakhs (240 lakhs + 800 lakhs).

Q-3 Gamma Limited is working on different projects which are likely to be completed within 3 years period. It recognizes revenue from these contracts on percentage of completion method for financial statements during 2014-2015, 2015-2016 and 2016-2017 for Rs. 11,00,000, Rs. 16,00,000 and Rs. 21,00,000 respectively. However, for Income-tax purpose, it has adopted the completed contract method under which it has recognized revenue of Rs. 7,00,000, Rs. 18,00,000 and Rs. 23,00,000 for the years 2014-2015, 2015-2016 and 2016-2017 respectively. Income-tax rate is 35%.

You are required to compute the amount of deferred tax asset/liability for the years 2014-2015, 2015-2016 and 2016-2017. Also describe how this amount of deferred tax asset/liability will be disclosed in the balance sheet of Omega Limited as per provisions of AS 22.

Ans :

Gamma Limited

Calculation of Deferred Tax Asset/Liability

Year	Accounting Income	Taxable Income	Timing Difference (Balance)	Deferred Tax Liability (Balance)
2014-2015	11,00,000	7,00,000	4,00,000	1,40,000
2015-2016	16,00,000	18,00,000	2,00,000	70,000
2016-2017	21,00,000	23,00,000	NIL	NIL
	48,00,000	48,00,000		

As per AS 22, deferred tax assets and liabilities should be distinguished from assets and liabilities representing current tax for the period. Deferred tax assets and liabilities should be disclosed under a separate heading in the balance sheet of the enterprise, separately from current assets and current liabilities. The break-up of deferred tax assets and deferred tax liabilities into major components of the respective balances should be disclosed in the notes to accounts.

Q-4 Rohit Ltd. has provided the following information

Particulars	Rs.
Depreciation as per accounting records	2,50,000
Depreciation as per tax records	5,50,000
Unamortised preliminary expenses as per tax record	40,000

There is adequate evidence of future profit sufficiency. How much deferred tax assets/liability should be recognized as transition adjustment when the tax rate is 50%?

Ans **Table showing calculation deferred tax asset/liability**

Particulars	Amount Rs.	Timing defirrence	Defferred tax	Amount @ 50% Rs.
Excess depreciation as per tax records (Rs.5,50,000 - Rs.2,50,000)	3,00,000	Timing	Deferred tax liability	1,50,000
Unamortised preliminary expenses as per tax records	40,000	Timing	Deferred tax assest	20,000
Net deffered tax liablity				1,30,000

Net deferred tax liablity amounting Rs.1,30,000 should be recognized as transition adjustment.

Q-5 The Accountant of Sohna Ltd. provides the following information for the year ended 31-03-2019:

Particulars	₹
Accounting Profit	7,50,000
Book Profit as per MAT	4,37,500
Profit as per Income Tax Act	90,000
Tax rate	20%
MAT rate	7.50%

You are required to calculate the deferred tax asset/ liability as per AS 22 and amount of tax to be debited to the Profit and Loss Account for the year.

Ans : Tax as per accounting profit 7,50,000 x 20% = ₹ 1,50,000

Tax as per Income-tax Profit 90,000 x 20% = ₹ 18,000

Tax as per MAT 4,37,500 x 7.50% = ₹ 32,812.50

Tax expense= Current Tax + Deferred Tax

₹ 1,50,000 = ₹ 18,000 + Deferred tax

Therefore, **Deferred Tax liability** as on 31-03-2019

= ₹ 1,50,000 - ₹ 18,000 = ₹ 1,32,000

Amount of tax to be debited in Profit and Loss account for the year 31-03-2019

Current Tax + Deferred Tax liability + Excess of MAT over current tax

= ₹ 18,000 + ₹ 1,32,00

Q-6 Is it permissible not to recognize deferred tax liability on the ground that the Company expects that there will be losses both for accounting and tax purposes in near future? You are required to give advise to the company.

Ans : The Company should provide for deferred tax liability on the timing differences irrespective for the fact that these timing differences will reverse in the period in which the Company expects to be in loss both from the accounting as well as tax point of view. It may, however, be added that the deferred tax liability recognized at the balance sheet date will give rise to future taxable income at the time of reversal thereof.

Q-7 Rama Ltd., has provided the following information:

	Rs.
Depreciation as per accounting records	= 2,00,000
Depreciation as per income tax records	= 5,00,000
Unamortized preliminary expenses as per tax record	= 30,000

There is adequate evidence of future profit sufficiency.

You are required to calculate the amount of deferred tax asset/liability to be recognized as transition adjustment assuming Tax rate as 50%.

Ans : Table showing calculation of deferred tax asset / liability

Particulars	**Amount Rs.**	**Timing differences**	**Deferred tax**	**Amount @50%**
Excess depreciation as per tax records (Rs.5,00,000 - Rs.2,00,000)	3,00,000	Timing	Deferred tax liability	1,50,000
Unamortized preliminary expenses as per tax records	30,000	Timing	Deferred tax assets	15,000
Net deferred tax liability				1,35,000

Q-8 Write short note on Timing differences and Permanent differences as per AS 22.

Ans. Accounting income and taxable income for a period are seldom the same. Permanent differences are those which arise in one period and do not reverse subsequently. For e.g., an income exempt from tax or an expense that is not allowable as a deduction for tax purposes. Timing differences are those which arise in one period and are capable of reversal in one or more subsequent periods. For e.g., Depreciation, Bonus, etc.

Q-9 Rama Ltd., has provided the following information:

	₹
Depreciation as per accounting records	6,00,000
Depreciation as per income tax records	10,00,000
Unamortized preliminary expenses as per tax record	60,000

There is adequate evidence of future profit sufficiency. You are required to calculate the amount of deferred tax asset/liability to be recognized as transition adjus tment assuming Tax rate as 30%.

Ans. Table showing calculation of deferred tax asset / liability

Particulars	**Amount**	**Timing differences**	**Deferred tax**	**Amount @ 30%**
	₹			**₹**
Excess depreciation as per tax records (₹ 10,00,000 – ₹ 6,00,000)	4,00,000	Timing	Deferred tax liability	1,20,000
Unamortized preliminary expenses as per tax records	60,000	Timing	Deferred tax asset	(18,000)
Net deferred tax liability				1,02,000

Q-10 Is it permissible not to recognize deferred tax liability on the ground that the Company expects that there will be losses both for accounting and tax purposes in near future? You are required to give advise to the company.

Ans. The Company should provide for deferred tax liability on the timing differences irrespective for the fact that these timing differences will reverse in the period in which the Company expects to be in loss both from the accounting as well as tax point of view. It may, however, be added that the deferred tax liability recognized at the balance sheet date will give rise to future taxable income at the time of reversal thereof.

Q-11 Beta Ltd. is a full tax free enterprise for the first ten years of its existence and is in the second year of its operation. Depreciation timing difference resulting in a tax liability in year 1 and 2 is Rs.1,000 lakhs and Rs.2,000 lakhs respectively. From the third year it is expected that the timing difference would reverse each year by Rs.50 lakhs. Assuming tax rate of 40%, you are required to compute to the deferred tax liability at the end of the second year and any charge to the Profit and Loss account.

Ans. As per para 13 of Accounting Standard (AS) 22, Accounting for Taxes on Income", deferred tax in respect of timing differences which originate during the tax holiday period and reverse during the tax holiday period, should not be recognized to the extent deduction from the total income of an enterprise is allowed during the tax holiday period as per the provisions of sections 10A and 10B of the Income-tax Act. Deferred tax in respect of timing differences which originate during the tax holiday period but reverse after the tax holiday period should be recognized in the year in which the timing differences originate. However, recognition of deferred tax assets should be subject to the consideration of prudence. For this purpose, the timing differences which originate first should be considered to reverse first.

Out of Rs. 1,000 lakhs depreciation, timing difference amounting Rs. 400 lakhs (Rs. 50 lakhs x 8 years) will reverse in the tax holiday period and therefore, should not be recognized. However, for Rs. 600 lakhs (Rs. 1,000 lakhs - Rs. 400 lakhs), deferred tax liability will be recognized for Rs. 240 lakhs (40% of Rs. 600 lakhs) in first year. In the second year, the entire amount of timing difference of Rs. 2,000 lakhs will

reverse only after tax holiday period and hence, will be recognized in full. Deferred tax liability amounting Rs. 800 lakhs (40% of Rs.2,000 lakhs) will be created by charging it to profit and loss account and the total balance of deferred tax liability account at the end of second year will be Rs. 1,040 lakhs (240 lakhs + 800 lakhs).

Q-12 The Accountant of Sohna Ltd. provides the following information for the year ended 31-03-2019:

Particulars	**₹**
Accounting Profit	7,50,000
Book Profit as per MAT	4,37,500
Profit as per Income Tax Act	90,000
Tax rate	20%
MAT rate	7.50%

You are required to calculate the deferred tax asset/ liability as per AS 22 and amount of tax to be debited to the Profit and Loss Account for the year.

Ans. Tax as per accounting profit 7,50,000 x 20% = ₹ 1,50,000

Tax as per Income-tax Profit 90,000 x 20% = ₹ 18,000

Tax as per MAT 4,37,500 x 7.50% = ₹ 32,812.50

Tax expense= Current Tax + Deferred Tax

₹ 1,50,000 = ₹ 18,000 + Deferred tax

Therefore, **Deferred Tax liability** as on 31-03-2019

= ₹ 1,50,000 - ₹ 18,000 = ₹ 1,32,000

Amount of tax to be debited in Profit and Loss account for the year 31-03-2019

Current Tax + Deferred Tax liability + Excess of MAT over current tax

= ₹ 18,000 + ₹ 1,32,000 + ₹ 14,812.50 (32,812.50 - 18,000)

= ₹ 1,64,812.50

Q-13 Rama Ltd., has provided the following information:

	Rs.
Depreciation as per accounting records	= 2,00,000
Depreciation as per income tax records	= 5,00,000
Unamortized preliminary expenses as per tax record	= 30,000

There is adequate evidence of future profit sufficiency.

You are required to calculate the amount of deferred tax asset/liability to be recognized as transition adjustment assuming Tax rate as 50%.

Ans. **Table showing calculation of deferred tax asset / liability**

Particulars	**Amount Rs.**	**Timing differences**	**Deferred tax**	**Amount @50%**
Excess depreciation as per tax records (Rs.5,00,000 - Rs.2,00,000)	3,00,000	Timing	Deferred tax liability	1,50,000
Unamortized preliminary expenses as per tax records	30,000	Timing	Deferred tax assets	15,000
Net deferred tax liability				1,35,000

Q-14 The following particulars are stated in the Balance Sheet of Deep Limited as on 31st March, 2020:

	(₹ 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 ₹ 70 Lakhs whereas Depreciation for Tax purposes was ₹ 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 ₹ 14 Lakhs.

(iii) Share issue expenses allowed under section 35(D) of the Income Tax Act, 1961 for the year 2020-21 [1110th of ₹ 70.00 lakhs incurred in 2019-20).

(iv) Repairs to Plant and Machinery were made during the year for ₹ 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.

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

Transactions	**Analysis**	**Nature of difference**	**Effect**	**Amount (₹)**
Difference in depreciation	Generally, written down value method of depreciation is adopted under IT Act which leads to higher depreciation in earlier years of useful life of the asset in comparison to later years.	Responding timing difference	Reversal of DTL	28 lakhs **x** 40% = ₹ 11.20 lakhs
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 **x** 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 **x** 40% = ₹ 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 **x** 40% =28 lakhs

Q-15 The following particulars are stated in the Balance Sheet of HS Ltd. as on 31 -3-2019:

Particulars	**(₹ in lakhs)**
Deferred Tax Liability (Cr.)	60.00
Deferred Tax Assets (Dr.)	30.00

The following transactions were reported during the year 2019-20:

Depreciation as per accounting records	160.00	
Depreciation as per income tax records	140.00	
Items disallowed for tax purposes in 2018-19 but allowed in 2019-20		20.00
Donation to Private Trust		20.00
Tax rate		30%

There were no additions to fixed assets during the year. You are required to show the impact of various items on Deferred Tax Assets and Deferred Tax Liability as on 31 -3-2020 as per AS-22.

Ans. Impact of various items in terms of AS 22 deferred tax liability/deferred tax asset

(1) Difference in Depreciation- Generally, written down value method of depreciation is adopted under income Tax Act which leads to higher depreciation in earlier years of useful life of the asset in comparison to later years. It is timing difference for which reversal of deferred tax liability is required.

Reversal of DTL= ₹ (160 - 140) Lakhs X 30% = ₹ 6 Lakhs

(2) Disallowances, as per IT Act of earlier years- Due to disallowance tax payable for the earlier years was higher on this account. It is responding timing difference which required Reversal of Deferred tax assets.

Reversal of Deferred tax assets = ₹ 20 Lakhs X 30% = ₹ 6 Lakhs

(3) Donations to private trusts is not an allowable expenditure under IT Act. It is permanent difference. Hence, no reversal of tax is required.

Q-16 From the following details of Aditya Limited for accounting year ended on 31st March, 2020:

Particulars	**₹**
Accounting profit	15,00,000
Book profit as per MAT	7,50,000
Profit as per Income tax Act	2,50,000
Tax Rate	20%
MAT Rate	7.5%

Calculate the deferred tax asset/liability as per AS 22 and amount of tax to be debited to the profit and loss account for the year.

Ans. Tax as per accounting profit 15,00,000x20%= ₹ 3,00,000

Tax as per Income-tax 2,50,000x20% =₹ 50,000

Profit Tax as per MAT 7,50,000x7.50%= ₹ 56,250

Tax expense= Current Tax +Deferred Tax

₹ 3,00,000 = ₹ 50,000+ Deferred tax

Therefore, Deferred Tax liability as on 31-03-2020

= ₹ 3,00,000 – ₹ 50,000 = ₹ 2,50,000

Amount of tax to be debited in Profit and Loss account for the year 31-03-2020

Current Tax + Deferred Tax liability + Excess of MAT over current tax

= ₹ 50,000 + ₹ 2,50,000 + ₹ 6,250 (56,250 – 50,000) = ₹ 3,06,250

Q-17 The following information is furnished in respect of Slate Ltd. for the year ending 31-3-2019:

(i) Depreciation as per books ₹ 2,80,000

Depreciation for tax purpose ₹ 1,90,000

The above depreciation does not include depreciation on new additions.

(ii) A new machinery purchased on 1.4.18 costing ₹ 1,20,000 on which 100% depreciation is allowed in the 1st year for tax purpose whereas Straight-line method is considered appropriate for accounting purpose with a life estimation of 4 years.

(iii) The company has made a profit of ₹ 6,40,000 before depreciation and taxes.

(iv) Corporate tax rate of 40%.

Prepare relevant extract of statement of Profit and Loss for the year ending 31-3-2019 and also show the

effect of above items on deferred tax liability/asset as per AS 22.

Ans. Statement of Profit and Loss for the year ended 31st March, 2019 (Extract)

			₹
Profit before depreciation and taxes			6,40,000
Less: Depreciation for accounting purposes (2,80,000+30,000)			(3,10,000)
Profit before taxes	(A)		3,30,000
Less: Tax expense	(B)		
Current tax (W.N.1) (3,30,000 x 40%)		1,32,000	
Deferred tax (W.N.2)		NIL	(1,32,000)
Profit after tax	(A-B)		1,98,000

Working Notes:

1. Computation of taxable income

	Amount (₹)
Profit before depreciation and tax	6,40,000
Less: Depreciation for tax purpose (1,90,000 + 1,20,000)	(3,10,000)
Taxable income	3,30,000
Tax on taxable income @ 40%	1,32,000

2. Impact of various items in terms of deferred tax liability / deferred tax asset

S. No.	Transactions	Analysis	Nature of difference	Effect	Amount (₹)
(i)	Difference in depreciation	Generally, written down value method of depreciation is adopted under IT Act which leads to higher depreciation in earlier years of useful life of the asset in comparison to later years.	Responding timing difference	Reversal of DTL	(2,80,000 - 1,90,000) x 40% = (36,000)

(ii)	Depreciation on new machinery	Due to allowance of full amount as expenditure under IT Act, tax payable in the earlier years is less.	Timing difference	Creation of DTL	(1,20,000 – 30,000) x 40% = 36,000
	Net impact				NIL

Q-18 What are the disclosure requirements for deferred tax assets and deferred tax liabilities in the balance sheet as per AS 22?

Ans. The break-up of deferred tax assets and deferred tax liabilities into major components of the respective balance should be disclosed in the notes to accounts. Deferred tax assets and liabilities should be distinguished from assets and liabilities represent ing current tax for the period. Deferred tax assets and liabilities should be disclosed under a separate heading in the balance sheet of the enterprise, separately from current assets and current liabilities. The nature of the evidence supporting the recognition of deferred tax assets should be disclosed, if an enterprise has unabsorbed depreciation or carry forward of losses under tax laws.

Q-19 Can an enterprise offset deferred tax assets and deferred tax liabilities? If yes, prescribe the conditions required for such offset as per provisions of AS 22. AS 24 Discontinuing Operations

Ans. Yes. It can offset deferred tax assets and deferred tax liabilities. As per AS 22, an enterprise should offset deferred tax assets and deferred tax liabilities if:

(i) the enterprise has a legally enforceable right to set off assets against liabilities representing current tax; and

(ii) the deferred tax assets and the deferred tax liabilities relate to taxes on income levied by the same governing taxation laws.

Q-20 The following transactions were reported by PQR Ltd. during the year 2020-2021:

I.	Tax Rate	30%
		(‘ in lakh)
II.	Items disallowed in 2019-2020 and allowed for tax purposesin 2020-2021.	20.00
III.	Interest to Financial Institutions accounted in the books onaccrual basis, but actual payment was made before the duedate of filing return and allowed for tax purpose also.	20.00
IV.	Donations to Private Trust made in 2020-2021 (not allowedunder Income Tax Laws).	10.00

You are required to show impact of the above items in terms of Deferred Tax Assets/Deferred Tax Liability for the year ended 31.03.2021.

Ans.(a) Impact of various items in terms of deferred tax liability/deferred tax asset as per AS 22

Transactions	Analysis	Nature of difference	Effect	Amount
Disallowances, as per IT Act, of earlier years	Tax payable for the earlier year was higher on this account.	Timing difference	Reversal of DTA	₹ 20 lakh x 30% = ₹ 6 lakh

Interest to financial institutions	It is allowed as deduction under IT Act, if the payment is made before the due date of filing the return of income	No timing difference	Not applicable	Not applicable
Donation to private trusts	Not an allowable expenditure under IT Act.	Permanent difference	Not applicable	Not applicable

AS-24 DISCOUNTING OPERATIONS

Q-1 (i) What are the disclosure and presentation requirements of AS 24 for discontinuing operations?

(ii) Give four examples of activities that do not necessarily satisfy criterion (a) of paragraph 3 of AS 24, but that might do so in combination with other circumstances.

Ans. (i) An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event (as de fined in paragraph 15) occurs:

(a) a description of the discontinuing operation(s);

(b) the business or geographical segment(s) in which it is reported as per AS 17, Segment Reporting;

(c) the date and nature of the initial disclosure event;

(d) the date or period in which the discontinuance is expected to be completed if known or determinable;

(e) the carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;

(f) the amounts of revenue an d expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;

(g) the amount of pre -tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto; and

(h) the amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial repor ting period.

(ii) Para 3 of AS 24 "Discontinuing Operations" explains the criteria for determination of discontinuing operations. According to Paragraph 9 of AS 24, examples of activities that do not necessarily satisfy criterion (a) of paragraph 3, but that might do so in combination with other circumstances, include:

(i) Gradual or evolutionary phasing out of a product line or class of service;

(ii) Discontinuing, even if relatively abruptly, several products within an ongoing line of business;

(iii) Shifting of some production or marketing activities for a particular line of business from one location to another; and

(iv) Closing of a facility to achieve productivity improvements or other cost savings.

An example in relation to consolidated financial st atements is selling a subsidiary whose activities are similar to those of the parent or other subsidiaries.

Q-2 A consumer goods producer has changed the product line as follows:

	Dish washing Bar (Per month)	Clothes washing Bar (Per month)
January 2016 - September 2016	2,00,000	2,00,000
October 2016 - December 2016	1,00,000	3,00,000
January 2017 - March 2017	Nil	4,00,000

The company has enforced a gradual enforcement of change in product line on the basis of an overall plan. The Board of Directors has passed a resolution in March 2016 to this effect. The company follows calendar year as its accounting year. You are required to advise whether it should it be treated as discontinuing operation as per AS 24?

Ans. As per AS 24 `Discontinuing Operations', a discontinuing operation is a component of an enterprise:

(i) that the enterprise, pursuant to a **single plan**, is:

(1) disposing of substantially in its entirety,

(2) disposing of piecemeal, or

(3) terminating through abandonment; and

(ii) that represents a separate major line of business or geographical area of operations; and

(iii) that can be distinguished operationally and for financial reporting purposes.

As per provisions of the standard, business enterprises frequently close facilities, abandon products or even product lines, and change the size of their work force in response to market forces. While those kinds of terminations generally are not, in themselves, discontinuing operations, they can occur in connection with a discontinuing operation. Examples of activities that do not necessarily satisfy criterion of discontinuing operation are gradual or evolutionary phasing out of a product line or class of service, discontinuing, even if relatively abruptly, several products within an ongoing line of business;

In the given case, the company has enforced a gradual enforcement of change in product line and does not represent a separate major line of business and hence is not a discontinued operation.If it were a discontinuing operation, the initial disclosure event is the occurrence of one of the following, whichever occurs earlier:

(i) the enterprise has entered into a binding sale agreement for substantially all of the assets attributable to the discontinuing operation; or

(ii) the enterprises board of directors or similar governing body has both approved a detailed, formal plan for discontinuance and made an announcement of the plan.

Q-3 Give four examples of activities that do not necessarily satisfy criterion (a) of paragraph 3 of AS 24, but that might do so in combination with other circumstances.

Ans : Para 3 of AS 24 "Discontinuing Operations" explains the criteria for determination of discontinuing operations. According to Paragraph 9 of AS 24, examples of activities that do not necessarily satisfy criterion (a) of paragraph 3, but that might do so in combination with other circumstances, include:

(i) Gradual or evolutionary phasing out of a product line or class of service;

(ii) Discontinuing, even if relatively abruptly, several products within an ongoing line ofbusiness;

(iii) Shifting of some production or marketing activities for a particular line of business from one location to another; and

(iv) Closing of a facility to achieve productivity improvements or other cost savings.

An example in relation to consolidated financial statements is selling a subsidiary whose activities are similar to those of the parent or other subsidiaries.

Q-4 What are the initial disclosure requirements of AS 24 for discontinuing operations?

Ans. An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:

A. A description of the discontinuing operation(s)

B. The business or geographical segment(s) in which it is reported as per AS 17

C. The date and nature of the initial disclosure event.

D. The date or period in which the discontinuance is expected to be completed if known or determinable

E. The carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled

F. The amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period

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

H. The amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

Q-5 (i) What are the disclosure and presentation requirements of AS 24 for discontinuing operations?

(ii) Give four examples of activities that do not necessarily satisfy criterion (a) of paragraph 3 of AS 24, but that might do so in combination with other circumstances.

Ans. (i) An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event (as defined in paragraph 15) occurs:

(a) a description of the discontinuing operation(s);

(b) the business or geographical segment(s) in which it is reported as per AS 17, Segment Reporting;

(c) the date and nature of the initial disclosure event;

(d) the date or period in which the discontinuance is expected to be completed if known or determinable;

(e) the carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;

(f) the amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;

(g) the amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto; and

(h) the amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

(ii) Para 3 of AS 24 “Discontinuing Operations” explains the criteria for determination of discontinuing operations. According to Paragraph 9 of AS 24, examples of activities that do not necessarily satisfy criterion (a) of paragraph 3, but that might do so in combination with other circumstances, include:

(i) Gradual or evolutionary phasing out of a product line or class of service;

(ii) Discontinuing, even if relatively abruptly, several products within an ongoing line of business;

(iii) Shifting of some production or marketing activities for a particular line of business from one location to another; and

(iv) Closing of a facility to achieve productivity improvements or other cost savings.

An example in relation to consolidated financial statements is selling a subsidiary whose activities are similar to those of the parent or other subsidiaries.

Q-6 What do you understand by Discontinuing Operations? What are the disclosure and presentation requirements of AS 24 for discontinuing operations? Explain in brief.

Ans. As per AS 24 "Discontinuing Operations", a discontinuing operation is a component of an enterprise:

a. That the enterprise, pursuant to a single plan, is:

(i) Disposing of substantially in its entirety, such as by selling the component in a single transaction or by demerger or spin-off of ownership of the component to the enterprise's shareholders or

(ii) Disposing of piecemeal, such as by selling off the component's assets and settling its liabilities individually or

(iii) Terminating through abandonment and

b. That represents a separate major line of business or geographical area of operations.

c. That can be distinguished operationally and for financial reporting purposes.

An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:

- A description of the discontinuing operation(s);
- The business or geographical segment(s) in which it is reported as per AS 17;
- The date and nature of the initial disclosure event.
- The date or period in which the discontinuance is expected to be completed if known or determinable,
- The carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;
- The amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;
- The amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto;
- The amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

Q-7 Rohini Limited is in the business of manufacture of passenger cars and commercial vehicles. The Company is working on a strategic plan to close the production of passenger cars and to produce only commercial vehicles over the coming 5 years. However, no specific plans have been drawn up for sale of neither the division nor its assets. As part of its prospective plan it will reduce the production of passenger cars by 20% annually. It also plans to establish another new factory for the manufacture of commercial vehicles and transfer surplus employees in a phased manner. You are required to comment:

(i) If mere gradual phasing out in itself can be considered as a `discontinuing operation' within the meaning of AS-24.

(ii) If the Company passes a resolution to sell some of the assets in the passenger car division and also to transfer few other assets of the passenger car division to the new factory, does this trigger the application of AS-24?

(iii) Would your answer to the above be different if the Company resolves to sell the assets of the passenger car division in a phased but time bound manner?

Ans. (i) As per AS 24, a discontinuing operation is a component of an enterprise:

(a) That the enterprise, pursuant to a single plan, is:

(i) Disposing of substantially in its entirety, such as by selling the component in a single transaction or by demerger or spin-off of ownership of the component to the enterprise's shareholders; or

(ii) Disposing of piecemeal, such as by selling off the component's assets and settling its liabilities individually; or

(iii) Terminating through abandonment; and

(b) That represents a separate major line of business or geographical area of operations; and

(c) That can be distinguished operationally and for financial reporting purposes.

Mere gradual phasing out is not considered as discontinuing operation as defined under AS 24, `Discontinuing Operations'. Examples of activities that do not necessarily satisfy criterion of the definition, but that might do so in combination with other circumstances, include:

(a) Gradual or evolutionary phasing out of a product line or class of service;

(b) Shifting of some production or marketing activities for a particular line of business from one location to another; and

(c) Closing of a facility to achieve productivity improvements or other cost savings.

In this case, it cannot be considered as Discontinuing Operation as per AS-24 as the company's strategic plan has no final approval from the board through a resolution and there is no specific time bound activities like shifting of assets and employees. Moreover, the new segment i.e. commercial vehicle production line in a new factory has not started.

(ii) No, the resolution is silent about stoppage of the car segment in definite time period. Though, sale of some assets and some transfer proposal were passed through a resolution to the new factory, but the closure road map and new segment starting roadmap are missing.

Hence, AS 24 will not be applicable and it cannot be considered as discontinuing operation.

(iii) Yes, phased and time bound program resolved in the board clearly indicates the closure of the passenger car segment in a definite time frame and will constitute a clear roadmap.

Hence, this action will attract compliance of AS 24 and it will be considered as Discontinuing Operation as per AS-24.

Q-8 Arzoo Ltd. is in the business of manufacture of passenger cars and commercial vehicles. The company is working on a strategic plan to shift from the passenger car segment to the commercial vehicles segment over the coming 5 years. However, no specific plans have been drawn up for sale of neither the division nor its assets. As part of its plan, it has planned that it will reduce the production of passenger cars by 20% annually. It also plans to commence another new factory for the manufacture of commercial vehicles plus transfer of employees in a phased manner. These plans have not approved from the Board of Directors and the new factory for manufacture of commercial vehicles has not yet started. You are required to comment if mere gradual phasing out in itself can be considered as a `Discontinuing Operation' within the meaning of AS 24.

Ans. Mere gradual phasing out is not considered as discontinuing operation as defined under AS 24, `Discontinuing Operations'.

Examples of activities that do not necessarily satisfy criterion of the definition, but that might do so in combination with other circumstances, include:

(1) Gradual or evolutionary phasing out of a product line or class of service;

(2) Discontinuing, even if relatively abruptly, several products within an ongoing line of business;

(3) Shifting of some production or marketing activities for a particular line of business from one location to another; and

(4) Closing of a facility to achieve productivity improvements or other cost savings. In view of the above, mere gradual phasing out in itself cannot be considered as discontinuing operation. The companies' strategic plan also has no final approval from the board through a resolution and there is no specific time bound activities like shifting of assets and employees. Moreover, the new segment i.e. commercial vehicle production line in a new factory has not started.

Q-9 What are discontinuing operations as per AS 24? Should an enterprise include prescribed information relating to a discontinuing operation in its financial statements?

Ans. A discontinuing operation is a component of an enterprise:

a. That the enterprise, pursuant to a single plan, is:

(i) Disposing of substantially in its entirety, such as by selling the component in a single transaction or by demerger or spin-off of ownership of the component to the enterprise's shareholders or

(ii) Disposing of piecemeal, such as by selling off the component's assets and settling its liabilities individually or

(iii) Terminating through abandonment and

b. That represents a separate major line of business or geographical area of operations.

c. That can be distinguished operationally and for financial reporting purposes.

An enterprise should include prescribed information relating to a discontinuing operation in its financial statements, as per requirements of AS 24, beginning with the financial statements for the period in which the initial disclosure event occurs.

Q-10

(i) What are the disclosure and presentation requirements of AS 24 fordiscontinuing operations?

(ii) Give four examples of activities that do not necessarily satisfy criterion (a) of paragraph 3 of AS 24, but that might do so in combination with other circumstances.

Ans. **(i)** An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:

(a) a description of the discontinuing operation(s);

(b) the business or geographical segment(s) in which it is reported as per AS 17 'Segment Reporting';

(c) the date and nature of the initial disclosure event;

(d) the date or period in which the discontinuance is expected to be completed if known or determinable;

(e) the carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;

(f) the amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;

(g) the amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto; and

(h) the amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

(ii) Para 3 of AS 24 "Discontinuing Operations" explains the criteria for determination of discontinuing operations. According to AS 24, examples of activities that do not necessarily satisfy criterion (a) of paragraph 3, but that might do so in combination with other circumstances, include:

(i) Gradual or evolutionary phasing out of a product line or class of service;

(ii) Discontinuing, even if relatively abruptly, several products within an ongoing line of business;

(iii) Shifting of some production or marketing activities for a particular line of business from one location to another; and

(iv) Closing of a facility to achieve productivity improvements or other cost savings.

An example in relation to consolidated financial statements is selling a subsidiary whose activities are similar to those of the parent or other subsidiaries.

AS-26 INTANGIBLE ASSETS

Q-1 A company acquired patent right for ₹ 1200 lakhs. The product life cycle has been estimated to be 5 years and the amortization was decided in the ratio of estimated future cash flows which are as under:

Year	**1**	**2**	**3**	**4**	**5**
Estimated future cash flows (₹ in lakhs)	600	600	600	300	300

After 3rd year, it was ascertained that the patent would have an estimated balance future life of 3 years and the estimated cash flow after 5th year is expected to be ₹ 150 lakhs. You are required to determine the amortization pattern under Accounting Standard 26.

Ans. **Amortization of cost of patent as per AS 26**

Year	**Estimated future cash flow (₹ in lakhs)**	**Amortization Ratio**	**Amortized Amount (₹ in lakhs)**
1	600	.25	300
2	600	.25	300
3	600	.25	300
4	300	.40 (Revised)	120
5	300	.40 (Revised)	120
6	150	.20 (Revised)	60
			1,200

In the first three years, the patent cost will be amortized in the ratio of estimated future cash flows i.e. (600: 600: 600: 300: 300).

The unamortized amount of the patent after third year will be ₹ 300 lakh (1,200-900) which will be amortized in the ratio of revised estimated future cash flows (300:300:150) in the fourth, fifth and sixth year.

Q-2 A Ltd. has got the license to manufacture particular medicines for 10 years at a license fee of Rs. 200 lakhs. Given below is the pattern of expected production and expected operating cash inflow:

Year	Production in bottles (in lakhs)	Net operating cash flow (Rs. in lakhs)
1	300	900
2	600	1,800
3	650	2,300
4	800	3,200
5	800	3,200
6	800	3,200
7	800	3,200
8	800	3,200
9	800	3,200
10	800	3,200

Net operating cash flow has increased for third year because of better inventory management and handling method. Suggest the amortization method.

Ans. As per AS 26 `Intangibles Assets', the amortization method used should reflect the pattern in which economic benefits are consumed by the enterprise. If pattern cannot be determined reliably, then straight-line method should be used.

In the instant case, the pattern of economic benefit in the form of net operating cash flow vis-à-vis production is determined reliably. A Ltd. should amortize the license fee of Rs. 200 lakhs as under:

Year	Net operating Cash in flow (Rs.)	Ratio	Amortize amount (Rs. in lakhs)
1	900	0.03	6
2	1,800	0.06	12
3	2,300	0.08	16
4	3,200	0.12	24
5	3,200	0.12	24
6	3,200	0.12	24
7	3,200	0.12	24
8	3,200	0.12	24
9	3,200	0.12	24
10	3,200	0.11 (bal.)	22
	27,400	1.00	200

Q-3 K Ltd. launched a project for producing product X in October, 2016. The Company incurred ₹ 40 lakhs towards Research and Development expenses upto 31st March, 2018. Due to prevailing market conditions, the Management came to conclusion that the product cannot be manufactured and sold in the market for the next 10 years. The Management hence wants to defer the expenditure write off to future years. Advise the Company as per the applicable Accounting Standard.

Ans. As per provisions of AS 26 "Intangible Assets", expenditure on research should be recognized as an expense when it is incurred. An intangible asset arising from development (or from the development phase of an internal project) should be recognized if, and only if, an enterprise can demonstrate all of

the conditions specified in para 44 of the standard. An intangible asset (arising from development) should be derecognized when no future economic benefits are expected from its use according to para 87 of the standard. Thus, the manager cannot defer the expenditure write off to future years in the given case. Hence, the expenses amounting ₹ 40 lakhs incurred on the research and development project has to be written off in the current year ending 31st March, 2018.

Q-4 Desire Ltd. acquired a patent at a cost of ₹ 1,00,00,000 for a period of 5 years and the product life-cycle is also 5 years. The company capitalized the cost and started amortizing the asset on SLM. After two years it was found that the product life-cycle may continue for another 5 years from then. The net cash flows from the product during these 5 years were expected to be ₹ 45,00,000, ₹ 42,00,000, ₹ 40,00,000, ₹ 38,00,000 and ₹ 35,00,000. Patent is renewable and company changed amortization method from 3rd year (i.e. from SLM to ratio of expected new cash flows).

You are required to compute the amortization cost of the patent for each of the years (1st year to 7th year).

Ans. Desire Limited amortised ₹ 20,00,000 per annum for the first two years i.e. ₹ 40,00,000.

The remaining carrying cost can be amortized during next 5 years on the basis of net cash flows arising from the sale of the product. The amortisation may be found as follows:

Year	Net cash flows ₹	Amortization Ratio	Amortization Amount ₹
I	-	0.200	20,00,000
II	-	0.200	20,00,000
III	45,00,000	0.225	13,50,000
IV	42,00,000	0.21	12,60,000
V	40,00,000	0.20	12,00,000
VI	38,00,000	0.19	11,40,000
VII	35,00,000	0.175	10,50,000
Total	2,00,00,000	1.000	1,00,00,000

It may be seen from above that from third year onwards, the balance of carrying amount i.e., ₹ 60,00,000 has been amortized in the ratio of net cash flows arising from the product of Desire Ltd.

Q-5 A Company with a turnover of ₹ 375 crores and an annual advertising budget of ₹ 3 crores had taken up the marketing of a new product. It was estimated that the company would have a turnover of ₹ 37.5 croes from the new product. The company had debited to its Profit and Loss account the total expenditure of ₹ 3 crores incurred on extensive special initial advertisement campaign for the new product.

Is the procedure adopted by the Company correct?

Ans. According to AS 26 `Intangible Assets', "expenditure on an intangible item should be recognized as an expense when it is incurred unless it forms part of the cost of an intangible asset".

In the given case, advertisement expenditure of ₹ 3 crores had been taken up for the marketing of a new product which may provide future economic benefits to an enterprise by having a turnover of ₹ 37.5 crores. Here, no intangible asset or another asset is acquired or created that can be recognized.

Therefore, the accounting treatment by the company of debiting the entire advertising expenditure of ₹ 3 crores to the Profit and Loss account of the year is correct.

Q-6 A company acquired a patent at a cost of ₹ 160 lakhs for a period of 5 years and the product life cycle is also 5 years. The company capitalized the cost and started amortising the asset at ₹ 16 lakhs per year based on the economic benefits derived from the product manufactured under the patent. After 2

years it was found that the product life cycle may continue for another 5 years from then (the patent is renewable and the company can get it renewed after 5 years). The net cash flows from the product during these 5 years were expected to be ₹ 50 lakhs, ₹ 30 lakhs, ₹ 60 lakhs, ₹ 70 lakhs and ₹ 40 lakhs. Find out the amortization cost of the patent for each of the years.

Ans. Company amortized ₹ 16,00,000 per annum for the first two years. Hence, Amortization for the first two years (₹ 16,00,000 X 2) = ₹ 32,00,000.

Remaining carrying cost after two years = ₹ 1,60,00,000 – ₹ 32,00,000 = ₹ 1,28,00,000

Since after two years it was found that the product life cycle may continue for another 5 years, hence the remaining carrying cost ₹ 128 lakhs will be amortized during next 5 years in the ratio of net cash arising from the sale of the products of Fast Limited.

The amortization cost of the patents may be computed as follows:

Year	Net cash flows ₹	Amortization Ratio	Amortization Amount ₹
I	-	0.1	16,00,000
II	-	0.1	16,00,000
III	50,00,000	0.2	25,60,000
IV	30,00,000	0.12	15,36,000
V	60,00,000	0.24	30,72,000
VI	70,00,000	0.28	35,84,000
VII	40,00,000	0.16	20,48,000
Total	250,00,000	1.000	160,00,000

Q-7 As per provision of AS- 26 ,how would you deal to the following situations:

(1) ₹ 23,00,000 paid by a manufacturing company to the legal advisor defending the patent of a product is treated as a capital expenditure.

(2) During the year 2018-19 a company spent ₹ 7,00,000 for publicity and research expenses on one of its new consumer product which was marketed in the same accounting year but proved to be a failure.

(3) A company spent ₹ 25,00,000 in the past three years to devlop a product ,these expenses were charged to profit and loss account since they did not meet AS -26 criteria for capitalization .In the current year approval of the concerned authority has been received. The company wishes to capitalize ₹ 25,00,000 by disclosing it as a prior period item.

(4) A company with a turnover of ₹ 200 crores and an annual advertising budget of ₹ 1, 50,00,000 had taken up for the marketing of a new product by a company.It was estimated that the company would have a turnover of ₹ 20 crore from the new product. The company had debited to its Profit & Loss Account the total expenditure of ₹ 50,00,000 incurred on extensive special intial advertisement campaign for the new product.

Ans. As per AS 26 "Intangible Assets", subsequent expenditure on an intangible asset after its purchase or its completion should be recognized as an expense when it is incurred unless (a) it is probable that the expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance; and (b) expenditure can be measured and attributed to the asset reliably. If these conditions are met, the subsequent expenditure should be added to the cost of the intangible asset.

(i) In the given case, the legal expenses to defend the patent of a product amounting ₹ 23,00,000 should not be capitalized and be charged to Profit and Loss Statement.

(ii) The company is required to expense the entire amount of ₹ 7,00,000 in the Profit and Loss account for the year ended 31st March, 2019 because no benefit will arise in the future.

(iii) As per AS 26, expenditure on an intangible item that was initially recognized as an expense by a reporting enterprise in previous annual financial statements should not be recognized as part of the cost of an intangible asset at a later date. Thus the company cannot capitalize the amount of ₹ 25,00,000 and it should be recognized as expense

(iv) Expenditure of ₹ 50,00,000 on advertising and promotional activities should always be charged to Profit and Loss Statement. Hence, the company has done the correct treatment by debiting the sum of 50 lakhs to Profit and Loss Account.

Q-8 A company acquired patent right for ₹ 1200 lakhs. The product life cycle has been estimated to be 5 years and the amortization was decided in the ratio of estimated future cash flows which are as under:

Year	**1**	**2**	**3**	**4**	**5**
Estimated future cash flows					
(₹ in lakhs)	600	600	600	300	300

After 3rd year, it was ascertained that the patent would have an estimated balance future life of 3 years and the estimated cash flow after 5th year is expected to be ₹ 150 lakhs. You are required to determine the amortization pattern under Accounting Standard 26.

Ans. **Amortization of cost of patent as per AS 26**

Year	**Estimated future cash flow (₹ in lakhs)**	**Amortization Ratio**	**Amortized Amount (₹ in lakhs)**
1	600	.25	300
2	600	.25	300
3	600	.25	300
4	300	.40 (Revised)	120
5	300	.40 (Revised)	120
6	150	.20 (Revised)	60
			1,200

Q-9 X Ltd. carried on business of manufacturing of Bakery products. The company has two trademarks "Sun" and "Surya''. One month before, the company comes to know through one of the marketing managers that both trademarks have allegedly been infringed by other competitors engaged in the same field. After investigation, legal department of the company informed that it had weak case on trademark "Sun" and strong case in regard to trademark "Surya"'. X Ltd. incurred additional legal fees to stop infringement on both trademarks. Both trademarks have a remaining legal life of 10 years. How should X Ltd. account for these legal costs incurred relating to the two trademarks?

Ans. As per AS 26, subsequent expenditure on an intangible asset after its purchase or its completion should be recognized as an expense. However, if the subsequent expenditure enables the asset to generate future economic benefits in excess of its originally assessed standard of performance or can be measured and attributed to the asset reliably, then such subsequent expenditure should be added to the cost of the intangible asset.

The legal costs incurred for both the trademarks do not enable them to generate future economic benefits in excess of its originally assessed standard of performance. They only ensure to maintain them if the case is decided in favour of the company.

Therefore, such legal costs incurred for both trademarks must be recognized as an expense.

Q-10 Sudesh Ltd. acquired a patent at a cost of ₹ 2,40,00,000 for a period of 5 years and the product life-cycle was also 5 years. The company capitalized the cost and started amortizing the asset at ₹ 48,00,000 per annum. After two years it was found that the product life-cycle may continue for another 5 years from then. The net cash flows from the product during these 5 years were expected to be ₹ 36,00,000, ₹ 46,00,000, ₹ 44,00,000, ₹ 40,00,000 and ₹ 34,00,000. Find out the amortization cost of the patent for each of the years if the patent was renewable and Sudesh Ltd. got it renewed after expiry of five years.

Ans. The entity amortised ₹ 48,00,000 per annum for the first two years i.e. ₹ 96,00,000. The remaining carrying cost can be amortized during next 5 years on the basis of net cash flows arising from the sale of the product. The amortisation may be found as follows:

Year	Net cash flows ₹	Amortization Ratio	Amortization Amount ₹
I	-	0.20	48,00,000
II	-	0.20	48,00,000
III	36,00,000	0.180	25,92,000
IV	46,00,000	0.230	33,12,000
V	44,00,000	0.220	31,68,000
VI	40,00,000	0.200	28,80,000
VII	34,00,000	0.170	24,48,000
Total	2,00,00,000	1.000	2,40,00,000

It may be seen from above that from third year onwards, the balance of carrying amount i.e., ₹ 1,44,00,000 has been amortized in the ratio of net cash flows arising from the product of Change Ltd.

Q-11 During 2020-21, an enterprise incurred costs to develop and produce a routine low risk computer software product, as follows:

Particular	₹
Completion of detailed program and design (Phase 1)	50,000
Coding and Testing (Phase 2)	40,000
Other coding costs (Phase 3 & 4)	63,000
Testing costs (Phase 3 & 4)	18,000
Product masters for training materials (Phase 5)	19,500
Packing the products (1,500 units) (Phase 6)	16,500

After completion of phase 2, it was established that the product is technically feasible for the market. You are required to state how the above cost to be recognized in the books of accounts as per AS 26.

Ans. As per AS 26, costs incurred in creating a computer software product should be charged to research and development expense when incurred until technological feasibility/asset recognition criteria has been established for the product. Technological feasibility/asset recognition criteria have been established upon completion of detailed program design or working model. In this case, ₹ 90,000 would be recorded as an expense (₹ 50,000 for completion of detailed program design and ₹ 40,000 for coding and testing to establish technological feasibility/asset recognition criteria).

Cost incurred from the point of technological feasibility/asset recognition criteria until the time when products costs are incurred are capitalized as software cost (63,000+ 18,000+ 19,500) = ₹ 1,00,500. Packing cost ₹ 16,500 should be recognized as expenses and charged to P & L A/c.

Q-12 A Company acquired for its internal use a software on 01.03.2020 from U.K. for £ 1,50,000. The exchange rate on the date was as ₹ 100 per £. The seller allowed trade discount @ 2.5%. The other expenditures were:

(i) Import Duty 10%

(ii) Additional Import Duty 5%

(iii) Entry Tax 2% (Recoverable later from tax department).

(iv) Installation expenses ₹ 1,50,000.

(v) Professional fees for clearance from customs ₹ 50,000.

Compute the cost of software to be capitalized as per relevant AS.

Ans. Calculation of cost of software (intangible asset) acquired for internal use

Purchase cost of the software	£ 1,50,000
Less: Trade discount @ 2.5%	£ (3,750)
	£1,46,250
Cost in ₹ (UK £1,46,250 x ₹ 100)	146,25,000
Add: Import duty on cost @ 10% (₹)	14,62,500
	160,87,500
Add: Additional import duty @ 5% (₹)	8,04,375
	168,91,875
Add: Installation expenses (₹)	1,50,000
Add: Professional fee for clearance from customs (₹)	50,000
Cost of the software to be capitalized (₹)	170,91,875

Note: Since entry tax has been mentioned as a recoverable / refundable tax, it is not included as part of the cost of the asset.

Q-13 Swift Limited acquired patent rights to manufacture Solar Roof Top Panels at a cost of ₹ 600 lacs. The product life cycle has been estimated to be 5 years and the amortization was decided in the ratio of future cash flows which are estimated as under:

Year	**1**	**2**	**3**	**4**	**5**
Cash Flows (₹ in lacs)	300	300	300	150	150

After 3rd year, it was estimated that the patents would have an estimated balance future life of 3 years and Swift Ltd. expected the estimated cash flow after 5th year to be ₹ 75 Lacs. Determine the amortization cost of the patent for each of the above years as per Accounting Standard 26. **[Sugg-Nov'20](5 Marks)**

Ans. Amortization of cost of patent as per AS 26

Year	**Estimated future cashflow (₹ in lakhs)**	**Amortization Ratio (₹ in lakhs)**	**Amortized Amount**
1	300	.25	150
2	300	.25	150
3	300	.25	150
4	150	.10	60
5	150	.10	60
6	75	.05	30
		1.00	600

In the first three years, the patent cost will be amortized in the ratio of estimated future cash flows i.e. (300: 300: 300: 150: 150).The unamortized amount of the patent after third year will be ₹ 150 lakh (600-450) which will be amortized in the ratio of revised estimated future cash flows (150:150:75 or 2:2:1) in the fourth, fifth and sixth year.

Q-14 M/s. Pasa Ltd. is developing a new production process. During the financial year ended 31st March, 2019, the total expenditure incurred on the process was ₹ 80 lakhs. The production process met the criteria for recognition as an intangible asset on 1st November, 2018. Expenditure incurred till this date was ₹ 42 lakhs.

Further expenditure incurred on the process for the financial year ending 31st March, 2020 was ₹ 90 lakhs. As on 31.03.2020, the recoverable amount of know how embodied in the process is estimated to be ₹ 82 lakhs. This includes estimates of future cash outflows and inflows.

You are required to work out :

(1) What is the expenditure to be charged to Profit and Loss Account for the year ended 31st March, 2019 ?

(2) What is the carrying amount of the intangible asset as on 31st March, 2019?

(3) What amount of expenditure to be charged to Profit and Loss Account for the year ended 31st March, 2020 ?

What is the carrying amount of the intangible asset as on 31st March, 2020?

Ans. As per AS 26 'Intangible Assets'

(i) **Expenditure to be charged to Profit and Loss account for the year ending31.03.2019** ₹ 42 lakhs is recognized as an expense because the recognition criteria were not met until 1st November, 2018. This expenditure will not form part of the cost of the production process recognized as an intangible asset in the balance sheet.

(ii) Carrying value of intangible asset as on 31.03.2019 At the end of financial year, on 31st March 2019, the production process will be recognized (i.e. carrying amount) as an intangible asset at a cost of ₹ 38 (80-42) lakhs (expenditure incurred since the date the recognition criteria were met, i.e., from 1st November 2018)

(iii) Expenditure to be charged to Profit and Loss account for the year ended 31.03.2020

	(₹ in lacs)
Carrying Amount as on 31.03.2019	38
Expenditure during 2019 – 2020	90
Book Value	128
Recoverable Amount	(82)
Impairment loss to be charged to Profit and loss account	46

₹ 46 lakhs to be charged to Profit and loss account for the year ending 31.03.2020.

(iv) Carrying value of intangible asset as on 31.03.2020

	(₹ in lacs)
Book Value	128
Less: Impairment loss	(46)
Carrying amount as on 31.03.2020	82

Q-15 Naresh Ltd. had the following transactions during the financial year 2019-2020:

(i) Naresh Ltd. acquired running business of Sunil Ltd. for ₹ 10,80,000 on 15th May, 2019. The fair value of Sunil Ltd.'s net assets was ₹ 5,16,000. Naresh Ltd. is of the view that due to popularity of Sunil Ltd.'s product in the market, its goodwill exists.

(ii) Naresh Ltd. had taken a franchise on July 2019 to operate a restaurant from Sankalp Ltd. for ₹ 1,80,000 and at an annual fee of 10% of net revenues (after deducting expenditure). The franchise expires after 6 years. Net revenues were ₹ 60,000 during the financial year 2019-2020.

(iii) On 20th August, 2019, Naresh Ltd, incurred costs of ₹ 2,40,000 to register the patent for its product. Naresh Ltd. expects the patent's economic life to be 8 years.

Naresh Ltd. follows an accounting policy to amortize all intangibles on straight line basis over the maximum period permitted by accounting standards taking a full year amortization in the year of acquisition. Goodwill on acquisition of business to be amortized over 5 years (SLM) as per AS 14.

Prepare a schedule showing the intangible assets section in Naresh Ltd. Balance Sheet at 31st March,2020.

Ans.

Naresh Ltd.

Balance Sheet (Extract relating to intangible asset) as on 31st March 2020

	Note No.	₹
Assets		
(1) Non-current assets		
Intangible assets	1	8,11,200

Notes to Accounts (Extract)

	₹	₹
1. Intangible assets		
Goodwill (Refer to note 1)	4,51,200	
Franchise (Refer to Note 2)	1,50,000	
Patents (Refer to Note 3)	2,10,000	8,11,200

Working Notes:

		₹
(1)	Goodwill on acquisition of business	
	Cash paid for acquiring the business (purchase consideration)	10,80,000
	Less: Fair value of net assets acquired	(5,16,000)
	Goodwill	5,64,000
	Less: Amortisation as per AS 14 ie. over 5 years (as per SLM)	(1,12,800)
	Balance to be shown in the balance sheet	4,51,200
(2)	Franchise	1,80,000
	Less: Amortisation (over 6 years)	(30,000)
	Balance to be shown in the balance sheet	1,50,000
(3)	Patent	2,40,000
	Less: Amortisation (over 8 years as per SLM)	(30,000)
	Balance to be shown in the balance sheet	2,10,000

Q-16 A company is showing an intangible asset at ₹ 88 lakhs as on 01.04.2021. This asset was acquired for ₹ 120 lakhs on 01.04.2017 and the same was available for use from that date. The company has been following the policy of amortization of the intangible assets over a period of 15 years on straight line basis. Comment on the accounting treatment of the above with reference to the relevant Accounting Standard.

Ans. As per AS 26 ₹Intangible Assets', the depreciable amount of an intangible asset should be allocated on systematic basis over the best estimate of its useful life. There is a rebuttable presumption that the useful life of an intangible asset will not exceed ten years from the date when the asset is available for use. Company has been following the policy of amortization of the intangible asset over a period of 15 years on straight line basis. The period of 15 years is more than the maximum period of 10 years specified as per AS 26. Accordingly, the company would be required to restate the carrying amount of intangible asset as on 01.04.2021 at ₹ 72 lakhs i.e. ₹ 120 lakhs less ₹ 48 lakhs

$$\left(\frac{₹\ 120\,\text{lakhs}}{10\ \text{years}} \times 4\ \text{years} = 48\,\text{Lakhs}\right)$$

The difference of ₹ 16 Lakhs (₹ 88 lakhs – ₹ 72 lakhs) will be adjusted against the opening balance of revenue reserve. The carrying amount of ₹ 72 lakhs will be amortized over remaining 6 years by amortizing ₹ 12 lakhs per year.

Q-17 PQR Ltd. has acquired a Brand from another company for ₹ 100 lakhs. PQR Ltd.

contends that since the said brand is a very popular and famous brand, no amortization needs to be provided. Comment on this in line with the Accounting Standards.

Ans. AS 26 'Intangible Assets" provides that an intangible asset should be measured initially at cost. After initial recognition, an intangible asset should be carried at cost less any accumulated amortization and any accumulated impairment losses. The amount of an intangible asset should be allocated on a systematic basis over the best estimate of its useful life for computing amortization. There is a rebuttable presumption that the useful life of an intangible asset will not exceed 10 years from the date when the asset is available for use. It must be ensured that the value of brand is amortized in accordance with AS 26, as brand is considered to be intangible asset. The contention of PQR Ltd. that Brand is very popular and famous, hence no amortization needs to be provided is not correct as there is no persuasive evidence that the useful life of the intangible asset will exceed 10 years.

Q-18 X Ltd. is engaged in the business of newspaper and radio broadcasting. It operates through different brand names. During the year ended 31st March, 2021, it incurred substantial amount on business communication and branding expenses by participation in various corporate social responsibility initiatives. The company expects to benefit by this expenditure by attracting new customers over a period of time and accordingly it has capitalized the same under brand development expenses and intends to amortize the same over the period in which it expects the benefits to flow. As the accountant of the company do you concur with these views? You are required to explain in line with provisions of Accounting Standards.

Ans. As per AS 26 on Intangible Assets, expenditure on an intangible item should be recognized as on expense when it is incurred unless it forms part of the cost of an intangible asset that meets the recognition criteria. An intangible asset should be recognized if, and only if: (i) it is probable that the future economic benefits that are attributable to the asset will flow to the enterprise; and (ii) the cost of the asset can be measured reliably. In the given case, no intangible assets or other asset is acquired or created that can be recognized, the accounting treatment by the company to amortize the entire expenditure over the period in which it expects the benefits to flow is not correct and the same should be debited to the profit and loss statement during the year ended 31st March, 2021.

Q-19 Surgical Ltd, is developing a new production process of surgical equipment. During the financial year ended 31st March 2020 the total expenditure incurred on the process was ₹ 67 lakhs. The production process met the criteria for recognition as an intangible asset on 1st January 2020. Expenditure incurred till this date was ₹ 35 lakhs.

Further expenditure incurred on the process for the financial year ending 31st March 2021 ₹ 105 lakhs. As on 31st March 2021, the recoverable amount of technique embodied in the process is estimated to be ₹ 89 lakhs. This includes estimates of future cash outflows and inflows.

Under the provisions of AS 26, you are required to ascertain:

(i) The expenditure to be charged to Profit and Loss Account for the year ended 31st March 2020;

(ii) Carrying amount of the intangible asset as on 31st March 2020;

(iii) Expenditure to be charged to Profit and Loss Account for the year ended 31st March 2021;

(iv) Carrying amount of the intangible asset as on 31st March 2021.

Ans. **As per AS 26 'Intangible Assets'**

(i) Expenditure to be charged to Profit and Loss account for the year ended 31.03.2020

₹ 35 lakhs is recognized as an expense because the recognition criteria were not met until 1stJanuary 2020. This expenditure will not form part of the cost of the production process recognized as an intangible asset in the balance sheet.

(ii) Carrying value of intangible asset as on 31.03.2020

At the end of financial year, on 31st March 2020, the production process will be recognized (i.e. carrying amount) as an intangible asset at a cost of ₹ 32 (67-35) lacs (expenditure incurred since the date the recognition criteria were met, i.e., from 1stJanuary 2020).

(iii) Expenditure to be charged to Profit and Loss account for the year ended 31.03.2021

	(₹ in lacs)
Carrying Amount as on 31.03.2020	32
Expenditure during 2020 – 2021	105
Book Value	137
Recoverable Amount	(89)
Impairment loss	48

₹ 48 lakhs to be charged to Profit and loss account for the year ending 31.03.2021.

(iv) **Carrying value of intangible asset as on 31.03.2021**

	(₹ in lacs)
Book Value	137
Less: Impairment loss	(48)
Carrying amount as on 31.03.2021	89

Q-20 PIL Ltd. is showing an intangible asset at ₹ 72 lakhs as on 31-3-2022. This asset was acquired for ₹ 120 lakhs as on 01-04-2016 and the same was used from that date. The company has been following the policy of amortization of the intangible assets over a period of 15 years, on straight line basis.

You are required to comment on the accounting treatment of asset with reference to AS 26 "Intangible Assets" and also give the necessary rectification journal entry in the books.

Ans. As per AS 26 'Intangible Assets', the depreciable amount of an intangible asset should be allocated on systematic basis over the best estimate of its useful life. There is a rebuttable presumption that the

useful life of an intangible asset will not exceed ten years from the date when the asset is available for use. The Company has been following the policy of amortization of the intangible asset over a period of 15 years on straight line basis. The period of 15 years is more than the maximum period of 10 years specified as per AS 26.

Accordingly, the company would be required to restate the carrying amount of intangible asset as on 31.3.2022 at ₹ 48 lakhs i.e. ₹ 120 lakhs less ₹ 72 lakhs (₹ 120 Lakhs / 10 years x 6 years = 72 Lakhs). The difference of ₹ 24 Lakhs (₹ 72 lakhs –₹ 48 lakhs) will be adjusted against the opening balance of revenue reserve. The carrying amount of ' 48 lakhs will be amortized over remaining 4 years by amortizing ₹ 12 lakhs per year**.**

The necessary journal entry (for rectification) will be

Revenue Reserves Dr. ₹ 24 Lakhs

To Intangible Assets ₹ 24 Lakhs

(Adjustment to reserves due to restatement of the carrying amount of intangible asset)

AS-29 PROVISIONS, CONTINGENT LIABILITIES

Q-1 With reference to AS 29, how would you deal with the following in the annual accounts of the company at the Balance Sheet dates:

(i) An organization operates an offshore oilfield where its licensing agreement requires it to remove the oil rig at the end of production and restore the seabed. Ninety percent of the eventual costs relate to the rem oval of the oil rig and restoration of damage caused by building it, and ten percent arise through the extraction of oil. At the balance sheet date, the rig has been constructed but no oil has been extracted.

(ii) During 2018-19 Ace Ltd. gives a guarantee of certain borrowings of Brew Ltd., whose financial condition at that time is sound. During 2019 -20, the financial condition of Brew Ltd. deteriorates and on 31st Dec. 2019, it goes into liquidation. (Balance Sheet date 31-3-19).

Ans. (i) The construction of the oil rig creates an obligation under the terms of the license to remove the rig and restore the seabed and is thus an obligating event. At the balance sheet date, however, there is no obligation to rectify the damage that will be cau sed by extraction of the oil. An outflow of resources embodying economic benefits in settlement is probable. Thus, a provision is recognized for the best estimate of ninety per cent of the eventual costs that relate to the removal of the oil rig and restor ation of damage caused by building it. These costs are included as part of the cost of the oil rig. However, there is no obligation to rectify the damage that will be caused by extraction of oil, as no oil has been extracted at the balance sheet date. So, no provision is required for the cost of extraction of oil at balance sheet date.

Ten per cent of costs that arise through the extraction of oil are recognized as a liability when the oil is extracted.

(ii) As per AS 29, for a liability to qualify for recognition there must be not only a present obligation but also the probability of an outflow of resources embodying economic benefits to settle that obligation.

The obligating event is the giving of the guarantee by Ace Ltd. for certain borrowings of Brew Ltd., which gives rise to an obligation. No outflow of benefits is probable at 31 March 2019.Thus no provision is recognized. The guarantee is disclosed as a contingent liability unless the probability of any outflow is regarded as remote.

During 2019-20, the financial condition of Brew Ltd. deteriorates and finally goes into liquidation. The obligating event is the giving of the guarantee, which gives rise to a legal obligation. At 31 March 2020, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation. Thus, provision is recognized for the best estimate of the obligation.

Q-2 An airline is required by law to overhaul its aircraft once in every five years. The pacific Airlines which operate aircrafts does not provide any provision as required by law in its final accounts. You are required to comment on the validity of the treatment done by the company in line with the provisions of AS 29.

Ans. A provision should be recognized only when an enterprise has a present obligation arising from a past event or obligation. In the given case, there is no present obligation but a future one, therefore no provision is recognized as per AS 29.

The cost of overhauling aircraft is not recognized as a provision because it is a future obligation and the incurring of the expenditure depends on the company's decision to continue operating the aircrafts. Even a legal requirement to overhaul does not require the company to make a provision for the cost of overhaul because there is no present obligation to overhaul the aircrafts. Further, the enterprise can avoid the future expenditure by its future action, for example by selling the aircraft. However, an obligation might arise to pay fines or penalties under the legislation after completion of five years. Assessment of probability of incurring fines and penalties depends upon the provisions of the legislation and the stringency of the enforcement regime. A provision should be recognized for the best estimate of any fines and penalties if airline continues to operate aircrafts for more than five years.

Q-3 Sun Ltd. has entered into a sale contract of ₹ 5 crores with X Ltd. during 2015-2016 financial year. The profit on this transaction is ₹ 1 crore. The delivery of goods to take place during the first month of 2016-2017 financial year. In case of failure of Sun Ltd. to deliver within the schedule, a compensation of ₹ 1.5 crores is to be paid to X Ltd. Sun Ltd. planned to manufacture the goods during the last month of 2015-2016 financial year. As on balance sheet date (31.3.2016), the goods were not manufactured and it was unlikely that Sun Ltd. will be in a position to meet the contractual obligation.

(i) Should Sun Ltd. provide for contingency as per AS 29? Explain.

(ii) Should provision be measured as the excess of compensation to be paid over the profit?

Ans.(i) AS 29 "Provisions, Contingent Liabilities and Contingent Assets" provides that when an enterprise has a present obligation, as a result of past events, that probably requires an outflow of resources and a reliable estimate can be made of the amount of obligation, a provision should be recognised. Sun Ltd. has the obligation to deliver the goods within the scheduled time as per the contract. It is probable that Sun Ltd. will fail to deliver the goods within the schedule and it is also possible to estimate the amount of compensation. Therefore, Sun Ltd. should provide for the contingency amounting ₹ 1.5 crores as per AS 29.

(ii) Provision should not be measured as the excess of compensation to be paid over the profit. The goods were not manufactured before 31st March, 2016 and no profit had accrued for the financial year 2015-2016. Therefore, provision should be made for the full amount of compensation amounting ₹ 1.50 crores.

Q-4 EXOX Ltd. is in the process of finalising its accounts for the year ended 31st March, 2017. The company seeks your advice on the following:

(i) The Company's sales tax assessment for assessment year 2014-15 has been completed on 14th February, 2017 with a demand of ₹ 2.76 crore. The company paid the entire due under protest without prejudice to its right of appeal. The Company files its appeal before the appellate authority wherein the grounds of appeal cover tax on additions made in the assessment order for a sum of 2.10 crore.

(ii) The Company has entered into a wage agreement in May, 2017 whereby the labour union has accepted a revision in wage from June, 2016. The agreement provided that the hike till May, 2017 will not be paid to the employees but will be settled to them at the time of retirement. The company agrees to deposit the arrears in Government Bonds by September, 2017.

You required to examine and give suggestions in line with the relevant Accounting Standards.

Ans.(i) Since the company is not appealing against the addition of Rs. 0.66 crore the same should be provided for in its accounts for the year ended on 31st March, 2017. The amount paid under protest can be kept under the heading `Loans & Advances' and disclosed along with the contingent liability of ₹ 2.10 crore.

(ii) The arrears for the period from June, 2016 to March, 2017 are required to be provided for in the accounts of the company for the year ended on 31st March, 2017.

Q-5 S Ltd. (a Public Sector Company) provides consultancy and engineering services to its clients. In the year 2016-17, the Government has set up a commission to decide about the pay revision.

The pay will be revised with respect from 1 -1-2012 based on the recommendations of the commission. The company makes the provision of Rs. 680 lakhs for pay revision in the financial year 2016-17 on the estimated basis as the report of the commission is yet to come. As per the contracts with the client on cost plus job, the billing is done on the actual payment made to the employees and allocated to jobs based on hours booked by these employee s on each job.

The company discloses through notes to accounts:

"Salaries and benefits include the provision of Rs. 680 lakhs in respect of pay revision. The amount chargeable from reimbursable jobs will be billed as per the contract when the actual payment is made".

The accountant feels that the company should also book/recognise the income by Rs. 680 lakhs in Profit and Loss Account as per the terms of the contract. Otherwise, it will be the violation of matching concept & understatement of profit. Comm ent on the opinion of the Accountant with reference to relevant accounting standards.

Ans. As per AS 29, `Provisions, Contingent Liabilities and Contingent Assets', where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognised when, and only when, it is v irtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognised for the reimbursement should not exceed the amount of the provision.

Accordingly, potential loss to an enterprise may be reduced or avoided because a contingent liability is matched by a related counter -claim or claim against a third party. In such cases, the amount of the provision is determined after taking into account the probable recovery under the claim if no significant uncertainty as to its measurability or collectability exists. In this case, the provision of salary to employees of Rs. 680 lakhs will be ultimately collected from the client, as per the terms of the contract. The refore, the liability of Rs. 680 lakhs is matched by the counter claim from the client. Hence, the provision for salary of employees should be matched with the reimbursable asset to be claimed from the client. It appears that the whole amount of Rs. 680 la khs is recoverable from client and there is no significant uncertainty about the collection. Hence, the net charge to profit and loss account should be nil.

The opinion of the accountant regarding recognition of income of Rs. 680 lakhs is not as per AS-29 and also the concept of prudence will not be followed if Rs. 680 lakhs is simultaneously recognized as income. Rs. 680 lakhs is not the revenue at present but only reimbursement of claim for which an asset is created. However, the accountant is correct to the extent as that non -recognition of Rs. 680 lakhs as income will result in the understatement of profit. To avoid this, in the statement of profit and loss, expense relating to provision may be presented net of the amount recognized for reimbursement.

Q-6 XYZ Ltd. has not made provision for warrantee in respect of certain goods due to the fact that the company can claim the warranty cost from the original supplier. Hence the accountant of the company says that the company is not having any liability for warrantees on a particular date as the amount gets reimbursed. You are required to comment on the accounting treatment done by the XYZ Ltd. in line with the provisions of AS 29.

Ans. As per para 46 of AS 29 "Provisions, Contingent Liabilities and Contingent Assets", where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognised when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognised for the reimbursement should not exceed the amount of the provision.

It is apparent from the question that the company had not made provision for warranty in respect of certain goods considering that the company can claim the warranty cost from the original supplier. However, the provision for warranty should have been made as per AS 29 and the amount claimable as reimbursement should be treated as a separate asset in the financial statements of the company rather than omitting the disclosure of such liability. Accordingly, it is viewed that the accounting treatment adopted by the company with respect to warranty is not correct.

Q-7 M/s. XYZ Ltd. is in a dispute with a competitor company. The dispute is regarding alleged infringement of Copyrights. The competitor has filed a suit in the court of law seeking damages of ₹ 200 lacs.

The Directors are of the view that the claim can be successfully resisted by the Company.

How would the matter be dealt in the annual accounts of the Company in the light of AS 29? Explain in brief giving reasons for your answer.

Ans : As per AS 29, `Provisions, Contingent Liabilities and Contingent Assets', a provision should be recognized when

(a) an enterprise has a present obligation as a result of a past event;

(b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

(c) a reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision should be recognized.

In the given situation, since, the directors of the company are of the opinion that the claim can be successfully resisted by the company, therefore there will be no outflow of the resources. Hence, no provision is required. The company will disclose the same as contingent liability by way of the following note:

"Litigation is in process against the company relating to a dispute with a competitor who alleges that the company has infringed copyrights and is seeking damages of ₹ 200 lakhs. However, the directors are of the opinion that the claim can be successfully resisted by the company."

Q-8 The company has not made provision for warrantee in respect of certain goods considering that the company can claim the warranty cost from the original supplier.

You are required to **examine** in line with the provisions of AS 29.

Ans. As per provisions of AS 29 "Provisions, Contingent Liabilities and Contingent Assets", where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognized when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognized for the reimbursement should not exceed the amount of the provision.

It is apparent from the question that the company had not made provision for warranty in respect of certain goods considering that the company can claim the warranty cost from the original supplier. However, the provision for warranty should have been made as per AS 29 and the amount claimable as reimbursement should be treated as a separate asset in the financial statements of the company rather than omitting the disclosure of such liability. Accordingly, it can be said that the accounting treatment adopted by the company with respect to warranty is not correct.

Q-9 A Ltd.provides after sales warranty for two years to its customers. Based on past experience, the company has the following policy for making provision for warranties on the invoice amount, on the remaining balance warranty period.

Less than 1 year: 2% provision

More than 1 year: 3% provision

The company has raised invoices as under:

Invoice Date	**Amount (₹)**
11th Feb,2017	60,000
25th Dec, 2017	40,000
04thOct,2018	1,35,000

Calculate the provision to be made for warranty under AS -29 as at 31st March ,2018 and 31st March 2019. Also compute amount to be debited to P & L account for the year ended 31st March 2019.

Ans. Provision to be made for warranty under AS 29 `Provisions, Contingent Liabilities and Contingent Assets'

As at 31st March, 2018 = ₹ 60,000 x .02 + ₹ 40,000 x .03

= ₹ 1,200 + ₹ 1,200 = ₹ 2,400

As at 31st March, 2019 = ₹ 40,000 x .02 + ₹ 1,35,000 x .03

= ₹ 800 + ` 4,050 = ₹ 4,850

Amount debited to Profit and Loss Account for year ended 31st March, 2019

	₹
Balance of provision required as on 31.03.2019	4,850
Less: Opening Balance as on 1.4.2018	(2,400)
Amount debited to profit and loss account	2,450

Note: No provision will be made on 31st March, 2019 in respect of sales amounting ₹ 60,000 made on 11th February, 2017 as the warranty period of 2 years has already expired.

Q-10 **(a)** How will you distinguish contingent assets with Contingent Liabilities. Explain in brief.

(b) Alpha Ltd. has entered into a sale contract of ₹ 7 crores with Gamma Ltd. during 2018-19 financial year. The profit on this transaction is ₹ 1 crore. The delivery of goods to take place during the first month of 2019-20 financial year. In case of failure of Alpha Ltd. to deliver within the schedule, a compensation of ₹2 crores is to be paid to Gamma Ltd. Alpha Ltd. planned to manufacture the goods during the last month of 2018-19 financial year. As on balance sheet date (31.3.2019), the goods were not manufactured and it was unlikely that Alpha Ltd. will be in a position to meet the contractual obligation. You are required to advise Alpha Ltd. on requirement of provision for contingency in the financial statements for the year ended 31st March, 2019, in line with provisions of AS 29?

Ans. **(a)** **A Contingent liability** is a possible obligation that arises from past events and the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise; or A present obligation that arises from past events but is not recognized because:

(i) It is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or

(ii) A reliable estimate of the amount of the obligation cannot be made.

An enterprise should not recognize a contingent liability but should be disclosed. A contingent liability is disclosed, unless the possibility of an outflow of resources embodying economic benefits is remote. **Contingent assets** usually arise from unplanned or other unexpected events that give rise to the possibility of an inflow of economic benefits to the enterprise. An example is a claim that an enterprise is pursuing through legal processes, where the outcome is uncertain. An enterprise should not recognize a contingent asset, since this may result in the recognition of income that may never be realized. However, when the realization of income is virtually certain, then the related asset is not a contingent asset and its recognition is appropriate. A contingent asset is not disclosed in the financial statements. It is usually disclosed in the report of the approving authority (Board of Directors in the case of a company, and, the corresponding approving authority in the case of any other enterprise), where an inflow of economic benefits is probable. Contingent assets are assessed continually and if it has become virtually certain that an inflow of economic benefits will arise, the asset and the related income are recognised in the financial statements of the period in which the change occurs.

(b) AS 29 "Provisions, Contingent Liabilities and Contingent Assets" provides that when an enterprise has a present obligation, as a result of past events, that probably requires an outflow of resources and a reliable estimate can be made of the amount of obligation, a provision should be recognized. Alpha Ltd. has the obligation to deliver the goods within the scheduled time as per the contract. It is probable that Alpha Ltd. will fail to deliver the goods within the schedule and it is also possible to estimate the amount of compensation. Therefore, Alpha Ltd. should provide for the contingency amounting ₹ 2 crores as per AS 29.

Q-11 ABC Ltd. has entered into a binding agreement with XYZ Ltd. to buy a custom-made machine amounting to Rs. 4,00,000. As on 31st March, 2020 before delivery of the machine, ABC Ltd. had to change its method of production. The new method will not require the machine ordered and so it shall be scrapped after delivery. The expected scrap value is `NIL'. Show the treatment of machine in the books of ABC Ltd.

Ans. A liability is recognized when outflow of economic resources in settlement of a present obligation can be anticipated and the value of outflow can be reliably measured. In the given case, ABC Ltd. should recognize a liability of ₹ 4,00,000 payable to XYZ Ltd. When flow of economic benefit to the enterprise beyond the current accounting period is considered improbable, the expenditure incurred is recognized as an expense rather than as an asset. In the present case, flow of future economic benefit from the machine to the enterprise is improbable. The entire amount of purchase price of the machine should be recognized as an expense. Hence ABC Ltd. should charge the amount of ₹ 4,00,000 (being loss due to change in production method) to Profit and loss statement and record the corresponding liability (amount payable to XYZ Ltd.) for the same amount in the books for the year ended 31st March, 2020.

Q-12 An airline is required by law to overhaul its aircraft once in every five years. The pacific Airlines which operate aircrafts does not provide any provision as required by law in its final accounts. You are required to comment on the validity of the treatment done by the company in line with the provisions of AS 29.

Ans. A provision should be recognized only when an enterprise has a present obligation arising from a past event or obligation. In the given case, there is no present obligation but a future one, therefore no provision is recognized as per AS 29.

The cost of overhauling aircraft is not recognized as a provision because it is a future obligation and the incurring of the expenditure depends on the company's decision to continue operating the aircrafts. Even a legal requirement to overhaul does not require the company to make a provision for the cost of overhaul because there is no present obligation to overhaul the aircrafts. Further, the enterprise can avoid the future expenditure by its future action, for example by selling the aircraft. However, an

obligation might arise to pay fines or penalties under the legislation after completion of five years. Assessment of probability of incurring fines and penalties depends upon the provisions of the legislation and the stringency of the enforcement regime. A provision should be recognized for the best estimate of any fines and penalties if airline continues to operate aircrafts for more than five years.

Q-13 Saharsh Ltd. is engaged in manufacturing of electric home appliances. The company is in the process of finalizing its accounts for the year ended 31.3.2020 and needs your expert advice on the following issues in line with the provisions of AS 29:

(i) A case has been filed against the company in the consumer court and a notice for levy of a penalty of ₹ 20 lakhs has been received. The company has appointed a lawyer to defend the case for a fee of ₹ 2 lakhs. 50% of the fees has been paid and balance 50% will be paid after finalisation of the case. There are 75% chances that the penalty may not be levied.

(ii) The company had committed to supply a consignment worth ₹ 1 crore to one of its dealers by the year-end. As per the contract, if delivery is not made on time, a compensation of 15% is to be paid on the value of delayed/lost consignment. While the consignment was in transit, one of the trucks carrying goods worth ₹ 30 lakhs met with an accident. It was however covered by Insurance. According to the surveyor's report, the policy amount is collectable, subject to 10% deduction. Before closing the books of accounts, the company has received the information that the policy amount has been processed and the dealer has also claimed the compensation for the consignment of goods worth ₹ 30 lakhs which was in transit.

Ans. (i) As per AS 29, an obligation is a present obligation if, based on the evidence available, its existence at the balance sheet date is considered probable, i.e., more likely than not.

Liability is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.

In the given case, there are 75% chances that the penalty may not be levied. Accordingly, Saharsh Ltd. should not make the provision for penalty.

However, a provision should be made for remaining 50% fees of the lawyer in the financial statements of financial year 2019-2020.

(ii)

Loss due to accident	₹ 30,00,000
Insurance claim receivable by company = ₹ 30,00,000 x 90% =	₹ 27,00,000
Loss to be recognised in the books for 2019-2020	₹ 3,00,000
Insurance claim receivable to be recorded in the books	₹ 27,00,000

Compensation claim by dealer against company to be provided for in the books

= ₹ 30,00,000 x 15% = ₹ 4,50,000

Q-14 A Limited sells goods with unlimited right of return from its customers. The following pattern has been observed in the Return of Sales:

Time frame of Return from date of purchase	% of Cumulative Sales
Between 0-1 month	6%
Between 1 -2 months	7%
Between 2-3 months	8%

The Company has made Sales of ₹ 36 Lakhs in the month of January, ₹ 48 Lakhs in the month of February and of ₹ 60 Lakhs in the month of March. The Total Sales for the Financial Year have been ₹ 400 Lakhs and the Cost of Sales was ₹ 320 Lakhs. You are required to determine the amount of Provision to be made and Revenue to be recognized for the year ended 31st March.

Ans. The goods are sold with a right to return. The existence of such right gives rise to a present obligation on the company as per AS 29, 'Provisions, Contingent Liabilities and Contingent Assets'. According to

the standard, a provision should be created on the Balance sheet date, for sales returns after the Balance Sheet date, at the best estimate of the loss expected, along with any estimated incremental cost that would be necessary to resell the goods expected to be returned.

Sales during	Sales value (₹ in lacs)	Sales value (cumulative) ₹ (in lacs)	Likely returns (%)	Likely returns ₹ (in lacs)	Provision @ 20% (₹ in lacs) (Refer W.N.)
March	60	60	6%	3.60	0.720
February	48	108	7%	7.56	1.512
January	36	144	8%	11.52	2.304
Total				22.68	4.536

Revenue to be recognized

Revenue in respect of sale of goods is recognized fully at the time of sale itself assuming that the company has complied with the conditions stated in AS 9 relating to recognition of revenue in the case of sale of goods. As per AS 9, in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:

(i) Seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) No significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods. AS 9 also provides that in case of retail sales offering a guarantee of ₹money back, if not completely satisfied, it may be appropriate to recognize the sale but to make a suitable provision for returns based on previous experiences.

Therefore, sale of ₹ 36 lakhs, ₹ 48 lakhs and ₹ 60 lakhs made in the months of January, February and March will be recognized at full value. Thus, total revenue to be recognized for ₹ 400 lacs for the year.

Working Note:

Calculation of Profit % on sales

	(₹ in lacs)
Sales for the year	400
Less: Cost of sales	(320)
Profit	80

Profit mark up on sales (80/400) x 100 = 20%

Q-15 With reference to AS 29, how would you deal with the following in the Annual Accounts of the company at the Balance Sheet date:

(i) The company operates an offshore oilfield where its licensing agreement requires it to remove the oil rig at the end of production and restore the seabed. Eighty five percent of the eventual costs relate to the removal of the oil rig and restoration of damage caused by building it, and fifteen percent arise through the extraction of oil.

At the balance sheet date, rig has been constructed but no oil has been extracted.

(ii) The Government introduces a number of changes to the taxation laws. As a result of these changes, the company will need to train a large proportion of its accounting and legal workforce in order to ensure continued compliances with tax law regulations. At the balance sheet date, no retraining of staff has taken place.

Ans. (i) The construction of the oil rig creates an obligation under the terms of the license to remove the rig and restore the seabed and is thus an obligating event. At the balance sheet date, however, there is no obligation to rectify the damage that will be caused by extraction of the oil. An outflow of resources embodying economic benefits in settlement is probable. Thus, a provision is recognized for the best estimate of 85% of the eventual costs that relate to the removal of the oil rig and restoration of damage caused by building it. These costs are included as part of the cost of the oil rig.

However, there is no obligation to rectify the damage that will be caused by extraction of oil, as no oil has been extracted at the balance sheet date. So, no provision is required for the cost of extraction of oil at balance sheet date. 15% of costs that arise through the extraction of oil are recognized as a liability when the oil is extracted.

(ii) As per AS 29, a provision for restructuring costs is recognized only when the recognition criteria for provisions are met. A restructuring provision does not include costs as of retraining or relocating continuing staff.

The expenditures of training the staff related to the future conduct of the business and are not liabilities for restructuring at the balance sheet date. Such expenditures are recognized on the same basis as if they arose independently of a restructuring.

At the balance sheet date, no such expenditure has been incurred hence no provision is required.

Q-16 The company has not made provision for warranty in respect of certain goods considering that the company can claim the warranty cost from the original supplier.

You are required to **examine** in line with the provisions of AS 29.

Ans. As per provisions of AS 29 "Provisions, Contingent Liabilities and Contingent Assets", where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognized when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognized for the reimbursement should not exceed the amount of the provision.

It is apparent from the question that the company had not made provision for warranty in respect of certain goods considering that the company can claim the warranty cost from the original supplier. However, the provision for warranty should have been made as per AS 29 and the amount claimable as reimbursement should be treated as a separate asset in the financial statements of the company rather than omitting the disclosure of such liability. Accordingly, it can be said that the accounting treatment adopted by the company with respect to warranty is not correct.

Q-17 Explain whether provision is required in the following situations in line with AS 29:

(i) There is a present obligation that probably requires an outflow of resources and a reliable estimate can be made of the amount of obligation;

(ii) There is a possible obligation or a present obligation that may, but probably will not, require an outflow of resources.

(iii) There is a possible obligation or a present obligation where the likelihood of an outflow of resources is remote.

Ans. (i) There is a present obligation that probably requires an outflow of resources and a reliable estimate can be made of the amount of obligation – Provision is recognised. Disclosures are required for the provision.

(ii) There is a possible obligation or a present obligation that may, but probably will not, require an outflow of resources – No provision is recognised. Disclosures are required for the contingent liability.

(iii) There is a possible obligation or a present obligation where the likelihood of an outflow of resources is remote – No provision is recognised. No disclosure is required.

Q-18 A company, incorporated as NPO under the Companies Act, is having main objective to promote the trade by organizing trade fairs / exhibitions. While organizing the trade fair and exhibitions, it decided to charge 5% contingency charges for the participants/outside agencies on the income received from them by the company , while in the case of fairs organized by outside agencies, 5% contingency charges are levied separately in the invoice, the contingency charges in respect of fairs organized by the company itself are inbuilt in the space rent charged from the participants. Both are credited to Income and Expenditure Account of the company.

The intention of levying these charges is to meet any unforeseen liability, which may arise in future. The instances of such unforeseen liabilities could be on account of injury/loss of life to visitors/ exhibitors, etc., due to fire, terrorist attack, stampede, natural calamities and other public and third party liability. The chances of occurrence of these events are high because of large crowds visiting the fair. The decision to levy 5% contingency charges was based on assessment only as actual liability on this account cannot be estimated.

The accounting treatment and disclosure was made by the company in its financial statements as: (i) 5% contingency charges are treated as income and matching provision for the same is also being made in accounts and (ii) suitable disclosure to this effect is also made in the notes forming part of accounts.

You are required to comment whether creation of provision for contingencies considering the facts and circumstances of the case is required in line with AS 29.

Ans. As per AS 29 "Provisions, Contingent Liabilities and Contingent Assets", a provision should be recognized when (a) An enterprise has a present obligation as a result of a past event and (b) It is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and (c) A reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision should be recognized.

From the above, it is clear that for the contingencies considered by the company, neither a present obligation exists because of past event, nor a reliable estimate can be made of the amount of the obligation. Accordingly, a provision cannot be recognized for such contingencies under the facts and circumstances of the case.

Q-19 An oil company has been contaminating land for several years. It does not clean up because there is no legislation requiring cleaning up. On 31st March 2021, it is virtually certain that a law requiring a clean-up of land already contaminated will be enacted shortly after the year end. Is provisioning presently necessary considering the circumstances in line with provisions of AS 29?

Ans. As per AS 29 `Provisions, Contingent Liabilities and Contingent Assets', a past event will lead to present obligation when the enterprise has no realistic alternative to settle the obligation created by the past event. However, when environmental damage is caused there may be no obligation to remedy the consequences. The causing of the damage will become an obligating event when a new law requires the existing damage to be rectified. Where details of a proposed new law have yet to be finalised, an obligation arises only when the legislation is virtually certain to be enacted. In the given case it is virtually certain that law will be enacted requiring clean-up of a land already contaminated. Therefore, an oil company has to provide for such clean-up cost in the year in which the law is virtually certain to be enacted.

Q-20 Chaos Limited is in the process of finalizing its accounts for the year ended31st March, 2020. It seeks your advice in the following cases:

(i) Chaos Limited has filed a court case in 2014-2015 against its competitors. Itbecame evident to its lawyers during the year ended 31st March, 2020 that Chaos Limited may lose the case and would

have to pay ₹ 3,00,000 being the cost of litigation. No entries/provisions have been made in the books.

(ii) A new regulation has been passed in 2019-2020 by the healthcare ministry to upgrade facilities. Deadline set by the government is 31.03.2021. The company estimates an expenditure of ' 10,00,000 for the said upgrade.

(iii) The company gives one year warranty for its healthcare equipment under the contract of sale that it will make good any manufacturing defect by repair or replacement. As per past experience, it is probable that there will be 1% such cases and estimated cost of repair / replacement is estimated at 10% of such sale value. During the year, the company has made a sale of ' 5 crores.

Kindly give your answer for each of above with proper reasoning according to the relevant Accounting Standard. Also state the principles for recognition of provision, as per AS 29

Ans. Principles for recognition of provisions: As per AS 29, "a provision shall be recognised when:

(i) an entity has a present obligation (legal or constructive) as a result of a past event;

(ii) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

(ii) a reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision shall be recognised."

Accounting treatment under the given scenarios:

(i) On 31st March, 2020, since it is evident to the lawyer that Chaos Limited may lose the case and also a reliable estimate of the outflow can be made as ₹ 3,00,000, there is a present obligation. Hence, provision should be recognised for ₹ 3,00,000 for the amount which may be required to settle the obligation.

(ii) Under new regulation, an entity is required to upgrade its facilities by 31st March, 2021. However, on 31st March, 2020, i.e. at the end of the reporting period, there is no obligation because there is no obligating event either for the costs of upgrading the facilities or for fines under the regulations. Hence, no provision should be recognized on 31st March, 2020 for upgrading the facilities by 31st March, 2021.

(iii) The obligating event is the sale of health care equipment with a warranty, which gives rise to a legal obligation. Here, an outflow of resources embodying economic benefits in settlement is probable for the warranties as a whole. Hence, a provision is recognized for the best estimate of the costs of making good under the warranty products sold before the end of the reporting period as follows:

Probability of warranty cases for the entity where repair/replacement may be

required as per past experience = 1% of ₹ 5,00,00,000 = ₹ 5,00,000

Estimated cost of repair / replacement = ₹ 5,00,000 x 10% = ₹ 50,000.

Q-21 (i) Bonfire Ltd. is in a dispute with a competitor company. The dispute is regarding alleged infringement of Copyrights. The competitor has filed a suit in the court of law seeking damages of ' 200 lacs.

The Directors are of the view that the claim can be successfully resisted by the Company.

How would the matter be dealt in the annual accounts of the Company in the light of AS 29 ?

Explain in brief giving reasons for your answer.

(ii) What is meant by "Restructuring Provision" as per AS 29? What costs are excluded while computing such provision as per the standard?

Ans.

(i) As per AS 29, 'Provisions, Contingent Liabilities and Contingent Assets', a provision should be recognized when

- an enterprise has a present obligation as a result of a past event;
- it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
- a reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision should be recognized.

In the given situation, since, the directors of the company are of the opinion that the claim can be successfully resisted by the company, therefore there will be no outflow of the resources.

Hence, no provision is required. The company will disclose the same as contingent liability by way of the following note:

"Litigation is in process against the company relating to a dispute with a competitor who alleges that the company has infringed copyrights and is seeking damages of ' 200 lakhs.

However, the directors are of the opinion that the claim can be successfully resisted by the company."

(ii) As per AS 29, a restructuring provision should include only the direct expenditures arising from the restructuring, which are those that are both: (a) necessarily entailed by the restructuring; and (b) Not associated with the ongoing activities of the enterprise. A restructuring provision does not include such costs as: (a) Retraining or relocating continuing staff; (b) Marketing; or (c) Investment in new systems and distribution networks.

Q-22 XYZ Ltd. has not made provision for warrantee in respect of certain goods due to the fact that the company can claim the warranty cost from the original supplier. Hence the accountant of the company says that the company is not having any liability for warrantees on a particular date as the amount gets reimbursed. You are required to comment on the accounting treatment done by the XYZ Ltd. in line with the provisions of AS 29.

Ans. As per AS 29 "Provisions, Contingent Liabilities and Contingent Assets", where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognised when, and only when, it is vi rtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognised for the reimbursement should not exceed the amount of the provision. It is apparent from the question that the company had not made provision for warranty in respect of certain goods considering that the company can claim the warranty cost from the original supplier. However, the provision for warranty should have been made as per AS 29 and the amount claimable as reimbursement should be treated as a separate asset in the financial statements of the company rather than omitting the disclosure of such liability. Accordingly, it is viewed that the accounting treatment adopted by the company with respect to warranty is not correct.

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NOTES

CHAPTER-2

PARTNERSHIP ACCOUNTS

Q-1 Ram, Wazir and Adil give you the following Balan ce Sheet as on 31st March, 2019:

Liabilities		₹	Assets		₹
Ram's Loan		15,000	Plant and Machinery at cost		30,000
Capital Accounts:			Fixtures and Fittings		2,000
Ram	30,000		Stock	10,400	
Wazir	10,000		Debtors	18,400	
Adil	2,000	42,000	Less: Provision	(400)	18,000
Sundry Creditors		17,800	Joint Life Policy		15,000
Loan on Hypothecation of			Patents and Trademarks		10,000
Stock		6,200	Cash at Bank		8,000
Joint Life Policy Reserve		12,400			
		93,400			**93,400**

The partners shared profits and losses in the ratio of Ram 4/9, Wazir 2/9 and Adil 1/3. Firm was dissolved on 31st March, 2019 and you are given the following information:

(a) Adil had taken a loan from insurers for ₹ 5,000 on the security of Joint Life Policy.

The policy was surrendered and Insurers paid a sum of ₹ 10,200 after deducting ₹ 5,000 for Adil's loan and ₹ 300 as interest thereon.

(b) One of the creditors took some of the patents whose book value was ₹ 6,000 at a valuation of ₹ 4,500. The balance to that creditor was paid in cash.

(c) The firm had previously purchased some shares in a joint stock company and had written them off on finding them useless. The shares were now found to be worth ₹ 3,000 and the loan creditor agreed to accept the shares at this value.

(d) The remaining assets realized the following amount:

	₹
Plant and Machinery	17,000
Fixtures and Fittings	1,000
Stock	9,000
Debtors	16,500
Patents	at 50% of their book value.

(e) The liabilities were paid and a total discount of ₹ 500 was allowed by the creditors.

(f) The expenses of realization amounted to ₹ 2,300.

You are required to prepare the Realization Account, Bank Account and Partners' Capital Accounts in columnar form. Also provide necessary working notes in your answer.

Ans.

Realization Account

	₹			₹
To Plant and machinery	30,000	By Provision for doubtful debts		
400				
To Fixtures and fittings	2,000	By Loan on hypothecation of stock		
		(W.N.3)		3,000
To Stock	10,400	By Creditors (W.N.2)		500
To Debtors	18,400	By Joint Life Policy A/c (W.N.4)		12,900
To Patents and Trademarks				
(W.N.5)	5,500	By Bank		
		Plant and machinery	17,000	
To Bank	2,300	Fixtures and fittings	1,000	
		Stock	9,000	
		Debtors	16,500	
		Patents and Trademarks	2,000	45,500
		By Partners' Capital Accounts		
		Ram	2,800	
		Wazir	1,400	
		Adil	2,100	6,300
	68,600			**68,600**

Bank Account

	₹		₹
To Balance b/d	8,000	By Adil's Capital A/c- drawings	5,300
To Joint Life Policy	15,500	By Loan on hypothecation of stock	3,200
To Realisation A/c	45,500		
To Adil's Capital A/c	5,400	By Creditors	12,800
		By Realisation A/c (expenses)	2,300
		By Ram's Loan A/c	15,000
		By Ram's Capital A/c	27,200
		By Wazir's Capital A/c	8,600
	74,400		**74,400**

Partners' Capital Accounts

	Ram ₹	Wazir ₹	Adil ₹		Ram ₹	Wazir ₹	Adil ₹
To Bank			5,300	By Balance b/d	30,000	10,000	2,000
To Realisation A/c	2,800	1,400	2,100				
To Bank (Bal. Fig.)	27,200	8,600		By Bank A/c			
				(bal.fig.)			5,400
	30,000	**10,000**	**7,400**		**30,000**	**10,000**	**7,400**

Working Notes:

1. **Ram's Loan Account**

	₹		₹
To Bank A/c	15,000	By Balance b/d	15,000
	15,000		**15,000**

2. **Sundry Creditors Account**

	₹		₹
To Patents and Trademarks A/c	4,500	By Balance b/d	17,800
To Realisation A/c	500		
To Bank A/c	12,800		
	17,800		**17,800**

3. **Loan on Hypothecation of Stock Account**

	₹		₹
To Realisation A/c	3,000	By Balance b/d	6,200
To Bank A/c	3,200		
	6,200		**6,200**

4. **Joint Life Policy Account**

	₹		₹
To Balance b/d	15,000	By Joint Life Policy Reserve A/c	12,400
To Realisation A/c	12,900	By Bank A/c (10,200 + 5,300)	15,500
	27,900		27,900

5. **Patents and Trademarks Account**

	₹		₹
To Balance b/d	10,000	By Creditors A/c	4,500
		By Realisation A/c	1,500
		By Realisation A/c (bal.fig.)	4,000*
	10,000		**10,000**

Q-2 The following is the Balance Sheet of M/s. Pratham and Kaushal as on 31st March, 2019:

Liabilities	₹	**Assets**	₹
Capital Accounts:		Machinery	54,000
Pratham	50,000	Furniture	5,000
Kaushal	30,000	Investments (non -trading)	50,000
Reserves		20,000	Stock
20,000			
Loan Account of Kaushal	15,000	Debtors	21,000
Creditors	40,000	Cash	5,000
	1,55,000		**1,55,000**

It was agreed that Mr. Rohan is to be admitted for a fourth share in the future profits from 1st April, 2019. He is required to contribute cash towards goodwill and ₹ 15,000 towards capital.

The following further information is furnished:

(a) Pratham & Kaushal share the profits in the ratio 3 : 2.

(b) Pratham was receiving salary of ₹ 750 p.m. from the very inception of the firm in 20 12 in addition to share of profit.

(c) The future profit ratio between Pratham, Kaushal & Rohan will be 2:1:1. Pratham will not get any salary after the admission of Rohan.

(d) It was agreed that the value of goodwill of the firm shall be determined on the basis of 3 years' purchase of the average profits from business of the last 5 years. The particulars of the profits are as under :

Year ended	Profit/(Loss)
31st March, 2015	25,000
31st March, 2016	12,500
31st March, 2017	(2,500)
31st March, 2018	35,000
31st March, 2019	30,000

The above Profits and Losses are after charging the Salary of Pratham. The Profit of the year ended 31st March, 2015 included an extraneous profit of ₹ 40,000 and the loss for the year ended 31st March, 2017 was on account of loss by strike to the extent of ₹ 20,000.

(e) The cash trading profit for the year ended 31st March, 2020 was ₹ 50,000 before depreciation.

(f) The partners had drawn each ₹ 1,000 p.m. as drawings.

(g) The value of other assets and liabilities as on 31st March, 2020 were as under:

	₹
Machinery (before depreciation)	60,000
Furniture (before depreciation)	10,000
Investment	50,000
Stock	15,000
Debtors	30,000
Creditors	20,000

(h) Provide depreciation @ 10% on Machinery and @ 5% on Furniture on the Closing Balance and interest is accumulated @ 6% on Kaushal's loan. The loan alon g with interest would be repaid within next 12 months.

(i) Investments (non -trading) are held from inception of the firm and interest is received @ 10% p.a.

(j) The partners applied for conversion of the firm into Karma Ltd. , a Private Limited Company. Certificate was received on 1st April, 2020. They decided to convert Capital Accounts of the partners into share capital in the ratio of 2:1:1 on the basis of a total Capital as on 31st March, 2020. If necessary, partners have to subscribe to fresh capital or withdraw.

Prepare the Profit and Loss Account of the firm for the year ended 31st March, 2020 and the Balance Sheet of the Company on 1st April, 2020.

Ans. **M/s Pratham, Kaushal and Rohan**

Profit and Loss Account for the year ending on 31st March, 2020

	₹		₹
To Depreciation on Machinery	6,000	By Trading Profit	50,000
To Depreciation on furniture	500	By Interest on Investment	5,000
To Interest on Kaushal's loan	900		
To Net Profit to :			
Pratham's Capital A/c	23,800		
Kaushal's Capital A/c	11,900		
Rohan's Capital A/c	11,900		
	55,000		**55,000**

Balance Sheet of the Karma Pvt. Ltd. as on 1st April, 2020

		Notes No.	₹
I	**Equity and Liabilities**		
	Shareholders' funds		
	Share capital		1,41,600
	Current liabilities		
	Short term borrowings	1	15,900
	Trade payables		20,000
	Total		1,77,500
II	Assets		
	Non-current assets		
	Property, plant & Equipment	2	63,500
	Non-current investments		50,000
	Current assets		
	Inventories		15,000
	Trade receivables		30,000
	Cash and cash equivalents		19,000
	Total		**1,77,500**
	Notes to Accounts		
			₹
	1. Short term borrowings		
	Loan from Kaushal		15,900
	2. PPE		
	Machinery	54,000	
	Furniture		9,500
	63,500		

Working Notes:

1. Calculation of goodwill

	2014-15	2015-16	2016-17	2017-18	2018-19
	₹	₹	₹	₹	₹
Profits/(Loss)	25,000	12,500	(2,500)	35,000	30,000
Adjustment for extraneous profit of 2014-15 and abnormal loss of 2016-17	(40,000)	-	20,000	—	—
	(15,000)	12,500	17,500	35,000	30,000
Add: Salary of Pratham (750 x12)	9,000	9,000	9,000	9,000	9,000
	(6,000)	21,500	26,500	44,000	39,000
Less: Interest on non -trading investment	(5,000)	(5,000)	(5,000)	(5,000)	(5,000)
	(11,000)	16,500	21,500	39,000	34,000
Total Profit from 2015-16 to 2018-19					1,11,000
Less: Loss for 2014 -15					(11,000)
					1,00,000
Average Profit					20,000
Goodwill equal to 3 years' purchase					60,000
Contribution from Rohan for ¼ share					15,000

2. Calculation of sacrificing ratio of Partners Pratham and Kaushal on admission of Rohan

	Old share	New share	Sacrificing share	Gaining share
Pratham	3/5	1/2	$\frac{3}{5}-\frac{1}{2}=\frac{6-5}{10}=\frac{1}{10}$	
Kaushal	2/5	1/4	$\frac{2}{5}-\frac{1}{4}=\frac{8-5}{20}=\frac{3}{20}$	
Rohan		1/4		1/4

3. Goodwill adjustment entry through Partners' capital accounts (in their sacrificing ratio of 2:3)

		₹	₹
Rohan' s capital A/c	Dr.	15,000	
To Pratham's capital A/c			6,000
To Kaushal' s capital A/c			9,000

(Rohan's share in goodwill adjusted through Pratham and Kaushal)

4. Partners' Capital Accounts

	Pratham ₹	Kaushal ₹	Rohan ₹		Pratham ₹	Kaushal ₹	Rohan ₹
To Drawings (1,000 x 12)	12,000	12,000	12,000	By Balance b/d	50,000	30,000	—
To Pratham			6,000	By General Reserve	12,000	8,000	—
To Kaushal			9,000	By Rohan	6,000	9,000	—
To Balance c/d	79,800	46,900	14,900	By Bank (15,000 + 15,000)	—	—	30,000
				By Profit & Loss A/c	23,800	11,900	11,900
	91,800	**58,900**	**41,900**		**91,800**	**58,900**	**41,900**

5. Balance Sheet of the firm as on 31st March, 2020

Liabilities	₹	₹	Assets	₹	₹
Pratham's Capital	79,800		Machinery	60,000	
Kaushal's Capital	46,900		Less: Depreciation	(6,000)	54,000
Rohan's Capital	14,900	1,41,600	Furniture	10,000	
			Less: Depreciation	(500)	9,500
Kaushal's Loan	15,000		Investments		50,000
Add: Interest due	900	15,900	Stock-in -trade		15,000
Creditors		20,000	Debtors		30,000
			Cash (W.N.6)		19,000
		1,77,500			**1,77,500**

6. **Cash balance as on 31.3.2020**

	₹	₹
Cash trading profit		50,000
Add: Investment Interest		5,000
Add: Decrease in Stock Balance		5,000
		60,000
Less: Increase in Debtors	9,000	
Less: Decrease in Creditors		20,000
(29,000)		
		31,000
Add: Opening cash balance		5,000
Add: Cash brought in by Rohan	30,000	35,000
		66,000
Less: Drawings (12,000 +12,000 +12,000)	36,000	
Less: Additions to Machine (60,000 - 54,000)	6,000	
Furniture (10,000 - 5,000)	5,000	(47,000)
Closing cash balance		19,000

7. **Distribution of shares – Conversion into Company**

		₹
Capital:	Pratham	79,800
	Kaushal	46,900
	Rohan	14,900
Share Capital		1,41,600
Distribution of shares:	Pratham (1/2)	70,800
	Kaushal (1/4)	35,400
	Rohan (1/4)	35,400

Pratham and Kaushal should withdraw capital of ₹ 9,000 (₹ 79,800 – ₹ 70,800) and ₹11,500 (₹ 46,900 – ₹ 35,400) respectively and Rohan should subscribe shares of ₹ 20,500 (₹35,400 – ₹ 14,900).

Q-3 Mohit, Neel and Om were Partners sharing Profits and Losses in the ratio of 5:3:2 respectively. The Trial Balance of the Firm on 31st March, 2019 was the following:

Particulars	₹	₹
Machinery at Cost	2,00,000	
Inventory	1,37,400	
Trade receivables	1,24,000	
Trade payables		1,69,400
Capital A/cs:		
Mohit		1,36,000
Neel		90,000
Om		46,000
Drawing A/cs:		
Mohit	50,000	
Neel	46,000	
Om	34,000	
Depreciation on Machinery		80,000
Profit for the year ended 31st March		2,48,600
Cash at Bank	1,78,600	
	7,70,000	**7,70,000**

Interest on Capital Accounts at 10% p.a. on the amount standing to the credit of Partners' Capital Account at the beginning of the year, was not provided before preparing the above Trial Balance. On the above date, they formed a MNO Private Limited Company with an Authorized Share Capital of 2,00,000 shares of ₹ 10 each to be divided in different classes to take over the business of Partnership firm.

You are provided the following information:

1. Machinery is to be transferred at ₹ 1,40,000.
2. Shares in the Company are to be issued to the partners, at par, in such numbers, and in such classes as will give the partners, by reason of their shareholdings alone, the same rights as regards interest on capital and the sharing of profit and losses as they had in the partnership.
3. Before transferring the business, the partners wish to draw from the partnership profits to such an extent that the bank balance is reduced to ₹ 1,00,000. For this purpose, sufficient profits of the year are to be retained in profit -sharing ratio.
4. Assets and liabilities except Machinery and Bank, are to be transferred at their book value as on the above date.

You are required to prepare:

(a) Statement showing the workings of the Number of Shares of each class to be issued by the company, to each partner.

(b) Capital Accounts showing all adjustments required to dissolve the Partnership.

(c) Balance Sheet of the Company immediately after acquiring the business of the Partnership and Issuing of Shares.

Ans. (a) Number of Shares to be issued to Partners

				₹
Assets: Machinery ₹ 1,40,000 + Inventory ₹ 1,37,400 +Trade Receivable ₹1,24,000 + Bank ₹ 1,00,000				5,01,400
Less: Liabilities taken over				(1,69,400)
Net Assets taken over (Purchase Consideration)				3,32,000
Classes of Shares to be issued :	**Mohit**	**Neel**	**Om**	**Total**
10% Preference Shares of ₹ 10 each (to retain rights as to Interest on Capital)	1,36,000	90,000	46,000	2,72,000
Balance in Equity Shares of ₹ 10 each (3,32,000 -2,72,000) (issued in profit sharing ratio)	30,000	18,000	12,000	60,000
	1,66,000	**1,08,000**	**58,000**	**3,32,000**

(b) **Partners' Capital Accounts**

Particulars	Mohit	Neel	Om	Particulars	Mohit	Neel	Om
To Drawings	50,000	46,000	34,000	By balance b/d	1,36,000	90,000	46,000
To 10% Preference share capital	1,36,000	90,000	46,000	By Interest on Capital	13,600	9,000	4,600
To Equity Shares	30,000	18,000	12,000	By profit for the year 5:3:2 (W.N. 1)	1,10,700	66,420	44,280
To Bank – Additional drawings (W.N. 2)	54,300	17,420	6,880	By Machinery* A/c	10,000	6,000	4,000
Total	**2,70,300**	**1,71,420**	**98,880**		**2,70,300**	**1,71,420**	**98,880**

* Gain on Transfer of Machinery = ₹ 1,40,000 – (₹ 2,00,000-₹ 80,000) = ₹ 20,000 in 5:3:2 ratio.

(c) Balance sheet of MNO Ltd. as on 31st March, 2019 (after Takeover of Firm)

		Note no.	₹
I Equity and Liabilities:			
(1) Shareholders Funds			
Share Capital		1	3,32,000
(2) Current Liabilities			
Trade Payables			1,69,400
	Total		5,01,400
II Assets			
(1) Non-Current Assets			
Property, plant & equipment			1,40,000
(2) Current Assets:			
(a) Inventories			1,37,400
(b) Trade Receivables			1,24,000
(c) Cash and Cash Equivalents			1,00,000
	Total		**5,01,400**

Notes to Accounts

	Particulars	₹
1.	Shares capital	
	Authorized shares capital	20,00,000
	Issued, Subscribed & paid up	
	6,000 Equity Shares of ₹ 10 each	60,000
	27,200 10% Preference Shares capital of ₹ 10 each	2,72,000
	(All above shares issued for consideration other than cash, in takeover of partnership firm)	3,32,000

Working Note :

1. Profit & Loss Appropriation Account for the year ended 31st March, 2019

	Particulars	₹	₹	Particulars	₹
	To Interest on Capital:			By Net Profit	2,48,600
	Mohit [₹ 1,36,000 x 10%]	13,600		(given)	
	Neel [₹ 90,000 x 10%]	9,000			
	Om [₹ 46,000 x 10%]	4,600	27,200		
To	Profits transferred to Capital in profit sharing ratio 5:3:2				
	Mohit	1,10,700			
	Neel	66,420			
	Om	44,280	**2,21,400**		
Total			**2,48,600**		**2,48,600**

2. Statement showing Additional Drawings in Cash

(a)	**Funds available for Drawings**		
	Total Drawing of Partners (given)		1,30,000
	Add: Further Funds available for Drawings (1,78,600-1,00,000)		78,600
			2,08,600
	Less: Interest on Capital		(27,200)
	Amount available for Additional Drawings		1,81,400

(b)	**Ascertainment of Additional Drawings**			
	Particulars	**Mohit**	**Neel**	**Om**
	As per above statement			
	₹ 1,81,400 (in profit sharing ratio)	90,700	54,420	36,280
	Add: Interest	13,600	9,000	4,600
		1,04,300	63,420	40,880
	Less: Already drawn	(50,000)	(46,000)	(34,000)
	Additional Drawings	54,300	17,420	6,880

Q-4 Differentiate on ordinary partnership firm with an LLP (Limited Liability Partnership) in respect of the following:

(1) Applicable Law
(2) Number of Partners
(3) Ownership of Assets
(4) Liability of Partners/Members

Ans. **Distinction between an ordinary partnership firm and an LLP**

Key Elements	Partnerships	LLPs
Applicable Law	Indian Partnership Act 1932	The Limited Liability Partnerships Act, 2008
Number of Partners	Minimum 2 and Maximum 20 (subject to 10 for banks)	Minimum 2 but no maximum limit
Ownership of Assets	Firm cannot own any assets. The partners own the assets of the firm.	The LLP as an independent entity can own assets
Liability of Partners/ Members	Unlimited: Partners are severally and jointly liable for actions of other partners and the firm and their liability extends to personal assets.	Limited to the extent of their contribution towards LLP except in case of intentional fraud or wrongful act of omission or commission by a partner.

Q-5 Ali and Beta were carrying on business, sharing profits and losses equally. The firm's balance sheet as at 31-12-2018 was:

Liabilities		**Rs.**	**Assets**		**Rs.**
Sundry Creditors		1,44,000	Stock		1,44,000
Bank Overdraft		84,000	Machinery		3,60,000
Capital A/c:			Debtors		1,68,000
			Joint Life Policy		21,600
Ali	3,36,000		Leasehold Premises		81,600
Beta	3,12,000	6,48,000	Profit & Loss A/c		62,400
			Drawing A/c:		
			Ali	24,000	
			Beta	14,400	38,400
		8,76,000			**8,76,000**

The business was carried on till 30-06-2019. The partners withdrew the amounts equal to half the amount of profit made during the period of six months ended on 30-06-2019, in equal proportion. The profit was calculated after charging depreciation at 10% p.a. on machinery and after writing off 5% on leasehold premises. In the half year, sundry creditors were reduced by Rs. 24,000 and bank overdraft by Rs. 36,000.

On 30-06-2019, stock was valued at Rs. 1,80,000 and debtors at Rs. 1,44,000; the Joint Life Policy had been surrendered for Rs. 21,600 before 30-06-2019 and other items remained the same as at 31-12-2018.

On 30-06-2019, the firm sold the business to a limited company. The value of goodwill was fixed at Rs. 2,40,000 and the rest of the assets were valued on the basis of the balance sheet as at 30-06-2019. The company paid the purchase consideration in equity shares of Rs. 10 each.

You are required to prepare:

(i) Balance Sheet of the firm as at 30-06-2019;

(ii) Realisation Account; and

(iii) Partners' Capital Accounts showing the final settlement between them.

(b) Explain the nature of Limited Liability Partnership. Who can be a designated partner in a Limited Liability Partnership?

Ans :

(a) Balance Sheet of the Firm as at 30.6.2019

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
Capital Accounts:			Machinery	3,60,000	
Ali balance as on 1.1.2019	2,80,800		Less: Depreciation		
			@ 10% p.a. for 6 months	(18,000)	3,42,000
Add: Profit for 6 months	28,320		Leasehold premises	81,600	
	3,09,120		Less: Written-off @ 5%		
Less: Drawings for 6 months	(14,160)	2,94,960	for 6 months	(4,080)	77,520
Beta balance as on 1.1.2019	2,66,400		Stock		1,80,000
Add: Profit for 6 months	28,320		Sundry Debtors		1,44,000
	2,94,720				
Less: Drawings for 6 months	(14,160)	2,80,560			
Sundry Creditors		1,20,000			
(1,44,000 . 24,000)					
Bank overdraft					
(84,000 - 36,000)		48,000			
		7,43,520			**7,43,520**

(b) Realization Account

Particulars		Rs.	Particulars		Rs.
To	Machinery A/c	3,42,000	By	Sundry Creditors A/c	1,20,000
To	Leasehold Premises A/c	77,520	By	Bank Overdraft A/c	48,000
To	Stock A/c	1,80,000	By	Purchasing Company A/c (W.N.1)	8,15,520
To	Sundry Debtors A/c	1,44,000			
To	Ali Capital A/c	1,20,000			
To	Beta Capital A/c	1,20,000			
		9,83,520			**9,83,520**

(c)

Partners' Capital Accounts

Date	Particulars	Ali Rs.	Beta Rs.	Date	Particulars	Ali Rs.	Beta Rs.
1.1.19	To Profit & Loss A/c	31,200	31,200	1.1.19	By Balance b/d	3,36,000	3,12,000
	To Drawings A/c	24,000	14,400				
29.6.19	Balance c/d	2,80,800	2,66,400				
		3,36,000	**3,12,000**			**3,36,000**	**3,12,000**
30.6.19	To Drawings A/c	14,160	14,160	30.6.19	By Balance b/d	2,80,800	2,66,400
	To Shares in Purchasing Company A/c	4,14,960	4,00,560	30.6.19	By Profit & Loss Appropriation A/c	28,320	28,320
					By Realization A/c	1,20,000	1,20,000
		4,29,120	**4,14,720**			**4,29,120**	**4,14,720**

Working Notes :

(1) Ascertainment of purchase consideration

	Rs.	Rs.
Assets:		
Stock		1,80,000
Sundry Debtors		1,44,000
Machinery less depreciation		3,42,000
Leasehold premises less written off		77,520
		7,43,520
Less: Liabilities:		
Sundry Creditors	1,20,000	
Bank overdraft	48,000	(1,68,000)
Closing Net Assets		5,75,520
Add: Goodwill		2,40,000
Purchase Consideration		8,15,520

(2) Ascertainment of profit for the 6 month ended 30th June, 2019

	Rs.	Rs.
Closing Net Assets		5,75,520
Less: Opening Combined Capital		
Ali - (3,36,000- 31,200-24,000)	2,80,800	
Beta - (3,12,000-31,200-14,400)	2,66,400	5,47,200
Profit after adjustment of Drawings		28,320
Add: Combined drawings during the 6 month (equal to profit)		28,320
Profit for 6 months		56,640

(b) Nature of Limited Liability Partnership: A limited liability partnership is a body corporate formed and incorporated under the LLP Act, 2008 and is a legal entity separate from that of its partners. A limited liability partnership shall have perpetual succession and any change in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liability partnership.

Designated partners: Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India.

In case of a limited liability partnership in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such limited liability partnership or nominees of such bodies corporate shall act as designated partners.

Q-6 The partners P, Q & R have called you to assist them in winding up the affairs of their partnership on 31.12.2016. Theirbalance sheet as on that date is given below:

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital Accounts:		Land & Building	50,000
P	65,000	Plants Machinery	46,000
Q	50,500	Furniture& Fixture	10,000
R	32,000	Stock	14,500
Creditors	16,000	Debtors	14,000
		Cash at Bank	9,000
		Loan P	13,000
		Loan Q	7,000
Total	**1,63,500**	**Total**	**1,63,500**

(a) The partners share profit and losses in the ratio of 4:3:2.

(b) Cash is distributed to the partners at the end of each month.

(c) A summary of liquidation transactions are as follows:

January 2017

- Rs. 9,000 - collected from debtors; balance is uncollectable.
- Rs. 8,000 - received from the sale of entire furniture
- Rs. 1,000 - Liquidation expenses paid.
- Rs. 6,000 - Cash retained in the business at the end of month

February 2017

- Rs. 1,000 - Liquidation expenses paid.
- As part payment of his capital, R accepted a machinery for Rs. 9,000 (book value Rs. 3,500)
- Rs. 2,000 - Cash retained in the business at the end of month

March2017

- Rs. 38,000 - received on the sale of remaining plant and machinery.
- Rs. 10,000 - received from the sale of entire stock.
- Rs. 1,700 - Liquidation expenses paid.
- Rs. 41,000 - Received on sale of land & building.
- No Cash is retained in the business.

You are required to prepare a schedule of cash payments amongst the partners by "Higher Relative Capital Method".

(b) Explain the nature of Limited Liability Partnership. Who can be a designated partner in a Limited Liability Partnership?

Ans :

Particulars	Cash	Creditors	Capital		
	Rs.	Rs.	P(Rs.)	Q(Rs.)	R(Rs.)
Balance due after loan		16,000	52,000	43,500	32,000
January					
Balance available	9,000				
Realization less expenses and cash retained	10,000				
Amount available and paid	19,000	(16,000)	-	-	(3,000)
Balance due	-	-	52,000	43,500	29,000

February					
Opening Balance	6,000				
Expenses paid and cash carried forward	3,000				
Available for distribution	3,000				
Cash paid to Q and Machinerygivento R		-	3,000	9,000	
Balance due	-		52,000	40,500	20,000
March					
Opening Balance	2,000				
Amount realized less expenses	87,300				
Amount paid to partners	89,300		41,689	32,767	14,844
Loss		10,311	7,733	5,156	

Workintg Note :

(i) Highest Relative Capital Basis

	P (Rs.)	Q.(Rs)	R(Rs.)
Scheme of payment for January 2017			
Balance of Capital Accounts	65,000	50,500	32,000
Less: Loans	(13,000)	(7,000)	-
(A)	52,000	43,500	32,000
Profit Sharing Ratio	4	3	2
Capital / Profit sharing Ratio	13,000	14,500	16,000
Capital in profit sharing ratio, taking P's capital as base (B)	52,000	39,000	26,000
Excess of R's capital and Q's Capital (A - B) (i)		4,500	6,000
Profit Sharing Ratio		3	2
Capital / Profit sharing Ratio		1,500	3,000
Capital in profit sharing ratio, taking Q'scapital as base (ii)		4,500	3,000
Excess of R's Capital over Q'scapital (i - ii)			3,000
(ii) Scheme of distribution of available cash for March:			
	P(Rs.)	**Q(Rs.)**	**R(Rs.)**
Balance of Capital Accounts at end of February (A)	52,000	40,500	20,000
Profit Sharing Ratio	4	3	2
Capital / Profit sharing Ratio	13,000	13,500	10,000
Capital in profit sharing ratio, taking R's capital as base (B) (i)	40,000	30,000	20,000
Excess of P's Capital and Q's Capital (A- B) (i)	12,000	10,500	
Profit Sharing Ratio	4	3	
Capital / Profit sharing Ratio	3,000	3,500	
Capital in profit sharing ratio taking P's capital as base (ii)	12,000	9,000	
Excess of Q's Capital over P's Capital (i - ii)	-	1,500	
Payment Rs. 1500 (C)		(1,500)	
Balance of Excess Capital (i -C)	12,000	9,000	
Payment Rs. 21000(0)	(12,000)	(9,000)	
Balance due (A-C-D)	40,000	30,000	20,000
Balance cash Payment (Rs. 89,300 - Rs. 22,500) = Rs. 66,800 (E)	(29,689)	(22,267)	(14,844)
Total Payment(Rs. 89,000) (C + D +E) (iii)	41,689	32,767	14,844
Loss(A-iii)	10,311	7,733	5,156

(b) Nature of Limited Liability Partnership: A limited liability partnership is a body corporate formed and incorporated under the LLP Act, 2008 and is a legal entity separate from that of its partners. A limited liability partnership shall have perpetual succession and any change in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liability partnership.

Designated partners: Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India.

In case of a limited liability partnership in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such limited liability partnership or nominees of such bodies corporate shall act as designated partners.

Q-7 X, Y and Z are in partnership sharing profits and losses in the ratio of 5:4:4. The Balance Sheet of the firm as on 31st March, 2016 is as below:

Liabilities	Rs.	Assets	Rs.
X's Capital	60,000	Factory Building	96,640
Ys Capital	40,000	Plant and Machinery	65,100
Z's Capital	50,000	Trade Receivable	21,600
Ys Loan	18,000	Inventories	49,560
Trade Payable	66,000	Cash at Bank	1,100
	2,34,000		**2,34,000**

On Balance Sheet date, all the three partners have decided to dissolve their partnership. Since the realisation of assets was protracted, they decided to distribute amounts as and when feasible and for this purpose they appoint Z who was to get as his remuneration 1% of the value of the assets realised other than cash at bank and 10% of the amount distributed to the partners.

Assets were realised piecemeal as under:

	Rs.
First instalment	74,600
Second instalment	69,301
Third instalment	40,000
Last instalment	28,000
Dissolution expenses were provided for estimated amount of	Rs.12,000
The creditors were settled finally for	Rs.63,600

You are required to prepare a statement showing distribution of cash amongst the partners by "Highest Relative Capital Method".

(b) State the circumstances when LLPcan be wound up by the Tribunal.

Ans : **Statement Showing Distribution of cash amongst the partners**

		Trade Payable	Y's Loan	Capitals X (Rs.)	Y (Rs.)	Z (Rs.)
Balance Due		66,000	18,000	60,000	40,000	50,000
Including 1st installment amount with the firm Rs.(1100 + 74,600)	75,700					
Less : Dissolution expenses provided for	12,000					
	63,700					
Less : Z's remuneration of 1% on assets realized (74,600 x 1%)	746					
	62,954					
Less : Payment made to Trade Payables	62,954	62,954				

Balance due	Nil	3046				
2nd installment realised	69,301					
Less: Z's remuneration of 1% on assets realized (69,301 x 1%)	693					
	68,608					
Less: Payment made to Trade Payables	646	646				
Transferred to P&L A/c		2,400				
	67,962					
Less: Payment for Y's loan A/c	18,000		18,000			
Amount available for distirbution to partners	49,962		Nil			
Less: Z's remuneration to 10% of the amount distributed to partners (49,962 x 10/110)	4,542					
Balance to be distributed to partners on the basis of HRCM	45,420					
Less : Paid to Z(W.N.)	2,000					2,000
	43,420					48,000
Less: Paid to X and Z in 5:4 (W.N.)	18,000			10,000	-	8,000
Balance due	25,420			50,000	40,000	40,000
Less: Paid to X, Y & Z in 5:4:4	25,420			9,778	7,821	7,821
	Nil					
Amount of 3rd installment	40,000			40,222	32,179	32,179
Less: Z's remuneration of 1% on assets realized (40,000 x 1%)	400					
	39,600					
Less: Z's remuneration of 10% of the amount distributed to partners (39,600 x 10/110)	3,600					
	36,000					
Less: Paid to X, Y, Z in 5:4:4 for (W.N.)	36,000			13,846	11,077	11,077
	Nil			26,376	21,102	21,102
Amount of 4th and last instalment	28,000					
Less: Z's remuneration of 1% on assets realized (28,000 x 1%)	280					
	27,720					
Less: Z's remuneration of 10% of the amount distributed to partment (27,720 x 10/110	2,520					
	25,200					
Less: Paid to X, Y and Z in 5:4:4	25,200			9,692	7,754	7,754
	Nil					
Loss suffered by partners				16,684	13,348	13,348

Working Note :

(i) Rs. 1100 added to the first instalment received on sale of assets represents the Cash in Bank

(ii) The amount due to Creditors at the end of the utilization of First Instalment is Rs. 3046. However, since the creditors were settled for Rs. 63,600 only the balance Rs.646 were paid and the balance Rs. 2400 was transferred to the Profit & Loss Account.

(iii) Highest Relative Capital Basis

		X Rs.	Y Rs.	Z Rs.
Balance of Capital Accounts	(A)	60,000	40,000	50,000
Profit sharing ratio		5	4	4
Capital Profit sharing ratio		12,000	10,000	12,500
Capital in profit sharing ratio taking Ys Capital as base	(B)	50,000	40,000	40,000
Excess of X's Capital and Z's Capital (A-B) =(C)		10,000	nil	10,000
Again repeating the process				
Profit sharing ratio		5		4
Capital Profit sharing ratio		2,000		2,500
Capital in profit sharing ratio taking X's Capital as base (D)		10,000		8,000
Excess of Z's Capital (C-D)=(E)		nil		2,000

Therefore, firstly Rs.2,000 is to be paid to Z, then X and Z to be paid in proportion of 5:4 upto Rs. 18,000 to bring the capital of all partners X, Y and Z in proportion to their profit sharing ratio. Thereafter, balance available will be paid in the profit sharing ratio 5:4:4 to all partners viz X, Y and Z.

(b) Under section 64 of the LLP Act, 2008, an LLP maybe wound up by the Tribunal:

- If the LLP decides that it should be wound up by the Tribunal;
- If for a period of more than six months, the number of partners of the LLP is reduced below two;
- If the LLP is unable to pay its debts;
- If the LLP has acted against the interests of the integrity and sovereignty of India, the security of the state or public order;
- If the LLP has defaulted in the filing of the Statement of Account and Solvency with the Registrar for five consecutive financial years;
- If the Tribunal is of the opinion that it is just and equitable that the LLP be wound up.

Q-8 L, M and N share profits and losses in the ratio of 5:3:2. Their firm was dissolved due to misconduct of M and their balance sheet on that date was as under:

Balance Sheet as at 31-3-2016

Liabilities		Rs.	Assets	Rs.
Capital Accounts :			Land and Building	2,00,000
L	3,00,000		Plants	2,00,000
M	2,00,000		Trade receivables	1,00,000
N	1,00,000	6,00,000	Inventories	1,50,000
Current Accounts:			Cash	1,00,000
L	50,000		Current Account:	
M	30,000	80,000	N	50,000
Trade payables		1,20,000		
		8,00,000		8,00,000

The whole business of the firm was sold to Preet Limited, on that day on the following terms:

(i) Preet Limited will issue the following securities in consideration for transfer of business: 10,000 equity shares @ Rs.15 each, 15,000 preference shares @ Rs.15 each; and 20,000 debentures @ Rs.14.725.

(ii) The agreed value of assets and liabilities of partnership firm are as follows:

Land & Building - Rs.3,00,000, Plants - Rs.1,50,000, Inventory - Rs.1,40,000, Trade Receivable - Rs.97,500, and Trade Payable - Rs.1,18,000.

It was mutually decided that preference shares and debentures will be distributed in profit sharing ratio and cash brought in by the partner (if any) will be shared equally by the remaining partners before distribution of equity shares. Equity shares are distributed on residual basis at the end.

You are required to prepare Realization Account, Cash Account, Partners' Current and Capital Accounts at the time of closing close the books of the firm.

(b) Explain the nature of Limited Liability Partnership. Who can be a designated partner in a Limited Liability Partnership?

Ans :

Realization Account

	Rs.	Rs.		Rs.
To Land & Building		2,00,000	By Trade Payables	1,20,000
To Plant		2,00,000	By Preet Limited (W.N.1)	6,69,500
To Inventories		1,50,000		
To Trade Receivable		1,00,000		
To Cash		1,00,000		
To Profit transferred to Capital A/c:				
L	19,750			
M	11,850			
N	7,900	39,500		
		7,89,500		7,89,500

Cash Account

	Rs.		Rs.
To N's Capital A/c	46,000	By L's Capital A/c	23,000
		By M's Capital A/c	23,000
	46,000		46,000

Partner's Current Account

	L	M	N		L	M	N
	Rs.	Rs.	Rs.		Rs.	Rs.	Rs.
To Balance b/d	-		50,000	By Balance b/d	50,000	30,000	-
To L's Capital A/c	69,750			By Realisation A/c	19,750	11,850	7,900
To M's Capital A/c		41,850		By N's Capital A/c			42,100
	69,750	41,850	50,000		69,750	41,850	50,000

Partner's Capital Accounts

	L	M	N		L	M	N
	Rs.	Rs.	Rs.		Rs.	Rs.	Rs.
To N's Current A/c	-	-	42,100	By Balance b/d	3,00,000	2,00,000	1,00,000
To Preference Shares in Preet Ltd. A/c	1,12,500	67,500	45,000	By L's Current A/c	69,750		
To Debentures A/c	1,47,250	88,350	58,900	By M's Current A/c		41,850	
To Cash A/c	23,000	23,000	-	By Cash A/c (bal.fig.)			46,000
To Equity Shares A/c	87,000	63,000	-				
	3,69,750	2,41,850	1,46,000		3,69,750	2,41,850	1,46,000

Working Notes:

1. Calculation of Purchase consideration

Net Payment Mehtod

		Rs.
Equity Shares	= 10,000 @ Rs.15	1,50,000
Preference Shares	= 15,000 @ Rs.15	2,25,000
Debentures	= 20,000 @ Rs.14,725	2,94,500
		6,69,500

2. As whole business of the firm was sold to Preet Limited, cash balance of the firm Rs.1,00,000 is also transferred to realization account. Cash brought in by N equal to Dr. balance appearing in his account, after distribution of preference shares and debentures in profit sharing ratio would be shared by L and M equally. The balance amount payable to L and M would be settled by transfer of equity shares in Preet Company.

(b) **Nature of Limited Liability Partnership**: A limited liability partnership is a body corporate formed and incorporated under the LLP Act, 2008 and is a legal entity separate from that of its partners. A limited liability partnership shall have perpetual succession and any change in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liability partnership.

Designated partners: Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India.

In case of a limited liability partnership in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such limited liability partnership or nominees of such bodies corporate shall act as designated partners.

Q-9 A and B are partners of AB & Co. sharing profits and losses in the ratio of 2:1 and C and D are partners of CD & Co. sharing profits and losses in the ratio of 3:2. On 1st April 2017, they decided to amalgamate and form a new firm M/s. AD & Co. wherein all the partners of both the firm would be partners sharing profits and losses in the ratio of 2:1:3:2 respectively to A, B, C and D.

Their balance sheets on that date w ere as under:

Liabilities	AB & Co. (Rs.)	CD & Co. (Rs.)	Assets	AB & Co. (Rs.)	CD & Co. (Rs.)
Capitals					
A	1,50,000	-	Building	75,000	90,000
B	1,00,000	-	Machinery	1,20,000	1,00,000
C	-	1,20,000	Furniture	15,000	12,000
D	-	80,000	Inventory	24,000	36,000
Reserve	66,000	54,000	Debtors	65,000	78,000
Creditors	52,000	35,000	Due from CD & Co.	47,000	-
Due to AB & Co.	-	47,000	Cash at Bank	18,000	15,000
			Cash in hand	4,000	5,000
	3,68,000	**3,36,000**		**3,68,000**	**3,36,000**

The amalgamated firm took over the business on the following terms:

(a) Building was taken over at Rs.1,00,000 and Rs.1,25,000 of AB & Co. and CD & Co. respectively and Machinery was taken over at Rs.1,25,000 and Rs.1,10,000 of AB & Co. and CD & Co. respectively.

(b) Goodwill of AB & Co. was worth Rs. 75,000 and that of CD & Co. was worth Rs. 50,000. Goodwill account was not to be opened in the books of the new firm, the adjustments being recorded through capital accounts of the partners.

(c) Provision for doubtful debts h as to be carried forward at Rs. 5,000 in respect of debtors of AB & Co. and Rs. 8,000 in respect of CD & Co.

You are required to:

(i) Compute the adjustments necessary for goodwill.

(ii) Pass the Journal Entries in the books of AD & Co. assuming that exces s/deficit capital (taking D's capital as base) with reference to share in profits are to be transferred t o current accounts.

(b) Under what circumstances, a partner may be called upon to pay the liabilities of LLP . Explain in brief.

Ans :

(a) (i) Adjustment for raising & writing off of goodwill

	Goodwill raised in old profit sharing ratio			Goodwill written off in new ratio	Difference
	AB & Co. Rs.	**CD & Co.** Rs.	**Total** Rs.	**AD & Co.** Rs.	Rs.
A	50,000		50,000 Cr.	31,250 Dr.	18,750 Cr.
B	25,000		25,000 Cr.	15,625 Dr.	9,375 Cr.
C	30,000	30,000 Cr.	46,875 Dr.	16,875 Dr.	
D	_____	20,000	20,000 Cr.	31,250 Dr.	11,250 Dr.
	75,000	50,000	1,25,000	1,25,000	

(ii) **In the books of AD & Co.**

Journal Entries

Date	Particulars		Debit Rs.	Credit Rs.
April 1, 2017	Building A/c	Dr.	1,00,000	
	Machinery A/c	Dr.	1,25,000	
	Furniture A/c	Dr.	15,000	
	Stock A/c	Dr.	24,000	
	Debtors A/c	Dr.	65,000	
	CD & Co. A/c	Dr.	47,000	
	Cash at bank A/c	Dr.	18,000	
	Cash in hand A/c	Dr.	4,000	
	To Provision for doubtful debts A/c			5,000
	To Creditors A/c			52,000
	To A's capital A/c (W.N. 2a)			2,10,667
	To B's capital A/c (W.N.2 a)			1,30,333
	(Being the sundry assets and liabilities of AB & Co. taken over at the values stated as per the agreement)			
April 1, 2017	Building A/c	Dr.	1,25,000	
	Machinery A/c	Dr.	1,10,000	
	Furniture A/c	Dr.	12,000	
	Stock A/c	Dr.	36,000	
	Debtors A/c	Dr.	78,000	
	Cash at bank A/c	Dr.	15,000	
	Cash in hand A/c	Dr.	5,000	
	To Provision for doubtful debts A/c			8,000
	To Creditors A/c			35,000
	To AB & Co. A/c			47,000
	To C's capital A/c (W.N. 2b)			1,74,600
	To D's capital A/c (W.N. 2b)			1,16,400

	(Being the sundry assets and liabilities of CD & Co. taken over at the values stated as per the agreement)			
	C's capital A/c	Dr.	16,875	
	D's capital A/c	Dr.	11,250	
	To A's capital A/c			18,750
	To B's capital A/c			9,375
	(Being adjustment in capital accounts of the partners on account of goodwill)			
	AB & Co. A/c	Dr.	47,000	
	To CD & Co. A/c			47,000
	(Being mutual indebtedness of AB & Co. and CD & Co. cancelled)			
	A's Capital A/c	Dr.	1,24,267	
	To A's Current A/c			1,24,267
	(Being excess amount in A's capital A/c transferred to A's current A/c - refer W.N.3)			
	B's Capital A/c	Dr.	87,133	
	To B's Current A/c			87,133
	(Being excess amount in B's capital A/c transferred to B's current A/c - refer W.N.3)			

Working Notes:

(1) Profit on Revaluation

	AB & Co. Rs.	CD & Co. Rs.
Building (1,00,000 – 75,000)	25,000	
(1,25,000 – 90,000)		35,000
Machinery (1,25,000 – 1,20,000)	5,000	
(1,10,000 – 1,00,000)		10,000
	30,000	45,000
Less: Provision for doubtful debts	(5,000)	(8,000)
	25,000	37,000

(2) Balance of capital accounts of partners on transfer of business to AD & Co.

(a) AB & Co.

	A's Capital Rs.	B's Capital Rs.
Balance as per the Balance Sheet	1,50,000	1,00,000
Reserves in the profits and losses sharing ratio	44,000	22,000
Profit on revaluation in the profits and losses sharing ratio (W.N.1)	16,667	8,333
	2,10,667	1,30,333

(b) CD & Co.

	C's Capital Rs.	D's Capital Rs.
Balance as per the Balance Sheet	1,20,000	80,000
Reserves in the profits and losses sharing ratio	32,400	21,600
Profit on revaluation in the profits and losses sharing ratio (W.N.1)	22,200	14,800
	1,74,600	**1,16,400**

(3) Calculation of capital of each partner in the new firm

Particulars	A Rs.	B Rs.	C Rs.	D Rs.
Balance as per W.N.2	2,10,667	1,30,333	1,74,600	1,16,400
Adjustment for goodwill	18,750	9,375	(16,875)	(11,250)
	2,29,417	1,39,708	1,57,725	1,05,150
Total capital Rs. 4,20,600*				
in the new ratio of 2:1:3:2	(1,05,150)	(52,575)	(1,57,725)	(1,05,150)
Transfer to Current Account	1,24,267 Cr.	87,133 Cr.	-	-

* Taking D's capital as the base which is 2/8th of total capital; total capital will be 1,05,150 x 8/2 i.e. Rs. 4,20,600.

(b) Under section 27 (3) of the LLP Act, 2008, any obligation of the LLP arising out of a contract or otherwise will be the sole obligation of the LLP. The partners of an LLP in the normal course of business are not liable for the debts of the LLP. However, under section 28 (2) of the LLP Act, 2008, a partner will be liable for his own wrongful acts or commissions, but will not be liable for the wrongful acts or commissions of other partners of the LLP.

Q-10 M, N and O were Partners sharing Profits and Losses in the ratio of 5:3:2 respectively. The Trial Balance of the Firm 31st March, 2017 was the following:

Particulars	Rs.	Rs.
Machinery at Cost	2,00,000	
Inventory	1,37,400	
Trade receivables	1,24,000	
Trade payables		1,69,400
Capital A/cs:		
M		1,36,000
N		90,000
O		46,000
Drawing A/cs:		
M	50,000	
N	46,000	
O	34,000	
Depreciation on Machinery		80,000
Profit for the year ended 31st March		2,48,600
Cash at Bank	1,78,600	
	7,70,000	**7,70,000**

Interest on Capital Accounts at 10% p.a. on the amount standing to the credit of Partners' Capital Account at the beginning of the year, was not provided before preparing the above Trial Balance. On the above date, they formed a company named MNO Private Limited Company with an Authorized Share Capital of 2,00,000 in shares of Rs. 10 each to be divided in different classes to take over the business of Partnership firm.

You are required as under:

1. Machinery is to be transferred at Rs. 1,40,000.
2. Shares in the Company are to be issued to the partners, at par, in such numbers, and in such classes as will give the partners, by reason of their shareholdings alone, the same rights as regards interest on capital and the sharing of profit and losses as they had in the partnership.
3. Before transferring the business, the partners wish to draw from the partnership profits to such an extent that the bank balance is reduced to Rs. 1,00,000. For this purpose, sufficient profits of the year are to be retained in profit-sharing ratio.
4. Assets and liabilities except Machinery and Bank, are to be transferred at their book value as on the above date.

You are required to prepare:

(i) Statement showing the workings of the Number of Shares of each class to be issued by the company, to each partner.

(ii) Capital Accounts showing all adjustments required to dissolve the Partnership.

(iii) Balance Sheet of the Company immediately after acquiring the business of the Partnership and Issuing of Shares.

(b) Can a partner be called upon to pay the liability of the LLP? If yes, under what circumstances?

Ans :

(i) Number of Shares to be issued to Partners

				Rs.
Assets: Machinery Rs. 1,40,000 + Inventory				
Rs. 1,37,400 + Trade Receivable Rs.1,24,000 + Bank Rs. 1,00,000				5,01,400
Less: Liabilities taken over				(1,69,400)
Net Assets taken over (Purchase Consideration)				3,32,000
Classes of Shares to be issued:	**M**	**N**	**O**	**Total**
10% Preference Shares of Rs. 10 each				
(to retain rights as to Interest on Capital)	1,36,000	90,000	46,000	2,72,000
Balance in Equity Shares of Rs. 10 each	30,000	18,000	12,000	60,000
(3,32,000 -2,72,000)				
(issued in profit sharing ratio)	**1,66,000**	**1,08,000**	**58,000**	**3,32,000**

(ii) Partners' Capital Accounts

Particulars	M	N	O	Particulars	M	N	O
To Drawings	50,000	46,000	34,000	By balance b/d	1,36,000	90,000	46,000
To 10% Preference share capital	1,36,000	90,000	46,000	By Interest on Capital	13,600	9,000	4,600
To Equity Shares	30,000	18,000	12,000	By profit for the year 5:3:2 (W.N. 1)	1,10,700	66,420	44,280
To Bank –Additional	54,300	17,420	6,880	By Machinery* A/c drawings (W.N. 2)	10,000	6,000	4,000
Total	**2,70,300**	**1,71,420**	**98,880**		**2,70,300**	**1,71,420**	**98,880**

* Gain on Transfer of Machinery = Rs. 1,40,000 – (Rs. 2,00,000-Rs. 80,000) = Rs. 20,000 in 5:3:2 ratio.

(iii) Balance sheet of MNO Ltd. as on 31st March, 2017 (after Takeover of Firm)

			Note no.	Rs.
I	**Equity and Liabilities:**			
	(1) Shareholders Funds			
	Share Capital		1	3,32,000
	(2) Current Liabilities			
	Trade Payables			1,69,400
		Total		5,01,400
II	**Assets**			
	(1) Non-Current Assets			
	Fixed Assets			
	Tangible Assets- Machinery			1,40,000
	(2) Current Assets:			
	(a) Inventories			1,37,400
	(b) Trade Receivables			1,24,000
	(c) Cash and Cash Equivalents			1,00,000
		Total		5,01,400

Notes to Accounts

	Particulars	Rs.
1.	Share capital	
	Authorized shares capital	20,00,000
	Issued, Subscribed & paid up	
	6,000 Equity Shares of Rs. 10 each	60,000
	27,200 10% Preference Shares capital of Rs. 10 each	2,72,000
	(All above shares issued for consideration other than cash,	
	in takeover of partnership firm)	**3,32,000**

Working Notes:

1. Profit & Loss Appropriation Account for the year ended 31st March, 2017

Particulars		Rs.	Rs.	Particulars	Rs.
To	Interest on Capital:			By Net Profit	2,48,600
	M [Rs. 1,36,000 x 10%]	13,600		(given)	
	N [Rs. 90,000 x 10%]	9,000			
	O [Rs. 46,000 x 10%]	4,600	27,200		
To	Profits transferred to Capital in				
	profit sharing ratio 5:3:2				
	M	1,10,700			
	N	66,420			
	O	44,280	2,21,400		
			2,48,600		**2,48,600**

2. Statement showing Additional Drawings in Cash

(a) Funds available for Drawings

	Total Drawing of Partners (given)	1,30,000
Add:	Further Funds available for Drawings (1,78,600-1,00,000)	78,600
		2,08,600
Less:	Interest on Capital	(27,200)
Amount available for Additional Drawings		1,81,400

(b) Ascertainment of Additional Drawings

Particulars	M	N	O
As per above statement Rs. 1,81,400			
(in profit sharing ratio)	90,700	54,420	36,280
Add: Interest	13,600	9,000	4,600
	1,04,300	63,420	40,880
Less: Already drawn	(50,000)	(46,000)	(34,000)
Additional Drawings	54,300	17,420	6,880

(c) Under section 27 (3) of the LLP Act, 2008, any obligation of the LLP arising out of a contract or otherwise will be the sole obligation of the LLP.

The partners of an LLP in the normal course of business are not liable for the debts of the LLP.

However, under section 28 (2) of the LLP Act, 2008, a partner will be liable for his own wrongful acts or commissions, but will not be liable for the wrongful acts or commissions of other partners of the LLP.

Thus a partner may be called to pay the liability of an LLP under exceptional circumstances.

Q-11 P, Q, R and S are sharing profits and losses in the ratio 3 : 3 : 2 : 1. Frauds committed by R during the year were found out and it was decided to dissolve the partnership on 31st March, 2019 when their Balance Sheet was as under:

Liabilities	Amount (₹)	Assets	Amount (₹)
Capitals:		Building	1,90,000
P	1,50,000	Stock	1,30,000
Q	1,50,000	Investments	50,000
R	-	Debtors	70,000
S	60,000	Cash	30,000
General reserve	40,000	R	40,000
Trade creditors	80,000		
Bills payable	30,000		
	5,10,000		**5,10,000**

Following information is given to you:

(i) A cheque for ₹ 7,000 received from debtor was not recorded in the books and was misappropriated by R.

(ii) Investments costing ₹ 8,000 were sold by R at ₹ 11,000 and the funds transferred to his personal account. This sale was omitted from the firm's books.

(iii) A creditor agreed to take over investments of the book value of ₹ 9,000 at ₹ 13,000. The rest of the creditors were paid off at a discount of 5%.

(iv) The other assets realized as follows:

Building 110% of book value

Stock ₹ 1,20,000

Investments The rest of investments were sold at a profit of ₹ 7,000

Debtors The rest of the debtors were realized at a discount of 10%

(v) The bills payable were settled at a discount of ₹ 500.

(vi) The expenses of dissolution amounted to ₹ 8,000

(vii) It was found out that realization from R's private assets would only be ₹ 7,000.

Prepare Realization Account, Cash Account and Partner's Capital Accounts. All workings should part of your answer.

Ans.

Realization Account

Particulars		₹	Particulars		₹
To Building		1,90,000	By Trade creditors		80,000
To Stock		1,30,000	By Bills payable		30,000
To Investment		50,000	By Cash		
To Debtors		70,000	Building	2,09,000	
To Cash-creditors paid (W.N.1)			63,650	Stock	1,20,000
To Cash-expenses		8,000	Investments (W.N.2)	40,000	
To Cash-bills payable (30,000-500)		29,500	Debtors (W.N. 3)	56,700	4,25,700
To Partners' Capital A/cs			By R – (Receipt from Debtors unrecorded)		7,000
P	4,183		By R - Receipt from Investments unrecorded		11,000
Q	4,183				
R	2,789				
S	1,395	12,550			
		5,53,700			**5,53,700**

Cash Account

Particulars		Amount ₹	Particulars	Amount ₹
To Balance b/d		30,000	By Realization-creditors paid	63,650
To Realization – assets realized			By Realization-bills payable	29,500
Building	2,09,000		By Realization-expenses	8,000
Stock	1,20,000		By Capital accounts:	
Investments	40,000		P	1,51,132
Debtors	56,700	4,25,700	Q	1,51,132
To R's capital A/c		7,000	S	59,286
		4,62,700		**4,62,700**

Partners' Capital Accounts

Particulars	P ₹	Q ₹	R ₹	S ₹	Particulars	P ₹	Q ₹	R ₹	S ₹
To Balance b/d			40,000		By Balance b/d	1,50,000	1,50,000	-	60,000
To Realization A/c-Debtors misappropriation			7,000		By General reserve	13,333	13,333	8,889	4,445
To Realization A/c-Investment - misappropriation			11,000		By Realization profit	4,183	4,183	2,789	1,395
To R's capital A/c (W.N. 4)	16,384	16,384		6,554	By Cash A/c			7,000	
To Cash A/c	1,51,132	1,51,132		59,286	By P's capital A/c			16,384	
					By Q's capital A/c			16,384	
					By S's capital A/c			6,554	
	1,67,516	**1,67,516**	**58,000**	**65,840**		**1,67,516**	**1,67,516**	**58,000**	**65,840**

Working Notes:

1. Amount paid to creditors in cash

	₹
Book value	80,000
Less: Creditors taking over investments	(13,000)
	67,000
Less: Discount @ 5%	(3,350)
	63,650

2. Amount received from sale of investments

	₹
Book value	50,000
Less: Misappropriated by R	(8,000)
	42,000
Less: Taken over by a creditor	(9,000)
	33,000
Add: Profit on sale of investments	7,000
Cash received from sale of remaining investment	40,000

3. Amount received from debtors

	₹
Book value	70,000
Less: Unrecorded receipt	(7,000)
	63,000
Less: Discount @ 10%	(6,300)
	56,700

4. Deficiency of R

	₹
Balance of capital as on 31st March, 2019	40,000
Debtors-misappropriation	7,000
Investment-misappropriation	11,000
	58,000
Less: Realization Profit	(2,789)
General reserve	(8,889)
Contribution from private assets	(7,000)
Net deficiency of capital	39,322

This deficiency of ₹ 39,322 in R's capital account will be shared by other partners P, Q and S in their capital ratio of 15 : 15 : 6.by

Accordingly,

P's share of deficiency = [39,322 x (15/36)] = ₹ 16,384

Q's share of deficiency = [39,322 x (15/36)] = ₹ 16,384

S's share of deficiency = [39,322 x (6/36)] = ₹ 6,554

Q-12 A partnership firm was dissolved on 30th June, 2018. Its Balance Sheet on the date of dissolution was as follows:

Capitals:			Cash	21,600
A	1,52,000		Sundry Assets	3,78,400
B	96,000			
C	72,000	3,20,000		
Loan A/c - B		20,000		
Sundry Creditors		60,000		
		4,00,000		4,00,000

The assets were realized in instalments and the payments were made on the proportionate capital basis. Creditors were paid Rs.58,000 in full settlement of their account. Expenses of realization were estimated to be Rs.10,800 but actual amount spent was Rs.8,000. This amount was paid on 15th September. Draw up a statement showing distribution of cash, which was realized as follows:

	Rs.
On 5th July, 2018	50,400
On 30th August, 2018	1,20,000
On 15th September, 2018	1,60,000

The partners shared profits and losses in the ratio of 2 : 2 :1. Prepare a statement showing distribution of cash amongst the partners by 'Highest Relative Capital' method.

Ans. Statement showing distribution of cash amongst the partners

2018		**Creditors Rs.**	**B's Rs.**	**A Rs.**	**B Rs.**	**C Rs.**
Jun-30						
Balance b/d		60,000	20,000	1,52,000	96,000	72,000
Cash balance less Provision for expenses (Rs.21,600-Rs.10,800)		10,800	-	-	-	-
Balances unpaid		49,200	20,000	1,52,000	96,000	72,000
Jul-05						
1st Instalment of Rs.50,400		47,200	3,200	-	-	-
Discount received on full settlement		2,000	16,800	1,52,000	96,000	72,000
Less: Transferred to Realisation A/c						
Aug-30						
2nd instalment of Rs.1, 20,000 (W.N. 2)			16,800	65,280	9,280	28,640
Balance unpaid				86,720	86,720	43,360
Sep-15						
Amount realised	Rs.1,60,000					
Add: Balance out of the Provision for Expenses A/c	2,800					
	1,62,800			65,120	65,120	32,560
Amount unpaid being loss on Realisation in the ratio of 2 : 2 : 1				21,600	21,600	10,800

Working Notes:

1. Heighest relative capital basis

	A	B	C
	Rs.	Rs.	Rs.
1. Present Capitals	1,52,000	96,000	72,000
2. Profit sharing ratio	2	2	1
3. Capital per unit of Profit share (1 + 2)	76,000	48,000	72,000
4. Proportionate capitals taking B, whose capital is the least, as the basis	96,000	96,000	48,000
5. Excess capital (1-4)	56,000	Nil	24,000
6. Profit-sharing ratio	2	-	1
7. Excess capital per unit of Profit share (5 + 6)	28,000	-	24,000
8. Proportionate capitals as between A and C taking C capital as the basis	48,000	-	24,000
9. Excess of A's Capital over C's Excess capital (5-8)	8,000	-	-
10. Balance of Excess capital (5-9)	48,000	-	24,000
11. Distribution sequence:			
First Rs.8,000 (2:0:0)	8,000	-	-
Next Rs.72,000 (2:0:1)	48,000	-	24,000
Over Rs.80,000 (2:2:1)			

2. Distribution of Second instalment

	Creditos	A	B	C
First Rs.16,800	16,800	-	-	-
Next Rs.8,000 (2:0:0)		8,000	-	-
Next Rs.72,000 (2:0:1)		48,000	-	24,000
Balance Rs.23,200 (2 : 2 : 1)	9,280	9,280	4,640	1,20,000
	16,800	65,280	9,280	28,640

Q-13 A, B and C are in partnership sharing profits and losses in the ratio of 5:4:4. The Balance Sheet of the firm as on 31st March, 2018 is as below:

Liabilities	Rs.	Assets	Rs.
A's Capital	1,20,000	Factory Building	1,93,280
B's Capital	80,000	Plant and Machinery	1,30,200
C's Capital	1,00,000	Trade Receivables	43,200
B's Loan	36,000	Inventories	99,120
Trade Payables	1,32,000	Cash at Bank	2,200
	4,68,000		4,68,000

On Balance Sheet date, all the three partners have decided to dissolve their partnership. The partners decided to distribute amounts as and when feasible and for this purpose they appoint C who was to get as his remuneration 1% of the value of the assets realised other than cash at bank and 10% of the amount distributed to the partners.

Assets were realised piecemeal as under:

	Rs.
First instalment	1,49,200
Second instalment	1,38,602
Third instalment	80,000
Last instalment	56,000
Dissolution expenses were provided for estimated amount of	Rs.2400
The trade payables were were settled finally for	Rs.1,27,000

You are required to prepare a statement showing distribution of cash amongst the partners by "Highest Relative Capital Method".

Ans. Statement showing distribution of cash amongst the partners.

		Trade Payable	B's Loan	A Rs.	B Rs.	C Rs.
Balance Due		1,32,000	36,000	1,20,000	80,000	1,00,000
Including 1st Instalment amount with the firm Rs.(2,200 + 1,49,200)	1,51,400					
Less: Dissolution expenses provided for	(24,000)					
	1,27,400					
Less: C's remuneration of 1% on assets realized (1,49,200x1%)	(1,492)					
	1,25,908					
Less: Payment made to Trade Payables	1,25,908	1,25,908				
Balance due	NIL	6,092				
2nd instalment realised	1,38,602					
Less: C's remuneration of 1% on assets realized (1,38,602x1%)	(1,386)					
	1,37,216					
Less: Payment made to Trade Payables	(1,292)	(1,292)				
Transferred to P& L A/c		4,800				
	1,35,924					
Less: Payment for B's loan A/c	36,000		36,000			
Amount available for distribution to partners	99,924		Nil			
Less: C's remuneration of 10% of the amount distributed to partners (99,924 x 10/110)	(9,084)					
Balance to be distributed to partners on the basis of HRCM	90,840					
Less: Paid to C (W.N.)	(4,000)					(4,000)
	86,840					96,000
Less: Paid to A and C in 5:4 (W.N.)	(36,000)			20,000		16,000
Balance due	50,840			1,00,000	80,000	80,000
Less: Paid to A, B & C in 5:4:4	50,840			(19,554)	15,643	(15,643)

	Nil					
Amount of 3rd instalment	80,000			80,446	64,357	64,357
Less: C's remuneration of 1% on assets realized (80,000x1%)	(800)					
	79,200					
Less: C's remuneration of 10% of the amount distributed to partners (79,200 x 10/110)	(7,200)					
	72,000					
Less: Paid to A, B, C in 5:4:4 for (W.N.)	(72,000)			(27,692)	22,154	(22,154)
	nil			52,754	42,203	42,203
Amount of 4th and last instalment	56,000					
Less: C's remuneration of 1% on assets realized (56,000x1%)	(560)					
	55,440					
Less: C's remuneration of 10% of the amount distributed to partners (55,440 x 10/110)	(5,040)					
Less: Paid to A, B and C in 5:4:4	50,400					
				(19.384)	15.508	(15.508)
Loss suffered by partners				33,370	26,695	26,695

Working Note:

(i) Rs.2,200 added to the first instalment received on sale of assets represents the Cash in Bank

(ii) The amount due to Creditors at the end of the utilization of First Instalment is Rs.6,092. However, since the creditors were settled for Rs. 1,27,200 only the balance Rs. 1,292 were paid and the balance Rs. 4,800 was transferred to the Profit & Loss Account.

(iii) **Highest Relative Capital Basis**

	A (Rs.)	B (Rs.)	C (Rs.)
Balance of Capital Accounts (1)	1,20,000	80,000	1,00,000
Profit sharing ratio	5	4	4
Capital Profit sharing ratio	24,000	20,000	25,000
Capital in profit sharing ratio taking B's Capital as base (2)	1,00,000	80,000	80,000
Excess of A's Capital and C's Capital 1 -2) =(3)	20,000	Nil	20,000
Again repeating the process			
Profit sharing ratio	5		4
Capital Profit sharing ratio	4,000		5,000
Capital in profit sharing ratio taking A's Capital as base (4)	20,000		16,000
Excess of C's Capital (3-4)=(5)	nil		4,000

Therefore, firstly Rs.4,000 is to be paid to C, then A and C to be paid in proportion of 5:4 up to Rs.36,000 to bring the capital of all partners A, B and C in proportion to their profit sharing ratio. Thereafter, balance available will be paid in the profit sharing ratio 5:4:4 to all partners viz A, B and C.

Q-14 Aman, Baal and Chand share profits and losses of a business as to 3:2:1 respectively. Their balance sheet as at 31st March, 2017 was as follows:

Liabilities	Rs.	Assets	Rs.
Capital Accounts:		Goodwill	10,000
Aman	70,000	Land	20,000
Baal	80,000	Buildings	1,10,000
Chand	10,000	Machinery	50,000
General Reserve	18,000	Motor Car	28,000
Investment Fluctuation Fund	4,000	Furniture	12,000
Chand's Loan	33,000	Investments	18,000
Mrs. Aman's loan	15,000	Loose tools	7,000
Creditors	96,000	Stock	18,000
Bills Payable	14,000	Bills receivable	20,000
Bank overdraft	60,000	Debtors: 40,000	
		Less; Provision 2,000	38,000
		Cash	1,000
		Chand's current A/c	56,000
		Profit and Loss A/c	12,000
	4,00,000		4,00,000

The partners decide to convert their firm into a Joint Stock Company. For this purpose ABC Ltd. was formed with an authorized capital of Rs.10,00,000 divided into Rs.100 equity Shares. The business of the firm was sold to the company as at the date of balance sheet given above on the following terms:

(i) Motor car, furniture, investments, loose tools, debtors and cash are not to be taken over by the company.

(ii) Liabilities for bills payable and bank overdraft are to be taken over by the company.

(iii) The purchase price is settled at Rs.1,95,500 payable as to Rs.75,500 in cash and the balance in company's fully paid shares of Rs.100 each.

(iv) The remaining assets and liabilities of the firm are directly disposed of by the firm as per details given below:

Investments are taken over by Aman for Rs.13,000; debtors realize in all Rs.20,000; Motor Car, furniture and loose tools fetch Rs.24,000, Rs.4,000, and Rs.1,000 respectively. Aman agrees to pay his wife's loan. The creditors were paid Rs.94,000 in final settlement of their claims. The realization expenses amount to Rs.500.

(v) The equity share received from the vendor company are to be divided among the partners in profit-sharing ratio.

You are required to ***prepare the necessary ledger accounts*** in the books of the partnership firm.

(b) ***Explain*** the Limitations of Liability of Limited Liability Partnership (LLP) and its partners.

Ans. **Necessary Ladger Accounts in the books of Partnership Firm**

Realization Account

Particulars	Rs.	Rs.	Particulars	Rs.	Rs.
To Goodwill		10,000	By provision to doubtful Debts		2,000
To land		20,000	By Trade creditors		96,000
To Buildings		1,10,000	By Bills Payable		14,000
To Machinery		50,000	By Bank overdraft		60,000
To Motor Car		28,000	By Mrs. Aman's loan		15,000
To Furniture		12,000	By ABC Ltd. (Purchase price)		1,95,500
To Investments		18,000	By Aman's Capital A/c (Investments taken over)		13,000
To Loose tools		7,000	By Cash A/c:		
To Stock		18,000	Debtors	20,000	
To Bill receivable		20,000	Motor Car	24,000	
To Debtors		40,000	Furniture	4,000	
To Aman's Capital A/c (Mrs. Aman's Loan)		15,000	Loose tools	1,000	49,000
To Cash A/c:					
Creditors	94,000				
Realization expenses	500	94,500			
To Profit on Realization t/fto:					
Aman's Capital A/c	1,000				
Baal's Capital A/c	667				
Chand's Capital A/c	333	2,000			
		4,44,500			4,44,500

ABC Ltd. Account

Particulars	Rs.	Particulars	Rs.
To Realization A/c	1,95,000	By Cash A/c	75,500
		By Share in ABC Ltd.	1,20,000
	1,95,500		1,95,500

Partners' Capital Account

Particulars	Aman Rs.	Baal Rs.	Chand Rs.	Particular	Aman Rs.	Baal Rs.	Chand Rs.
To Profit and Loss A/c	6,000	4,000	2,000	By Balance c/d	70,000	80,000	10,000
To Realization A/c	13,000	-	-	By Chand's Loan A/c	-	-	33,000
To Chand's Current A/c	-	-	56,000	By General reserve	9,000	6,000	3,000
To shares in ABC Ltd.	60,000	40,000	20,000	By Investment Fluctuation Fund*	2,000	1,333	667
To Cash A/c	18,000	44,000	-	By Realization A/c	1,000	667	333
				By Realization A/c (Mrs. Aman's loan A/c)	15,000	-	-
				By Cash A/c	-		31,000
	97,000	**88,000**	**78,000**		**97,000**	**88,000**	**78,000**

*Alternatively, Investment Fluctuation Fund Account may be transferred to Realization Account.

Chand's Current Account

Particulars	Rs.	Particulars	Rs.
To Balance b/d	56,000	By Chand's Capital A/c transfer	56,000
	56,000		56,000

Share in ABC Ltd. Account

Particulars	Rs.	Particulars	Rs.
To ABC Ltd. Account	1,20,000	By Aman's Capital A/c	60,000
		By Baal's Capital A/c	40,000
		By Chand's Capital A/c	20,000
	1,20,000		1,20,000

Cash Account

Particulars	Rs.	Particulars	Rs.
To Balance b/d	1,000	By Realization A/c (Liabilities and expenses)	94,500
To ABC Ltd.	75,500	By Aman's Capital A/c	18,000
To Realization A/c (sale of assets)	49,000	By Baal's Capital A/c	44,000
To Chand's Capital A/c	31,000		-
	1,56,500		1,56,500

(b) Under section 27 (3) of the LLP Act, 2008 an obligation of an LLP arising out of a contract or otherwise, shall be solely the obligation of the LLP. The limitations of liability of an LLP and its partners are as follows:

* The Liabilities of an LLP shall be met out of the properties of the LLP;
* A partner is not personally liable, directly or indirectly (for an obligation of an LLP arising out of a contract or otherwise), solely by reason of being a partner in the LLP;
* An LLP is not bound by anything done by a partner in dealing with a person, if:
  - The partner does not have the authority to act on behalf of the LLP in doing a particular act; and
  - The other person knows that the partner has no authority or does not know or believe him to be a partner in the LLP
* The liability of the LLP and the partners perpetrating fraudulent dealings shall be unlimited for all or any of the debts or other liabilities of the LLP.

Q-15 The following is the Balance Sheet of M/s Red and Black as on 31st March, 2018:

Liabilities		(₹)	Assets	(₹)
Red's Capital	80,000		Building	1,00,000
Black's Capital	1,00,000	1,80,000	Closing Stock	60,000
Red's Loan		20,000	Sundry Debtors	40,000
General Reserve		20,000	Investment	40,000
Sundry Creditors		40,000	(6% Debentures in Cool Ltd.)	
			Cash	20,000
		2,60,000		**2,60,000**

It was agreed that Mr. White is to be admitted for a fifth share in the future profits from 1st April, 2018. He is required to contribute cash towards goodwill and ₹ 20,000 towards capital.

(a) The following further information is furnished:

(i) The partners Red and Black shared the profits in the ratio of 3 : 2.

(ii) Mr. Red was receiving a salary of ₹ 1,000 p.m. from the very inception of the firm in addition to the share of profit.

(iii) The future profit ratio between Red, Black and White will be 3 : 1 : 1. Mr. Red will not get any salary after the admission of Mr. White.

(iv) The goodwill of the firm should be determined on the basis of 2 years' purchase of the average profits from business of the last 5 years. The particulars of profits/losses are as under :

Year Ended	(₹)	Profit/Loss
31.3.2014	40,000	Profit
31.3.2015	20,000	Loss
31.3.2016	40,000	Profit
31.3.2017	50,000	Profit
31.3.2018	60,000	Profit

The above profits and losses are after charging the salary of Mr. Red. The profit of the year ended 31st March, 2014 included an extraneous profit of ₹ 60,000 and the loss for the year ended 31st March, 2015 was on account of loss by strike to the extent of ₹ 40,000.

(v) It was agreed that the value of the goodwill should not appear in the books of the firm.

(b) Trading profit for the year ended 31st March, 2019 was ₹ 80,000 (Before charging depreciation)

(c) Each partner had drawn ₹ 2,000 per month as drawing during the year 2018-19.

(d) On 31st March, 2019 the following balances appeared in the books:

Building (Before Depreciation)	₹ 1,20,000
Closing Stock	₹ 80,000
Sundry Debtors	Nil
Sundry Creditors	Nil
Investment	₹ 40,000

(e) Interest was @ 6% per annum on Red's loan was not paid during the year.

(f) Interest on Debenture was received during the year.

(g) Depreciation is to be provided @ 5% on Closing Balance of Building.

(h) Partners applied for conversion of the firm into a private Limited Company i.e. RBW Private Limited. Certificate received on 1.4.2019.

They decided to convert Capital accounts of the partners into share capital, in the ratio of 3: 1: 1 (on the basis of total Capital as on 31.3.2019). If necessary, partners have to subscribe to fresh capital or withdraw. You are required to prepare :

(1) Profit & Loss Account for the year ended 31st March, 2019 in the books of M/s Red and Black.

(2) Balance Sheet as on 1st April, 2019 in the books of RBW Private Limited.

Ans.

M/s Red, Black and White

Statement of Profit & Loss for the year ended on 31st March, 2019

	₹		₹
To Depreciation on Building (1,20,000 x 5%)	6,000	By Trading Profit	80,000
To Interest on Red's loan (20,000 x 6%)	1,200	By Interest on Debentures	2,400
To Net Profit to :			
Red's Capital A/c	45,120		
Black's Capital A/c	15,040		
White's Capital A/c	15,040		
	82,400		**82,400**

Balance Sheet of the RBW Pvt. Ltd. as on 1-4-2019

		Notes No.	₹
I **Equity and Liabilities**			
Shareholders funds			
2,39,040			
Non-current liabilities			
Long term borrowings		1	21,200
		Total	2,60,240
II **Assets**			
Non-current assets			
Property, Plant & Equipment			
Tangible assets		2	1,14,000
Non-current investments			40,000
Current assets			
Inventories			80,000
Cash and cash equivalents			26,240
		Total	**2,60,240**

Notes to Accounts

		₹	
1. Borrowings			
Loan from Red		21,200	
2. Tangible assets			
Land and Building ₹ (1,20,000 - 6,000)		1,14,000	

Working Notes :

1. Calculation of goodwill

Year ended March, 31

	2014 ₹	2015 ₹	2016 ₹	2017 ₹	2018 ₹
Book Profits	40,000	(20,000)	40,000	50,000	60,000
Adjustment for extraneous profit of 2014 and abnormal loss for 2015	(60,000)	40,000	-	-	-
	(20,000)	20,000	40,000	50,000	60,000
Add Back: Remuneration of Red	12,000	12,000	12,000	12,000	12,000
	(8,000)	32,000	52,000	62,000	72,000
Less: Debenture Interest being non-operating income	(2,400)	(2,400)	(2,400)	(2,400)	(2,400)
	(10,400)	29,600	49,600	59,600	69,600
Total Profit from 2015 to 2018					2,08,400
Less: Loss for 2014					(10,400)
Accumulated Profit					1,98,000
Average Profit					39,600
Goodwill equal to 2 years' purchase					79,200
Contribution from White, equal to 1/5					15,840

2. **Partners' Capital Accounts**

	Red ₹	Black ₹	White ₹		Red ₹	Black ₹	White ₹
To Drawings	24,000	24,000	24,000	By Balance b/d	80,000	1,00,000	-
To Black A/c			15,840	By General	12,000	8,000	-
To Balance c/d	1,13,120	1,14,880	11,040	Reserve			
				By White A/c		15,840	-
				By Bank A/c	-	-	35,840
				By Profit & Loss A/c	45,120	15,040	15,040
	1,37,120	**1,38,880**	**50,880**		**1,37,120**	**1,38,880**	**50,880**

3. Balance Sheet as on 31st March, 2019

Liabilities	₹	₹	**Assets**	₹	₹
Red's Capital		1,13,120	Land & Building	1,20,000	
Black's Capital		1,14,880	Less: Depreciation	(6,000)	1,14,000
White's Capital		11,040	Investments		40,000
Red's Loan	20,000		Stock-in-trade		80,000
Add: Interest due	1,200	21,200	Cash (Balancing figure)		26,240*
		2,60,240			**2,60,240**

4. Conversion into Company

		₹
Capital:	Red	1,13,120
	Black	1,14,880
	White	11,040
Share Capital		2,39,040
Distribution of share:	Red (3/5)	1,43,424
	Black (1/5)	47,808
	White (1/5)	47,808

Red should subscribe shares of ₹ 30,304 (₹ 1,43,424 - ₹ 1,13,120) and White should subscribe shares of ₹ 36,768 (₹ 47,808 less 11,040). Black withdraws ₹ 67,072 (₹ 47,808 - ₹ 1,14,880).

5 Adjustment for Goodwill

	To be raised in old Raio	To be written off in new ratio	Difference
Red	47,520	47,520	Nil
Black	31,680	15,840	15,840 Cr.
White		15,840	15,840 Dr.

6. Closing cash balance* can also be derived as shown below:

	₹	₹
Trading profit (assume realised)		80,000
Add: Debenture Interest		2,400
Add: Decrease in Debtors Balance		40,000
		1,22,400

Less: Increase in stock	20,000	
Less: Decrease in creditors	40,000	(60,000)
Cash Profit		62,400
Add: Opening cash balance		20,000
Add: Cash brought in by White		35,840
		1,18,240
Less: Drawings	72,000	
Less: Additions to Building	20,000	(92,000)
		26,240

Q-16 Aman, a readymade garment trader, keeps his books of account under single entry system. On the closing date, i.e. on 31st March, 2017 his statement of affairs stood as follows:

Liabilities	Amount ₹	Assets	Amount ₹
Aman's Capital	4,80,000	Building	3,25,000
Loan	1,50,00	Furniture	50,000
Creditors	3,10,00	Motor car	90,000
		Stock	2,00,000
		Debtors	1,70,00
		Cash in hand	20,000
		Cash at bank	85,000
	9,40,00		**9,40,000**

Riots occurred and a fire broke out on the evening of 31st March, 2018, destroying the books of accounts. On that day, the cashier had absconded with the available cash. You are furnished with the following information:

1. Sales for the year ended 31st March, 2018 were 20% higher than the previous year's sales, out of which, 20% sales were for cash. He always sells his goods at cost plus 25%. There were no cash purchases.
2. Collection from debtors amounted to ₹ 14,00,000, out of which ₹ 3,50,000 was received in cash.
3. Business expenses amounted to ₹ 2,00,000, of which ₹ 50,000 were outstanding on 31st March, 2018 and ₹ 60,000 paid by cheques.
4. Gross profit as per last year's audited accounts was ₹ 3,00,000.
5. Provide depreciation on building and furniture at 5% each and motor car at 20%.
6. His private records and the Bank Pass Book disclosed the following transactions for the year 2017-18:

	₹
Payment to creditors (paid by cheques)	13,75,000
Perosnal drawings (paid by cheques)	75,000
Repairs (paid by cash)	10,000
Travelling expenses (paid by cash)	15,000
Cash deposited in bank	7,15,000
Cash withdran from bank	1,20,000

7. Stock level was maintained at ₹ 3,00,000 all throughout the year.
8. The amount defalcated by the cashier is to be written off to the Profit and Loss Account.

You are required to prepare Trading and Profit and Loss A/c for the year ended 31st March, 2018 and Balance Sheet as on that date of Aman. All the workings should form part of the answer.

Ans : Trading and Profit and Loss Account of Aman for the year ended 31st March, 2018

	₹		₹
To Opening Stock	2,00,000	By Sales	18,00,000
To Purchases (Bal. fig.)	15,40,000	By Closing Stock	3,00,000
To Gross Profit c/d	3,60,000		
	21,00,000		21,00,000
To Business Expenses	2,00,000	By Gross Profit b/d	3,60,00
To Repairs	10,000		
To Depreciation :			
Building 16,250			
Machinery 2,500			
Motor Car 18,000	36,750		
To Travelling Expenses	15,000		
To Loss by theft (cash defalcated	20,000		
To Net profit	78,250		
	3,60,000		3,60,000

Balance Sheet of Aman as at 31st March, 2018

Liabilites	₹	₹	Assets	₹	₹
Capital	4,80,000		Building	3,25,000	
Add:			Less : Depreciation	16,250	3,08,750
Net Profit	78,250		Furniture	50,000	
Drawings	75,000	4,83,250	Less : Depreciation	2,500	47,500
Loan		1,50,000	Motor Car	90,000	
			Less : Depreciation	18,000	72,000
Sundry Creditors		4,75,000	Stock in Trade		3,00,000
Outstanding business			Sundry Debtors		2,10,000
Expenses		50,000	Bank Balance		2,20,000
		11,58,250			11,58,250

Working Notes :

1. Cash and Bank Account

Particular	Cash	Bank	Particulars	Cash	Bank
To Balance b/d	20,000	85,000	By Payment to Creditors	-	13,75,000
To Collection from Debtors	3,50,000	10,50,000	By Business Expenses	90,000	60,000
To Sales (18,00,000 x 20%)	3,60,000	-	By Repair	10,000	-
To Cash (C)	-	7,15,000	By Cash (C) (withdrawal)		1,20,000
			By Bank (c)	7,15,000	
To Bank (C)	1,20,000	-	By Travelling Expenses	15,000	-
			By Private Drawings	-	75,000
			By Balance c/d		2,20,000
			By Cash defalcated (balancing fig.)	20,000	
	8,50,000	18,50,000		8,50,000	18,50,000

2. Calculation of sales during 2017-18

Gross profit (last year i.e. for year ended 31-3-2017)	3,00,000
Goods sold at cost plus 25% i.e. 20% of sales	15,00,000
Sales for 2016-17 3,00,000/0.2	
Sales for 2017-18 (15,00,000 x 1.2)	18,00,000
Credit sales for 2017-18	17,40,000 (80% of 18,00,000)

3. Debtors Acounting

To Bal. b/d	1,70,000	By	Cash	3,50,000
To Sales (18,00,000 x 80%)	14,40, 000	By	Bank	10,50,000
		By	Bal. c/d	2,10,000
	16,10,000			16,10,000

4. Creditors Account

To Bank	13,75,000	By	Bal. b/d	3,10,000
To Bal. c/d (bal. fig.)	4,75,000	By	Purchases	15,40,000
	18,50,000			18,50,000

Q-17 A and B carrying on business in partnership sharing profits and losses equally, wished to dissolve the firm and sell the business to AB Limited Company on 31.03.2018 when the firm's position was as follows:

Liabilities	Rs.	Assets	Rs.
A's Capital	7,50,000	Land & Building	5,00,000
B's Capital	5,00,000	Furniture	2,00,000
Sundry Creditors	3,00,000	Stock	5,00,000
		Debtors	3,30,000
		Cash	20,000
	15,50,000		**15,50,000**

The arrangement with AB Limited Company was as follows:

(I) Land and Building was purchased at 20% more than the book value.

(II) Furniture and stock were purchased at book value less 15%.

(III) The Goodwill of the firm was valued at ₹ 2,00,000.

(IV) The firm's debtors, cash and creditors were not to be taken over, but the company agreed to collect the book debts of the firm and discharge the creditors of the firm as an agent, for which services the company was to be paid 5% on all collections from the firm's debtors and 3% on cash paid to firm's creditors.

(v) The purchase price was to be discharged by the company in fully paid equity shares of ₹ 10 each at a premium of ₹ 2 per share.

The company collected all the amounts from the debtors. The creditors were paid off less by ₹ 5,000 allowed as discount. The company paid the balance due to the vendors in cash.

Prepare the Realisation A/c, the Capital Accounts of the Partners and the Cash Account in the books of the Partnership firm.

(b) Write short notes on extent of liability of LLP and its Partners.

Ans.

(a) **In the Books of Partnership Firm - Realization Account**

	Rs.			Rs.
To Land & Building	5,00,000	By Sdundry Creditors		3,00,000
To Funiture	2,00,000	By AB Ltd. Co. Puchase		13,95,000
To Stock	5,00,000	consideration - (W.N.1)		
To Debtors	3,30,000	By AB Ltd. Company	3,30,000	
		Sundry Debtors		
To AB Ltd. Co. Sundry Creditors	2,95,000	Less :Commission		
(3,00,000 Less 5,000)		5% on 3,30,000	16,500	3,13,500
To AB Ltd. Co.	8,850			
(Commission 3% on 2,95,000)				
To Profit transferred to :				
A's Capital A/c 87,325				
B's Capital A/c 87,325	1,74,650			
	20,08,500		20,08,500	

Capital Account of Partners

	A	B		A	B
	₹	₹		₹	₹
To Shares in AB Ltd.Co. (W.N.2)	8,19,900	5,75,100	By Balance b/d	7,50,000	5,00,000
To Cash - Final Payment	17,425	12,225	By Realization a/c Profit	87,325	87,325
	8,37,325	5,87,325		8,37,325	5,87,325

Cash Account

	₹		₹
To Balance b/d	20,000	By A's capital A/c Final payment	17,425
To AB Ltd. Co. (Amount realized		By B's Capital A/c Final Payment	12,225
from Debtors less amount			
paid to creditors) - (W.N.3)	9,6,50		
	29,650		29,650

Working Notes:

1. **Calculation of Purchases Consideration :**

Land & Building	6,00,000
Furniture	1,70,000
Stock	4,25,000
Goodwill	2,00,000
	13,95,000

2. **Distribution of shares among partners**

The shares received from the company have been distributed between the two partners A & B in the ratio of their final claims i.e., 8,37,325: 5,87,325*.

No. of shares received from the company = 13,95,000/12= 1,16,250

A gets [(1,16,250 X 8,37,325)/14,24,650] = 68,325 shares valued at 68,325 x 12 = Rs.8,19,900. B gets the remaining 47,925 shares, valued at Rs. 5,75,100 (47,925 x 12)

3. **Calculation of net amount received from AB Ltd on account of amount realized from debtors less amount paid to creditors.**

	Rs.
Amount realized from Debtors	3,30,000
Less: Commision for realization from debtors (5% on 3,30,000)	16,500
	3,13,500
Less: Amount paid to creditor	2,95,000
	18,500
Less: Commission for cash paid to creditors (3% on 2,95,000)	8,850
Net amount received	9,650

"Note: In the above situation, shares received from AB Ltd. Company have been

distributed between two partners A and B in the ratio of their final claims. Alternatively, shares received from AB Ltd. can be distributed among the partners in their profit sharing ratio i.e. ₹ 13,95,000 x 1/2 = ₹ 6,97,500 each. In that case, firm will pay cash amounting ₹ 1,39,825 to A and will receive cash ₹ 1,10,175 from B. Partners' capital accounts and cash account will, accordingly get changed.

(b) Extent of Liability of LLP and its partners

Every partner of an LLP for the purpose of its business is an agent of the LLP but is not an agent of other partners. Obligations of LLP are solely its obligations and liabilities of LLP are to be met out of properties of LLP.

The partners of an LLP in the normal course of business are not liable for the debts of the LLP. The LLP is liable if a partner of LLP is liable to any person as a result of wrongful or omission on his part in the course of business of the LLP or with his authority. However, a partner will be liable for his own wrongful acts or commissions, but will not be liable for the wrongful acts or commissions of other partners of the LLP. Thus a partner may be called to pay the liability of an LLP under exceptional circumstances.

If an LLP or any of its partners act with the intent to defraud creditors of the LLP or any other person or for any fraudulent purpose, then the liability of the LLP and the concerned partners is unlimited. However, where the fraudulent act is carried out by a partner, the LLP is not liable if it is established by the LLP that the act was without the knowledge or authority of the LLP. Where the business is carried out with fraudulent intent or for fraudulent purpose, every person who was knowingly a party is punishable with imprisonment and fine.

Q-18 M, N and O were Partners sharing Profits and Losses in the ratio of 5:3:2 respectively. The Trial Balance of the Firm as on 31st March, 2020 was the following:

Particulars	₹	₹
Machinery at Cost	2,00,000	
Inventory	1,37,400	
Trade receivables	1,24,000	
Trade payables		1,69,400
Capital A/cs:		
M		1,36,000
N		90,000
O		46,000

Drawing A/cs:		
M	50,000	
N	46,000	
O	34,000	
Depreciation on Machinery		80,000
Profit for the year ended 31st March		2,48,600
Cash at Bank	1,78,600	
	7,70,000	**7,70,000**

Interest on Capital Accounts at 10% p.a. on the amount standing to the credit of Partners' Capital Accounts at the beginning of the year, was not provided before preparing the above Trial Balance.

On the above date, they formed MNO Private Limited Company with an Authorized Share Capital of 2,00,000 in shares of ₹ 10 each to be divided in different classes to take over the business of Partnership firm.

You are given terms and conditions as under:

1. Machinery is to be transferred at ₹ 1,40,000.
2. Shares in the Company are to be issued to the partners, at par, in such numbers, and in such classes as will give the partners, by reason of their shareholdings alone, the same rights as regards interest on capital and the sharing of profit and losses as they had in the partnership.
3. Before transferring the business, the partners wish to draw from the partnership profits to such an extent that the bank balance is reduced to ₹ 1,00,000. For this purpose, sufficient profits of the year are to be retained in profit -sharing ratio.
4. Assets and liabilities except Machinery and Bank, are to be transferred at their book value as on the above date.

You are required to prepare:

(i) Statement showing the workings of the Number of Shares of each class to be issued by the company, to each partner.

(ii) Capital Accounts showing all adjustments required to dissolve the Partnership.

(iii) Balance Sheet of the Company immediately after acquiring the business of the Partnership and Issuing of Shares.

Ans.

(i) Number of Shares to be issued to Partners

	₹
Assets: Machinery ₹ 1,40,000 + Inventory ₹ 1,37,400 + Trade Receivable ₹ 1,24,000 + Bank ₹ 1,00,000	5,01,400
Less: Liabilities taken over	(1,69,400)
Net Assets taken over (Purchase Consideration)	3,32,000

Classes of Shares to be issued:	**M**	**N**	**O**	**Total**
10% Preference Shares of ₹ 10 each (to retain rights as to Interest on Capital)	1,36,000	90,000	46,000	2,72,000
Balance in Equity Shares of ₹ 10 each (3,32,000 -2,72,000) (issued in profit sharing ratio)	30,000	18,000	12,000	60,000
	1,66,000	**1,08,000**	**58,000**	**3,32,000**

(ii) **Partners' Capital Accounts**

Particulars	M	N	O	Particulars	M	N	O
To Drawings	50,000	46,000	34,000	By balance b/d	1,36,000	90,000	46,000
To 10% Preference share capital	1,36,000	90,000	46,000	By Interest on Capital	13,600	9,000	4,600
To Equity Shares	30,000	18,000	12,000	By profit for the year 5:3:2 (W.N. 1)	1,10,700	66,420	44,280
To Bank – Additional Drawings (W.N. 2)	54,300	17,420	6,880	By Machinery* A/c	10,000	6,000	4,000
Total	**2,70,300**	**1,71,420**	**98,880**		**2,70,300**	**1,71,420**	**98,880**

(iii) Balance sheet of MNO Ltd. as on 31st March, 2020 (after Takeover of Firm)

Note no.			₹
I	**Equity and Liabilities:**		
	(1) Shareholders Funds		
	Share Capital	1	3,32,000
	(2) Current Liabilities		
	Trade Payables		1,69,400
	Total		5,01,400
II	**Assets**		
	(1) Non-Current Assets		
	Property, plant and equipment - Machinery		1,40,000
	(2) Current Assets:		
	(a) Inventories		1,37,400
	(b) Trade Receivables		1,24,000
	(c) Cash and Cash Equivalents		1,00,000
	Total		5,01,400

Notes to Accounts

	Particulars	₹
1.	Share capital	
	Authorized shares capital	20,00,000
	Issued, Subscribed & paid up	
	6,000 Equity Shares of ₹ 10 each	60,000
	27,200 10% Preference Shares capital of ₹ 10 each	2,72,000
	(All above shares issued for consideration other than cash, in takeover of partnership firm)	**3,32,000**

Working Notes:

1. **Profit & Loss Appropriation Account for the year ended 31st March, 2020**

Particulars	₹	₹	Particulars	₹
To Interest on Capital:			By Net Profit	2,48,600
M [₹ 1,36,000 x 10%]	13,600		(given)	
N [₹ 90,000 x 10%]	9,000			
O [₹ 46,000 x 10%]	4,600	27,200		
To Profits transferred to Capital in profit sharing ratio 5:3:2				
M	1,10,700			
N	66,420			
O	44,280	2,21,400		
		2,48,600		**2,48,600**

(b) A Ltd. holds 80% of the equity capital and voting power in B Ltd. A Ltd sells inventories costing ₹ 180 lacs to B Ltd at a price of ₹ 200 lacs. The entire inventories remain unsold with B Ltd at the financial year end i.e. 31 March 2020. What will be the accounting treatment for this transaction in the consolidated financial statements of A Ltd?

Ans. This would be the case of downstream transaction. In the consolidated profit and loss account for the year ended 31 March 2020, entire transaction of sale and purchase of ₹ 200 lacs each, would be eliminated by reducing both sales and purchases (cost of sales). Further, the unrealized profits of ₹ 20 lacs (i.e. ₹ 200 lacs – ₹ 180 lacs), would be eliminated from the consolidated financial statements for financial year ended 31 March 2020, by reducing the consolidated profits/ increasing the consolidated losses, and reducing the value of closing inventories as of 31 March 2020.

Q-19 Amit, Sumit and Kumar are partners sharing profit and losses in the ratio 2:2:1. The partners decided to dissolve the partnership on 31st March, 2020 when their Balance Sheet was as under:

Liabilities	Amount	Assets		Amount
Capital Accounts:		Land & Building		1,35,000
Amit	55,200	Plant & Machinery		45,000
Sumit	55,200	Furniture		25,500
General Reserve	61,500	Investments		15,000
Kumar's Loan A/c	15,000	Book Debts	60,000	
Loan from D	1,20,000	Less: Prov. for bad debts	(6,000)	54,000
Trade Creditors	30,000	Stock		36,000
Bills Payable	12,000	Bank		13,500
Outstanding Salary	7,500	Capital Withdrawn:		
		Kumar		32,400
Total	**3,56,400**	**Total**		**3,56,400**

The following information is given to you:

(i) Realization expenses amounted to ₹ 18,000 out of which ₹ 3,000 was borne by Amit.

(ii) A creditor agreed to takeover furniture of book value ₹ 12,000 at ₹ 10,800. The rest of the creditors were paid off at a discount of 6.25%.

(iii) The other assets realized as follows:

Furniture - Remaining taken over by Kumar at 90% of book value

Stock - Realized 120% of book value

Book Debts - ₹ 12,000 of debts proved bad, remaining were fully realized

Land & Building - Realized ₹ 1,65,000

Investments - Taken over by Amit at 15% discount

(iv) For half of his loan, D accepted Plant & Machinery and ₹ 7,500 cash. The remaining amount was paid at a discount of 10%.

(v) Bills payable were due on an average basis of one month after 31st March, 2020, but they were paid immediately on 31st March @ 6% discount "per annum".

Prepare the Realization Account, Bank Account and Partners' Capital Accounts in columnar form in the books of Partnership firm.

Ans. **Realization Account**

To	Land and Building		1,35,000	By	Provision for bad debts		6,000
To	Plant and Machinery		45,000	By	Loan from D		1,20,000
To	Furniture		25,500	By	Trade creditors		30,000
To	Investments		15,000	By	Bills payable		12,000
To	Book debts		60,000	By	Outstanding salary		7,500
To	Stock		36,000	By	Kumar - Furniture taken over (13,500 x .9)		12,150
To	Bank (Realization expenses)		15,000	By	Bank A/c - Stock Realized	43,200	
To	Amit– Realization expenses		3,000		Land & Building	1,65,000	
					Debtors	48,000	2,56,200
To	Bank A/c - Bill payable		11,940	By	Amit (Investment taken over)		12,750
	D's Loan		7,500				
	D's Loan		54,000				
	Creditors		18,000				
	Salary		7,500				
To	Profit trs/f to partners' capital Accounts						
	Amit	9,264					
	Sumit	9,264					
	Kumar	4,632	23,160				
			4,56,600				**4,56,600**

Bank Account

		₹			₹
To	Balance b/d	13,500	By	Realization A/c (payment of liabilities: 11,940+ 7,500 + 54,000 + 15,000 + 18,000 + 7,500)	1,13,940
To	Realization A/c (assets realized)	2,56,200	By	Amit	79,314
To	Kumar	12,618	By	Sumit	89,064
		2,82,318			**2,82,318**

Partners' Capital Accounts

		Amit ₹	Sumit ₹	Kumar ₹			Amit ₹	Sumit ₹	Kumar ₹
To	Balance b/d			32,400	By	Balance b/d	55,200	55,200	
					By	Kumar's Loan			15,000
To	Realization A/c (Investment taken over)	12,750			By	General Reserve	24,600	24,600	12,300
To	Realization A/c (Furniture taken over)			12,150	By	Realization A/c (expense)	3,000		
To	Bank A/c	79,314	89,064		By	Realization A/c (profit)	9,264	9,264	4,632
					By	Bank A/c			12,618
		92,064	**89,064**	**44,550**			**92,064**	**89,064**	**44,550**

Working Notes:

1. Payment for Bills Payable

Particulars	Amount (₹)
Bills Payable as per Balance Sheet	12,000
Less: Discount for early payment {12,000 x 6% x (1/12)}	60
Amount Paid in Cash	11,940

2. **Payment to D's Loan**

Particulars	Amount (₹)
D's Loan as per Balance Sheet	120,000.00
50% of Loan adjusted as below:	
Plant & Machinery accepted at Book Value (₹ 45,000) and ₹ 7,500 in cash.	7,500
Balance 50% of Loan adjusted as below:	
In cash after allowing discount of 10% i.e. ₹ 60,000 – ₹ 6,000 = ₹ 54,000.	54,000

3. **Payment to Trade Creditors**

Particulars	Amount (₹)
Trade Creditors as per Balance Sheet	30,000
Less: Furniture of Book Value ₹ 12,000 accepted at value ₹ 10,800	10,800
	19,200
Less: Discount @ 6.25%	1,200
Amount paid in Cash	18,000

4. Furniture taken over by Kumar

Particulars	Amount
Furniture as per Balance Sheet	25,500
Less: Furniture of Book Value ₹ 12000 accepted by trade creditors	12,000
	13,500
Less: 10% of Book Value	1,350
Value of Furniture taken over by Kumar	12,150

Q-20 Explain the provisions related with liability of Limited Liability Partnership (LLP) and its partners as per LLP Act, 2008.

Ans. Under section 27 (3) of the LLP Act, 2008 an obligation of an LLP arising out of a contract or otherwise, shall be solely the obligation of the LLP. The limitations of liability of an LLP and its partners are as follows:

- The Liabilities of an LLP shall be met out of the properties of the LLP;
- A partner is not personally liable, directly or indirectly (for an obligation of an LLP arising out of a contract or otherwise), solely by reason of being a partner in the LLP;
- An LLP is not bound by anything done by a partner in dealing with a person, if:
  - The partner does not have the authority to act on behalf of the LLP in doing a particular act; and
  - The other person knows that the partner has no authority or does not know or believe him to be a partner in the LLP
- The liability of the LLP and the partners perpetrating fraudulent dealings shall be unlimited for all or any of the debts or other liabilities of the LLP.

Q-21 What are circumstances when LLP can be wound up by the Tribunal. Explain in brief.

Ans. Under section 64 of the LLP Act, 2008, an LLP may be wound up by the Tribunal:

- If the LLP decides that it should be wound up by the Tribunal;
- If for a period of more than six months, the number of partner s of the LLP is reduced below two;
- If the LLP is unable to pay its debts;
- If the LLP has acted against the interests of the integrity and sovereignty of India, the security of the state or public order;
- If the LLP has defaulted in the filing of the Statement of Account and Solvency with the Registrar for five consecutive financial years;

Q-22 P, Q, R and S are sharing profits and losses in the ratio 3 : 3 : 2 : 1. Frauds committed by R during the year were found out and it was decided to dissolve the partnership on 31st March, 2021 when their Balance Sheet was as under:

Equity & Liabilities	Amount (₹)	Assets	Amount (')
Capitals:		Building	1,90,000
P	1,50,000	Stock	1,30,000
Q	1,50,000	Investments	50,000
R	-	Debtors	70,000
S	60,000	Cash	30,000
General reserve	40,000	R's capital	40,000
Trade creditors	80,000	(overdrawn)	
Bills payable	30,000		
	5,10,000		**5,10,000**

Following information is given to you:

(i) A cheque for ₹ 7,000 received from debtor was not recorded in the books and was misappropriated by R.

(ii) Investments costing ₹ 8,000 were sold by R at ₹ 11,000 and the funds transferred to his personal account. This sale was omitted from the firm's books.

(iii) A creditor agreed to take over investments of the book value of ₹ 9,000 at ₹ 13,000. The rest of the creditors were paid off at a discount of 5%.

(iv) The other assets realized as follows:

Building 110% of book value

Stock ₹ 1,20,000

Investments The rest of investments were sold at a profit of ₹ 7,000

Debtors The rest of the debtors were realized at a discount of 10%

(v) The bills payable were settled at a discount of ₹ 500.

(vi) The expenses of dissolution amounted to ₹ 8,000

(vii) It was found out that realization from R's private assets would only be ₹ 7,000.

Prepare Realization Account, Cash Account and Partners' Capital Accounts. All workings should part of your answer.

Ans. **Realization Account**

Particulars	₹	Particulars		₹
To Building	1,90,000	By Trade creditors	80,000	
To Stock	1,30,000	By Bills payable	30,000	
To Investment	50,000	By Cash		
To Debtors	70,000	Building	2,09,000	
To Cash-creditors paid(W.N.1)	63,650	Stock	1,20,000	
To Cash-expenses	8,000	Investments (W.N.2)	40,000	
To Cash-bills payable(30,000-500)	29,500	Debtors (W.N. 3)	56,700	4,25,700
To Partners' Capital A/cs		By R – (Receipt fromDebtors unrecorded)		7,000
P 4,183				
Q 4,183		By R - Receipt from Investments unrecorded		11,000
R 2,789				
S 1,395	12,550			
	5,53,700			**5,53,700**

Cash Account

Particulars		Amount ₹	Particulars		Amount ₹
To Balance b/d		30,000	By Realization-creditorspaid		63,650
To Realization – assets realized			By Realization-bills payable		29,500
Building		2,09,000	By Realization-expenses		8,000
Stock		1,20,000	By Capital accounts:		
Investments	40,000		P	1,51,132	
Debtors	56,700	4,25,700	Q	1,51,132	
To R's capital A/c	7,000		S	59,286	
		4,62,700			**4,62,700**

Partners' Capital Accounts

Particulars	P ₹	Q ₹	R ₹	S ₹	Particulars	P ₹	Q ₹	R ₹	S ₹
To Balance b/d			40,000		By Balance b/d	1,50,000	1,50,000	-	60,000
To RealizationA/c-Debtors misappropriation			7,000		By General reserve	13,333	13,333	8,889	4,445
To RealizationA/c-Investment misappropriation			11,000		By Realization profit	4,183	4,183	2,789	1,395
To R's capital A/c (W.N. 4)	16,384	16,384		6,554	By Cash A/c	7,000			
To Cash A/c	1,51,132	1,51,132		59,286	By P's capitalA/c			16,384	
					By Q's capitalA/c			16,384	
					By S's capitalA/c				6,554
	1,67,516	**1,67,516**	**58,000**	**65,840**		**1,67,516**	**1,67,516**	**58,000**	**65,840**

Working Notes:

1. Amount paid to creditors in cash

	₹
Book value	80,000
Less: Creditors taking over investments	(13,000)
	67,000
Less: Discount @ 5%	(3,350)
	63,650

2. **Amount received from sale of investments**

	₹
Book value	50,000
Less: Misappropriated by R	(8,000)
	42,000
Less: Taken over by a creditor	(9,000)
	33,000
Add: Profit on sale of investments	7,000
Cash received from sale of remaining investment	40,000

3. Amount received from debtors

	₹
Book value	70,000
Less: Unrecorded receipt	(7,000)
	63,000
Less: Discount @ 10%	(6,300)
	56,700

4. Deficiency of R

		₹
Balance of capital as on 31st March, 2021		40,000
Debtors-misappropriation		7,000
Investment-misappropriation		11,000
	58,000	
Less:	Realization Profit	(2,789)
	General reserve	(8,889)
	Contribution from private assets	(7,000)
	Net deficiency of capital	39,322

This deficiency of ₹ 39,322 in R's capital account will be shared by other partners P, Q and S in their capital ratio of 15 : 15 : 6.by

Accordingly,

P's share of deficiency	= [39,322 x (15/36)]	= ₹ 16,384
Q's share of deficiency	= [39,322 x (15/36)]	= ₹ 16,384
S's share of deficiency	= [39,322 x (6/36)]	= ₹ 6,554

Q-23 M, N and O were Partners sharing Profits and Losses in the ratio of 5:3:2 respectively. The Trial Balance of the Firm as on 31st March, 2020 was the following:

Particulars	₹	₹
Machinery at Cost	2,00,000	
Inventory	1,37,400	
Trade receivables	1,24,000	
Trade payables		1,69,400
Capital A/cs:		
M		1,36,000
N		90,000
O		46,000
Drawing A/cs:		
M	50,000	
N	46,000	
O	34,000	
Depreciation on Machinery		80,000
Profit for the year ended 31st March, 2020		2,48,600
Cash at Bank	1,78,600	
	7,70,000	**7,70,000**

Interest on Capital Accounts at 10% p.a. on the amount standing to the credit of Partners' Capital Accounts at the beginning of the year, was not provided before preparing the above Trial Balance. On the above date, they formed MNO Private Limited Company with an Authorized Share Capital of 2,00,000 shares of ₹ 10 each to be divided in different classes to take over the business of Partnership firm.

You are given terms and conditions as under:

1. Machinery is to be transferred at ₹ 1,40,000.
2. Shares in the Company are to be issued to the partners, at par, in such numbers, and in such classes as will give the partners, by reason of their shareholdings alone, the same rights as regards interest on capital and the sharing of profit and losses as they had in the partnership.
3. Before transferring the business, the partners wish to draw from the partnership profits to such an extent that the bank balance is reduced to ₹ 1,00,000. For this purpose, sufficient profits of the year are to be retained in profit-sharing ratio.
4. Assets and liabilities except Machinery and Bank, are to be transferred at their book value as on the above date.

   You are required to prepare:

   (i) Statement showing the workings of the Number of Shares of each class to be issued by the company, to each partner.

   (ii) Capital Accounts showing all adjustments required to dissolve the Partnership.

   (iii) Balance Sheet of the Company immediately after acquiring the business of the Partnership and Issuing of Shares.

Ans. (i) Number of Shares to be issued to Partners

				₹
Assets: Machinery ₹ 1,40,000 + Inventory ₹ 1,37,400 + Trade Receivable ₹ 1,24,000 + Bank ₹ 1,00,000				5,01,400
Less: Liabilities taken over				(1,69,400)
Net Assets taken over (Purchase Consideration)				3,32,000
Classes of Shares to be issued: M N O Total				
10% Preference Shares of ₹ 10 each (to retain rights as to Interest on Capital)	1,36,000	90,000	46,000	2,72,000
Balance in Equity Shares of ₹ 10 each (3,32,000 -2,72,000) (issued in profit sharing ratio)	30,000	18,000	12,000	60,000
	1,66,000	1,08,000	58,000	3,32,000

(ii) Partners' Capital Accounts

Particulars	M	N	O	Particulars	M	N	O
To Drawings	50,000	46,000	34,000	By balance b/d	1,36,000	90,000	46,000
To 10% Preference share capital	1,36,000	90,000	46,000	By Interest on Capital	13,600	9,000	4,600
To Equity Shares	30,000	18,000	12,000	By profit for the year 5:3:2 (W.N. 1)	1,10,700	66,420	44,280
To Bank -Additional Drawings (W.N. 2)	54,300	17,420	6,880	By Machinery* A/c	10,000	6,000	4,000
Total	**2,70,300**	**1,71,420**	**98,880**		**2,70,300**	**1,71,420**	**98,880**

***** Gain on Transfer of Machinery = ₹ 1,40,000 – (₹ 2,00,000-₹ 80,000) = ₹ 20,000 in 5:3:2 ratio.

(iii) Balance sheet of MNO Ltd. as at 31st March, 2020 (after Takeover of Firm)

		Note no.	₹
I	Equity and Liabilities:		
	(1) Shareholders Funds		
	Share Capital	1	3,32,000
	(2) Current Liabilities		
	Trade Payables		1,69,400
	Total		**5,01,400**
II	**Assets**		
	(1) Non-Current Assets		
	Property, plant and equipment - Machinery		1,40,000
	(2) Current Assets:		
	(a) Inventories		1,37,400
	(b) Trade Receivables		1,24,000
	(c) Cash and Cash Equivalents		1,00,000
	Total		**5,01,400**

Notes to Accounts

Particulars	₹
1. Share capital	
Authorized shares capital	
2,00,000 Equity Shares of ₹ 10 each	20,00,000
Issued, Subscribed & paid up	
6,000 Equity Shares of ₹ 10 each	60,000
27,200 10% Preference Shares capital of ₹ 10 each	2,72,000
(All above shares issued for consideration other than cash, in takeover of partnership firm)	**3,32,000**

Working Notes:

1. Profit & Loss Appropriation Account for the year ended 31st March, 2020

Particulars	₹	₹	**Particulars**	₹
To Interest on Capital:			By Net Profit (given)	2,48,600
M [₹ 1,36,000 x 10%]	13,600			
N [₹ 90,000 x 10%]	9,000			
O [₹ 46,000 x 10%]	4,600	27,200		
To Profits transferred to Capital in profit sharing ratio 5:3:2				
M	1,10,700			
N	66,420			
O	44,280	2,21,400		
		2,48,600		**2,48,600**

Statement showing Additional Drawings in Cash

(a) Funds available for Drawings

Total Drawing of Partners (given)		1,30,000
Add:	Further Funds available for Drawings (1,78,600-1,00,000)	78,600
		2,08,600
Less:	Interest on Capital	(27,200)
	Amount available for Drawings	1,81,400

(b) Ascertainment of Additional Drawings

Particulars	**M**	**N**	**O**
As per above statement ₹ 1,81,400 (in profit sharing ratio)	90,700	54,420	36,280
Add: Interest	13,600	9,000	4,600
1,04,300	63,420	40,880	
Less: Already drawn	(50,000)	(46,000)	(34,000)
Additional Drawings	54,300	17,420	6,880

Q-24 A Partnership firm C & Co. consists of partners P and Q sharing Profits and Losses in the ratio of 4:1. The firm H & Co. consists of Partners Q and R sharing Profits and Losses in the ratio of 3:2. On 31st March, 2021, it was decided to amalgamate both the firms and form a new firm CH & Co., wherein P, Q, R would be partners sharing Profits and Losses in the ratio of 6:3:1. The summarized Balance Sheets of both the firms as on 31st March, 2021 were as follows:

Liabilities	**C & Co. (₹ in 000)**	**H & Co. (₹ in 000)**	**Assets**	**C & Co. (₹ in 000)**	**H & Co. (₹ in 000)**
Capital			Cash in hand/bank	160	120
P	600	-	Debtors	240	320
Q	400	300	Stock	200	80
R	-	200	Vehicles	-	350
Reserve	200	150	Machinery	480	-
Creditors	480	220	Building	600	-
Total	1,680	870	Total	1,680	870

The following were the terms of amalgamation:

(i) Goodwill of C & Co. was valued at ₹ 2,80,000 and the Goodwill of H & Co. was valued at ₹ 1,60,000. Goodwill account is not to be opened in the books of the new firm but to be adjusted through the Capital accounts of the partners.

(ii) Building, Machinery and Vehicles are to be taken over at ₹ 8,00,000, ₹ 4,00,000 and ₹ 3,00,000, respectively.

(iii) Provision for doubtful debts at ₹ 20,000 in respect of C & Co. and ₹ 10,000 in respect of H & Co. are to be provided.

You are required to:

(i) Show how the Goodwill value will be adjusted amongst the partners.

(ii) Prepare the Balance Sheet of CH & Co as at 31st March, 2021 by keeping Partners' capitals in their profit sharing ratio taking capital of ₹Q' as the basis. The excess or deficiency to be kept in the respective Partner's Current Account.

Ans. (a) (i) Adjustment for raising and writing off of goodwill

	Raised in old profit-sharing ratio		Total	Written off in new ratio	Difference
	C & Co. 4:1 ₹	H & Co. 3:2 ₹	₹	6:3:1 ₹	₹
P	2,24,000	-	2,24,000 Cr.	2,64,000 Dr.	40,000 Dr.
Q	56,000	96,000	1,52,000 Cr.	1,32,000 Dr.	20,000 Cr.
R	-	64,000	64,000 Cr.	44,000 Dr.	20,000 Cr.
	2,80,000	1,60,000	4,40,000	4,40,000	Nil

(ii) Balance Sheet of CH & Co. (New firm) as on 31.3.2021

Liabilities	₹	Assets	₹
Capital Accounts:		Vehicle	3,00,000
P	16,68,000	Machinery	4,00,000
Q	8,34,000	Building	8,00,000
R	2,78,000	Stock	2,80,000
Creditors	7,00,000	Debtors	5,30,000
		Cash & Bank	2,80,000
		Current Accounts:	
		P	8,68,000
		R	22,000
	34,80,000		**34,80,000**

Working Notes:

1. Balance of Capital Accounts at the time of amalgamation of firms

C & Co.

Particulars	P's Capital (₹)	Q's Capital (₹)
C & Co. Profit and loss sharing ratio 4:1		
Balance as per Balance Sheet	6,00,000	4,00,000
Add: Reserves	1,60,000	40,000
Revaluation profit (Building) *	1,60,000	40,000
Less: Revaluation loss (Machinery)	(64,000)	(16,000)
Provision for doubtful debt	(16,000)	(4,000)
	8,40,000	4,60,000

H & Co.

Particulars	Q's Capital (₹)	R's Capital (₹)
H & Co. Profit and loss sharing ratio 3:2		
Balance as per Balance sheet	3,00,000	2,00,000
Add: Reserves	90,000	60,000
Less: Revaluation (vehicle)	(30,000)	(20,000)
Provision for doubtful debts	(6,000)	(4,000)
	3,54,000	2,36,000

2. Balance of Capital Accounts in the balance sheet of the new firm as on 31.3.2021

Particulars	P ₹	Q ₹	R ₹
Balance b/d: C & Co.	8,40,000	4,60,000	—
H & Co.	—	3,54,000	2,36,000
	8,40,000	8,14,000	2,36,000
Adjustment for goodwill	(40,000)	20,000	20,000
	8,00,000	8,34,000	2,56,000
Total capital ₹ 27,80,000 (Q's capital i.e. ₹ 8,34,000 x 10/3) to be contributed in 6:3:1 ratio.	16,68,000	8,34,000	2,78,000
Deficiency Transferred to Current Account	8,68,000	—	22,000

Q-25 Ananya Enterprises is a partnership firm is which A, B and C are three partners sharing profits and losses in the ratio of 5: 3: 2. The Balance Sheet of the firm as on 31st October, 2019 is as below:

Liabilities	₹	Assets	₹
Capital:			
A	95,00,000	Land & Buildings	45,00,000
B	75,00,000	Plant & Machinery	65,00,000
C	30,00,000	Furniture & Fixtures	18,00,000
Sundry Creditors	11,00,000	Stock	13,50,000
		Sundry Debtors	7,50,000
		Cash	7,00,000
		Loan A	25,00,000
		Loan B	30,00,000
	2,11,00,000		**2,11,00,000**

On the Balance Sheet date all the three partners have decided to dissolve their partnership and called you to assist them in winding up the affairs of the firm. They also agreed that asset realization is distributed among them at the end of each month.

A summary of liquidation transactions is as follows:

November, 2019:

- ₹ 3,00,000 - collected from debtors, balance is uncollectable
- ₹ 11,00,000 - received from the sale of entire furniture
- ₹ 2,00,000 - liquidation expenses paid
- ₹ 6,00,000 - Cash retained in the business at the end of month

December, 2019:

- ₹ 2,20,000 - Liquidation expenses paid
- As part payment of his capital, C accepted a machinery for ₹ 9,00,000 (Book value 6,00,000)
- ₹ 2,00,000 - Cash retained in the business at the end of month.

January, 2020:

- ₹ 28,00,000 - Received on the sale of remaining plant & machinery
- ₹ 9,00,000 - Received from the sale of entire stock

- ₹ 1,50,000 - Liquidation expenses paid
- ₹ 63,00,000 - Received on sale of Land & Buildings
- No cash is retained in the business.

You are required to prepare a schedule of cash payments amongst the partners by "Highest Relative Capital Method" as on 31st January, 2020.

Ans. Statement showing distribution of cash

		Creditors	Capitals		
Particulars	**₹**	**₹**	**A (₹)**	**B (₹)**	**C (₹)**
Balance Due after loan		11,00,000	70,00,000	45,00,000	30,00,000
Nov. 2019					
Balance available	7,00,000				
Realization less expenses					
and cash retained	6,00,000				
Amount available and paid	13,00,000	11,00,000	-	1,20,000	80,000
Balance due			70,00,000	43,80,000	29,20,000
Dec. 2019					
Opening balance	6,00,000				
Expenses paid and					
balance carried forward	4,20,000				
Available for distribution	1,80,000				
Cash paid to B and			—		
Machinery given to C				1,80,000	9,00,000
Balance due			70,00,000	42,00,000	20,20,000
Jan.2020					
Opening balance	2,00,000				
Amount realized less	98,50,000				
expenses					
Amount available and paid					
to partners	100,50,000				
First, ₹ 31,20,000 is paid to A and B					
in the ratio of 5:3			19,50,000	11,70,000	
Balance (100,50,000 -31,20,000)					
₹ 69,30,000 is paid to A,B and C					
in the ratio of 5:3:2			34,65,000	20,79,000	13,86,000
Total amount paid			54,15,000	32,49,000	13,86,000
Total loss			15,85,000	9,51,000	6,34,000

Working note:

Calculation of Highest Relative Capital Basis

(1) Scheme of payment for November

Particulars	A ₹	B ₹	C ₹
Balance of Capital Accounts	95,00,000	75,00,000	30,00,000
Less: Loans	(25,00,000)	(30,00,000)	
	70,00,000	45,00,000	30 00 000
Profit-sharing ratio	5	3	2
Capital Profit sharing ratio	14,00,000	15,00,000	15,00,000
Capital in profit sharing ratio, taking A's capital as base	70,00,000	42,00,000	28,00,000
Excess of C's Capital and B's Capital (A-B)		3,00,000	2,00,000
Profit-sharing ratio		3	2

It means realization up to ₹ 5,00,000 is distributed among B and C in the ratio of 3:2. So excess amount of ₹ 2,00,000 after paying creditors is distributed among B and C in the ratio of 3:2 i.e. ₹ 1,20,000 and 80,000 respectively.

(2) Scheme of payment for December

In the month of December C has received machinery amounting ₹ 9,00,000 against his excess capital of ₹ 1,20,000 (2,00,000 - 80,000). Excess capital of B is ₹ 3,00,000 out of which ₹ 1,20,000 already paid to him, so balance ₹ 1,80,000 available in the month of December will be paid to B.

(3) Scheme of payment for January

Particulars	A ₹	B ₹	C ₹
Balance of Capital Accounts at the end of December	70,00,000	42,00,000	20,20,000
Profit-sharing ratio	5	3	2
Capital Profit sharing ratio	14,00,000	14,00,000	10,10,000
Capital in profit sharing ratio, taking C's capital as base	50,50,000	30,30,000	20,20,000
Excess Capital	19,50,000	11,70,000	

Since ₹ 19,50,000 and 11,70,000 is already in the ratio of 5:3, so amount realized up to ₹ 31,20,000 is distributed among A and B in the ratio of 5:3.

After that any amount realized is distributed among all the three partners in the ratio of 5:3:2.

Q-26 Mohan and Sohan were carrying business in partnership, sharing profit and losses equally.

The Balance Sheet of the firm as on 31st March, 2019 stood as under:

Liabilities		₹	Assets		₹
Partners' Capital			Accounts:Leasehold Premises		40,800
- Mohan	1,68,000		Plant & Machinery		1,80,000
-Sohan	1,56,000	3,24,000	Inventories		72,000
Bank Overdraft		42,000	Trade Receivables		84,000
Trade Payables		72,000	Joint Life Policy		10,800
Profit & Loss Account		31,200			
Partners' Current Accounts:					
			-Mohan	12,000	
			-Sohan	7,200	19,200
		4,38,000			**4,38,000**

The business was carried on till 30th September, 2019. The partners withdrew the amounts equal to half the amount of profit made during the period of six months ended on 30th September, 2019 equally. The profit was calculated after charging depreciation @5% per annum on Leasehold premises and 10% per annum on Plant & Machinery.

In the half year, the amounts of Bank Overdraft and Trade Payables stood reduced by ₹ 18,000 and ₹ 12,000 respectively. On 30th September, 2019, the inventories were valued at ₹ 90,000 and Trade Receivables at ₹ 72,000. The Joint Life Policy had been surrendered for ₹ 10,800 before 30th September, 2019 and all other items remained the same as at 31st March, 2019.

On 30th September, 2019, the firm sold off its business to PKR Limited. The value of Goodwill was fixed at ₹ 1,20,000 and the rest of the assets and liabilities were valued on the basis of their book values as at 30th September, 2019. PKR Ltd. paid the purchase consideration in equity shares of ₹10 each.

You are requested to prepare the following:

(1) Balance Sheet of the Firm as at 30th September, 2019;

(2) Realization Account;

(3) Partners' Capital Account showing the final settlement between them.

Ans. (i) Balance Sheet of the Firm as at 30.9.2019

Liabilities	₹	₹	**Assets**	₹	₹
Capital Accounts:			Machinery	1,80,000	
Mohan balance as			@10% p.a. for 6	(9,000)	1,17,000
on 30.9.2019	1,40,400		months		
Less: Depreciation	15,180				
Add: Profit for 6	1,55,580				
months					
Less: Drawings for					
6 months	(7,590)	1,47,990	Leasehold	40,800	
premises Less:			Written-off @ 5%		
Sohan balance as			for 6 months	(1,020)	39,780
on 30.9.2019	1,33,200				
Add: Profit for 6	15,180		Inventory		90,000
months					
		1,48,380	Trade receivables		72,000
Less: Drawings for	(7,590)	1,40,790			
6 months					
Trade payables		60,000			
(72,000 – 12,000)					
Bank overdraft					
(42,000 – 18,000)		24,000			
		3,72,780			**3,72,780**

(ii) **Realization Account**

Particulars		'	Particulars		'
To	Machinery A/c	1,71,000	By	Trade payables A/c	60,000
To	Leasehold Premises A/c	39,780	By	Bank Overdraft A/c	24,000
To	Inventory A/c	90,000	By	PKR Ltd. A/c	4,08,780
To	Trade receivables A/c	72,000		(W.N.1)	
To	Mohan Capital A/c	60,000			
To	Sohan Capital A/c	60,000			
		4,92,780			**4,92,780**

(iii) Partners' Capital Accounts

Date	Particulars	Mohan ₹	Sohan ₹	Date	Particulars	Mohan ₹	Sohan ₹
1.4.19	To Profit & Loss A/c	15,600	15,600	1.4.19	By Balance b/d	1,68,000	1,56,000
	To Current A/c	12,000	7,200				
30.9.19	Balance c/d	1,40,400	1,33,200				
		1,68,000	**1,56,000**			**1,68,000**	**1,56,000**
30.9.19	To Drawings A/c	7,590	7,590	30.9.19	By Balance b/d	1,40,400	1,33,200
	To Shares in PKR Ltd A/c	2,07,990	2,00,790	30.9.19	By Profit & Loss Appropriation A/c	15,180	15,180
					By Realization A/c	60,000	60,000
		2,15,580	**2,08,380**			**2,15,580**	**2,08,380**

Working Notes:

(1) Ascertainment of purchase consideration

	₹	₹
Assets:		
Inventory		90,000
Trade receivables		72,000
Machinery less depreciation		1,71,000
Leasehold premises less written off		39,780
		3,72,780
Less: Liabilities:		
Trade payables	60,000	
Bank overdraft	24,000	(84,000)
Closing Net Assets		2,88,780
Add: Goodwill		1,20,000
Purchase Consideration		4,08,780

(2) Ascertainment of profit for the 6 month ended 30th September,2019

	₹	₹
Closing Net Assets		
Less: Opening Combined Capital		2,88,780
Mohan – (1,68,000- 15,600-12,000)	1,40,400	
Sohan – (1,56,000-15,600-7,200)	1,33,200	
Profit after adjustment of Drawings		
		(2,73,600)
Add: Combined drawings during the 6 month (equal to profit)		15,180
		15,180
Profit for 6 months		30,360

Q-27 Om, Sai and Radhe share profits and losses of a business as to 3:2:1 respectively. Their balance sheet as at 31st March, 2020 was as follows:

Liabilities	₹	**Assets**	₹
Capital Accounts:		Land and Building	1,40,000
Om	70,000	Machinery	50,000
Sai	80,000	Motor Car	28,000
Radhe	10,000	Furniture	12,000
General Reserve	22,000	Investments	18,000
Radhe's Loan	33,000	Stock	18,000
Mrs. Om's loan	15,000	Bills receivable	20,000
Creditors	96,000	Loose tools	7,000
Bills Payable	14,000	Debtors	38,000
Bank overdraft	60,000	Cash	1,000
		Radhe's current A/c	56,000
		Profit and Loss A/c	12,000
	4,00,000		**4,00,000**

The partners decide to convert their firm into a Joint Stock Company. For this purpose ABC Ltd. was formed with an authorized capital of ₹ 10,00,000 divided into ₹ 100 equity Shares. The business of the firm was sold to the company as at the date of balance sheet given above on the following terms:

(i) Motor car, furniture, investments, loose tools, debtors and cash are not to be taken over by the company.

(ii) Liabilities for bills payable and bank overdraft are to be taken over by the company.

(iii) The purchase price is settled at ₹ 1,95,500 payable as to ₹ 75,500 in cash and the balance in company's fully paid shares of ₹100 each.

(iv) The remaining assets and liabilities of the firm are directly disposed of by the firm as per details given below:

Investments are taken over by Om for ₹ 13,000; debtors realize in all ₹ 20,000; Motor Car, furniture and loose tools fetch ₹ 24,000, ₹ 4,000, and ₹ 1,000 respectively. Om agrees to pay his wife's loan. The creditors were paid ₹ 94,000 in final settlement of their claims. The realization expenses amount to ₹ 500. Radhe's loan was transferred to his capital account.

(v) The equity share received from the vendor company are to be divided among the partners in profit-sharing ratio.

You are required to prepare Realization account, Partners' capital accounts, Cash account, ABC Ltd. account and Shares in ABC Ltd. account in the books of the partnership firm.

Ans. **In the books of Partnership Firm**

Realization Account

Particulars	₹	₹	Particulars	₹	₹
To Land and Building		1,40,000	By Trade creditors		96,000
To Machinery		50,000	By Bills Payable		14,000
To Motor Car		28,000	By Bank overdraft		60,000
To Furniture		12,000	By Mrs. Om's loan		15,000
To Investments		18,000	By ABC Ltd. (Purchase price)		1,95,500
To Loose tools		7,000	By Om's Capital A/c (Investments taken over)		13,000
To Stock		18,000	By Cash A/c:		
To Bill receivable		20,000	Debtors	20,000	
To Debtors		38,000	Motor Car	24,000	
			Furniture	4,000	
To Om's Capital A/c (Mrs. Om's Loan)		15,000	Loose tools	1,000	49,000
To Cash A/c:					
Creditors	94,000				
Realization expenses	500	94,500			
To Profit on Realization transferred to:					
Om's Capital A/c	1,000				
Sai's Capital A/c	667				
Radhe's Capital A/c	333	2,000			
		4,42,500			**4,42,500**

ABC Ltd. Account

Particulars	₹	Particulars	₹
To Realization A/c	1,95,500	By Cash A/c	75,500
		By Shares in ABC Ltd.	1,20,000
	1,95,500		1,95,500

Partners' Capital Accounts

Particulars	Om ₹	Sai ₹	Radhe ₹	Particulars	Om ₹	Sai ₹	Radhe ₹
To Profit and Loss A/c	6,000	4,000	2,000	By Balance b/d	70,000	80,000	10,000
To Realization A/c	13,000	-	-	By Radhe's Loan A/c	-	-	33,000
To Radhe's Current A/c	-	-	56,000	By General reserve	11,000	7,333	3,667
To shares in ABC Ltd.	60,000	40,000	20,000	By Realization A/c	1,000	667	333
To Cash A/c	18,000	44,000	-	By Realization A/c (Mrs. Om's loan A/c)	15,000	-	-
				By Cash A/c	-		31,000
	97,000	**88,000**	**78,000**		**97,000**	**88,000**	**78,000**

Shares in ABC Ltd. Account

Particulars	₹	Particulars	₹
To ABC Ltd. Account	1,20,000	By Om's Capital A/c	60,000
		By Sai's Capital A/c	40,000
		By Radhe's Capital A/c	20,000
	1,20,000		1,20,000

Cash Account

Particulars	₹	Particulars	₹
To Balance b/d	1,000	By Realization A/c (Liabilities and expenses)	94,500
To ABC Ltd.	75,500	By Om's Capital A/c	18,000
To Realization A/c (realization of assets)	49,000	By Sai's Capital A/c	44,000
To Radhe's Capital A/c	31,000		-
	1,56,500		1,56,500

Q-28 X, Y and Z are in partnership sharing profits and losses in the ratio of 5:4:4. The Balance Sheet of the firm as on 31st March, 2020 is as below:

Liabilities	₹	Assets	₹
X's Capital	60,000	Factory Building	96,640
Y's Capital	40,000	Plant and Machinery	65,100
Z's Capital	50,000	Trade Receivable	21,600
Y's Loan	18,000	Inventories	49,560
Creditors	66,000	Cash at Bank	1,100
	2,34,000		**2,34,000**

On Balance Sheet date, all the three partners have decided to dissolve their partnership. Since the realisation of assets was protracted, they decided to distribute amounts as and when feasible and for this purpose they appoint Z who was to get as his remuneration 1% of the value of the assets realised other than cash at bank and 10% of the amount distributed to the partners.

Assets were realised piecemeal as under:

	₹
First instalment	74,600
Second instalment	69,301
Third instalment	40,000
Last instalment	28,000
Dissolution expenses were provided for estimated amount of	₹ 12,000
The creditors were settled finally for	₹ 63,600

You are required to prepare a statement showing distribution of cash amongst the partners by "Highest Relative Capital Method".

Ans.(a) Statement showing distribution of cash amongst the partners

		Creditors	Y's Loan	Capitals		
				X (₹)	Y (₹)	Z (₹)
Balance Due		66,000	18,000	60,000	40,000	50,000
Including 1st Instalment amount with the firm ₹ (1100 + 74,600)	75,700					
Less: Dissolution expenses provided for	(12,000)					
	63,700					
Less: Z's remuneration of 1% on assets realized (74,600 x 1%)	(746)					
	62,954					
Less: Payment made to creditors	(62,954)	(62,954)				
Balance due	Nil	3046				
2nd instalment realised	69,301					
Less: Z's remuneration of 1% on assets realized (69,301 x 1%)	(693)					
	68,608					
Less: Payment made to creditors	(646)	(646)				
Transferred to P& L A/c		2,400				
	67,962					
Less: Payment for Y's loan A/c	(18,000)		(18,000)			

Amount available for distribution to partners	49,962	nil			
Less: Z's remuneration of 10% of the amount distributed to partners (49,962 x 10/110)	(4,542)				
Balance to be distributed to partners on the basis of HRCM1	45,420				
Less: Paid to Z (W.N.)	(2,000)				(2,000)
	43,420				48,000
Less: Paid to X and Z in 5:4 (W.N.)	(18,000)		(10,000)	-	(8,000)
Balance due	25,420		50,000	40,000	40,000
Less: Paid to X, Y & Z in 5:4:4	25,420		(9,778)	(7,821)	(7,821)
	Nil				
Amount of 3rd instalment	40,000		40,222	32,179	32,179
Less: Z's remuneration of 1% on assets realized (40,000 x 1%)	(400)				
	39,600				
Less: Z's remuneration of 10% of the amount distributed to partners (39,600 x 10/110)	(3,600)				
	36,000				
Less: Paid to X, Y, Z in 5:4:4 for (W.N.)	(36,000)		(13,846)	(11,077)	(11,077)
	Nil		26,376	21,102	21,102
Amount of 4th and last instalment	28,000				
Less: Z's remuneration of 1% on assets realized (28,000 x 1%)	(280)				
	27,720				
Less: Z's remuneration of 10% of the amount distributed to partners (27,720 x 10/110)	(2,520)				
	25,200				
Less: Paid to X, Y and Z in 5:4:4	(25,200)		(9,692)	(7,754)	(7,754)
Nil					
Loss suffered by partners			16,684	13,348	13,348

Working Note:

(i) ₹ 1100 added to the first instalment received on sale of assets represents the Cash in Bank

(ii) The amount due to Creditors at the end of the utilization of First Instalment is ₹ 3046. However, since the creditors were settled for ₹ 63,600 only the balance ₹646 were paid and the balance ₹ 2400 was transferred to the Profit & Loss Account.

(iii) **Highest Relative Capital Basis**

		X ₹	Y ₹	Z ₹
Balance of Capital Accounts	(A)	60,000	40,000	50,000
Profit sharing ratio		5	4	4
Capital Profit sharing ratio		12,000	10,000	12,500
Capital in profit sharing ratio taking Y's Capital as base	(B)	50,000	40,000	40,000
Excess of X's Capital and Z's Capital	(A-B) = (C)	10,000	nil	10,000
Again repeating the process				
Profit sharing ratio		5		4
Capital Profit sharing ratio		2,000		2,500
Capital in profit sharing ratio taking X's Capital as base	(D)	10,000		8,000
Excess of Z's Capital	(C-D) = (E)	nil		2,000

Therefore, firstly ₹2,000 is to be paid to Z, then X and Z to be paid in proportion of 5:4 upto ₹ 18,000 to bring the capital of all partners X, Y and Z in proportion to their profit sharing ratio. Thereafter, balance available will be paid in the profit sharing ratio 5:4:4 to all partners viz X, Y and Z.

Q-29 Write short note on Designated Partners in a Limited Liability Partnership and what are their liabilities.

Ans. **"Designated partner"** means any partner designated as such pursuant to section 7 of the Limited Liability Partnerships (LLPs) Act, 2008. As per section 7 of the LLP Act, every limited Liability Partnership shall have at least 2 designated Partners who are individuals and at least one of them shall be a resident in India.

Provided that in case of Limited Liability Partnership in which all the partners are bodies corporate or in which one or more partners are Individuals and bodies corporate, at least 2 individuals who are partners of such limited liability Partnership or Nominees of such Bodies corporate shall act as designated partners.

"Liabilities of designated partners"

As per Section 8 of LLP Act, unless expressly provided otherwise in this Act, a designated partner shall be-

(a) responsible for the doing of all acts, matters and things as are required to be done by the limited liability partnership in respect of compliance of the provisions of this Act including filing of any document, return, statement and the like report pursuant to the provisions of this Act and as may be specified in the limited liability partnership agreement; and;

(b) liable to all penalties imposed on the limited liability partnership for any contravention of those provisions.

Q-30 P and Q were partners sharing profits equally of P & Q Co. Their Balance Sheet as on March 31, 2021 was as follows:

Balance Sheet as on 31st March, 2021

Equity and Liabilities		₹	Assets	₹
Capitals:			Bank	30,000
P	1,00,000		Debtors	25,000
Q	50,000	1,50,000	Stock	35,000
Creditors		20,000	Furniture	40,000
Q's current account		10,000	Machinery	60,000
Reserves		15,000	P's current account	10,000
Bank overdraft		5,000		
		2,00,000		2,00,000

The firm was dissolved on the above date:

P took over 50% of the stock at 10% less on its book value, and the remaining stock was sold at a gain of 15%. Furniture and Machinery realized for ₹ 30,000 and ₹ 50,000 respectively; There was an unrecorded investment which was sold for ₹ 25,000; Debtors realized 90% only and ₹ 1,245 were recovered for bad debts written off last year; There was an outstanding bill for repairs which had to be paid for ₹ 2,000.

You are required to prepare Realization Account, Partners' capital accounts (including transfer of current account balances) and Bank Account in the books of the firm.

Ans.(a)

Books of P & Q Co.

Realization Account

	Particulars		₹		Particulars		₹
To	Debtors	25,000		By	Creditors		20,000
To	Stock	35,000		By	Bank overdraft		5,000
To	Furniture	40,000		By	Bank:		
To	Machinery	60,000	1,60,000		Investment	25,000	
To	Bank:				Furniture	30,000	
	Creditors	20,000			Machinery	50,000	
	Bank overdraft	5,000			Debtors (90%)	22,500	
	Outstanding bill	2,000	27,000		Stock	20,125	
To	Profit transferred				Bad debts		
	to:				Recovered	1,245	1,48,870
	P's capital	1,310		By	P's capital		15,750
	Q's capital	1,310	2,620		(stock taken over)		
			1,89,620				1,89,620

Partners' Capital Accounts

		P	Q			P	Q
To	P's current Account	16,940		By	Balance b/d	1,00,000	50,000
To	Bank			By	Q's current Account		18,810
		83,060	68,810				
		1,00,000	**68,810**			**1,00,000**	**68,810**

Bank Account

	₹		₹
To Balance b/d	30,000	By Realization	27,000
To Realization	1,48,870	By P's capital	83,060
		By Q's capital	68,810
	1,78,870		1,78,870

Working Note:

Partners' Current Accounts

	P	Q		P	Q
To Balance b/d	10,000		By Balance b/d		10,000
To Realization	15,750		By Reserves	7,500	7,500
To Q's capital	18,810		By Realization (profit)	1,310	1,310
			By P's Capital	16,940	
	25,750	18,810		25,750	18,810

Q-31 Differentiate on ordinary partnership firm with an LLP (Limited Liability Partnership) in respect of the following:

(1) Applicable Law

(2) Perpetual Succession

(3) Ownership of Assets

(4) Liability of Partners/Members

(5) Principal-Agent Relationship.

Ans.

Key Elements	Partnerships	LLPs
Applicable Law	Indian Partnership Act 1932	The Limited Liability Partnerships Act, 2008
Perpetual Succession	Partnerships do not have perpetual succession	It has perpetual succession and individual partners may come and go
Ownership of Assets	Firm cannot own any assets. The partners own the assets of the firm	The LLP as an independent entity can own assets
Liability of Partners/ Members	Unlimited: Partners are severally and jointly liable for actions of other partners and the firm and their liability extends to personal assets	Limited to the extent of their contribution towards LLP except in case of intentional fraud or wrongful act of omission or commission by a partner.
Principal-Agent Relationship	Partners are the agents of the firm and of each other	Partners are agents of the firm only and not of other partners

Q-32 The following is the Balance Sheet of M/s. R and S as on 31st March, 2019:

Equity and Liabilities		₹	Assets	₹
Capital Accounts:			Machinery	54,000
R	50,000		Furniture	5,000
S	30,000		Investments (non-trading)	50,000
Reserves	20,000		Stock	20,000
Loan Account of S		15,000	Debtors	21,000
Creditors		40,000	Cash	5,000
		1,55,000		1,55,000

It was agreed that Mr. T is to be admitted for a fourth share in the future profits from 1st April, 2019. He is required to contribute cash towards goodwill and ₹ 15,000 towards capital.

The following further information is furnished:

(a) R & S share the profits in the ratio 3 : 2.

(b) R was receiving salary of ₹ 750 per month from the very inception of the firm in 2012 in addition to share of profit.

(c) The future profit ratio between R, S & T will be 2:1:1. R will not get any salary after the admission of T.

(d) It was agreed that the value of goodwill of the firm shall be determined on the basis of 3 years' purchase of the average profits from business of the last 5 years. Goodwill was not to be raised in the books. The particulars of the profits are as under:

Year ended	Profit/(Loss)
31st March, 2015	25,000
31st March, 2016	12,500
31st March, 2017	(2,500)
31st March, 2018	35,000
31st March, 2019	30,000

The above Profits and Losses are after charging the Salary of R. The Profit of the year ended 31st March, 2015 included an extraneous profit of ₹ 40,000 and the loss for the year ended 31st March, 2017 was on account of loss by strike to the extent of ₹ 20,000.

(e) The cash trading profit for the year ended 31st March, 2020 was ₹ 50,000 before depreciation.

(f) The partners had drawn each ₹ 1,000 per month as drawings.

(g) The value of other assets and liabilities as on 31st March, 2020 were as under:

	₹
Machinery (before depreciation)	60,000
Furniture (before depreciation)	10,000
Investment	50,000
Stock	15,000
Debtors	30,000
Creditors	20,000

(h) Provide depreciation @ 10% on Machinery and @ 5% on Furniture on the closing balance and interest is accumulated @ 6% on S's loan. The loan along with interest would be repaid within next 12 months.

(i) Investments (non -trading) are held from inception of the firm and interest is received @ 10% p.a.

(j) The partners applied for conversion of the firm into Karma Ltd., a Private Limited Company. Certificate was received on 1st April, 2020. They decided to convert Capital Accounts of the partners into share capital in the ratio of 2:1:1 on the basis of a total capital as on 31st March, 2020. If necessary, partners have to subscribe to fresh capital or withdraw.

Prepare the Profit and Loss Account of the firm for the year ended 31st March, 2020 and the Balance Sheet of the Company as at 1st April, 2020.

Ans.

M/s R, S and T

Profit and Loss Account for the year ending on 31st March, 2020

		₹			₹
To	Depreciation on Machinery	6,000	By	Trading Profit	50,000
To	Depreciation on furniture	500	By	Interest on Investment	5,000
To	Interest on S's loan	900			
To	Net Profit to :				
	R's Capital A/c	23,800			
	S's Capital A/c	11,900			
	T's Capital A/c	11,900			
		55,000			55,000

Balance Sheet of the Karma Pvt. Ltd. as at 1st April, 2020

		Notes No.	₹
I	**Equity and Liabilities**		
	Shareholders' funds		
	Share capital		1,41,600
	Current liabilities		
	Short term borrowings	1	15,900
	Trade payables		20,000
	Total		1,77,500
II	**Assets**		
	Non-current assets		
	Property, plant & Equipment (PPE)	2	63,500
	Non-current investments		50,000
	Current assets		
	Inventories		15,000
	Trade receivables		30,000
	Cash and cash equivalents		19,000
	Total		1,77,500

Notes to Accounts

			₹
1.	**Short term borrowings**		
	Loan from S		15,900
2.	**PPE**		
	Machinery	54,000	
	Furniture	9,500	63,500

Working Notes:

1. Calculation of goodwill

	2014-15 ₹	2015-16 ₹	2016-17 ₹	2017-18 ₹	2018-19 ₹
Profits/(Loss)	25,000	12,500	(2,500)	35,000	30,000
Adjustment for extraneous profit of 2014-15 and abnormal loss of 2016-17	(40,000)	-	20,000	—	—
	(15,000)	12,500	17,500	35,000	30,000
Add: Salary of R (750 x12)	9,000	9,000	9,000	9,000	9,000
	(6,000)	21,500	26,500	44,000	39,000
Less: Interest on nontrading investment	(5,000)	(5,000)	(5,000)	(5,000)	(5,000)
	(11,000)	16,500	21,500	39,000	34,000
Total Profit from 2015-16 to 2018-19					1,11,000
Less: Loss for 2014-15					(11,000)
					1,00,000
Average Profit					20,000
Goodwill equal to 3 years' purchase					60,000
Contribution from T for ¼ share					15,000

2. Calculation of sacrificing ratio of Partners R and S on admission of T

	Old share	New share	Sacrificing share	Gaining share
R	3/5	1/2	$\frac{3}{5}-\frac{1}{2}=\frac{6-5}{10}=\frac{1}{10}$	
S	2/5	1/4	$\frac{2}{5}-\frac{1}{4}=\frac{8-5}{20}=\frac{3}{20}$	
T		1/4		1/4

3. Goodwill adjustment entry through Partners' capital accounts (in their sacrificing ratio of 2:3)

		₹	₹
T' s capital A/c	Dr.	15,000	
To R's capital A/c			6,000
To S' s capital A/c			9,000
(T's share in goodwill adjusted through R and S)			

4. **Partners' Capital Accounts**

	R ₹	S ₹	T ₹		R ₹	S ₹	T ₹
To Drawings (1,000 x 12)	12,000	12,000	12,000	By Balance b/d	50,000	30,000	—
To R		6,000		By General Reserve	12,000	8,000	—
To S		9,000		By T	6,000	9,000	—
To Balance c/d	79,800	46,900	14,900	By Bank (15,000 + 15,000)	—	—	30,000
				By Profit & Loss A/c	23,800	11,900	11,900
	91,800	58,900	41,900		91,800	58,900	41,900

5. **Balance Sheet of the firm as on 31st March, 2020**

Equity and Liabilities	₹	₹	Assets	₹	₹
R's Capital	79,800		Machinery	60,000	
S's Capital	46,900		Less: Depreciation	(6,000)	54,000
T's Capital	14,900	1,41,600	Furniture	10,000	
			Less: Depreciation	(500)	9,500
S's Loan	15,000		Investments		50,000
Add: Interest due	900	15,900	Stock-in-trade		15,000
Creditors		20,000	Debtors		30,000
			Cash (W.N.6)		19,000
		1,77,500			1,77,500

6. **Cash balance as on 31.3.2020**

	₹	₹
Cash trading profit		50,000
Add: Investment Interest		5,000
Add: Decrease in Stock Balance		5,000
		60,000
Less: Increase in Debtors	9,000	
Less: Decrease in Creditors	20,000	(29,000)
		31,000
Add: Opening cash balance	5,000	
Add: Cash brought in by T	30,000	35,000
		66,000
Less: Drawings (12,000 +12,000 +12,000)	36,000	
Less: Additions to Machine (60,000 - 54,000)	6,000	
Furniture (10,000 - 5,000)	5,000	(47,000)
Closing cash balance		19,000

7. Distribution of shares – Conversion into Company

		₹
Capital:	R	79,800
	S	46,900
	T	14,900
Share Capital		1,41,600
Distribution of shares:	R (1/2)	70,800
	S (1/4)	35,400
	T (1/4)	35,400

R and S should withdraw capital of ₹9,000 (₹ 79,800 – ₹ 70,800) and ₹11,500 (₹ 46,900 – ₹ 35,400) respectively and T should subscribe shares of ₹ 20,500 (₹35,400 – ₹ 14,900).

Q-33 TJM & Sons is a partnership firm consisting of T, J and M who share profits and loses in the ratio of 2:2:1 and JEK Limited is another company doing similar business .

The firm (TJM & Sons) and the company (JEK Ltd) provide you the following ledger balances as on 31.03.2021:

	TJM Sons (₹)	JEK Ltd. (₹)
Debit Balances:		
Plant & Machinery	7,50,000	24,00,000
Furniture & Fixtures	75,000	3,37,500
Inventories	3,00,000	12,75,000
Trade receivables	3,00,000	12,37,500
Cash at Bank	15,000	6,00,000
Cash in hand	60,000	1,50,000
Credit Balances		
Equity share capital: Equity shares of ₹ 10 each		30,00,000
Partners Capitals		
T	3,00,000	
J	4,50,000	
M	1,50,000	
General Reserve	1,50,000	10,50,000
Trade Payables	4,50,000	19,50,000

On the balance sheet date, it was decided that the firm TJM & Sons be dissolved and all the assets (except cash in hand and cash at bank) and all the liabilities of the firm be taken over by JEK Limited by issuing 75,000 shares of ₹ 10/- each at a premium of ₹ 4/- per share. Plant & Machinery and Furniture & Fixtures are to be revalued at ₹ 8,50,000 and ₹ 1,00,000.

Partners of TJM & Sons agreed to divide the shares issued by JEK Limited in the profit - sharing ratio and bring necessary cash for settlement of their capital.

The trade payables of TJM & Sons include ₹ 1,50,000 payables to JEK Limited. An unrecorded liability of ₹ 37,500 of TJM & Sons must also be taken over by JEK Ltd.

You are required to prepare:

(i) Realization account, Partners' capital accounts and cash in hand/Bank account in the books of TJM & Sons.

(ii) Pass journal entries in the books of JEK Limited for acquisition of TJM & Sons.

(b) State the circumstances when Garner v/s Murray rule is not applicable.

Answer

(a) (i) **In the books of TJM& Sons**

Realization Account

	Particulars		₹		Particulars	₹
To	Plant & Machinery		7,50,000	By	Trade payable	4,50,000
To	Furniture & Fixture		75,000	By	JEK Ltd. (Refer W.N.)	10,50,000
To	Inventories		3,00,000			
To	Trade receivables		3,00,000			
To	Partners' Capital Accounts (Profit):					
	T's Capital A/c	30,000				
	J's Capital A/c	30,000				
	M's Capital A/c	15,000	75,000			
			15,00,000			**15,00,000**

Partners' Capital Accounts

Particulars		T	J	M	Particulars		T	J	M
		₹	₹	₹			₹	₹	₹
To	Shares in JEK Ltd.	4,20,000	4,20,000	2,10,000	By	Balance b/d	3,00,000	4,50,000	1,50,000
To	Cash	-	1,20,000		By	General Reserve	60,000	60,000	30,000
					By	Realization A/c	30,000	30,000	15,000
					By	Cash	30,000	-	15,000
		4,20,000	5,40,000	2,10,000			4,20,000	5,40,000	2,10,000

Cash and Bank Account

Particulars		Cash	Bank	Particulars		Cash	Bank
		₹	₹			₹	₹
To	Balance b/d	60,000	15,000	By	Cash A/c (Contra)*		15,000
To	Bank A/c (Contra)*	15,000		By	J		1,20,000
To	T	30,000					
To	M	15,000					
		1,20,000	**15,000**			**1,20,000**	**15,000**

(ii) Journal Entries in the Books of JEK Ltd.

			Dr. (₹)	Cr. (₹)
1.	Business Purchase Account	Dr.	10,50,000	
	To Liquidators of TJM& Sons			10,50,000
	(Being business of TJM& Sons purchased and payment due)			
2.	Plant and Machinery A/c	Dr.	8,50,000	
	Furniture and Fixture A/c	Dr.	1,00,000	

	Inventories A/c	Dr.	3,00,000	
	Trade Receivables A/c	Dr.	3,00,000	
	To Trade Payables			4,50,000
	To Unrecorded Liability			37,500
	To Business Purchase Account			10,50,000
	To Capital Reserve (B.F.)			12,500
	(Being take over of all assets and liabilities)			
3.	Liquidators of TJM& Sons	Dr.	10,50,000	
	To Equity Share Capital Account			7,50,000
	To Securities Premium Account			3,00,000
	(Being purchase consideration discharged in the form of shares of ₹ 10 each issued at a premium of ₹ 4 each)			
4.	Trade Payables Account	Dr.	1,50,000	
	To Trade Receivables Account			1,50,000
	(Being mutual owing eliminated)			

*It is assumed that cash at bank has been withdrawn to pay to Partner J.

Working Note:

Computation of purchase consideration:

75,000 Equity shares of ₹14 each = ₹ 10,50,000

Equity shares to be given to partners :

T = 30,000 Shares @ ₹ 14 = ₹ 4,20,000

J = 30,000 shares @ ₹ 14 = ₹ 4,20,000

M = 15,000 shares @ ₹ 14 = ₹ 2,10,000

(b) Non-Applicability of Garner vs Murray rule:

1. When the solvent partner has a debit balance in the capital account.
   Only solvent partners will bear the loss of capital deficiency of insolvent partner in their capital ratio. If incidentally, a solvent partner has a debit balance in his capital account, he will escape the liability to bear the loss due to insolvency of another partner.
2. When the firm has only two partners.
3. When there is an agreement between the partners to share the deficiency in capital account of the insolvent partner.
4. When all the partners of the firm are insolvent.

Q-34 The following is the summarized Balance Sheet of M/s Red and Black as on 31st March, 2021:

Liabilities		**(₹)**	**Assets**	**(₹)**
Red's Capital	80,000		Building	1,00,000
Black's Capital	1,00,000	1,80,000	Closing Stock	60,000
Red's Loan		20,000	Sundry Debtors	40,000
General Reserve		20,000	Investment	40,000
Sundry Creditors		40,000	(6% Debentures in XYZ Ltd.)	
			Cash	20,000
		2,60,000		**2,60,000**

It was agreed that Mr. White is to be admitted for a fifth share in the future profits from 1st April, 2021. He is required to contribute cash towards goodwill and ₹ 20,000 towards capital.

(a) The following further information is furnished:

(i) The partners Red and Black shared the profits in the ratio of 3 : 2.

(ii) Mr. Red was receiving a salary of ₹ 1000 p.m. from the very inception of the firm in addition to the share of profit.

(iii) The future profit ratio between Red, Black and White will be 3 : 1 : 1. Mr. Red will not get any salary after the admission of Mr. White.

(iv) The goodwill of the firm should be determined on the basis of 2 years' purchase of the average profits from business of the last 5 years. The particulars of profits/losses are as under:

Year Ended	(₹)	Profit/Loss
31.3.2017	40,000	Profit
31.3.2018	20,000	Loss
31.3.2019	40,000	Profit
31.3.2020	50,000	Profit
31.3.2021	60,000	Profit

The above profits and losses are after charging the salary of Mr. Red. The profit of the year ended 31st March, 2017 included an extraneous profit of ₹ 60,000 and the loss of the year ended 31st March, 2018 was on account of loss by strike to the extent of '40,000.

(v) It was agreed that the value of the goodwill should not appear in the books of the firm.

(b) Trading profit for the year ended 31st March, 2022 was ₹ 80,000 (Before charging depreciation)

(c) Each partner had drawn ₹ 2,000 per month as drawing during the year 2021-22.

(d) On 31st March, 2022 the following balances appeared in the books:

Building (Before Depreciation)	₹ 1,20,000
Closing Stock	₹ 80,000
Sundry Debtors	Nil
Sundry Creditors	Nil
Investment	₹40,000

(e) Interest@ 6% per annum on Red's loan was not paid during the year.

(f) Interest on Debentures received during the year.

(g) Depreciation is to be provided @ 5% on closing balance of Building.

(h) Partners applied for conversion of the firm into a private Limited Company; i.e. RBW Private Limited. Certificate received on 1.4.2022.

They decided to convert Capital accounts of the partners into share capital, in the ratio of 3: 1: 1 (on the basis of total Capital as on 31.3.2022). If necessary, partners have to subscribe to fresh capital or withdraw.

You are required to prepare: (1) Profit & Loss Account for the year ended 31st March, 2022 in the books of M/s Red and Black and (2) Balance Sheet as on 1st April, 2022 in the books of RBW Private Limited.

Ans **M/s Red, Black and White**

Statement of Profit & Loss for the year ended on 31st March, 2022

		₹		₹
To	Dep. Building (1,20,000x5%)	6,000	By Trading Profit	80,000
To	Interest on Red's loan (20,000 x 6%)	1,200	By Interest on Debentures	2,400

To	Net Profit to :		
	Red's Capital A/c	45,120	
	Black's Capital A/c	15,040	
	White's Capital A/c	15,040	
		82,400	**82,400**

Balance Sheet of the RBW Pvt. Ltd. as at 1-4-2022

		Notes No.	₹
I	Equity and Liabilities		
	Shareholders funds		2,39,040
	Non-current liabilities		
	Long term borrowings	1	21,200
	Total		2,60,240
	Assets		
	Non-current assets		
	PPE	2	1,14,000
	Non-current investments		40,000
	Current assets		
	Inventories		80,000
	Cash and cash equivalents		26,240
	Total		2,60,240

Notes to Accounts

		₹
1.	Borrowings	
	Loan from Red	21,200
2.	PPE	
	Land and Building (1,20,000 – 6,000)	1,14,000

Working Notes:

1. Calculation of goodwill:

				Year ended March, 31	
	2017	**2018**	**2019**	**2020**	**2021**
	₹	₹	₹	₹	v
Book Profits	40,000	(20,000)	40,000	50,000	60,000
Adjustment for extraneous profit 2017 and abnormal loss 2018	(60,000)	40,000	—	—	—
	(20,000)	20,000	40,000	50,000	60,000
Add Back: Remuneration of Red	12,000	12,000	12,000	12,000	12,000
	(8,000)	32,000	52,000	62,000	72,000
Less: Debenture Interest being nonoperating income	(2,400)	(2,400)	(2,400)	(2,400)	(2,400)
	(10,400)	29,600	49,600	59,600	69,600
Total Profit from 2018 to 2021					2,08,400
Less: Loss for 2017					(10,400)

Accumulated Profit	1,98,000
Average Profit	39,600
Goodwill equal to 2 years' purchase	79,200
Contribution from White, equal to 1/5	15,840

2.

Partners' Capital accounts

	Red	Black	White			Red	Black	White
	₹	₹	₹			₹	₹	₹
To Drawings	24,000	24,000	24,000	By	Balance b/d	80,000	1,00,000	—
To Black			15,840					
To Balance c/d	1,13,120	1,14,880	11,040	By	General Reserve	12,000	8,000	—
				By	White		15,840	—
				By	Bank	—	—	35,840
				By	Profit & Loss A/c	45,120	15,040	15,040
	1,37,120	**1,38,880**	**50,880**			**1,37,120**	**1,38,880**	**50,880**

3.

Balance Sheet as on 31st March, 2022

Liabilities	₹	₹	**Assets**	₹	₹
Red's Capital		1,13,120	Land & Building	1,20,000	
Black's Capital		1,14,880	*Less* : Dep.	(6,000)	1,14,000
White's Capital		11,040	Investments		40,000
Red's Loan	20,000		Stock-in-trade		80,000
Add: Int. due	1,200	21,200	Cash (Balancing figure)		26,240*
		2,60,240			**2,60,240**

4.

Conversion into Company

		₹
Capital :	Red	1,13,120
	Black	1,14,880
	White	11,040
Share Capital		2,39,040
Distribution of share:	Red (3/5)	1,43,*424*
	Black (1/5)	47,808
	White (1/5)	47,808

Red should subscribe shares of ₹ 30,304 (₹1,43,424 – ₹1,13,120) and White should subscribe shares of ₹ 36,768 (₹ 47,808 less 11,040). Black withdraws ₹ 67,072 (₹ 47,808 – ₹ 1,14,880).

5. Adjustment for Goodwill amounting ₹ 79,200

	To be raised in old Ratio	To be written off in new ratio	Difference
Red	47,520	47,520	Nil
Black	31,680	15,840	15,840 Cr.
White		15,840	15,840 Dr.

* Also the closing cash balance can be derived as shown below:

Trading profit (assume realised)		80,000
Add: Debenture Interest		2,400
Add: Decrease in Debtors Balance		40,000
		1,22,400
Less: Increase in stock	20,000	
Less: Decrease in creditors	40,000	(60,000)
Cash Profit		62,400
Add: Opening cash balance		20,000
Add: Cash brought in by White		35,840
		1,18,240
Less: Drawings	72,000	
Less: Additions to Building	20,000	(92,000)
		26,240

Q-35 A partnership firm was dissolved on 30th June, 2020. Its Balance Sheet on the date of dissolution was as follows:

Equity & Liabilities	₹	₹	**Assets**	₹
Capitals:			Cash	10,800
A	76,000		Sundry Assets	1,89,200
B	48,000			
C	36,000	1,60,000		
Loan A/c – B		10,000		
Sundry Creditors		30,000		
		2,00,000		**2,00,000**

The assets were realized in instalments and the payments were made on the proportionate capital basis. Creditors were paid ₹ 29,000 in full settlement of their account. Expenses of realization were estimated to be ₹ 5,400 but actual amount spent was ₹ 4,000. This amount was paid on 15th September. Draw up a statement showing distribution of cash, which was realized as follows:

	₹
On 5th July, 2020	25,200
On 30th August, 2020	60,000
On 15th September, 2020	80,000

The partners shared profits and losses in the ratio of 2 : 2 : 1. Prepare a statement showing distribution of cash amongst the partners by 'Highest Relative Capital' method.

Ans. Statement showing distribution of cash amongst the partners

		Creditors	B's Loan	A	B	C
2020		₹	₹	₹	₹	₹
Balance b/d		30,000	10,000	76,000	48,000	36,000
Cash balance less Provision for expenses (₹ 10,800 – ₹ 5,400)		5,400	-	-	-	-
Balances unpaid		24,600	10,000	76,000	48,000	36,000
July 5						
1st Instalment of ₹ 25,200		23,600	1,600	-	-	-
Discount received on full settlement		1,000	8,400	76,000	48,000	36,000
Less: Transferred to Realization A/c		1,000				
		Nil				
August 30						
2nd instalment of ₹ 60,000 (W.N. 2)			8,400	32,640	4,640	14,320
Balance unpaid		Nil	43,360	43,360	21,680	
September 15						
Amount realised	₹ 80,000					
Add: Balance out of the Provision for Expenses A/c	1,400					
	81,400			32,560	32,560	16,280
Amount unpaid being loss on Realization in the ratio of 2 : 2 : 1				10,800	10,800	5,400

Working Notes:

1. **Highest relative capital basis**

		A	B	C
		₹	₹	₹
1.	Present Capitals	76,000	48,000	36,000
2.	Profit-sharing ratio	2	2	1
3	Capital per unit of Profit share (1 ÷ 2)	38,000	24,000	36,000
4.	Proportionate capitals taking B, whose capital is the least, as the basis	48,000	48,000	24,000
5.	Excess capital (1-4)	28,000	Nil	12,000
6.	Profit-sharing ratio	2	-	1
7.	Excess capital per unit of Profit share (5 ÷ 6)	14,000		12,000
8.	Proportionate capitals as between A and C taking C capital as the basis	24,000	-	12,000
9.	Excess of A's Capital over C's Excess capital (5-8)	4,000	-	-
10.	Balance of Excess capital (5-9)	24,000		12,000
11.	Distribution sequence:			

First ₹ 4,000 (2 : 0 : 0)	4,000	-	-
Next ₹ 36,000 (2 : 0 : 1)	24,000	-	12,000
Over ₹ 40,000 (2 : 2 : 1)			

2. **Distribution of Second instalment**

			Creditors	A	B	C
First	₹	8,400	8,400	-	-	-
Next	₹	4,000 (2 : 0 : 0)		4,000	-	-
Next	₹	36,000 (2 : 0 : 1)		24,000	-	12,000
Balance	₹	11,600 (2 : 2 : 1)		4,640	4,640	2,320
		60,000	8,400	32,640	4,640	14,320

Q-36 Explain Garner v/s Murray rule applicable in the case of partnership firms. State the conditions when this rule is not applicable.

Ans. Garner vs. Murray rule: When a partner is unable to pay his debt due to the firm, he is said to be insolvent and the share of loss is to be borne by other solvent partners in accordance with the decision held in the English case of Garner vs. Murray. According to this decision, normal loss on realisation of assets is to be brought in cash by all partners (including insolvent partner) in the profit sharing ratio but a loss due to insolvency of a partner has to be borne by the solvent partners in their capital ratio. In order to calculate the capital ratio, no adjustment will be made in case of fixed capitals. However, in case of fluctuating capitals, ratio should be calculated on the basis of adjusted capital before considering profit or loss on realization at the time of dissolution.

Non-Applicability of Garner vs Murray rule:

1. When the solvent partner has a debit balance in the capital account.

   Only solvent partners will bear the loss of capital deficiency of insolvent partner in their capital ratio. If incidentally a solvent partner has a debit balance in his capital account, he will escape the liability to bear the loss due to insolvency of another partner.
2. When the firm has only two partners.
3. When there is an agreement between the partners to share the deficiency in capital account of insolvent partner.
4. When all the partners of the firm are insolvent.

Q-37 A Ltd. holds 80% of the equity capital and voting power in B Ltd. A Ltd sells inventories costing ₹ 180 lacs to B Ltd at a price of ₹ 200 lacs. The entire inventories remain unsold with B Ltd at the financial year end i.e. 31 March 2020. What will be the accounting treatment for this transaction in the consolidated financial statements of A Ltd?

Ans. This would be the case of downstream transaction. In the consolidated profit and loss account for the year ended 31 March 2020, entire transaction of sale and purchase of ₹ 200 lacs each, would be eliminated by reducing both sales and purchases (cost of sales). Further, the unrealized profits of ₹ 20 lacs (i.e. ₹ 200 lacs – ₹ 180 lacs), would be eliminated from the consolidated financial statements for financial year ended 31 March 2020, by reducing the consolidated profits/ increasing the consolidated losses, and reducing the value of closing inventories as of 31 March 2020.

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NOTES

CHAPTER-3

ACCOUNTING FOR EMPLOYEE STOCK OPTION PLANS

Q-1 On 1st April, 2019, a company offered 100 shares to each of its 400 employees at ₹ 25 per share. The employees are given a month to accept the shares. The shares issued under the plan shall be subject to lock -in to transfer for three years from the grant date i.e. 30th, April 2019. The market price of shares of the company on the grant date is ₹ 30 per share.

Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at ₹ 28 per share.

Up to 30th April, 2019, 50% of employees accepted the offer and paid ₹ 25 per share purchased. Nominal value of each share is ₹ 10. You are required to record the issue of shares in the books of the company under the aforesaid plan.

Ans. Fair value of an option = ₹ 28

Difference between Fair value and Issue Price = ₹ 28 – ₹ 25 = 3.

Number of employees accepting the offer = 400 employees x 50% = 200 employees

Number of shares issued = 200 employees x 100 shares/employee = 20,000 shares

Employee Compensation Expenses recognized in 2019 -20 =20,000 shares x ₹ 3 = ₹ 60,000

Securities Premium A/c = ₹ 28 – 10 = ₹ 18 per share = 20,000 x 18 = ₹ 3,60,000

Journal Entry

Date	Particulars		₹	₹
30.04.2019	Bank (20,000 shares x ₹ 25)	Dr.	5,00,000	
	Employees compensation expense A/c	Dr.	60,000	
	To Share Capital			2,00,000
	To Securities Premium			3,60,000
	(Being stock purchase option accepted by 200 employees for 100 shares each at ₹ 25 per share on a Fair Value of ₹ 28 per share)			

Note: Employees compensation expenses amounting ₹ 60,000 will ultimately be charged to profit & loss account.

Q-2 On 1st April, 2018, a company offered 100 shares to each of its 500 employees at Rs. 50 per share. The employees are given a year to accept the offer. The shares issued under the plan shall be subject to lock-in on transfer for three years from the grant date. The market price of shares of the company on the grant date is Rs. 60 per share. Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at Rs. 56 per share. On 31st March, 2019, 400 employees accepted the offer and paid Rs. 50 per share purchased. Nominal value of each shares is Rs. 10.

Record the issue of shares in the books of the company under the aforesaid plan.

Ans. Fair value of an option = Rs. 56 – Rs. 50 = Rs. 6

Number of shares issued = 400 employees x 100 shares/employee = 40,000 shares

Fair value of ESOP = 40,000 shares x Rs. 6 = Rs. 2,40,000

Vesting period = 1 month

Expenses recognized in 2018-19 = Rs. 2,40,000

Date	Particulars		Rs.	Rs.
31.03.2019	Bank (40,000 shares x Rs. 50)	Dr.	20,00,000	
	Employees compensation expense A/c	Dr.	2,40,000	
	To Share Capital			
	(40,000 shares x Rs.10)			4,00,000
	To Securities Premium			
	(40,000 shares x Rs. 46)			18,40,000
	(Being option accepted by 400 employees			
	& payment made @ Rs. 56 share)			
	Profit & Loss A/c	Dr.	2,40,000	
	To Employees compensation expenseA/c			2,40,000
	(Being Employees compensation expense			
	transferred to Profit & Loss A/c)			

Q-3 A company has its share capital divided into shares of ₹ 10 each. On 1-1-20X1, it granted 5,000 employees stock options at ₹ 50, when the market price was ₹ 140. The options were to be exercised between 1-3-20X2 to 31-03-20X2. The employees exercised their options for 4,800 shares only; remaining options lapsed. Pass the necessary journal entries for the year ended 31-3-20X2, with regard to employees' stock options.

Ans. Journal Entries in the books of company

Date	Particulars		Dr. ₹	Cr. ₹
1-3-X2 to	Bank A/c	Dr.	2,40,000	
31-3-X2	Employees compensation expenses A/c	Dr.	4,32,000	
	To Equity Share Capital A/c			48,000
	To Securities Premium A/c			6,24,000
	(Being allotment to employees 4,800 shares of			
	₹ 10 each at a premium of Rs. 130 at an exercise			
	price of ₹ 50 each)			
31-3-X2	Profit and Loss account	Dr.	4,32,000	
	To Employees compensation expenses A/c			4,32,000
	(Being transfer of employees compensation expenses)			

Working Note:

1. Employee Compensation Expenses = Discount between Market Price and option price = ₹ 140 – ₹ 50 = ₹ 90 per share = ₹ 90 x 4,800 = ₹ 4,32,000/- in total.
2. The Employees Compensation Expense is transferred to Securities Premium Account.
3. Securities Premium Account = ₹ 50 – ₹ 10 = ₹ 40 per share + ₹ 90 per share on account of discount of option price over market price = Rs. 130 per share = ₹ 130 x 4,800 = ₹ 6, 24,000/- in total.

Q-4 Explain the concept of graded vesting under an employee stock option plan.

Ans. Graded vesting under an employee stock option plan: In case the options/shares granted under an employee stock option plan do not vest on one date but have graded vesting schedule, total plan should be segregated into different groups, depending upon the vesting dates. Each of such groups would be having different vesting period and expected life and, therefore, each vesting date should be considered as a separate option grant and evaluated and accounted for accordingly. For example, suppose an employee is granted 100 options which will vest @ 25 options per year at the end of the third, fourth, fifth and sixth years. In such a case, each lot of 25 options would be evaluated and accounted for separately.

Q-5 A company has its share capital divided into shares of ₹ 10 each. On 1-1-20X1, it granted 5,000 employees stock options at ₹ 50, when the market price was ₹ 140. The options were to be exercised between 1-3-20X2 to 31-03-20X2. The employees exercised their options for 4,800 shares only; remaining options lapsed. Pass the necessary journal entries for the year ended 31-3-20X2, with regard to employees' stock options.

Ans. **Journal Entries in the books of company**

Date	Particulars		Dr. ₹	Cr. ₹
1-3-X2 to	Bank A/c	Dr.	2,40,000	
31-3-X2	Employees compensation expenses A/c	Dr.	4,32,000	
	To Equity Share Capital A/c			48,000
	To Securities Premium A/c			6,24,000
	(Being allotment to employees 4,800 shares of ₹ 10 each at a premium of ₹ 130 at an exercise price of ₹ 50 each)			
31-3-X2	Profit and Loss account	Dr.	4,32,000	
	To Employees compensation expenses A/c			4,32,000
	(Being transfer of employees compensation expenses)			

Working Note:

1. Employee Compensation Expenses = Discount between Market Price and option price = ₹ 140 – ₹ 50 = ₹ 90 per share = ₹ 90 x 4,800 = ₹ 4,32,000/- in total.
2. The Employees Compensation Expense is transferred to Securities Premium Account.
3. Securities Premium Account = ₹ 50 – ₹ 10 = ₹ 40 per share + ₹ 90 per share on account of discount of option price over market price = Rs. 130 per share = ₹ 130 x 4,800 = ₹ 6, 24,000/- in total.

Q-6 The following particulars in respect of stock options granted by a company are available: Grant date April 1, 2016

Number of employees covered	50
Number of options granted per employee	1,000
Fair value of option per share on grant date (₹)	9

The options will vest to employees serving continuously for 3 years from vesting date, provided the share price is ₹ 65 or above at the end of 2018-19.

The estimates of number of employees satisfying the condition of continuous employment were 48 on 31/03/17, 47 on 31/03/18. The number of employees actually satisfying the condition of continuous employment was 45.

The share price at the end of 2018-19 was ₹ 68.

You are required to compute expenses to be recognised in each year in the books of the company.

Ans. The vesting of options is subject to satisfaction of two conditions viz. service condition of continuous employment for 3 years and market condition that the share price at the end of 2018-19 is not less than ₹ 65. The company should recognise value of option over 3-year vesting period from 2016-17 to 2018-19.

Year 2016-17

Fair value of option per share = ₹ 9

Number of shares expected to vest under the scheme = 48 × 1,000 = 48,000

Fair value = 48,000 × ₹ 9 = ₹ 4,32,000

Expected vesting period = 3 years

Value of option recognised as expense in 2016-17 = ₹ 4,32,000 /3 = ₹ 1,44,000

Year 2017-18

Fair value of option per share = ₹ 9

Number of shares expected to vest under the scheme = 47 × 1,000 = 47,000

Fair value = 47,000 × ₹ 9 = ₹ 4,23,000

Expected vesting period = 3 years

Cumulative value of option to recognise as expense in 2016-17 and 2017-18

= (₹ 4,23,000/ 3) × 2 = ₹ 2,82,000

Value of option recognised as expense in 2016-17 = ₹ 1,44,000

Value of option recognised as expense in 2017-18

= ₹2,82,000 – ₹ 1,44,000 = ₹ 1,38,000

Year 2018-19

Fair value of option per share = ₹ 9

Number of shares actually vested under the scheme = 45 × 1,000 = 45,000

Fair value = 45,000 × ₹ 9 = ₹ 4,05,000

Vesting period = 3 years

Cumulative value of option to recognise as expense in 2016-17, 2017-18 and 2018-19 = ₹ 4,05,000

Value of option recognised as expense in 2016-17 and 2017-18 = ₹ 2,82,000

Value of option recognised as expense in 2018-19 = ₹ 4,05,000 – ₹ 2,82,000 = ₹ 1,23,000

Q-7 A company has its share capital divided into shares of ₹ 10 each. On 1-1-20X1, it granted 7,500 employees stock options at ₹ 50, when the market price was ₹ 140. The options were to be exercised between 1-3-20X2 to 31-03-20X2. The employees exercised their options for 7,200 shares only; remaining options lapsed. Pass the necessary journal entries for the year ended 31-3-20X2, with regard to employees' stock options.

Ans. **In the books of Company**

Journal Entries

Date	Particulars		Dr. ₹	Cr. ₹
1-3-X2 to	Bank A/c (7,200 x 50)	Dr.	3,60,000	
31-3-X2	Employees compensation expenses A/c	Dr.	6,48,000	
	To Equity Share Capital A/c (7,200 x 10)			72,000
	To Securities Premium A/c (7,200 x ₹ 130)			9,36,000
	(Being allotment to employees 7,200 shares of ₹ 10 each at a premium of ₹ 130 at an exercise price of ₹ 50 each)			
31-3-X2	Profit and Loss account	Dr.	6,48,000	
	To Employees compensation expenses A/c			6,48,000

(Being transfer of employees compensation expenses)

Working Notes:

1. Employee Compensation Expenses = Discount between Market Price and option price = ₹ 140 – ₹ 50 = ₹ 90 per share = ₹ 90 x 7,200 = ₹ 6,48,000 in total.
2. Securities Premium Account = ₹ 50 – ₹ 10 =₹ 40 per share + ₹ 90 per share on account of discount of option price over market price = ₹ 130 per share = ₹ 130 x 7,200= ₹ 9,36,000 in total.

Q-8 JKS Ltd. has its share capital divided into equity shares of ₹ 10 each. On 1.1.2018 it granted 5,000 employee stock options at ₹ 30 per share, when the market price was ₹ 50 per share. The options were to be exercised between 15th March, 2018 and 31st March, 2018. The employees exercised their options for 3,600 shares only and the remaining options lapsed. The company closes its books on 31st March every year. You are required to prepare journal entries (with narration) as would appear in the books of the company up to 31st March, 2018.

Ans. **Journal Entries in the books of JKS Ltd**

			₹	₹
15.03.2018	Bank A/c (3,600 x ₹ 30)	Dr.	1,08,000	
to 31.3.18	Employee compensation expense A/c (3,600 x ₹ 20)	Dr.	72,000	
	To Equity share capital A/c (3600 x ₹ 10)			36,000
	To Securities premium A/c (3600 x ₹ 40)			1,44,000
	(Being shares issued to the employees against the options vested to them in pursuance of Employee Stock Option Plan)			
31.3.18	Profit and Loss A/c	Dr.	72,000	
	To Employee compensation expenses A/c			72,000
	(Being transfer of employee compensation expenses transfer to Profit and Loss Account)			

Working Notes:

1. No entry is passed when stock options are granted to employees. Hence, no entry will be passed on 1st January 2018;
2. Market Price = ₹ 50 per share and stock option price = ₹ 30, Hence, the difference ₹ 50 – ₹ 30 = ₹ 20 per share is equivalent to employee cost or employee compensation expense and will be charged to P &L Account as such for the number of options exercised i.e. 3,600 shares.

Q-9 At the beginning of year 1, the enterprise grants 1,000 stock options to each member of its sales team, conditional upon the employees remaining in the employment of the enterprise for three years, and the team selling more than 50,000 units of a particular product over the three-year period. The fair value of the stock options is ₹ 15 per option at the date of grant.

During year 2, the enterprise increases the sales target to 1,00,000 units. By the end of year 3, the enterprise has sold 55,000 units, and the stock options do not vest.

Twelve members of the sales team have remained in service for the three-year period. You are required to examine and give comment in light of the relevant Guidance Note that whether the company should recognise the expenses on the base of options granted or not.

Also state will your answer differ if, instead of modifying the performance target, the enterprise had increased the number of years of service required for the stock options to vest from three years to ten years.

Ans. Paragraph 19 of the Guidance Note on Share Based Payments requires, for a performance condition that is not a market condition, the enterprise to recognize the services received during the vesting

period based on the best available estimate of the number of shares or stock options expected to vest and to revise that estimate, if necessary, if subsequent information indicates that the number of shares or stock options expected to vest differs from previous estimates. On vesting date, the enterprise revises the estimate to equal the number of instruments that ultimately vested. However, paragraph 24 of the Guidance Note requires, irrespective of any modifications to the terms and conditions on which the instruments were granted, or a cancellation or settlement of that grant of instruments, the enterprise to recognize, as a minimum, the services received, measured at the grant date fair value of the instruments granted, unless those instruments do not vest because of failure to satisfy a vesting condition (other than a market condition) that was specified at grant date.

Furthermore, paragraph 26(c) of the Guidance Note specifies that, if the enterprise modifies the vesting conditions in a manner that is not beneficial to the employee, the enterprise does not take the modified vesting conditions into account when applying the requirements for treatment of vesting conditions as specified in Guidance Note.

Therefore, because the modification to the performance condition made it less likely that the stock options will vest, which was not beneficial to the employee, the enterprise takes no account of the modified performance condition when recognizing the services received. Instead, it continues to recognize the services received over the three-year period based on the original vesting conditions. Hence, the enterprise ultimately recognizes cumulative remuneration expense of ₹ 1,80,000 over the three-year period (12 employees × 1,000 options × ₹ 15).

The same result would have occurred if, instead of modifying the performance target, the enterprise had increased the number of years of service required for the stock options to vest from three years to ten years. Because such a modification would make it less likely that the options will vest, which would not be beneficial to the employees, the enterprise would take no account of the modified service condition when recognizing the services received. Instead, it would recognize the services received from the twelve employees who remained in service over the original three-year vesting period.

Q-10 PQ Ltd. grants 100 stock options to each of its 1,000 employees on 1-4-2015, conditional upon the employee remaining in the company for 2 years. The fair value of the option is ₹ 18 on the grant date and the exercise price is ₹ 55 per share. The other information is given as under:

(i) Number of employees expected to satisfy service condition are 930 in the 1st yearand 850 in the 2nd year.

(ii) 40 employees left the company in the 1st year of service and 880 employees haveactually completed 2 year vesting period.

You are required to calculate ESOP cost to be amortized by PQ Ltd. in the years 2015- 2016 and 2016-2017.

Ans. Calculation of ESOP cost to be amortized

	2015-2016	**2016-2017**
Fair value of options pershare	₹ 18	₹ 18
No. of options expected tovest under the scheme	93,000 (930 x 100)	88,000 (880 x 100)
Fair value of options	₹ 16,74,000	₹ 15,84,000
Value of options recognizedas expenses	(₹ 16,74,000 / 2)	(₹ 15,84,000 – ₹ 8,37,000)
	8,37,000	7,47,000

Q-11 Bee Ltd. has its share capital divided into Equity Shares of ₹ 10 each. On 1st April, 2017, the company offered 250 shares to each of its 520 employees at ₹ 60 per share, when the market price was ₹ 150 per share. The options were to be exercised between 01-03-2018 to 31-03-2018.

410 employees accepted the offer and paid ₹ 60 per share on purchased shares and the remaining options lapsed.

The company closes its books on 31st March every year.

You are required to show Journal Entries (with narrations) as would appear in the books of Bee Ltd. for the year ended 31st March, 2018 with regard to employees stock options.

Ans. **Journal Entries in the books of Bee Ltd.**

			₹	₹
1.3.18	Bank A/c (1,02,500 x ₹ 60)	Dr.	61,50,000	
to	Employee compensation expense A/c			
31.3.18	(1,02,500 x ₹90)	Dr.	92,25,000	
	To Equity share capital A/c (1,02,500 x ₹10)			10,25,000
	To Securities premium A/c (1,02,500 x ₹140)			1,43,50,000
	(Being shares issued to the employees against the options vested to them in pursuance of Employee Stock Option Plan)			
31.3.18	Profit and Loss A/c	Dr.	92,25,000	
	To Employee compensation expense A/c			92,25,000
	(Being transfer of employee compensation expenses to Profit and Loss Account)			

Q-12 Lucky Ltd. grants 100 stock options to each of its 1,500 employees on 1-4-2014 for ₹ 40, depending upon the employees at the time of vesting of options. Options would be exercisable within a year it is vested. The market price of the share is ₹ 70 each. These options will vest at the end of year 1 if the earning of Lucky Ltd. is 15%, or it will vest at the end of the year 2 if the average earning of two years is 13% or lastly it will vest at the end of the third year if the average earning of 3 years will be 10% 8,000, unvested options lapsed on 31-3-2015. 6,000 unvested options lapsed on 31-3-2016 and finally 4,000 unvested options lapsed on 31-3-2017.

The earnings of Lucky Ltd. for the three financial years ended on 31st March, 2015; 2016 and 2017 are 14%, 10% and 8% respectively.

1,250 employees exercised their vested options within a year and remaining options were unexercised at the end of the contractual life.

You are required to give the necessary journal entries for the above and also prepare the statement showing compensation expense to be recognized at the end of each year.

Ans.

Date	Particulars		₹	₹
31.3.2015	Employees compensation expense A/c	Dr.	21,30,000	
	To ESOS outstanding A/c			21,30,000
	(Being compensation expenserecognized in respect of the ESOP i.e. 100options each granted to 1,500 employees at adiscount of ₹ 30 each, amortised on straightline basis over vesting years (Refer W.N.)			
	Profit and Loss A/c	Dr.	21,30,000	
	To Employees compensationexpenses A/c			21,30,000
	(Being expenses transferred to profit and LossA/c)			

31.3.2016	Employees compensation expenses A/c	Dr.	5,90,000	
	To ESOS outstanding A/c			5,90,000
	(Being compensation expense recognized inrespect of the ESOP- Refer W.N.)			
	Profit and Loss A/c	Dr.	5,90,000	
	To Employees compensationexpenses A/c			5,90,000
	(Being expenses transferred to profit and LossA/c)			
31.3.2017	Employees compensation Expenses A/c	Dr.	12,40,000	
	To ESOS outstanding A/c			12,40,000
	(Being compensation expense recognized inrespect of the ESOP- Refer W.N.)			
	Profit and Loss A/c		12,40,000	
	To Employees compensationexpenses A/c			12,40,000
	(Being expenses transferred to profit and LossA/c)			
2018-19	Bank A/c (1,250 x100 x40)	Dr.	50,00,000	
	ESOS outstanding A/c[(39,60,000 x 1,25,000/ 1,32,000]	Dr.	37,50,000	
	To Equity share capital (1250 x 100 x 10)			12,50,000
	To Securities premium A/c [(1250 x 100x (70-10)]			75,00,000
	(Being 1,25,000 options exercised at anexercise price of ₹ 40 each)			
31.3.2019	ESOS outstanding A/c	Dr.	2,10,000	
	To General Reserve A/c			2,10,000
	(Being ESOS outstanding A/c on lapse of 7,000options at the end of exercise of option periodtransferred to General Reserve A/c)			

Working Note:

Statement showing compensation expense to be recognized at the end of:

Particulars	Year 12014-15	Year 22015-16	Year 32016-17
Number of options expectedto vest*	1,42,000 options	1,36,000 options	1,32,000 options
Total compensation expense accrued (70-40)	₹ 42,60,000	₹ 40,80,000	₹ 39,60,000
Compensation expense ofthe year	42,60,000 x 1/2 = ₹ 21,30,000	40,80,000 x 2/3 = ₹ 27,20,000	₹ 39,60,000
Compensation expenserecognized previously	Nil	₹ 21,30,000	₹ 27,20,000
Compensation expenses tobe recognized for the year	₹ 21,30,000	₹ 5,90,000	₹ 12,40,000

*It is assumed that each share is of ₹ 10 each and Lucky Ltd. expects all the options to be vested after deducting actual lapses during the year.

Q-13 Suvidhi Ltd. offered 50 shares to each of its 1500 employees on 1st April 2017 for ₹ 30. Option would be exercisable within a year it is vested. The shares issued under the plan shall be subject to lock-in on transfer for three years from the grant date. The market price of shares of the company is ₹ 50 per share on grant date. Due to post vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at ₹ 38 per share.

On 31st March, 2018,1200 employees accepted the offer and paid ₹ 30 per share purchased. Nominal value of each share is ₹ 10.

Record the issue of shares in the books of the company under the aforesaid plan.

Ans. **Journal Entries in the books of Suvidhi Ltd.**

Date	Particulars		Dr. (₹)	Cr. (₹)
31.3.18	Bank A/c (60,000 shares x ₹ 30)	Dr.	18,00,000	
	Employees stock compensation expense A/c	Dr.	4,80,000	
	To Share Capital A/c (60,000 shares x ₹ 10)			6,00,000
	To Securities Premium (60,000 shares x ₹ 28)			16,80,000
	(Being shares issued under ESOP @ ₹ 30 to 1,200 employees)			
	Profit & Loss A/c	Dr.	4,80,000	
	To Employees stock compensation expense A/c			4,80,000
	(Being Employees stock compensation expense			
Q-14	transferred to Profit & Loss A/c)			

Working Note:

Fair value of an option = ₹38 – ₹30 = ₹ 8

Number of shares issued = 1,200 employees x 50 shares/employee = 60,000 shares

Fair value of ESOP which will be recognized as expenses in the year 2017-2018

= 60,000 shares x ₹ 8 = ₹ 4,80,000

Vesting period = 1 year

Expenses recognized in 2017-2018 = ₹ 4,80,000.

Q-14 Suvidhi Ltd. offered 50 stock options to each of its 1500 employees on 1st April 2019 for ₹ 30.

Option was exercisable within a year it was vested. The shares issued under this plan shall be subject to lock-in on transfer for three years from the grant date. The market price of shares of the company is ₹ 50 per share on grant date. Due to post vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at ₹ 38 per share. On 31st March, 2020,1200 employees accepted the offer and paid ₹ 30 per share purchased. Nominal value of each share is ₹ 10. Record the issue of shares in the books of the company under the aforesaid plan.

Ans. **Journal Entries in the books of Suvidhi Ltd.**

Date	Particulars		Dr. (₹)	Cr. (₹)
31.3.20	Bank A/c (60,000 shares x ₹ 30)	Dr.	18,00,000	
	Employees stock compensation expense A/c	Dr.	4,80,000	
	To Share Capital A/c (60,000 shares x ₹ 10)			6,00,000
	To Securities Premium			16,80,000
	(60,000 shares x ₹ 28)			
	(Being shares issued under ESOP @ ₹ 30 to 1,200			
	employees)			

Profit & Loss A/c	Dr.	4,80,000	
To Employees stock compensation expense A/c			4,80,000
(Being Employees stock compensation expense transferred to Profit & Loss A/c)			

Working Note:

Fair value of an option = ₹ 38 – ₹ 30 = ₹ 8

Number of shares issued = 1,200 employees x 50 shares = 60,000 shares

Fair value of ESOP which will be recognized as expenses in the year 2019-2020

= 60,000 shares x ₹ 8 = ₹ 4,80,000

Vesting period = 1 year

Expenses recognized in 2019-2020 = ₹ 4,80,000

Q-15 Kaushal Ltd. has its share capital divided into equity shares of ₹ 10 each. On 1.1.2020 it granted 5,000 employee stock options at ₹ 30 per share, when the market price was ₹ 50 per share. The options were to be exercised till the month of March, 2020. The employees exercised their options for 3,600 shares only and the remaining options lapsed. Show Journal entries (with narration) as would appear in the books of the company till the month of March, 2020 relating to ESOPs as the company closes its books on 31st March every year.

Ans. **Journal Entries in the books of Kaushal Ltd.**

			₹	₹
1.3.2020	Bank A/c	Dr.	1,08,000	
to	Employee compensation expense A/c	Dr.	72,000	
31.3.2020	To Equity share capital A/c			36,000
	To Securities premium A/c			1,44,000
	(Being shares issued to the employees against the options vested to them in pursuance of Employee Stock Option Plan)			
31.3.2020	Profit and Loss A/c	Dr.	72,000	
	To Employee compensation expenses A/c			72,000
	(Being transfer of employee compensation expenses transfer to Profit and Loss Account)			

Working Note:

Market Price = ₹ 50 per share and stock option price = ₹ 30, Hence, the difference ₹ 50 – ₹ 30 = ₹ 20 per share is equivalent to employee cost or employee compensation expense and will be charged to P&L Account as such for the number of options exercised i.e. 3,600 shares.

Q-16 Raja Ltd. has its share capital divided into equity shares of ₹ 10 each. On 01-08-2019, it granted 2,500 employees stock options at ₹ 50 per share, when the market price was ₹ 140 per share. The options were to be exercised between 1-10-2019 to 31-03-2020. The employees exercised their options for 2,400 shares only and the remaining options lapsed. Raja Ltd. closes its books of accounts on 31st March, every year.

You are to required to pass the necessary Journal Entries (including narration) for the year ended 31-03-2020, with regard to employees' stock options and give working notes also.

Ans. **Journal Entries in the books of Raja Ltd.**

			₹	₹
1.10.19	Bank A/c	Dr.	1,20,000	
to 31.3.20	Employee compensation expense A/c	Dr.	2,16,000	
	To Equity share capital A/c			24,000
	To Securities premium A/c			3,12,000
	(Being shares issued to the employees against the options vested to them in pursuance of Employee Stock Option Plan)			
31.3.20	Profit and Loss A/c	Dr.	2,16,000	
	To Employee compensation expense A/c			2,16,000
	(Being transfer of employee compensation expenses to Profit and Loss Account)			

No entry is passed when stock options are granted to employees. Hence, no entry will be passed on 1st August, 2019;

Working Note:

Market Price = ₹ 140 per share and stock option price = 50, Hence, the difference 140 – 50 = ₹ 90 per share is equivalent to employee cost or employee compensation expense and will be charged to P&L Account as such for the number of options exercised i.e. 2,400 shares. Hence, Employee compensation expenses will be 2,400 shares X ₹ 90 = ₹ 2,16,000

Q-17 On 1st October, 2020, A Limited granted 25,000 Employees' Stock Option at ₹ 70 per share. The market price of share was ₹ 130 per share. The options were to be exercised between 1st December, 2020 and 31st March, 2021. The face value of shares is ₹ 10 each. The employees exercised option for 18,000 shares only and the balance options lapsed. The company closes its books of accounts on 31st March every year.

Pass necessary journal entries with narration to record the transaction in the books of the company.

Ans. **Journal Entries in the books of A Ltd.**

Date	Particulars		Dr. (₹)	Cr. (₹)
01.12.2020 to	Bank A/c (18,000 x ₹ 70)	Dr.	12,60,000	
31.03.2021	Employee compensation expenses account [18,000 x (₹ 130- ₹ 70)]	Dr.	10,80,000	
	To Equity share capital account (18,000 x ₹ 10)			1,80,000
	To Securities premium account (18,000 x ₹ 120)			21,60,000
	(Being 18,000 employees stock option exercised at an exercise price of ₹ 70 each)			
31.3.2021	Profit and Loss account	Dr.	10,80,000	
	To Employee compensation expenses account			10,80,000
	(Being transfer of employee compensation expenses account to profit and loss account)			

Working Note:

Fair value of an option = Market price of a share – Exercise price of a share

= ₹ 130 – ₹ 70 = ₹ 60 per share

Q-18 At the beginning of the year 1, Harmony Limited grants 600 options to each of its 1000 employees. The contractual life of option granted is 6 years.

Other relevant information is as follows:

Vesting Period	3 years
Exercise period	3 years
Expected Life	5 years
Exercise Price	₹ 100
Market Price	₹ 100
Expected Forfeitures per year	3%

The option granted vest according to a graded schedule of 25% at the end of the year 1, 25% at the end of the year 2 and the remaining 50% at the end of the year 3.

You are required to calculate total compensation expenses for the options expected to vest and cost and cumulative cost to be recognized at the end of all the three years assuming that expected forfeiture rate does not change during the vesting period when the Intrinsic value of the options at the grant date is ₹ 7 per option.

Ans. Since the options granted have a graded vesting schedule, the enterprise segregates the total plan into different groups, depending upon the vesting dates and treats each of these groups as a separate plan. The enterprise determines the number of options expected to vest under each group as below:

Vesting Date (Year-end)		**Options expected to vest**
1.	600 options x 1,000 employees x 25% x 0.97	1,45,500 options
2.	600 options x 1,000 employees x 25% x 0.97 x 0.97	1,41,135 options
3.	600 options x 1,000 employees x 50% x 0.97x 0.97 x 0.97	2,73,802 options
Total option expected to vest		5,60,437 options

In case of intrinsic value method, total compensation expense for the options expected to vest would be

Vesting Date (End of year)	**Expected Vesting (No. of Options)**	**Value per Option (₹)**	**Compensation Expense (₹)**
1	1,45,500	7	10,18,500
2	1,41,135	7	9,87,945
3	2,73,802	7	19,16,614
	5,60,437		39,23,059

Total compensation expense of ₹ 39,23,059, determined at the grant date, would be attributed to the years 1, 2 and 3 as below:

Vesting Date (End of year)	Cost to be recognized Year 1	Year 2	Year 3
1.	10,18,500		
2.	4,93,972.50*	4,93,972.50	
3.	6,38,871	6,38,871	6,38,872
Cost for the year	21,51,343.50	11,32,843.50	6,38,872
Cumulative cost	21,51,343,50	32,84,187	39,23,059

* Alternatively, it may be rounded off as ₹ 4,93,972 in year 1 and ₹ 4,93,973 in year 2.

Q-19 Sun Ltd. grants 100 stock options to each of its 1200 employees on 01.04.2016 for ₹ 30, depending upon the employees at the time of vesting of options. Options would be exercisable within a year it is vested. The market price of the share is ₹ 60 each. These options will vest at the end of the year 1 if the earning of Sun Ltd. is 16% or it will vest at the end of year 2 if the average earning of two years is 13%, or lastly it will vest at the end of the third year, if the average earning of 3 years is 10%. 6000 unvested options lapsed on 31.3.2017, 5000 unvested options lapsed on 31.03.2018 and finally 4000 unvested options lapsed on 31.03.2019.

The earnings of Sun Ltd. for the three financial years ended on 31st March, 2017, 2018 and 2019 are 15%, 10% and 6%, respectively.

1000 employees exercised their vested options within a year and remaining options were unexercised at the end of the contractual life.

You are requested to give the necessary journal entries for the above and prepare the statement showing compensation expenses to be recognized at the end of each year.

Ans.

Date	Particulars		₹	₹
31.3.2017	Employees compensation expense A/c	Dr.	17,10,000	
	To ESOS outstanding A/c			17,10,000
	(Being compensation expenserecognized in respect of the ESOP i.e.100 options each granted to 1,200employees at a discount of ₹ 30 each, amortized on straight line basis over vesting years (Refer W.N.)			
	Profit and Loss A/c	Dr.	17,10,000	
	To Employees compensation expenses A/c			17,10,000
	(Being expenses transferred to profit and Loss A/c)			
31.3.2018	Employees compensation expenses A/c	Dr.	4,70,000	
	To ESOS outstanding A/c			4,70,000
	(Being compensation expense recognized in respect of the ESOPRefer W.N.)			
	Profit and Loss A/c	Dr.	4,70,000	
	To Employees compensation expenses A/c			4,70,000
	(Being expenses transferred to profit and Loss A/c)			

31.3.2019	Employees compensation Expenses A/c	Dr.	9,70,000	
	To ESOS outstanding A/c			9,70,000
	(Being compensation expense recognized in respect of the ESOPRefer W.N.)			
	Profit and Loss A/c		9,70,000	
	To Employees compensation expenses A/c			9,70,000
	(Being expenses transferred to profit and Loss A/c)			
2019-20	Bank A/c (1,00,000 x ₹ 30)	Dr.	30,00,000	
	ESOS outstanding A/c [(31,50,000/1,05,000) x 1,00,000]	Dr.	30,00,000	
	To Equity share capital (1,00,000 x ₹ 10)			10,00,000
	To Securities premium A/c (1,00,000 x ₹ 50)			50,00,000
	(Being 1,00,000 options exercised at an exercise price of ` 30 each)			
31.3.2020	ESOS outstanding A/c	Dr.	1,50,000	
	To General Reserve A/c			1,50,000
	(Being ESOS outstanding A/c on lapse of 5,000 options at the end of exercise ofoption period transferred to GeneralReserve A/c)			

Working Note:

Statement showing compensation expense to be recognized at the end of:

Particulars	**Year 1 (31.3.2017)**	**Year 2 (31.3.2018)**	**Year 3 (31.3.2019)**
Number of options expected to vest	1,14,000 options	1,09,000 options	1,05,000 options
Total compensation expense accrued (60-30)	₹ 34,20,000	₹ 32,70,000	₹ 31,50,000
Compensation expense of the year	34,20,000 x 1/2 = ₹ 17,10,000	32,70,000 x 2/3 = ₹ 21,80,000	₹ 31,50,000
Compensation expense recognized previously	Nil	₹ 17,10,000	₹ 21,80,000
Compensation expenses to be **recognized for the year**	**₹ 17,10,000**	**₹ 4,70,000**	**₹ 9,70,000**

Q-20 Define the following terms:

(i) Vesting Period;

(ii) Grant Date.

Ans.

(i) Vesting Period: It is the time period between grant date and the date on which all the specified vesting conditions of an employee share-based payment plan is to be satisfied.

(ii) **Grant Date:** It is the date at which the enterprise and its employees agree to the terms of an employee share-based payment plan. At grant date, the enterprise confers on the employees the right to cash or shares of the enterprise, provided the specified vesting conditions, if any, are met. If that agreement is subject to an approval process, (for example, by shareholders), grant date is the date when that approval is obtained.

Q-21 PQ Ltd. grants 100 stock options to each of its 1,000 employees on 1-4-2018, conditional upon the employee remaining in the company for 2 years. The fair value of the option is ₹ 18 on the grant date and the exercise price is ₹ 55 per share. Number of employees expected to satisfy service conditions are 930 in the 1st year and 850 in the 2nd year. However, 880 employees actually completed 2 year vesting period.

You are required to calculate ESOP cost to be amortized by PQ Ltd. in the years 2018-2019 and 2019-2020.

Ans. **Calculation of ESOP cost to be amortized**

	2018-2019	**2019-2020**
Fair value of options per share	₹ 18	₹ 18
No. of options expected to vest under the scheme	93,000 (930 x 100)	88,000 (880 x 100)
Fair value of options	₹ 16,74,000	₹ 15,84,000
Value of options recognized as expenses	8,37,000 (₹ 16,74,000 / 2)	7,47,000 (₹ 15,84,000 – ₹ 8,37,000)

Q-22 On 1st April, 2020, XYZ Ltd., offered 150 shares to each of its 750 employees at ₹ 60 per share. The employees are given a year to accept the offer. The shares issued under the plan shall be subject to lock-in period on transfer for three years from the grant date. The market price of shares of the company on the grant date is ₹ 72 per share. Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at ₹ 67 per share on the grant date. On 31st March, 2021, 600 employees accepted the offer and paid ₹ 60 per share purchased. Face value of each share is ₹ 10. You are required to record the issue of shares in the books of the XYZ Ltd., under the aforesaid plan.

Ans. Fair value of an option = ₹ 67 – ₹ 60 = ₹ 7

Number of shares issued = 600 employees x 150 shares/employee = 90,000 shares

Fair value of ESOP = 90,000 shares x ₹ 7 = ₹ 6,30,000

Vesting period = 1 year

Expenses recognized in 2020-21 = ₹ 6,30,000

Date	Particulars		₹	₹
31.03.2021	Bank (90,000 shares x ₹ 60)	Dr.	54,00,000	
	Employees stock compensation expense A/c	Dr.	6,30,000	
	To Share Capital (90,000 shares x ₹ 10)			9,00,000
	To Securities Premium (90,000 shares x ₹ 57)			51,30,000
	(Being option accepted by 600 employees & payment made @ ₹ 60 per share)			
	Profit & Loss A/c	Dr.	6,30,000	
	To Employees stock compensation expense A/c			6,30,000
	(Being Employees stock compensation expense transferred to Profit & Loss A/c)			

Q-23 Define the following terms:

(i) Vesting

(ii) Exercise Period

(iii) Grant date

(iv) Exercise Price

Ans.

(i) **Vesting**: It means the process by which the employee is given the right to apply for the sharesof the company against the option granted to him under the employees' stock option plan.

(ii) **Exercise Period:** It is the time period after vesting within which the employee should exercise his right to apply for shares against the option vested in him in pursuance of the employees' stock option plan.

(iii) **Grant Date**: It is the date at which the enterprise and its employees agree to the terms of an employee share-based payment plan. At grant date, the enterprise confers on the employees the right to cash or shares of the enterprise, provided the specified vesting conditions, if any, are met.

(iv) **Exercise Price**: It is the price payable by the employee for exercising the option granted to him in pursuance of employees' stock option scheme.

Q-24 Raja Ltd. has its share capital divided into equity shares of ₹ 10 each. On 01-08-2019, it granted 2,500 employees stock options at ₹ 50 per share, when the market price was ₹ 140 per share. The options were to be exercised between 1-10-2019 to 31-03-2020. The employees exercised their options for 2,400 shares only and the remaining options lapsed. Raja Ltd. closes its books of accounts on 31st March, every year.

You are to require to pass the necessary Journal Entries (including narration) for the year ended 31-03-2020, with regard to employees' stock options and give working notes also.

Ans. **Journal Entries in the books of Raja Ltd.**

			₹	₹
1.10.19	Bank A/c Dr. 1,20,000	Dr.		
to	Employee compensation expense A/c	Dr.	2,16,000	
31.3.20	To Equity share capital A/c			24,000
	To Securities premium A/c 3,12,000			
	(Being shares issued to the employees			
	against the options vested to them in			
	pursuance of Employee Stock Option Plan)			
31.3.20	Profit and Loss A/c	Dr.	2,16,000	
	To Employee compensation expense A/c			2,16,000
	(Being transfer of employee compensation			
	expenses to Profit and Loss Account)			

Working Note:

Market Price = ₹ 140 per share and stock option price = 50, Hence, the difference 140 - 50 = ₹ 90 per share is equivalent to employee cost or employee compensation expense and will be charged to P&L Account as such for the number of options exercised i.e. 2,400 shares. Hence, Employee compensation expenses will be 2,400 shares x ₹ 90 = ₹ 2,16,000

Q-25 Define the following terms:

(i) Vesting

(ii) Grant date

(iii) Exercise Price

Ans. (i) **Vesting** means to become an entitlement. Under an employee stock option plan,a counterparty's right to receive cash, other assets or equity instruments of the enterprise vests when the counterparty's entitlement is no longer conditional on the satisfaction of any vesting conditions.

(ii) **Grant Date** is the date at which the enterprise and another party (i.e. an employee) agree to an employee stock option plan, being when the enterprise and the counterparty have a shared understanding of the terms and conditions of the arrangement. At grant date, the enterprise confers on the counterparty the right to cash, other assets, or equity instruments of the enterprise, provided the specified vesting conditions, if any, are met. If that agreement is subject to an approval process (for example, by shareholders), grant date is the date when that approval is obtained.

(iii) **Exercise Price** is the price payable by the counterparty for exercising the option granted to him/her/it in pursuance of the employee stock option plan.

Q-26 Noor Ltd. has its share capital divided into equity shares of ₹ 10 each. On 1.1.2021it granted 4,000 employee stock options at ₹ 40 per share, when the market pricewas ₹ 60 per share. Fair value per option was ₹ 20. The options were to be exercised between 15th March, 2021 and 31st March, 2021. The employees exercised their options for 2,500 shares only and the remaining options lapsed. The company closes its books on 31st March every year. You are required to give Journal entries (with narration) as would appear in the books of the company for the year ended 31st March, 2021.

Ans. **Journal Entries in the books of Noor Ltd.**

			₹	₹
15.03.2021	Bank A/c (2,500 shares x ₹ 40)	Dr.	1,00,000	
to	Employee compensation expense A/c	Dr.	50,000	
31.3.2021	(2,500 shares x ₹ 20)			
	To Equity share capital A/c			25,000
	(2,500 shares x ₹ 10)			
	To Securities premium A/c			1,25,000
	(2,500 shares x ₹ 50)			
	(Being shares issued to the employeesagainst the options vested to them inpursuance of Employee Stock OptionPlan)			
31.3.2021	Profit and Loss A/c	Dr.	50,000	
	To Employee compensation expenses A/c			50,000
	(Being transfer of employee compensation expenses transfer toProfit and Loss Account)			

Working Notes:

1. No entry is passed when stock options are granted to employees. Hence no entry will be passed on 1 January 2021.
2. Fair value per option i.e. ₹ 20 per option is the employee cost or employee compensation expense and will be charged to P&L Account for the number of options exercised.

Q-27 A company grants 2,000 Employees Stock Options on 1st April 2018 at ₹ 60 when the market price is ₹ 170. The vesting period is 2.5 years, and the maximum exercise period is 1 year. 600 unvested options lapse on 01.05.2020, 1200 options are exercised on 30.06.2021. 200 vested options lapse at the end of the exercise period. You required to pass necessary journal entries with narrations.

Ans. **Journal Entries in the books of Company**

Date	Particulars		Dr. (₹)	Cr. (₹)
31.3.2019	Employees compensation expense account	Dr.	88,000	
	To Employee stock option outstanding account			88,000
	(Being compensation expenses recognized in respect of the employee stock option			
	Profit and loss account	Dr.	88,000	
	To Employees compensation expenses account			88,000
	(Being expenses transferred to profit and loss account at year end)			
31.3.2020	Employees compensation expenses account	Dr.	88,000	
	To Employee stock option outstanding account			88,000

	(Being compensation expense recognized in respect of the employee stock)			
	Profit and loss account	Dr.	88,000	
	To Employees compensation expenses account			88,000
	(Being expenses transferred to profit and loss account at year end)			
31.3.2021	Employee stock option outstanding account (W.N.2)	Dr.	22,000	
	To General Reserve account (W.N.2)			22,000
	(Being excess of employees compensation expenses transferred to general reserve account)			
30.6.2021	Bank A/c (1,200 × ₹ 60)	Dr.	72,000	
	Employee stock option outstanding account (1,200 × ₹ 110)	Dr.	1,32,000	
	To Equity share capital account (1,200 × ₹ 10)			12,000
	To Securities premium account (1,200 x ₹ 160)			1,92,000
	(Being 1,200 employee stock option exercised at an exercise price of ₹ 60 each)			
01.10.2021	Employee stock option outstanding account (W.N.3)	Dr.	22,000	
	To General reserve account (W.N.3)			22,000
	(Being ESOS outstanding A/c on lapse of 200 options at the end of exercise of option period transferred to General Reserve A/c)			

Weighted average number of equity shares outstanding during the period is increased by the weighted average number of additional equity shares which would have been outstanding assuming the conversion of all dilutive potential equity shares.

Working Notes:

1 Compensation expenses recognized in respect of the employee stock option:
2,000 options granted to employees at a discount of ₹ 110 each to be amortized on Straight line basis over 2-1/2 years i.e.
2,000 stock options x ₹ 110 / 2.5 years = ₹ 88,000

2. On 31.3.2021, company will examine its actual forfeitures and make necessary adjustments, if any, to reflect expenses for the number of options that actually vested.
Considering that 1400 stock options have completed 2.5 years vesting period, the expense to be recognized during the year is in negative i.e.

No. of options actually vested 1,400 x 110 (170 – 60 = 110)	₹ 1,54,000
Less: Expenses recognized ₹ (88,000 + 88,000)	(₹ 1,76,000)
Excess expense transferred to general reserve	₹ 22,000

3. Similarly, on 1.10.2021, Employee Stock Option Outstanding Account will be

No. of options actually vested (1,200 x 110)	₹ 1,32,000
Less: Expenses recognized	(₹ 1,54,000)
Excess expense transferred to general reserve	₹ 22,000

Q-28 Shiv Ltd. has its share capital divided into Equity Shares of ₹ 10 each. On 1st April, 2021, the company offered 250 shares to each of its 520 employees at ₹ 60 per share, when the market price was ₹ 150 per share. The options were to be exercised between 01-03-2022 to 31-03-2022.

410 employees accepted the offer and paid ₹ 60 per share on purchased shares and the remaining options lapsed. You are required to show Journal Entries (with narrations) as would appear in the books of Shiv Ltd. for the year ended 31st March, 2022 with regard to employee stock options.

Ans.

Journal Entries in the books of Shiv Ltd.

			₹	₹
1.3.22	Bank A/c (1,02,500 x ₹ 60)	Dr.	61,50,000	
to 31.3.22	Employee compensation expense A/c (1,02,500 x ₹ 90)	Dr.	92,25,000	
	To Equity share capital A/c (1,02,500x ₹ 10)			10,25,000
	To Securities premium A/c (1,02,500 x ₹ 140)			1,43,50,000
	(Being shares issued to the employees against the options vested to them in pursuance of Employee Stock Option Plan)			
31.3.22	Profit and Loss A/c	Dr.	92,25,000	
	To Employee compensation expense A/c			92,25,000
	(Being transfer of employee compensation expenses to Profit and Loss Account)			

Q-29 Suvidhi Ltd. offered 50 stock options to each of its 1500 employees on 1st April 2019 for ₹ 30.

Option was exercisable within a year it was vested. The shares issued under this plan shall be subject to lock-in on transfer for three years from the grant date. The market price of shares of the company is ₹ 50 per share on grant date. Due to post vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at ₹ 38 per share. On 31st March, 2020,1200 employees accepted the offer and paid ₹ 30 per share purchased. Nominal value of each share is ₹ 10. Record the issue of shares in the books of the company under the aforesaid plan.

Ans.

Journal Entries in the books of Suvidhi Ltd.

Date	Particulars		Dr. (₹)	Cr. (₹)
31.3.20	Bank A/c (60,000 shares x ₹ 30)	Dr.	18,00,000	
	Employees stock compensation expense A/c	Dr.	4,80,000	
	To Share Capital A/c (60,000 shares x ₹ 10)			6,00,000
	To Securities Premium (60,000 shares x ₹ 28)			16,80,000

(Being shares issued under ESOP @ ₹ 30 to 1,200 employees)

Profit & Loss A/c	Dr.	4,80,000	
To Employees stock compensation expense A/c			4,80,000

(Being Employees stock compensation expense transferred to Profit & Loss A/c)

Working Note:

Fair value of an option = ₹ 38 – ₹ 30 = ₹ 8

Number of shares issued = 1,200 employees x 50 shares = 60,000 shares

Fair value of ESOP which will be recognized as expenses in the year 2019-2020

= 60,000 shares x ₹ 8 = ₹ 4,80,000

Vesting period = 1 year

Expenses recognized in 2019-2020 = ₹ 4,80,000

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NOTES

CHAPTER-4

BUY-BACK OF SHARES AND EQUITY SHARES WITH DIFFERENT RIGHTS

Q-1 The following was the Balance Sheet of C Ltd. as on 31st March ,2019:

Equity & Liabilities	₹ Lakhs	Assets	₹ Lakhs
Share Capital:		Fixed Assets	14,000
Equity shares of ₹ 10 each Fully Paid Up 8,000		Investments	2,350
10% Redeemable Pref. Shares of ₹ 10 each Fully Paid Up	2,500	Cash at Bank	2,300
Reserves & Surplus		Other Current Assets	8,250
Capital Redemption Reserve	1,000		
Securities Premium	800		
General Reserve	6,000		
Profit & Loss Account	300		
Secured Loans:			
9% Debentures	5,000		
Current Liabilities:			
Trade payables	2,300		
Sundry Provisions	1,000		
	26,900		**26,900**

On 1st April, 2019 the Company redeemed all its Preference Shares at a Premium of 10% and bought back 10% of its Equity Shares at ₹ 20 per Share. In order to make cash available, the Company sold all the Investments for ₹ 2,500 lakhs.

You are required to pass journal entries for the above and prepare the Company's Balance sheet immediately after buyback of equity shares and redemptio n of preference shares.

Ans.

(i) **Journal Entries in the books of C Ltd.** **(₹ in lakhs)**

	Particulars			
1	Bank A/c	Dr.	2,500	
	To Investments A/c			2,350
	To Profit and Loss A/c			150
	(Being investment sold on profit for the purpose of buy-back)			
2	10% Redeemable Preference Share Capital A/c	Dr.	2,500	
	Premium on Redemption of Preference Shares A/c	Dr.	250	
	To Preference Shareholders A/c			2,750
	(Being redemption of preference share capital at premium of 10%)			
3	Securities Premium A/c	Dr.	250	
	To Premium on Redemption of Preference Shares A/c			250
	(Being premium on redemption of preference shares adjusted through securities premium)			

4	Equity Share Capital A/c	Dr.	800	
	Premium on buyback	Dr.	800	
	To Equity buy-back A/c			1,600
	(Being Equity Share bought back, Share Capital cancelled, and Premium on Buyback accounted for)			
5	Securities Premium A/c (800-250)	Dr.	550	
	General Reserve A/c		250	
	To Premium on Buyback A/c			800
	(Being premium on buyback provided first out of securities premium and the balance out of general reserves.)			
6	Preference Shareholders A/c		2,750	
	Equity buy-back A/c		1,600	
	To Bank A/c			4,350
	(Being payment made to preference shareholders and equity shareholders)			
7	General Reserve Account		3,300	
	To Capital Redemption Reserve Account			3,300
	(Being amount transferred to capital redemption reserve account towards face value of preference shares redeemed and equity shares bought back)			

(ii) Balance Sheet of C Ltd. (after Redemption and Buyback)

	Particulars	Note No	(₹ Lakhs) Amount
	EQUITY AND LIABILITIES		₹
(I)	**Shareholders' Funds:**		
	(a) Share Capital	1	7,200
	(b) Reserves and Surplus	2	7,200
(2)	Non-Current Liabilities:		
	(a) Long Term Borrowings	3	5,000
(3)	Current Liabilities:		
	(a) Trade payables		2,300
	(b) Short Term Provisions		1,000
	Total		22,700
(II)	**ASSETS**		
	(1) Non-Current Assets		
	PPE		14,000
	Current Assets:		
	(a) Cash and Cash equivalents (W N)		450
	(b) Other Current Assets		8,250
			22,700

Notes to Accounts

₹ in Lakhs

1.	**Share Capital**			
	720 lakh Equity Shares of ₹ 10 each Fully Paid up (80 lakh Equity Shares bought back)			7,200
2.	**Reserves and Surplus**			
	General Reserve	6,000		
	Less: Adjustment for premium paid on buy back	(250)		
	Less: Transfer to CRR	(3,300)	2,450	
	Capital Redemption Reserve	1,000		
	Add: Transfer due to buy-back of shares from Gen. res.	3,300	4,300	
	Securities premium	800		
	Less: Adjustment for premium paid on redemption of preference shares	(250)		
	Less: Adjustment for premium paid on buy back	(550)	-	
	Profit & Loss A/c	300		
	Add: Profit on sale of investment	150	450	7,200
3.	**Long-term borrowings**			
	Secured			
	9 % Debentures			5,000

Working Note:

Bank Account

Receipts	Amount (₹ Lakhs)	Payments	Amount (₹ Lakhs)
To balance b/d	2,300	By Preference Shareholders A/c	2,750
To Investment A/c (sale Proceeds)	2,500	By Equity Shareholders A/c	1,600
		By Balance c/d (Balancing figure)	450
	4,800		**4,800**

Q-2 The following was the summarized balance sheet of Mukta Ltd. as on 31st March, 2019 :

Equity & liability	Rs. (in lakhs)	Assets	Rs. (in lakhs)
Authorised Capital:		Fixed Assets	1,12,000
Equity shares of Rs. 10 each	80,000	Investments	24,000
Issued Capital		Cash at Bank	13,200
Equity Shares of Rs.10 each Fully Paid Up	64,000	Trade Receivables	66,000
10% Redeemable Preference Shares of 10 each, Fully Paid Up	20,000		
Reserves & Surplus:			
Capital Redemption Reserve	8,000		
Securities Premium	6,400		
General Reserve	48,000		
Profit & Loss Account	2,400		
9% Debentures	40,000		
Trade Payables	26,400		
	2,15,200		**2,15,200**

On 1st April,2019 the Company redeemed all its Preference Shares at a Premium of 10% and bought back 25% of its Equity Shares at Rs.20 per Share. In order to make Cash available, the Company sold all the Investments for Rs.25,200 Lakhs and raised a Bank Loan amounting to Rs.16,000 lakh on the Security of the Company's Plant.

Give the necessary Journal Entries considering that the buy back is authorised by the articles of company and necessary resolution is passed by the company for this. The amount of Securities premium will be utilized to the maximum extents allowed by law.

Ans. Journal entries

In the books of Mukta Ltd.

			Dr.	Cr.
				Rs. in lakhs
1	Bank A/c	Dr.	25,200	
	To Investments A/c			24,000
	To Profit and Loss A/c			1,200
	(Being Investments sold and, profit being credited to Profit and Loss Account)			
2	10% Redeemable Preference Share Capital A/c	Dr.	20,000	
	Premium payable on Redemption of Preference SharesA/c	Dr.	2,000	
	To Preference Shareholders A/c			22,000
	(Being amount payable on redemption of Preference shares, at a Premium of 10%)			
3	Securities Premium A/c	Dr.	2,000	
	To Premium payable on Redemption of Preference Shares A/c			2,000
	(Being Securities Premium utilised to provide Premiumon Redemption of Preference Shares)			
4	Equity Share Capital A/c	Dr.	16,000	
	Premium payable on Buyback A/c	Dr.	16,000	
	To Equity Share buy back A/c			32,000
	(Being the amount due on buy-back)			
5	Securities Premium A/c (6,400 – 2,000)	Dr.	4,400	
	General Reserve A/c (balancing figure)	Dr.	11,600	
	To Premium payable on Buyback A/c			16,000
	(Being premium on buyback provided first out of Securities Premium and the balance out of GeneralReserves.)			
6	Bank A/c	Dr.	16,000	
	To Bank Loan A/c			16,000
	(Being Loan taken from Bank to finance Buyback)			

7	Preference Shareholders A/c	Dr.	22,000	
	Equity Shares buy back A/c	Dr.	32,000	
	To Bank A/c			54,000
	(Being payment made to Preference Shareholders and Equity Shareholders)			
8	General Reserve Account	Dr.	36,000	
	To Capital Redemption Reserve Account			36,000
	(Being amount transferred to Capital Redemption Reserve Account to the extent of face value of preference shares redeemed and equity Shares boughtback) (20,000 + 16,000)			

Q-3 W, X, Y and Z hold equity share capital in the proportion of 40:30:10:20. A, B, C and D hold preference share capital in the proportion of 30:40:20:10. If the paid up capital of the company is Rs. 40 Lakh and Preference share capital is Rs. 20 Lakh, Find their voting rights in case of resolution of winding up of the company.

Ans. W, X, Y and Z hold Equity capital is held by in the proportion of 40:30:10:20 and A, B, C and D hold preference share capital in the proportion of 30:40:20:10. As the paid up equity share capital of the company is Rs. 40 Lakhs and Preference share capital is Rs. 20 Lakh (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be.

W	=	2/3 x 40/100	=	4/15
X	=	2/3 x 30/100	=	3/15
Y	=	2/3 x 10/100	=	1/15
Z	=	2/3 x 20/100	=	2/15
A	=	1/3 x 30/100	=	1/10
B	=	1/3 x 40/100	=	2/15
C	=	1/3 x 20/100	=	1/15
D	=	1/3 x 10/100	=	1/30

Q-4 SMM Ltd. has the following capital structure as on 31st March, 2017: **₹ in crore**

	Particulars	Situation	Situation
(i)	Equity share capital (shares of ₹ 10 each)	1,200	1,200
(ii)	Reserves:		
	General Reserves	1,080	1,080
	Securities Premium	400	400
	Profit & Loss	200	200
	Infrastructure Development Reserve (Statutory Reserve)	320	320
(iii)	Loan Funds	3,200	6,000

The company has offered buy back price of Rs. 30 per equity share.

You are required to calculate maximum permissible number of equity shares that can be bought back in both situations and also required to pass necessary Journal Entries.

Ans. **Statement determining the maximum number of shares to be bought back**

Particulars	Number of shares (in crores) When loan fund is ₹ 3,200 crores	₹ 6,000 crores
Shares Outstanding Test (W.N.1)	30	30
Resources Test (W.N.2)	24	24
Debt Equity Ratio Test (W.N.3)	32	Nil
Maximum number of shares that can be bought back [least of the above]	24	Nil

Journal Entries for the Buy Back

(applicable only when loan fund is ₹ 3,200 crores)

₹ in crores

			Debit	Credit
(a)	Equity share buyback account	Dr.	720	
	To Bank account			720
	(Being payment for buy back of 24 crores equity shares of ₹ 10 each @ ₹ 30 per share)			
(b)	Equity share capital account	Dr.	240	
	Premium Payable on buyback account	Dr.	480	
	To Equity share buyback account			720
	(Being cancellation of shares bought back)			
	Securities Premium account	Dr.	400	
	General Reserve / Profit & Loss A/c	Dr.	80	
	To Premium Payable on buyback account			480
	(Being Premium Payable on buyback account charged to securities premium and general reserve/Profit & Loss A/c)			
(c)	General Reserve / Profit & Loss A/c	Dr.	240	
	To Capital redemption reserve account			240
	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out of redeemed through free reserves)			

Working Notes:

1. Shares Outstanding Test

Particulars	(Shares in crores)
Number of shares outstanding	120
25% of the shares outstanding	30

2. Resources Test

Particulars	(₹ in crores)
Paid up capital	1,200
Free reserves (₹ in crores) (1,080 + 400 +200)	1,680
Shareholders' funds (Rs. in crores)	2,880
25% of Shareholders fund (₹ in crores)	₹ 720 crores
Buy back price per share	₹ 30
Number of shares that can be bought back	24 crores shares

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy Back

Particulars		When loan fund is ₹ 3,200 crores	When loan fund is ₹ 6,000 crores
(a)	Loan funds (Rs.)	3,200	6,000
(b)	Minimum equity to be maintained after buy back in the ratio of 2:1 (₹) (a/2)	1,600	3,000
(c)	Present equity shareholders fund (₹)	2,880	2,880
(d)	Future equity shareholders fund (₹) (see W.N.4)	2,560 (2,880-320)	N.A.
(e)	Maximum permitted buy back of Equity (₹) [(d) – (b)]	960	Nil
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share	32 crore shares	Nil
	As per the provisions of the Companies Act, 2013, company	Qualifies	Does not Qualify

4 Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method

Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y' Then

Equation 1 : (Present Equity- Transfer to CRR)- Minimum Equity to be maintained = Maximum Permitted Buy Back

$= (2,880 - x) - 1,600 = y$

$= 1280 - x = y$ (1)

Equation 2: Maximum Permitted Buy Back *X* Nominal Value Per Share/Offer Price Per Share

$= \left(\frac{y}{30} \times 10\right) = x$ or $3x = y$ (2)

by solving the above two equations we get

x= Rs. 320

y = Rs. 960

Q-5 The following was the Balance Sheet of Omega Ltd. as on 31st March ,2016.

Equity & Liabilities	₹ Lakhs	Assets	₹ Lakhs
Share Capital:		Fixed Assets	14,000
Equity shares of ₹ 10 each Fully Paid Up	8,000	Investments	3,000
10% Redeemable Pref. Shares of ₹ 10 each Fully Paid Up	2,500	Cash at Bank	1,650
Reserves & Surplus		Other Current Assets	8,250
Capital Redemption Reserve	1,000		
Securities Premium	800		
General Reserve	6,000		
Profit & Loss Account	300		
Secured Loans:			
9% Debentures	5,000		
Current Liabilities:			
Trade payables	2,300		
Sundry Provisions	1,000		
	26,900		**26,900**

On 1st April, 2016 the Company redeemed all its Preference Shares at a Premium of 10% and bought back 15% of its Equity Shares at ₹ 20 per Share. In order to make cash available, the Company sold all the Investments for ₹ 3,150 lakhs and raised a Bank Loan amounting to ₹ 400 lakh on the Security of the Company's Plant.

You are required to prepare:

(i) Journal entries for the above and

(ii) Company's Balance sheet immediately thereafter.

Ans. (i) Journal Entries in the books of Omega Ltd. **(₹ in lakhs)**

	Particulars			
1	Bank A/c	Dr.	3,150	
	To Investments A/c			3,000
	To Profit and Loss A/c			150
	(Being investment sold on profit for the purpose of buy-back)			
2	10% Redeemable Preference Share Capital A/c	Dr.	2,500	
	Premium on Redemption of Preference Shares A/c	Dr.	250	
	To Preference Shareholders A/c			2,750
	(Being redemption of preference share capital at premium of 10%)			
3	Securities Premium A/c	Dr.	250	
	To Premium on Redemption of Preference Shares A/c			250
	(Being premium on redemption of preference shares adjusted through securities premium)			
4	Equity Share Capital A/c	Dr.	1,200	
	Premium on buyback	Dr.	1,200	
	To Equity buy-back A/c			2,400
	(Being Equity Share bought back, Share Capital cancelled and Premium on Buyback accounted for)			
5	Securities Premium A/c (800-250)	Dr.	550	
	General Reserve A/c		650	
	To Premium on Buyback A/c			1,200
	(Being premium on buyback provided first out of securities premium and the balance out of general reserves.)			
6	Bank A/c		400	
	To Bank Loan A/c			400
	(Being loan taken from bank to finance buyback and redemption of shares)			
7	Preference Shareholders A/c		2,750	
	Equity buy-back A/c		2,400	
	To Bank A/c			5,150
	(Being payment made to preference shareholders and equity shareholders)			
8	General Reserve Account		3,700	
	To Capital Redemption Reserve Account			3,700
	(Being amount transferred to capital redemption reserve account towards face value of preference shares redeemed and equity shares bought back)			

(ii) Balance Sheet of Omega Ltd. (after Redemption and Buyback) (Rs. Lakhs)

	Particulars	Note No	Amount
	EQUITY AND LIABILITIES	₹	
(1)	Shareholders' Funds:		
	(a) Share Capital	1	6,800
	(b) Reserves and Surplus	2	6,800
(2)	Non-Current Liabilities:		
	(a) Long Term Borrowings	3	5,400
(3)	Current Liabilities:		
	(a) Trade payables		2,300
	(b) Short Term Provisions		1,000
	Total		**22,300**

(II)	ASSETS	
(1)	Non-Current Assets	
	Fixed Assets	14,000
	Current Assets:	
	(a) Cash and Cash equivalents (W N)	50
	(b) Other Current Assets	8,250
		22,300

Notes to Accounts

				₹ in Lakhs
1.	**Share Capital**			
	680 lakh Equity Shares of ₹ 10 each Fully Paid up (120 lakh Equity Shares bought back)			6,800
2.	**Reserves and Surplus**			
	General Reserve	6,000		
	Less: Adjustment for premium paid on buy back	(650)		
	Less: Transfer to CRR	(3,700)	1,650	
	Capital Redemption Reserve	1,000		
	Add: Transfer due to buy-back of shares from Gen. res.	3,700	4,700	
	Securities premium	800		
	Less: Adjustment for premium paid on redemption of preference shares	(250)		
	Less: Adjustment for premium paid on buy back	(550)	-	
	Profit & Loss A/c	300		
	Add: Profit on sale of investment	150	450	6,800
3.	**Long-term borrowings**			
	Secured			
	9 % Debentures		5,000	
	Term Loans – From Banks		400	5,400

Working Note

Bank Account

Receipts	Amount (₹ Lakhs)	Payments	Amount (₹ Lakhs)
To balance b/d	1,650	By Preference Sharesholders A/c	2,750
To Investment A/c (sale Proceeds)	3,150	By Equity Shareholders A/c	2,400
To Bank Loan A/c (Loan received)	400	By Balance c/d (Balancing figure)	50
	5,200		**5,200**

Income tax on the above will not be included in Revenue A/c of an insurance company.

Q-6 Following is the summarized Balance Sheet of Complicated Ltd. as on 31st March, 2016 :

Liabilities	**Amount (Rs.)**
Equity shares of Rs. 10 each, fully paid up	12,50,000
Bonus shares of Rs. 10 each, fully paid up	1,00,000
Share option outstanding Account	4,00,000
Revenue Reserve	15,00,000
Securities Premium	2,50,000
Profit & Loss Account	1,25,000
Capital Reserve	2,00,000
Unpaid dividends	1,00,000
12% Debentures (Secured)	18,75,000
Advance from related parties (Unsecured)	10,00,000
Current maturities of long term borrowings	16,50,000
Application money received for allotment due for refund	2,00,000
	86,50,000
Fixed Assets	46,50,000
Current Assets	40,00,000
	86,50,000

The Company wants to buy back 25,000 equity shares of Rs. 10 each, on 1st April, 2016 at Rs. 20 per share. Buy back of shares is duly authorized by its Articles and necessary resolution has been passed by the Company towards this. The buy -back of shares by the Company is also within the provisions of the Companies Act, 2013. The payment for buy back of shares will be made by the Company out of sufficient bank balance available shown as par t of Current Assets.

You are required to prepare the necessary journal entries towards buy back of shares and prepare the Balance Sheet after buy back of shares.

Ans. As per the information given in the question, buy -back of 25,000 shares @ Rs. 20, as desired by the company, is within the provisions of the Companies Act, 2013.

Journal Entries for buy-back of shares

			Debit (Rs.)	**Credit (Rs.)**
(a)	Equity shares buy-back account	Dr.	5,00,000	
	To Bank account			5,00,000
	(Being buy back of 25,000 equity shares of Rs. 10 each @ Rs. 20 per share)			
(b)	Equity share capital account	Dr.	2,50,000	
	Securities premium account	Dr.	2,50,000	
	To Equity shares buy-back account			5,00,000
	(Being cancellation of shares bought back)			
(c)	Revenue reserve account	Dr.	2,50,000	
	To Capital redemption reserve account			2,50,000
	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of capital bought back through free reserves)			

Balance Sheet of Complicated Ltd.
as on 1st April, 2016

Particulars	Note No	Amount Rs.
EQUITY AND LIABILITIES		
1 Shareholders' funds		
(a) Share capital	1	11,00,000
(b) Reserves and Surplus	2	22,25,000
2 Non-current liabilities		
(a) Long-term borrowings	3	28,75,000
3 Current liabilities		
(a) Other current liabilities	4	19,50,000
Total		81,50,000
ASSETS		
1 Non-current assets		
(a) Fixed assets		46,50,000
2 Current assets (40,00,000-5,00,000)		35,00,000
Total		81,50,000

Notes to Accounts

			Rs.	Rs.
1.	Share Capital			
	Equity share capital			
	1,10,000 Equity shares of Rs.10 each			11,00,000
2.	Reserves and Surplus			
	Profit and Loss A/c		1,25,000	
	Revenue reserves	15,00,000		
	Less: Transfer to CRR	(2,50,000)	12,50,000	
	Securities premium	2,50,000		
	Less: Utilization for share buy -back	(2,50,000)	-	
	Share Option Outstanding Account		4,00,000	
	Capital Reserve		2,00,000	
	Capital Redemption Reserve		2,50,000	22,25,000
3.	Long-term borrowings			
	Secured			
	12% Debentures		18,75,000	
	Unsecured loans		10,00,000	28,75,000
4.	Other Current Liabilities			
	Current maturities of long term borrowings		16,50,000	
	Unpaid dividend		1,00,000	
	Application money received for allotment due for refund		2,00,000	19,50,000

Q-7 L, M, N and O hold Equity capital in the proportion of 30:30:20:20 in AB Ltd. X, Y, Z and K hold preference share capital in the proportion of 40:30:20:10.

You are required to identify the voting rights of shareholders in case of resolution of winding up of the company if the paid -up capital of the company is Rs. 80 Lakh and Preference share capital is Rs. 40 Lakh.

Ans. L, M, N and O hold Equity capital is held by in the proportion of 30:30:20:20 and X, Y, Z and K hold preference share capital in the proportion of 40:30:20:10. As the paid -up equity share capital of the company is Rs. 80 Lakhs and Preference share capital is Rs. 40 Lakh (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be

L	= 2/3X30/100	= 3/15
M	= 2/3X30/100	= 3/15
N	= 2/3X20/100	= 2/15
O	= 2/3X20/100	= 2/15
X	= 1/3X40/100	= 2/15
Y	= 1/3X30/100	= 1/10
Z	= 1/3X20/100	= 1/15
K	= 1/3X10/100	= 1/30

Q-8 Umesh Ltd. resolves to buy back 4 lakhs of its fully paid equity shares of ₹ 10 each at ₹ 22 per share. This buyback is in compliance with the provisions of the Companies Act and does not exceed 25% of Company's paid up capital in the financial year. For the purpose, it issues 1 lakh 11 % preference shares of ₹ 10 each at par, the entire amount being payable with applications. The company uses ₹ 16 lakhs of its balance in Securities Premium Account apart from its adequate balance in General Reserve to fulfill the legal requirements regarding buy-back. Give necessary journal entries to record the above transactions.

Ans. **Journal Entries in the books of Umesh Ltd.**

			₹	₹
1.	Bank A/c	Dr.	10,00,000	
	To 11% Preference share application & allotment A/c			10,00,000
	(Being receipt of application money on preference shares)			
2.	11% Preference share application & allotment A/c	Dr.	10,00,000	
	To 11% Preference share capital A/c			10,00,000
	(Being allotment of 1 lakh preference shares)			
3.	General reserve A/c	Dr.	30,00,000	
	To Capital redemption reserve A/c			30,00,000
	(Being creation of capital redemption reserve for buy back of shares)			
4.	Equity share capital A/c	Dr.	40,00,000	
	Premium payable on buyback A/c	Dr.	48,00,000	
	To Equity shareholders/Equity shares buy back A/c			88,00,000
	(Amount payable to equity shareholder on buy back)			

5.	Equity shareholders/ Equity shares buy back A/c	Dr.	88,00,000	
	To Bank A/c			88,00,000
	(Being payment made for buy back of shares)			
6.	Securities Premium A/c	Dr.	16,00,000	
	General reserve A/c		32,00,000	
	To Premium payable on buyback A/c			48,00,000
	(Being premium on buyback charged from securities premium and general reserve)			

Working Notes:

1. Calculation of amount used from General Reserve Account

		₹
Amount paid for buy back of shares (4,00,000 shares x ₹ 22)		88,00,000
Less: Proceeds from issue of Preference Shares (1,00,000 shares x ₹ 10)		(10,00,000)
Less: Utilization of Securities Premium Account		(16,00,000)
Balance used from General Reserve Account		62,00,000
* Used under Section 68 for buy back	32,00,000	
Used under Section 69 for transfer to CRR (W.N 2)	30,00,000	
	62,00,000	

2. Amount to be transferred to Capital Redemption Reserve account

	₹
Nominal value of shares bought back (4,00,000 shares x ₹ 10)	40,00,000
Less: Nominal value of Preference Shares issued for such buy back (1,00,000 shares x ₹ 10)	(10,00,000)
Amount transferred to Capital Redemption Reserve Account	30,00,000

Q-9 Alpha Limited furnishes the following summarized Balance Sheet as at 31st March, 2017:

Liabilities	**(₹ in lakhs)**	**Assets**	**(₹ in lakhs)**
Equity share capital	2,400	Machinery	3,600
(fully paid up shares of ₹ 10 each)		Furniture	450
Securities premium	350	Investment	148
General reserve	530	Inventory	1,200
Capital redemption reserve	400	Trade receivables	500
Profit & loss A/c	340	Cash at bank	1,500
12% Debentures	1,500		
Trade payables	1,400		
Other current liabilities	478		
	7,398		**7,398**

On 1st April, 2017, the company announced the buy back of 25% of its equity shares @ ₹ 15 per share. For this purpose, it sold all of its investments for ₹ 150 lakhs.
On 5th April, 2017, the company achieved the target of buy back.
You are required to:
(1) Pass necessary journal entries for the buy-back.
(2) Prepare Balance Sheet of Alpha Limited after buy-back of the shares.

Ans. **In the books of Alpha Limited**

Journal Entries

Date 2017	Particulars		Dr. (₹ in lakhs)	Cr.
April 1	Bank A/c	Dr.	150	
	To Investment A/c			148
	To Profit on sale of investment			2
	(Being investment sold on profit)			
April 5	Equity share capital A/c	Dr.	600	
	Securities premium A/c	Dr.	300	
	To Equity shares buy back A/c			900
	(Being the amount due to equity shareholders on buy back)			
	Equity shares buy back A/c	Dr.	900	
	To Bank A/c			900
	(Being the payment made on account of buy back of 60 Lakh Equity Shares)			
April 5	General reserve A/c	Dr.	530	
	Profit and Loss A/c	Dr.	70	
	To Capital redemption reserve A/c			600
	(Being amount equal to nominal value of bought back shares from free reserves transferred to capital redemption reserve account as per the law)			

Balance Sheet (After buy back)

	Particulars	Note No	Amount (₹ in Lakhs)
I.	Equity and Liabilities		
	(1) Shareholder's Funds		
	(a) Share Capital	1	1,800
	(b) Reserves and Surplus	2	1,322
	(2) Non-Current Liabilities		
	(a) Long-term borrowings - 12% Debentures		1,500
	(3) Current Liabilities		
	(a) Trade payables		1,400
	(b) Other current liabilities		478
	Total		6,500
II.	Assets		
	(1) Non-current assets		
	(a) Property, Plant & Equipment		
	(i) Tangible assets	3	4,050
	(2) Current assets		
	(a) Current investments		
	(b) Inventory		1,200
	(c) Trade receivables		5,00
	(d) Cash and cash equivalents (W.N.)		750
	Total		6,500

Notes to Accounts

				(₹ in Lakhs)
1.	Share Capital			
	Equity share capital (Fully paid up shares of ₹ 10 each)			1800
2.	Reserves and Surplus			
	General Reserve	530		
	Less: Transfer to CRR	(530)	-	
	Capital Redemption Reserve	400		
	Add: Transfer due to buy-back of shares from P/L	70		
	Transfer due to buy-back of shares from Gen. res.	530	1,000	
	Securities premium	350		
	Less: Adjustment for premium paid on buy back	(300)	50	
	Profit & Loss A/c	340		
	Add: Profit on sale of investment	2		
	Less: Transfer to CRR	(70)	272	1,322
3.	Tangible assets			
	Machinery		3,600	
	Furniture		450	4,050

Working Note:

Cash at bank after buy-back

	₹ in lakhs
Cash balance as on 1st April, 2017	1,500
Add: Sale of investments	150
	1,650
Less: Payment for buy back of shares	(900)
	750

Q-10 The following summarized Balance Sheet Pee Limited (a non-listed company) furnishes as at 31st March, 2017:

	₹	₹
Equity & Liabilities		
Share capital:		
Authorised capital		
2,50,000 Equity shares of ₹ 10 each fully paid up	25,00,000	
5,000, 10% Preference shares of ₹ 100 each	5,00,000	30,00,000
Issued and subscribed capital:		
2,40,000 Equity shares of ₹ 10 each fully paid up	24,00,000	
3,000, 10% Preference shares of ₹ 100 each	3,00,000	27,00,000
(Issued two months back for the purpose of buy back)		
Reserves and surplus:		
Capital reserve	10,00,000	
Revenue reserve	25,00,000	
Securities premium	27,00,000	
Profit and loss account	35,00,000	97,00,000
Current liabilities		
Trade payables	13,00,000	
Other current Liabilities	3,00,000	16,00,000
		1,40,00,000

Assets		
Tangible assets		
Building	25,00,000	
Machinery	31,00,000	
furniture	20,00,000	76,00,000
Non-current Investments	30,00,000	
Current assets		
Inventory	12,00,000	
Trade receivables	7,00,000	
cash and bank balance	15,00,000	34,00,000
		1,40,00,000

On 1st April, 2017, the company passed a resolution to buy back 20% of its equity capital @ ₹ 60 per share. For this purpose, it sold all of its investment for ₹ 25,00,000.

The company achieved its target of buy-back. You are required to:

(a) Give necessary journal entries and

(b) Give the Balance Sheet of the company after buy back of shares.

Ans. **Journal Entries in the books of Pee Limited**

	Particulars		Dr.	Cr.
(i)	Bank Account	Dr.	25,00,000	
	Profit and Loss Account	Dr.	5,00,000	
	To Investment Account			30,00,000
	(Being the investments sold at loss for the purpose of buy back)			
(ii)	Equity Share capital account	Dr.	4,80,000	
	Premium payable on buy back Account	Dr.	24,00,000	
	To Equity shares buy back Account			28,80,000
	(Being the amount due on buy back)			
(iii)	Securities Premium Account	Dr.	24,00,000	
	To Premium payable on buy back Account			24,00,000
	(Being the premium payable on buy back adjusted against securities premium account)			
(iv)	Revenue Reserve Account	Dr.	1,80,000	
	To Capital Redemption Reserve Account			1,80,000
	(Being the amount equal to nominal value of equity shares bought back out of free reserves transferred to capital redemption reserve account (4,80,000-3,00,000)			
(v)	Equity shares buy-back Account	Dr.	28,80,000	
	To Bank Account			28,80,000
	(Being the payment made on buy back)			

Balance Sheet of Pee Limited as on 1st April, 2017
(After buy back of shares)

	Particulars	Note No	(₹)
I.	Equity and Liabilities		
(1)	Shareholder's Funds		
	(a) Share Capital	1	22,20,000
	(b) Reserves and Surplus	2	68,00,000
(2)	Current Liabilities		16,00,000
	Total		1,06,20,000
II.	Assets		
(1)	Non-current assets		
	(a) Fixed assets		76,00,000
(2)	Current assets		30,20,000
	Total		1,06,20,000

Notes to Accounts

				₹
1	Share Capital			
	Authorised capital:			30,00,000
	Issued and subscribed capital:			
	1,92,000 Equity shares of ₹ 10 each fully paid up		1,92,0000	
	3,000 10% Preference shares of ₹ 100 each fully paid up		3,00,000	22,20,000
	Reconciliation of share capital			
	Opening no. of shares		2,40,000	
	Buy back of shares during the year		48,000	1,92,000
	During the year the company has buy back of 48,000 shares			
2	Reserves and Surplus			
	Capital reserve		10,00,000	
	Capital redemption reserve		1,80,000	
	Securities Premium	27,00,000		
	Less: Premium payable on buy back of shares	24,00,000	3,00,000	
	Revenue reserve	25,00,000		
	Less: Transfer to Capital redemption reserve	1,80,000	23,20,000	
	Profit and loss A/c	35,00,000		
	Less: Loss on investment	5,00,000	30,00,000	68,00,000

Q-11 Following is the summarized Balance Sheet of Complicated Ltd. as on 31st March, 2016 :

Liabilities	Amount(₹)
Equity shares of ₹ 10 each, fully paid up	12,50,000
Bonus shares of ₹ 10 each, fully paid up	1,00,000
Share option outstanding Account	4,00,000
Revenue Reserve	15,00,000
Securities Premium	2,50,000
Profit & Loss Account	1,25,000
Capital Reserve	2,00,000
Unpaid dividends	1,00,000

12% Debentures (Secured)	18,75,000
Advance from related parties (Unsecured)	10,00,000
Current maturities of long term borrowings	16,50,000
Application money received for allotment due for refund	2,00,000
	86,50,000
Fixed Assets	46,50,000
Current Assets	40,00,000
	86,50,000

The Company wants to buy back 25,000 equity shares of ₹ 10 each, on 1st April, 2016 at ₹ 20 per share. Buy back of shares is duly authorized by its Articles and necessary resolution has been passed by the Company towards this. The buy-back of shares by the Company is also within the provisions of the Companies Act, 2013. The payment for buy back of shares will be made by the Company out of sufficient bank balance available shown as part of Current Assets.

You are required to prepare the necessary journal entries towards buy back of shares and prepare the Balance Sheet after buy back of shares.

Ans. As per the information given in the question, buy-back of 25,000 shares @ ₹ 20 , as desired by the company, is within the provisions of the Companies Act, 2013.

Journal Entries for buy-back of shares

			Debit (₹)	Credit (₹)
(a)	Equity shares buy-back account	Dr.	5,00,000	
	To Bank account			5,00,000
	(Being buy back of 25,000 equity shares of ₹ 10 each @ ₹ 20 per share)			
(b)	Equity share capital account	Dr.	2,50,000	
	Securities premium account	Dr.	2,50,000	
	To Equity shares buy-back account			5,00,000
	(Being cancellation of shares bought back)			
(c)	Revenue reserve account	Dr.	2,50,000	
	To Capital redemption reserve account			2,50,000
	(Being transfer of free reserves to capitalredemption reserve to the extent of nominal valueof capital bought back through free reserves)			

Balance Sheet of Complicated Ltd.
as on 1st April, 2016

	Particulars	Note No	Amount ₹
	EQUITY AND LIABILITIES		
1	Shareholders' funds		
	(a) Share capital	1	11,00,000
	(b) Reserves and Surplus	2	22,25,000
2	Non-current liabilities		
	(a) Long-term borrowings	3	28,75,000
3	Current liabilities		
	(a) Other current liabilities	4	19,50,000
	Total		**81,50,000**

ASSETS

1	Non-current assets	
	(a) Fixed assets	46,50,000
2	Current assets (40,00,000-5,00,000)	35,00,000
	Total	**81,50,000**

Notes to Accounts

			₹	₹
1.	Share Capital			
	Equity share capital			
	1,10,000 Equity shares of ₹ 10 each			11,00,000
2.	Reserves and Surplus			
	Profit and Loss A/c		1,25,000	
	Revenue reserves	15,00,000		
	Less: Transfer to CRR	(2,50,000)	12,50,000	
	Securities premium	2,50,000		
	Less: Utilization for share buy-back	(2,50,000)	-	
	Share Option Outstanding Account		4,00,000	
	Capital Reserve		2,00,000	
	Capital Redemption Reserve		2,50,000	22,25,000
3.	Long-term borrowings			
	Secured			
	12% Debentures		18,75,000	
	Unsecured loans		10,00,000	28,75,000
4.	Other Current Liabilities			
	Current maturities of long term borrowings		16,50,000	
	Unpaid dividend		1,00,000	
	Application money received for allotment duefor refund		2,00,000	19,50,000

Q-12 Following is the summarized Balance Sheet of Super Ltd. as on 31st March, 2018.

Liabilities	**In ₹**
Share Capital	
Equity Shares of ₹ 10 each fully paid up	17,00,000
Reserves & Surplus	
Revenue Reserve	23,50,000
Securities Premium	2,50,000
Profit & Loss Account	2,00,000
Infrastructure Development Reserve	1,50,000
Secured Loan	
9% Debentures	22,50,000
Unsecured Loan	8,50,000
Current Maturities of Long term borrowings	15,50,000
	93,00,000

Assets	
Fixed Assets	
Tangible Assets	58,50,000
Current Assets	
Current Assets	34,50,000
	93,00,000

Super Limited wants to buy back 35,000 equity shares of ₹ 10 each fully paid up on 1st April, 2018 at ₹ 30 per share.

Buy Back of shares is fully authorised by its articles and necessary resolutions have been passed by the company towards this. The payment for buy back of shares will be made by the company out of sufficient bank balance available as part of the Current Assets.

Comment with calculations, whether the Buy Back of shares by the company is within the provisions of the Companies Act, 2013.

Ans. Determination of maximum no. of shares that can be bought back as per the Companies Act, 2013

1. **Shares Outstanding Test**

Particulars	**(Shares)**
Number of shares outstanding	1,70,000
25% of the shares outstanding	42,500

2. **Resources Test: Maximum permitted limit 25% of Equity paid up capital + Free** Reserves

Particulars	
Paid up capital (₹)	17,00,000
Free reserves (₹) (23,50,000 + 2,50,000 + 2,00,000)	28,00,000
Shareholders' funds (₹)	45,00,000
25% of Shareholders fund (₹)	11,25,000
Buy back price per share	₹ 30
Number of shares that can be bought back (shares)	37,500
Actual Number of shares proposed for buy back	35,000

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Shareholder's Funds post Buy Back

	Particulars	₹
(a)	Loan funds (₹) (22,50,000+8,50,000+15,50,000)	46,50,000
(b)	Minimum equity to be maintained after buy back in the ratio of 2:1 (₹) (a/2)	23,25,000
(c)	Present equity/shareholders fund (₹)	45,00,000
(d)	Future equity/shareholders fund (₹) (see W.N.) (45,00,000 – 5,43,750)	39,56,250*
(e)	Maximum permitted buy back of Equity (₹) [(d) – (b)]	16,31,250
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share	54,375 shares
(g)	Actual Buy Back Proposed	35,000 Shares

Summary statement determining the maximum number of shares to be bought back

Particulars	Number of shares
Shares Outstanding Test	42,500
Resources Test	37,500
Debt Equity Ratio Test	54,375
Maximum number of shares that can be bought back [least of the above]	37,500

Company qualifies all tests for buy-back of shares and it can buy back maximum 37,500 shares on 1st April, 2018.

However, company wants to buy-back only 35,000 equity shares @ ₹ 30. Therefore, buy-back of 35,000 shares, as desired by the company is within the provisions of the Companies Act, 2013.

Working Note:

Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.

Then (45,00,000 – x) – 23,25,000 = y (1)

$\left(\frac{y}{30} \times 10\right) = x$ Or 3x = y (2)

by solving the above equation, we get

x = ₹ 5,43,750

y = ₹ 16,31,250

Q-13 Equity capital is held by L, M, N and O in the proportion of 30:40:20:10. A, B, C and D hold Preference share capital in the proportion of 40:30:10:20. If the paid up Equity Share capital of the company is ₹ 60 lakhs and Preference share capital is ₹ 30 lakhs, find the voting rights of shareholders (in percentage) in case of resolution of winding up of the company.

Ans. L, M, N and O hold Equity capital is held by in the proportion of 30:40:20:10 and A, B, C and D hold preference share capital in the proportion of 40:30:10:20. As the paid up equity share capital of the company is ₹ 60 Lakhs and Preference share capital is ₹ 30 Lakh (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3.

The respective voting right of various shareholders will be

L = 2/3 x 30 /100 = 3/15 = 20% M = 2/3 x 40 /100 = 4/15 = 26.67%

N = 2/3 x 20 /100 = 2/15 = 13.33% O = 2/3 x 10 /100 = 1/15 = 6.67%

A = 1/3 x 40 /100 = 4/30= 13.33% B = 1/3 x 30 /100 = 3/30 = 10%

C = 1/3 x 10 /100 = 1/30 = 3.33% D = 1/3 x 20 /100 = 2/30 = 6.67%

Q-14 Alpha Ltd. furnishes the following summarized Balance Sheet as at 31st March, 2017:

	₹ In lakhs	₹ In lakhs
Equity & Liabilities		
Shareholders' Funds		
Equity share capital (fully paid up shares of ₹ 10 each)		2,400
Reserves and Surplus		
Securities Premium	350	
General Reserve	530	
Capital Redemption Reserve	400	
Profit & Loss Account	340	1,620
Non-current Liabilities		
12% Debentures	1,500	
Current Liabilities		
Trade Payables	1,490	
Other Current Liabilities	390	1,880
Total		7,400
Assets		
Non-current Assets		
Fixed Assets		4,052
Current Assets		
Current Investments	148	
Inventories	1,200	
Trade Receivables	520	
Cash and Bank	1,480	3,348
Total		7,400

(i) On 1st April, 2017, the company announced buy-back of 25% of its equity shares@ ₹ 15 per share. For this purpose, it sold all its investment for ₹ 150 lakhs.

(ii) On 10th April, 2017 the company achieved the target of buy-back.

(iii) On 30th April, 2017, the company issued one fully paid up equity share of ₹ 10 each by way of bonus for every four equity shares held by the equity shareholders by capitalization of Capital Redemption Reserve.

You are required to pass necessary journal entries and prepare the Balance Sheet of Alpha Ltd. after bonus issue.

Ans. **In the books of Alpha Limited**

Journal Entries

Date 2017	Particulars		Dr. (₹ in lakhs)	Cr.
April 1	Bank A/c	Dr.	150	
	To Investment A/c			148
	To Profit on sale of investment			2
	(Being investment sold on profit)			
April 10	Equity share capital A/c	Dr.	600	
	Securities premium A/c	Dr.	300	
	To Equity shares buy back A/c			900
	(Being the amount due to equity shareholders on buyback)			
	Equity shares buy back A/c	Dr.	900	
	To Bank A/c			900
	(Being the payment made on account of buy back of 60 Lakh Equity Shares)			
April 10	General reserve A/c	Dr.	530	
	Profit and Loss A/c	Dr.	70	
	To Capital redemption reserve (CRR) A/c			600
	(Being amount equal to nominal value of buy back sharesfrom free reserves transferred to capital redemptionreserve account as per the law)			
April 30	Capital redemption reserve A/c	Dr.	450	
	To Bonus shares A/c (W.N.1)			450
	(Being the utilization of capital redemption reserve toissue bonus shares)			
	Bonus shares A/c	Dr.	450	
	To Equity share capital A/c			450
	(Being issue of one bonus equity share for every fourequity shares held)			
	Profit on sale of Investment	Dr.	2	
	To Profit and Loss A/c			2
	(Profit on sale transfer to Profit and Loss A/c)			

Note: For transferring amount equal to nominal value of buy back shares from free reserves to capital redemption reserve account, the amount of ₹ 340 lakhs from P & L A/c and the balance from general reserve may also be utilized. The combination of different set of amounts (from General Reserve and Profit and Loss Account) aggregating ₹ 600 lakhs may also be considered for the purpose of transfer to CRR.

Balance Sheet (After buy back and issue of bonus shares)

	Particulars	Note No	Amount (₹ in Lakhs)
I.	Equity and Liabilities		
	(1) Shareholder's Funds		
	(a) Share Capital	1	2,250
	(b) Reserves and Surplus	2	872

	(2) Non-Current Liabilities		
	(a) Long-term borrowings - 12% Debentures		1,500
	(3) Current Liabilities		
	(a) Trade payables		1,490
	(b) Other current liabilities		390
	Total		6,502
II.	Assets		
	(1) Non-current assets		
	(a) Fixed assets		
	(i) Tangible assets		4,052
	(2) Current assets		
	(a) Current investments		
	(b) Inventory		1,200
	(c) Trade receivables		520
	(d) Cash and cash equivalents (W.N. 2)		730
	Total		6,502

Notes to Accounts

				₹ In lakhs
1.	Share Capital			
	Equity share capital (225 lakh fully paid up shares of ₹ 10 each)			2,250
2.	Reserves and Surplus			
	General Reserve	530		
	Less: Transfer to CRR	(530)	-	
	Capital Redemption Reserve	400		
	Add: Transfer due to buy-back of shares from P/L	70		
	Add: Transfer due to buy-back of shares from Gen. res.	530		
	Less: Utilisation for issue of bonus shares	(450)	550	
	Securities premium	350		
	Less: Adjustment for premium paid on buy back	(300)	50	
	Profit & Loss A/c	340		
	Add: Profit on sale of investment	2		
	Less: Transfer to CRR	(70)	272	872

Working Notes:

1. **Amount of equity share capital** = 2,400 - 600 (buyback) + 450 (Bonus shares) = 2,250
2. **Cash at bank after issue of bonus shares**

	₹ in lakhs
Cash balance as on 1st April, 2017	1480
Add: Sale of investments	150
	1630
Less: Payment for buy back of shares	(900)
	730

Q-15 X Ltd. furnishes the following summarized Balance Sheet as at 31-03-2018.

Liabilities	**(in ₹)**	**(In ₹)**
Share Capital		
Equity Share Capital of ₹ 20 each fully paid up	50,00,000	
10,000, 10 % Preference Share of ₹ 100 each fully paid up	10,00,000	60,00,000
Reserves & Surplus		
Capital Reserve	1,00,000	
Security Premium	12,00,000	
Revenue Reserve	5,00,000	
Profit and Loss	20,00,000	
Dividend Equalization Fund	5,50,000	43,50,000
Non-Current Liabilities		
12% Debenture		12,50,000
Current Liabilities and Provisions		5,50,000
Total:		**1,21,50,000**
Assets		
Fixed Assets		
Tangible Assets		1,00,75,000
Current Assets		
Investment	3,00,000	
Inventory	2,00,000	
Cash and Bank	15,75,000	20,75,000
Total :		**1,21,50,000**

The shareholders adopted the resolution on the date of the above mentioned Balance Sheet to:

(1) Buy back 25% of the paid up capital and i was decided to offer a price of 20% over market price. The prevailing market value of the company's share is ₹ 30 per share.

(2) To finance the buy back of share company :

(a) Issue 3000, 14 % debenture of 100 each at a premium of 20 %

(b) Issue 2500, 10 % preference share of ₹ 100 each

(3) Sell investment worth ₹ 1,00,000 for ₹ 1,50,000.

(4) Maintain a balance of ₹ 2,00,000 in Revenue Reserve.

(5) Later the company issue three fully paid up equity share of ₹ 20 each by way of bonus share for every 15 equity share held by the equity shareholder.

You are required to pass the necessary journal entries to record the above transactions and prepare Balance Sheet after buy back.

Ans. **In the books of X Limited**

Journal Entries

	Particulars		Dr. ₹	Cr. ₹
1.	Bank A/c Dr.		3,60,000	
	To 14 % Debenture A/c			3,00,000
	To Securities Premium A/c			60,000
	(Being 14 % debentures issued to finance buy back)			
2.	Bank A/c	Dr.	2,50,000	
	To 10% preference share capital A/c			
	(Being 10% preference share issued to finance buy back)			2,50,000
3.	Bank A/c Dr.		1,50,000	
	To Investment A/c			1,00,000
	To Profit on sale of investment			50,000
	(Being investment sold on profit)			
4.	Equity share capital A/c (62,500 x ₹20)	Dr.	12,50,000	
	Securities premium A/c (62,500 x ₹16)	Dr.	10,00,000	
	To Equity shares buy back A/c (62,500 x ₹36)			22,50,000
	(Being the amount due to equity shareholders on buy back)			
5.	Equity shares buy back A/c	Dr.	22,50,000	
	To Bank A/c			22,50,000
	(Being the payment made on account of buy back of 62,500 Equity Shares as per the Companies Act)			
6.	Revenue reserve	Dr.	3,00,000	
	Securities premium	Dr.	2,60,000	
	Profit and Loss A/c	Dr.	4,40,000	
	To Capital redemption reserve A/c*			10,00,000
	(Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law) [12,50,000 less 2,50,000]			
7.	Capital redemption reserve A/c	Dr.	7,50,000	
	To Bonus shares A/c (W.N.1)			7,50,000
	(Being the utilization of capital redemption reserve to issue 37,500 bonus shares)			

8.	Bonus shares A/c	Dr.	7,50,000	
	To Equity share capital A/c			7,50,000
	(Being issue of 3 bonus equity share for every 15 equity shares held)			

*Alternatively, entry for combination of different amounts (from Revenue reserve, Securities premium and profit and Loss account.) may be passed for transferring the required amount to CRR.

Note: It may be noted that as per the provisions of the Companies Act, no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other **specified securities**. Issue of debentures has been excluded for the purpose of "**specified securities**" and the entire amount of ₹ 10,00,000 (after deducting only pref. share capital) has been credited to CRR while solving the question.

Balance Sheet (After buy back and issue of bonus shares)

Particulars	Note No	Amount ₹
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	57,50,000
(b) Reserves and Surplus	2	27,10,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	15,50,000
(3) Current Liabilities		
(a) Trade payables		-
(b) current liabilities & Provisions		5,50,000
Total		**1,05,60,000**
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment		1,00,75,000
(2) Current assets		
(a) Investments		2,00,000
(b) Inventory		2,00,000
(c) Cash and cash equivalents (W.N. 2)		85,000
Total		**1,05,60,000**

Notes to Accounts

			₹
1.	Share Capital		
	Equity share capital (Fully paid up shares of ₹ 20 each)		
	(2,50,000-62,500+37,500 shares)	45,00,000	
	10% preference shares @ ₹ 100 each (10,00,000 + 2,50,000)	12,50,000	57,50,000
2.	Reserves and Surplus		
	Capital Reserve	1,00,000	

	Revenue reserve		2,00,000	
	Securities premium	12,00,000		
	Add: Premium on debenture	60,000		
	Less: Adjustment for premium paid on buy back	(10,00,000)		
	Less: Transfer to CRR	(2,60,000)	Nil	
	Capital Redemption Reserve			
	Transfer due to buy-back of shares from P&L			
		10,00,000		
	Less: Utilisation for issue of bonus shares	(7,50,000)	2,50,000	
	Profit & Loss A/c	20,00,000		
	Add: Profit on sale of investment	50,000		
	Less: Transfer to CRR	(4,40,000)	16,10,000	
	Dividend equalization reserve	(5,50,000)	5,50,000	27,10,000
3	Long-term borrowings - 12% Debentures	12,50,000		
	- 14% Debentures	3,00,000		15,50,000

Working Notes:

1. Amount of bonus shares = [(2,50,000 -25%)3/15] x 20 = 37,500 x 20=7,50,000
2. Cash at bank after issue of bonus shares

	₹
Cash balance as on 30.3.2018	15,75,000
Add: Issue of debenture	3,60,000
Add: issue of preference shares	2,50,000
Add: Sale of investments	1,50,000
	23,35,000
Less: Payment for buy back of shares	(22,50,000)
	85,000

Q-16 On 1st April,2018 , XYZ Ltd. offered 150 shares to each of its 750 employees at 60 per share.The employees are given a year to accept the offer. The shares issued under the plan shall be subject to lock-in period on transfer for three years from the grant date. The market price of shres of the company of the grant date is ₹ 72 per share.Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at ₹ 67 per share.

On 31syt March ,2019, 6000 emplyees accepted the offer and paid 60 per share purchased. Nominal value of each share is ₹ 10.

You are required to record the issue of shares in the books of the XYZ Ltd, under the aforesaid plan.

Ans. Fair value of an option = ₹ 67(considered on grant date) – ₹ 60 = ₹ 7

Number of shares issued = 600 employees x 150 shares/employee = 90,000 shares

Fair value of ESOP = 90,000 shares x ₹ 7 = ₹ 6,30,000

Vesting period = 1 year

Expenses recognized in 2018-19 = ₹ 6,30,000

Date	Particulars		₹	₹
31.03.2019	Bank (90,000 shares x ₹ 60)	Dr.	54,00,000	
	Employees stock compensation expense A/c	Dr.	6,30,000	
	To Share Capital (90,000 shares x ₹ 10)			9,00,000
	To Securities Premium (90,000shares x ₹ 57)			51,30,000
	(Being option accepted by 600 employees & payment made @ ₹ 60 per share)			
	Profit & Loss A/c	Dr.	6,30,000	
	To Employees stock compensation expense A/c			6,30,000
	(Being Employees stock compensation expense transferred to Profit & Loss A/c)			

Q-17 The following was the summarized balance sheet of Bhoomi Ltd. as on 31st March, 2020:

Equity & liability	₹ (in lakhs)	Assets	₹ (in lakhs)
Authorised Capital:		Property, plant and equipment	1,12,000
Equity shares of ₹ 10 each	80,000	Investments	24,000
Issued Capital		Cash at Bank	13,200
Equity Shares of ₹10 each Fully Paid up	64,000	Trade Receivables	66,000
10% Redeemable Preference Shares of 10 each, Fully Paid Up	20,000		
Reserves & Surplus:			
Capital Redemption Reserve	8,000		
Securities Premium	6,400		
General Reserve	48,000		
Profit & Loss Account	2,400		
9% Debentures	40,000		
Trade Payables	26,400		
	2,15,200		**2,15,200**

On 1st April,2020 the Company redeemed all its Preference Shares at a Premium of 10% and bought back 25% of its Equity Shares at ₹20 per Share. In order to make Cash available, the Company sold all the Investments for ₹25,000 Lakhs and raised a Bank Loan amounting to ₹16,000 lakh on the Security of the Company's Plant.

Give the necessary Journal Entries considering that the buy back is authorised by the articles of company and necessary resolution is passed by the company for this. The amount of Securities premium may be utilized to the maximum extent allowed by law.

Ans.

Journal entries
In the books of Bhoomi Ltd.

			Dr.	Cr.
				₹ *in lakhs*
1	Bank A/c	Dr.	25,000	
	To Investments A/c			24,000
	To Profit and Loss A/c			1,000
	(Being Investments sold and, profit being credited to Profit and Loss Account)			
2	10% Redeemable Preference Share Capital A/c	Dr.	20,000	
	Premium payable on Redemption of Preference Shares A/c	Dr.	2,000	
	To Preference Shareholders A/c			22,000
	(Being amount payable on redemption of Preference shares, at a Premium of 10%)			
3	Securities Premium A/c	Dr.	2,000	
	To Premium payable on Redemption of Preference Shares A/c			2,000
	(Being Securities Premium utilised to provide Premium on Redemption of Preference Shares)			
4	Equity Share Capital A/c	Dr.	16,000	
	Premium payable on Buyback A/c	Dr.	16,000	
	To Equity Share buy back A/c			32,000
	(Being the amount due on buy-back)			
5	Securities Premium A/c (6,400 – 2,000)	Dr.	4,400	
	General Reserve A/c (balancing figure)	Dr.	11,600	
	To Premium payable on Buyback A/c			16,000
	(Being premium on buyback provided first out of Securities Premium and the balance out of General Reserves.)			
6	Bank A/c	Dr.	16,000	
	To Bank Loan A/c			16,000
	(Being Loan taken from Bank to finance Buyback)			
7	Preference Shareholders A/c	Dr.	22,000	
	Equity Shares buy back A/c	Dr.	32,000	
	To Bank A/c			54,000
	(Being payment made to Preference Shareholders and Equity Shareholders)			
8	General Reserve Account	Dr.	36,000	
	To Capital Redemption Reserve Account			36,000
	(Being amount transferred to Capital Redemption Reserve Account to the extent of face value of preference shares redeemed and equity Shares bought back) (20,000 + 16,000)			

Q-18 Pratham Ltd. (a non-listed company) has the following Capital structure as on 31st March, 2020:

Particulars	₹	₹
Equity Share Capital (shares of ₹ 10 each fully paid		30,00,000
Reserves & Surplus		
General Reserve	32,50,000	
Security Premium Account	6,00,000	
Profit & Loss Account	4,30,000	
Revaluation Reserve	6,20,000	49,00,000
Loan Funds		42,00,000

You are required to compute by Debt Equity Ratio Test, the maximum number of shares that can be bought back in the light of above information, when the offer price for buy back is ₹ 30 per share.

Ans. **Debt Equity Ratio Test**

	Particulars	₹
(a)	Loan funds 42,00,000	
(b)	Minimum equity to be maintained after buy back in the ratio of 2:1 (₹ in crores)	21,00,000
(c)	Present equity shareholders fund (₹ in crores)	72,80,000
(d)	Future equity shareholder fund (₹ in crores) (See Note 2)	59,85,000 (72,80,000-12,95,000)
(e)	Maximum permitted buy back of Equity (₹ in crores) [(d) – (b)] (See Note 2)	38,85,000 (by simultaneous equation)
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share (shares in crores) (See Note 2)	1,29,500 (by simultaneous equation)

Working Notes:

1. Shareholders' funds

Particulars	₹
Paid up capital	30,00,000
Free reserves (32,50,000 +6,00,000+4,30,000)	42,80,000
	72,80,000

2. As per section 68 of the Companies Act, 2013, amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

Suppose amount equivalent to nominal value of bought back shares transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.

Equation 1 :(Present equity – Nominal value of buy-back transfer to CRR) – Minimum equity to be maintained = Maximum permissible buy-back of equity

(72,80,000 –x)-21,00,000 = y (1)

Since 51,80,000 – x = y

Equation 2: $\left(\frac{\text{Max imum buy - back}}{\text{Offer price for buy - back}} \times \text{Nominal Value}\right)$

= Nominal value of the shares bought –back to be transferred to CRR

$$= \left(\frac{y}{30} \times 10\right) = x$$

3x = y

x = ₹ 12,95,000 crores and y = ₹ 38,85,000 crores

Q-19 What do you mean by equity shares with differential rights. Explain in brief. Can preference shares be also issued with differential rights?

Ans. Equity shares with Differential Rights means the share with dissimilar rights as to dividend, voting or otherwise. No; the preference shares cannot be issued with differential rights.

Q-20 E, F, G and H hold Equity Capital in Alpha Co. in the proportion of 30:30:20:20. S, T,U and V hold preference share capital in the proportion of 40:30:10:20. If the paid up capital of the company is ₹ 120 Lakh and Preference share capital is ₹ 60 Lakh, You are required to calculate their voting rights in case of resolution of winding up of the company.

Ans. E, F, G and H hold Equity capital is held by in the proportion of 30:30:20:20 and S,T,U and V hold preference share capital in the proportion of 40:30:10:20. As the paid up equity share capital of the company is ₹ 120 Lakhs and Preference share capital is ₹ 60 Lakhs (ratio of 2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be:

E	=	2/3 x 30/100	=	3/15
F	=	2/3 x 30/100	=	3/15
G	=	2/3 x 20/100	=	2/15
H	=	2/3 x 20/100	=	2/15
S	=	1/3 x 40/100	=	2/15
T	=	1/3 x 30/100	=	1/10
U	=	1/3 x 10/100	=	1/30
V	=	1/3 x 20/100	=	1/15

Q-21 SM Limited gives the following information as on 31st March, 2020:

		₹
Share capital		
(60,000 Equity Shares of ₹ 10 Each)		6,00,000
Reserve & Surplus:		
Security premium	₹ 70,000	
General reserve	₹ 63,000	
Profit and Loss	₹ 1,40,000	2,73,000
Non-current liability:		
9% debentures (secured)		3,00,000

Current Liabilities:		
Term loan		40,000
Creditors		65,000
Provision for taxation		15,000
Property plant and equipment		6,00,000
Non-current investment		1,50,000
Current assets:		
Stock	₹ 2,00,000	
Debtors	₹ 2,60,000	
Bank	₹ 83,000	5,43,000

The shareholders adopted the resolution on 31st March, 2020 to:

(i) Buy back 25% of the paid up capital @ ₹ 15 each.

(ii) Issue 10% debentures of ₹ 60,000 at a premium of 10% to finance the buyback of shares.

(iii) Maintain a balance of ₹ 20,000 in General Reserve.

(iv) Sell investments worth ₹ 1,00,000 for ₹ 80,000.

(v) Buy back expenses were ₹ 2,000.

You are required to pass necessary journal entries to record the above transactions and prepare Ledger account of Bank. **[MTP-Nov'21](8 + 4 + 8 = 20 Marks)**

Ans. **In the books of SM Limited**

Journal Entries

	Particulars		**Dr.** ₹	**Cr.** ₹
1.	Equity share capital A/c (15,000 x f 10)	Dr.	1,50,000	
	Premium on buyback A/c (15,000 x f5)	Dr.	75,000	
	To Equity shares buy back or Equity shareholders A/c (15,000 x f 15)			2,25,000
	(Being the amount due to equity shareholders on buy back)			
2.	Equity shares buy back/Equity shareholders A/c	Dr.	2,25,000	
	To Bank A/c			2,25,000
	(Being the payment made on account of buy back of 15,000 Equity Shares as per the Companies Act)			
3.	Bank A/c	Dr.	66,000	
	To 10 % Debentures A/c			60,000
	To Securities Premium A/c			6,000
	(Being 14 % debentures issued to finance buy back)			
4.	Buyback Expenses A/c			
	To Bank A/c (Buyback expenses paid)	Dr.	2,000	
				2,000

5.	Bank A/c	Dr.	80,000	
	Profit and Loss A/c (Loss on sale of investment)	Dr.	20,000	
	To Investment A/c			1,00,000
	(Being investment sold at loss)			
6.	General reserve	Dr.	43,000	
	Profit and Loss A/c	Dr.	1,07,000	
	To Capital redemption reserve A/c			1,50,000
	(Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law)			
7.	Securities Premium	Dr.	75,000	
	Profit and Loss A/c	Dr.	2,000	
	To Premium on buyback			75,000
	To Buyback Expenses A/c			2,000
	(Being premium on buyback and buyback expenses charged to securities premium and profit and lossaccount)			

Bank Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance b/d	83,000	By Equity Shareholders A/c	2,25,000
To Investment A/c	80,000	By Expenses on buy back of shares	2,000
To 10% Debentures and Securities premium	66,000	By Balance c/d	2,000
Total	**2,29,000**	**Total**	**2,29,000**

Note: It may be noted that as per the provisions of the Companies Act, no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities. Issue of debentures has been excluded for the purpose of "specified securities" and the entire amount of ₹ 1,50,000 has been credited to CRR while solving the question.

Q-22 The following details are provided by Bhoomi Ltd. as on 31st March, 2020:

	₹(in lakhs)
Issued Capital:	
Equity Shares of ?10 each Fully Paid up	64,000
10% Redeemable Preference Shares of 10 each, Fully Paid Up	20,000
Capital Redemption Reserve	8,000
Securities Premium	6,400
General Reserve	48,000
Profit & Loss Account	2,400
9% Debentures	40,000
Trade Payables	26,400

Property, plant and equipment	1,12,000
Investments	24,000
Cash at Bank	13,200
Trade Receivables	66,000

On 1st April,2020 the Company redeemed all its Preference Shares at a Premium of 10% and bought back 25% of its Equity Shares at ₹20 per Share. In order to make cash available, Bhoomi Ltd. sold all the Investments for ₹25,000 Lakhs and raised a Bank Loan amounting to ₹16,000 lakh on the Security of the Company's Plant.

Give the necessary Journal Entries considering that the buy back is authorised by the articles of company and necessary resolution is passed by the company for this. The amount of Securities premium may be utilized to the maximum extent allowed by law.

Ans. **Journal entries**

In the books of Bhoomi Ltd.

			Dr.	Cr. ₹ in lakhs
1	Bank A/c	Dr.	25,000	
	To Investments A/c			24,000
	To Profit and Loss A/c			1,000
	(Being Investments sold and, profit being credited to Profit and Loss Account)			
2	10% Redeemable Preference Share Capital A/c	Dr.	20,000	
	Premium payable on Redemption of Preference Shares A/c	Dr.	2,000	
	To Preference Shareholders A/c			22,000
	(Being amount payable on redemption of Preference shares, at a Premium of 10%)			
3	Securities Premium A/c	Dr.	2,000	
	To Premium payable on Redemption of Preference Shares A/c			2,000
	(Being Securities Premium utilised to provide Premium on Redemption of Preference Shares)			
4	Equity Share Capital A/c	Dr.	16,000	
	Premium payable on Buyback A/c	Dr.	16,000	
	To Equity Share buy back A/c			32,000
	(Being the amount due on buy-back)			
5	Securities Premium A/c (6,400 - 2,000)	Dr.	4,400	
	General Reserve A/c (balancing figure)	Dr.	11,600	
	To Premium payable on Buyback A/c			16,000
	(Being premium on buyback provided first out of Securities Premium and the balance out of General Reserves.)			

6	Bank A/c	Dr.	16,000	
	To Bank Loan A/c			16,000
	(Being Loan taken from Bank to finance Buyback)			
7	Preference Shareholders A/c	Dr.	22,000	
	Equity Shares buy back A/c	Dr.	32,000	
	To Bank A/c			54,000
	(Being payment made to Preference Shareholders and Equity Shareholders)			
8	General Reserve Account	Dr.	36,000	
	To Capital Redemption Reserve Account			36,000
	(Being amount transferred to Capital Redemption Reserve Account to the extent of face value of preference shares redeemed and equity Shares bought back) (20,000 + 16,000)			

Q-23 A company provides the following 2 possible Capital Structures as on 31st March, 2021:

Particulars	Situation 1 (₹)	Situation 2 (₹)
Equity Share Capital (Shares of ₹ 10 each, fully paid up)	30,00,000	30,00,000
Reserves & Surplus:		
General Reserve	12,00,000	12,00,000
Securities Premium	6,00,000	6,00,000
Profit & Loss	2,10,000	2,10,000
Statutory Reserve	4,20,000	4,20,000
Loan Funds	25,00,000	1,20,00,000

The company is planning to offer buy back of Equity Share at a price of ₹ 30 per equity share.

You are required to calculate maximum permissible number of equity shares that can be bought back in both the situations as per Companies Act, 2013 and are also required to pass necessary Journal Entries in the situation where the buyback is possible.

Ans. Statement determining the maximum number of shares to be bought back

Number of shares(₹ in crores)

Particulars	When loan fund is	
	₹ 25,00,000	₹ 1,20,00,000
Shares Outstanding Test (W.N.1)	75,000	75,000
Resources Test (W.N.2)	41,750	41,750
Debt Equity Ratio Test (W.N.3)	94,000	Nil
Maximum number of shares that can be bought back [least of the above]	41,750	Nil

Journal Entries for the Buy-Back (applicable only when loan fund is ₹ 25,00,000)

	Particulars		Debit	₹ Credit
(a)	Equity shares buy-back account	Dr.	12,52,500	
	To Bank account			12,52,500
	(Being payment for buy-back of 41,750 equity shares of ₹ 10 each @ ₹ 30 per share)			
(b)	Equity share capital account	Dr.	4,17,500	
	Premium Payable on buy-back account	Dr.	8,35,000	
	To Equity shares buy-back account			12,52,500
	(Being cancellation of shares bought back)			
	Securities Premium account	Dr.	6,00,000	
	General Reserve / Profit & Loss A/c	Dr.	2,35,000	
	To Premium Payable on buy-back account			8,35,000
	(Being Premium Payable on buy-back account charged to securities premium and general reserve /Profit & Loss A/c)			
(c)	General Reserve*	Dr.	4,17,500	
	To Capital redemption reserve account			4,17,500
	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out of redeemed through free reserves)			

*Profit and Loss account balance amounting ₹ 2,10,000 may also be used and General Reserve may be debited for the balance amount.

Working Notes:

1. Shares Outstanding Test

Particulars	(Shares in crores)
Number of shares outstanding	3,00,000
25% of the shares outstanding	75,000

2. Resources Test

Particulars	
Paid up capital (₹)	30,00,000
Free reserves (₹) (12,00,000+6,00,000+2,10,000)	20,10,000
Shareholders' funds (₹)	50,10,000
25% of Shareholders fund (₹)	₹ 12,52,500
Buy-back price per share	₹ 30
Number of shares that can be bought back	41,750 shares

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back

	Particulars	When loan fund is	
(a)	Loan funds(₹)	₹ 25,00,000	₹ 1,20,00,000
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1(₹) (a/2)	12,50,000	60,00,000
(c)	Present equity shareholders fund (₹)	50,10,000	50,10,000

Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method

Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y' Then

Equation 1: (Present Equity- Transfer to CRR) - Minimum Equity to be maintained
= Maximum Permitted Buy-Back
= (50,10,000 - x) - 12,50,000 = y
= 37,60,000 - x =y (1)

Equation 2: Maximum Permitted Buy-Back X Nominal Value per Share/Offer Price per Share
Y/30 x 10 = x

Or

3x = y (2)

By solving the above two equations we get

x = 9,40,000 and

y = 28,20,000

In situation 2, first equation will be negative. Buy back not possible in this situation.

Q-24 The Directors of Umang Ltd. passed a resolution to buyback 5,00,000 of its fully paid equity shares of ₹ 10 each at ₹ 15 per share. This buyback is in compliance with the provisions of the Companies Act, 2013. For this purpose, the company

(i) Sold its investments of ₹ 30,00,000 for ₹ 25,00,000.

(ii) Issued 20,000, 12% preference shares of ₹ 100 each at par, the entire amount being payable with application.

(iii) Used ₹ 15,00,000 of its Securities Premium Account apart from its adequate balance in General Reserve to fulfill the legal requirements regarding buy-back.

(iv) The company has necessary cash balance for the payment to shareholders.

You are required to pass necessary Journal Entries (including narration) regarding buy-back of shares in the books of Umang Ltd.

Ans. **Journal Entries in the books of Umang Ltd.**

			Dr. ₹	Cr. ₹
1.	Bank A/c	Dr.	25,00,000	
	Profit and Loss A/c	Dr.	5,00,000	
	To Investment A/c			30,00,000
	(Being investment sold for the purpose of buy-back of Equity Shares)			
2.	Bank A/c	Dr.	20,00,000	
	To 12% Pref. Share capital A/c			20,00,000
	(Being 12% Pref. Shares issued for ₹ 20,00,000)			
3.	Equity share capital A/c	Dr.	50,00,000	
	Premium payable on buy-back	Dr.	25,00,000	
	To Equity shares buy-back A/c/ Equity shareholders A/c			75,00,000

	(Being the amount due on buy-back of equity shares)			
4.	Equity shares buy-back A/c/ Equity shareholders A/c	Dr.	75,00,000	
	To Bank A/c			75,00,000
	(Being payment made for buy-back of equity shares)			
5.	Securities Premium A/c	Dr.	15,00,000	
	General Reserve A/c	Dr.	10,00,000	
	To Premium payable on buy-back			25,00,000
	(Being premium payable on buy-back charged from Securities premium)			
6.	General Reserve A/c	Dr.	30,00,000	
	To Capital Redemption Reserve A/c			30,00,000
	(Being creation of capital redemption reserve to the extent of the equity shares bought back after deducting fresh pref. shares issued)			

Q-25 M/s. Vriddhi Infra Ltd. (a non-listed company) provide the following information as on 31.3.2020:

	(₹)
Land and Building	21,50,000
Plant & Machinery	15,00,000
Non- current Investment	2,00,000
Trade Receivables	5,50,000
Inventories	1,80,000
Cash and Cash Equivalents	40,000
Share capital:1,00,000 Equity Shares of ‘ 10 each fully paid up	10,00,000
Securities Premium	3,00,000
General Reserve	2,50,000
Profit & Loss Account (Surplus)	1,50,000
10% Debentures (Secured by floating charge on all assets)	20,00,000
Unsecured Loans	8,00,000
Tarde Payables	1,20,000

On 21st April, 2020 the Company announced the buy back of 15,000 of its equity shares @ ₹ 15 per share. For this purpose, it sold all its investment for ₹ 2.50 lakhs.

On 25th April, 2020, the company achieved the target of buy back. On 1st May, 2020 the company issued one fully paid up share of ₹ 10 each by way of bonus for every eight equity shares held by the equity shareholders.

You are required to pass necessary Journal Entries for the above transactions.

Ans. **In the books of Vriddhi Infra Ltd.**

Journal Entries

Date 2020	Particulars		Dr. ₹	Cr. ₹
April 21	Bank A/c	Dr.	2,50,000	
	To Investment A/c			2,00,000
	To Profit on sale of investment			50,000
	(Being investment sold on profit)			
April 25	Equity share capital A/c	Dr.	1,50,000	
	Securities premium A/c	Dr.	75,000	
	To Equity shares buy back A/c			2,25,000
	(Being the amount due to equity shareholders on buy back)			
	Equity shares buy back A/c	Dr.	2,25,000	
	To Bank A/c			2,25,000
	(Being the payment made on account of buy back of 15,000 Equity Shares)			
	General Reserve A/c OR P&L A/c	Dr.	1,50,000	
	To Capital redemption reserve A/c			1,50,000
	(Being amount equal to nominal value of buy back shares transferred from free reserves to capital redemption reserve account as per the law)			
May 1	Capital redemption reserve A/c	Dr.	1,06,250	
	To Bonus shares A/c (W.N.1)			1,06,250
	(Being the utilization of capital redemption reserve to issue bonus shares)			
	Bonus shares A/c	Dr.	1,06,250	
	To Equity share capital A/c			1,06,250
	(Being issue of one bonus equity share for every ten equity shares held)			

Working Note:

Amount of bonus shares = $\left[(1,00,000 - 15,000) \times \frac{1}{8}\right] = ₹\ 1,06,250$

Q-26 Rohan Ltd. furnishes the following information as at 31-03-2021.

	(in ₹)	(in ₹)
Share Capital:		
Equity Share Capital of ₹ 20 each fully paid up	50,00,000	
10,000, 10% Preference Shares of ₹ 100 each fully paid up	10,00,000	60,00,000
Reserves & Surplus:		

Capital Reserve	1,00,000	
Security Premium	12,00,000	
Revenue Reserve	5,00,000	
Profit and Loss	25,50,000	43,50,000
12% Debentures		12,50,000
Current Liabilities and Provisions		5,50,000
Property, Plant and Equipment		1,00,75,000
Current Assets:		
Investment	3,00,000	
Inventory	2,00,000	
Cash and Bank	15,75,000	20,75,000

The shareholders adopted the following resolution on 31st March, 2021:

(1) Buy back 25% of the paid-up capital and it was decided to offer a price of 20% over market price. The prevailing market value of the company's share is ₹ 30 per share.

(2) To finance the buy-back of shares, company:

(a) Issues 3,000, 14% debentures of ₹ 100 each at a premium of 20%.

(b) Issues 2,500, 10% preference shares of ₹ 100 each.

(3) Sell investment worth ₹ 1,00,000 for ₹ 1,50,000.

(4) Maintain a balance of ₹ 2,00,000 in Revenue Reserve.

(5) Later, the company issue three fully paid up equity shares of ₹ 20 each by way of bonus for every 15 equity shares held by the equity shareholders.

You are required to pass the necessary journal entries to record the above transactions.

Ans. **In the books of Rohan Limited**

Journal Entries

	Particulars		**Dr.** ₹	**Cr.** ₹
1.	Bank A/c	Dr.	3,60,000	
	To 14 % Debenture A/c			3,00,000
	To Securities Premium A/c			60,000
	(Being 14 % debentures issued to finance buy back)			
2.	Bank A/c	Dr.	2,50,000	
	To 10% preference share capital A/c			2,50,000
	(Being 10% preference share issued to finance buy back)			
3.	Bank A/c	Dr.	1,50,000	
	To Investment A/c			1,00,000
	To Profit on sale of investment			50,000
	(Being investment sold on profit)			
4.	Equity share capital A/c (62,500 x ₹20)	Dr.	12,50,000	
	Premium on buyback or Securities premium A/c (62,500 x ₹16)	Dr.	10,00,000	
	To Equity shares buy back A/c (62,500 x ₹36)			22,50,000
	(Being the amount due to equity shareholders on buy back)			

5.	Equity shares buy back A/c	Dr.	22,50,000	
	To Bank A/c			22,50,000
	(Being the payment made on account of buy back of 62,500 Equity Shares as per the Companies Act)			
6.	Revenue reserve	Dr.	3,00,000	
	Securities premium	Dr.	2,60,000	
	Profit and Loss A/c	Dr.	4,40,000	
	To Capital redemption reserve A/c			10,00,000
	(Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law) [12,50,000 less 2,50,000]			
7.	Capital redemption reserve A/c	Dr.	7,50,000	
	To Bonus shares A/c			7,50,000
	(Being the utilization of capital redemption reserve to issue 37,500 bonus shares)			
8.	Bonus shares A/c	Dr.	7,50,000	
	To Equity share capital A/c 7,50,000			
	(Being issue of 3 bonus equity share for every 15equity shares held)			

Q-27 Complicated Ltd. (an unlisted company) gives the following information as on 31.3.2021:

Particulars	**Amount (₹)**
Equity shares of ₹ 10 each, fully paid up	13,50,000
Share option outstanding Account	4,00,000
Revenue Reserve	15,00,000
Securities Premium	2,50,000
Profit & Loss Account	1,25,000
Capital Reserve	2,00,000
Unpaid dividends	1,00,000
12% Debentures (Secured)	18,75,000
Advance from related parties (Long term - Unsecured)	10,00,000
Current maturities of long term borrowings	16,50,000
Application money received for allotment due for refund	2,00,000
Property, plant and equipment	46,50,000
Current assets	40,00,000

The Company wants to buy back 25,000 equity shares of ₹ 10 each, on 1st April, 2021 at ₹ 15 per share. Buy back of shares is duly authorized by its Articles and necessary resolution has been passed by the Company for this. The buy-back of shares by the Company is also within the provisions of the Companies Act, 2013. The payment for buy back of shares was made by the Company out of sufficient bank balance available shown as part of Current Assets.

You are required to prepare the necessary journal entries towards buy back of shares and prepare the Balance Sheet of the company after buy back of shares.

Ans. As per the information given in the question, buy-back of 25,000 shares @ ₹ 15, as desired by the company, is within the provisions of the Companies Act, 2013.

Journal Entries for buy-back of shares

			Debit (₹)	Credit (₹)
(a)	Equity shares buy-back account	Dr.	3,75,000	
	To Bank account			3,75,000
	(Being buy back of 25,000 equity shares of ₹ 10each @ ₹ 15 per share)			
(b)	Equity share capital account	Dr.	2,50,000	
	Premium payable on buyback account	Dr.	1,25,000	
	To Equity shares buy-back account			3,75,000
	(Being cancellation of shares bought back)			
(c)	Securities premium account	Dr.	1,25,000	
	To Premium payable on buyback account			1,25,000
	(Being Premium payable on buyback adjusted against securities premium account)			
(d)	Revenue reserve account	Dr.	2,50,000	
	To Capital redemption reserve account			2,50,000
	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of capital bought back through free reserves)			

Balance Sheet of Complicated Ltd. as at 1st April, 2021

Particulars		Note No	Amount ₹
EQUITY AND LIABILITIES			
1	**Shareholders' funds**		
	(a) Share capital	1	11,00,000
	(b) Reserves and Surplus	2	23,50,000
2	**Non-current liabilities**		
	(a) Long-term borrowings	3	28,75,000
3	**Current liabilities**		
	(a) Short-term borrowings	4	16,50,000
	(b) Other current liabilities	5	3,00,000
	Total		82,75,000
ASSETS			
1	**Non-current assets**		
	(a) Property, Plant and Equipment		46,50,000
2	**Current assets**		36,25,000
	(₹ 40,00,000 – ₹ 3,75,000)		
	Total		82,75,000

Notes to Accounts

			₹	₹
1.	Share Capital			
	Equity share capital			
	1,10,000 Equity shares of ₹10 each			11,00,000
2.	Reserves and Surplus			
	Capital Reserve		2,00,000	
	Capital Redemption Reserve		2,50,000	
	Securities premium	2,50,000		
	Less: Utilization for share buy-back	(1,25,000)	1,25,000	
	Share Option Outstanding Account		4,00,000	
	Revenue reserves	15,00,000		
	Less: Transfer to CRR	(2,50,000)	12,50,000	
	Surplus i.e. Profit and Loss A/c		1,25,000	23,50,000
3.	Long-term borrowings			
	Secured			
	12% Debentures		18,75,000	
	Unsecured loans		10,00,000	28,75,000
4.	Short-term borrowings			
	Current maturities of long-term borrowings			16,50,000
5.	Other Current Liabilities			
	Unpaid dividend		1,00,000	
	Application money received for allotment due for refund		2,00,000	3,00,000

Q-28 (i) Can preference shares be also issued with differential rights? Explain in brief.

(ii) Explain the conditions under Companies (Shares Capital and Debentures) Rules 2014, to deal with equity shares with differential rights.

Ans. (i) No; the preference shares cannot be issued with differential rights. It is only the equity shares, which are issued. Equity shares with Differential Rights means the share with dissimilar rights as to dividend, voting or otherwise.

(ii) As per Share Capital and Debentures Rules, 2014, for equity shares with differential rights, following conditions to be compulsorily complied with:

- The articles of association of the company authorizes the issue of shares with differential rights;
- The issue of shares is authorized by an ordinary resolution passed at a general meeting of the shareholders: Provided that where the equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot;
- The voting power in respect of shares with differential rights shall not exceed seventy four percent of the total voting power including voting power in respect of equity shares with differential rights issued at any point of time;

- The company has not defaulted in filing financial statements and annual returns for three financial years immediately preceding the financial year in which it is decided to issue such shares;
- The company has no subsisting default in the payment of a declared dividend to its shareholders or repayment of its matured deposits or redemption of its preference shares or debentures that have become due for redemption or payment of interest on such deposits or debentures or payment of dividend;
- The company has not defaulted in payment of the dividend on preference shares or repayment of any term loan from a public financial institution or State level financial institution or scheduled Bank that has become repayable or interest payable thereon or dues with respect to statutory payments relating to its employees to any authority or default in crediting the amount in Investor Education and Protection Fund to the Central Government;

  Provided that a company may issue equity shares with differential rights upon expiry of five years from the end of financial year in which such default was made good.
- The company has not been penalized by Court or Tribunal during the last three years of any offence under the Reserve Bank of India Act, 1934, the Securities and Exchange Board of India Act, 1992, the Securities Contracts Regulation Act, 1956, the Foreign Exchange Management Act, 1999 or any other special Act, under which such companies being regulated by sectoral regulators.

Q-29 Mohan Ltd. furnishes the following summarised Balance Sheet on 31st March 2021.

	(₹ in Lakhs)
	Amount
Equity and Liabilities:	
Shareholders' fund	
Share Capital	
Equity Shares of ₹ 10 each fully paid up	780
6% Redeemable Preference shares of ₹ 50 each fully Paid up	240
Reserves and Surplus	
Capital Reserves	58
General Reserve	625
Securities Premium	52
Profit & Loss	148
Revaluation Reserve	34
Infrastructure Development Reserve	16
Non-current liabilities	
7% Debentures	268
Unsecured Loans	36
Current Liabilities	**395**
	2652
Assets:	
Non-current Assets	
Plant and Equipment less depreciation	725
Investment at cost	720
Current Assets	1207
	2652

Other Information :

(1) The company redeemed preference shares at a premium of 10% on 1st April,2021.

(2) It also offered to buy back the maximum permissible number of equity shares of ₹ 10 each at ₹ 30 per share on 2nd April 2021.

(3) The payment for the above was made out of available bank balance, which appeared as a part of the current assets.

(4) The company had investment in own debentures costing ₹ 60 lakhs (face value ₹75 lakhs). These debentures were cancelled on 2nd April 2021.

(5) On 4th April 2021 company issued one fully paid-up equity share of ₹ 10 each by way of bonus for every five equity shares held by the shareholders.

You are required to:

(a) Calculate maximum possible number of equity shares that can be bought back as per the Companies Act, 2013 and

(b) Record the Journal Entries for the above-mentioned information.

Ans.(a) (i) Statement determining the maximum number of shares to be bought back

	Number of shares (in lakhs)
Particulars	When loan fund is ₹ 304 lakhs
Shares Outstanding Test (W.N.1)	19.5
Resources Test (W.N.2)	11.175
Debt Equity Ratio Test (W.N.3)	29.725
Maximum number of shares that can be bought back [least of the above]	11.175

Thus, the company can buy 11,17,500 Equity shares at ₹ 30 each.

Working Notes:

1. Shares Outstanding Test

Particulars	**(Shares in lakh)**
Number of shares outstanding	78
25% of the shares outstanding	19.5

2. Resources Test

Particulars	
Paid up capital (₹ in lakh)	780
Free reserves (₹ in lakh) (625+52+148-24-240*)	561
Shareholders' funds (₹ in lakh)	1341
25% of Shareholders fund (₹ in lakh)	335.25
Buy-back price per share	30
Number of shares that can be bought back	11.175

*Amount transferred to CRR is excluded from free reserves.

Premium on redemption also reduced.

• Loan funds have been taken without considering current liabilities. Alternatively, If current liabilities are considered, then the maximum number of shares that can be bought back as per debt equity ratio test will be 24.7875 lakhs.

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back

	Particulars	**₹ In lakh**
(a)	Loan funds (₹)	304
(b)	Minimum equity to be maintained after buyback in the ratio of 2:1 (₹) (a/2)	152
(c)	Present equity shareholders fund (₹)	1341
(d)	Future equity shareholders fund (₹) (see W.N.4)	1043.75 (1341-297.25)
(e)	Maximum permitted buy-back of Equity (₹) [(d) – (b)]	891.75
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share	29.725
	As per the provisions of the Companies Act, 2013, company	Qualifies

Alternatively, when current liabilities are considered as part of loan funds, in that case Debt Equity Ratio Test will be done as follows:

	Particulars	₹ in lakh
(a)	Loan funds (₹)	699
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (₹) (a/2)	349.5
(c)	Present equity shareholders fund (₹)	1341
(d)	Future equity shareholders fund (₹) (see W.N.4)	1093.125 (1341-247.875)
(e)	Maximum permitted buy-back of Equity (₹) [(d) – (b)]	743.625
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share	24.7875
	As per the provisions of the Companies Act, 2013, company	Qualifies

4. Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method

Suppose amount transferred to CRR account is 'x' and maximum permitted buy - back of equity is 'y' Then

Equation 1: (Present Equity- Transfer to CRR) - Minimum Equity to be maintained = Maximum Permitted Buy-Back

= (1341 – x) – 152 = y

= 1189 – x =y (1)

Equation 2: Maximum Permitted Buy-Back x Nominal Value Per Share/Offer Price Per Share

y/30 x 10 = x or 3x = y (2)

by solving the above two equations we get

x = ₹ 297.25 and y = ₹ 891.75

Alternatively, when current liabilities are considered as part of loan funds, in that case

Equation 1: (Present Equity- Transfer to CRR)- Minimum Equity to be maintained = Maximum Permitted Buy-Back

= (1341 – x) – 349.5 = y

= 991.5 – x =y (1)

Equation 2: Maximum Permitted Buy-Back X Nominal Value Per Share/Offer Price Per Share

y/30 x 10 = x or 3x = y (2)

by solving the above two equations we get x = 247.875 and y = 743.625

(ii)

Journal Entries for Buy Back

(₹ in lakhs)

Date	Particulars		Debit	Credit
2021				
1st April	6% Redeemable preference share capital A/c	Dr.	240	
	Premium on redemption of preference shares A/c	Dr.	24	
	To Preference shareholders A/c			264
	(Being preference share capital transferred to shareholders account)			
	Preference shareholders A/c	Dr.	264	
	To Bank A/c 264			
	(Being payment made to shareholders)			
	General Reserve or P&L A/c*	Dr.	24	
	To Premium on redemption of preference shares A/c			24
	(Being premium on redemption of preference shares adjusted through securities premium)			
2nd April	Equity shares buy-back A/c	Dr.	335.25	
	To Bank A/c			335.25
	(Being 11.175 lakhs equity shares of ₹ 10 each bought back @ ₹ 30 per share)			
	Equity share capital A/c	Dr.	111.75	
	Securities Premium A/c	Dr.	52	
	General Reserve or P&L A/c	Dr.	171.50	
	To Equity Shares buy-back A/c			335.25
	(Being cancellation of shares bought back)			
	General reserve A/c	Dr.	351.75	
	To Capital redemption reserve A/c			351.75
	(Being creation of capital redemption reserve account to the extent of the face value of preference shares redeemed and equity shares bought back as per the law ie. 240+ 111.75 lakhs)			

2nd April	7% Debentures A/c	Dr.	75	
	To Investment (own debentures) A/c			60
	To Profit on cancellation of own debentures A/c			15
	(Being cancellation of own debentures costing ₹ 60 lakhs, face value being ₹ 75 lakhs and the balance being profit on cancellation of debentures)			
4th April	Capital Redemption Reserve	Dr.	133.65	
	To Bonus Shares A/c			133.65
	(Being issue of one bonus equity share for every five equity shares held)			
	Bonus shares A/c	Dr.	133.65	
	To Equity share capital A/c			133.65
	(Being bonus shares issued)			

Working Note: Bonus Share to be issued =66.825 (78 - 11.175) lakh shares divided by 5 = 13.365 lakh shares.

Note: *Securities premium has not been utilized for the purpose of premium payable on redemption of preference shares assuming that the company referred in the question is governed by Section 133 of the Companies Act, 2013 and complies with the Accounting Standards prescribed for them. Alternative entry considering otherwise is also possible by utilizing securities premium amount.

Q-30 Complicated Ltd. (an unlisted company) gives the following information as on 31.3.2021:

Particulars	**Amount (₹)**
Equity shares of ₹ 10 each, fully paid up	13,50,000
Share option outstanding Account	4,00,000
Revenue Reserve	15,00,000
Securities Premium	2,50,000
Profit & Loss Account	1,25,000
Capital Reserve	2,00,000
Unpaid dividends	1,00,000
12% Debentures (Secured)	18,75,000
Advance from related parties (Long term - Unsecured)	10,00,000
Current maturities of long term borrowings	16,50,000
Application money received for allotment due for refund	2,00,000
Property, plant and equipment	46,50,000
Current assets	40,00,000

The Company wants to buy back 25,000 equity shares of ₹ 10 each, on 1st April, 2021 at ₹ 15 per share. Buy back of shares is duly authorized by its Articles and necessary resolution has been passed by the Company for this. The buy-back of shares by the Company is also within the provisions of the Companies Act, 2013. The payment for buy back of shares was made by the Company out of sufficient bank balance available shown as part of Current Assets.

You are required to prepare the necessary journal entries towards buy back of shares and prepare the Balance Sheet of the company after buy back of shares.

Ans. As per the information given in the question, buy-back of 25,000 shares @ ₹ 15, as desired by the company, is within the provisions of the Companies Act, 2013.

Journal Entries for buy-back of shares

			Debit (₹)	Credit (₹)
(a)	Equity shares buy-back account	Dr.	3,75,000	
	To Bank account			3,75,000
	(Being buy back of 25,000 equity shares of ₹ 10each @ ₹ 15 per share)			
(b)	Equity share capital account	Dr.	2,50,000	
	Premium payable on buyback account	Dr.	1,25,000	
	To Equity shares buy-back account			3,75,000
	(Being cancellation of shares bought back)			
(c)	Securities premium account	Dr.	1,25,000	
	To Premium payable on buyback account			1,25,000
	(Being Premium payable on buyback adjusted against securities premium account)			
(d)	Revenue reserve account	Dr.	2,50,000	
	To Capital redemption reserve account			2,50,000
	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of capital bought back through free reserves)			

Balance Sheet of Complicated Ltd. as at 1st April, 2021

Particulars		Note No	Amount ₹
EQUITY AND LIABILITIES			
1	**Shareholders' funds**		
	(a) Share capital	1	11,00,000
	(b) Reserves and Surplus	2	23,50,000
2	**Non-current liabilities**		
	(a) Long-term borrowings	3	28,75,000
3	**Current liabilities**		
	(a) Short-term borrowings	4	16,50,000
	(b) Other current liabilities	5	3,00,000
	Total		82,75,000
ASSETS			
1	**Non-current assets**		
	(a) Property, Plant and Equipment		46,50,000
2	**Current assets**		36,25,000
	(₹ 40,00,000 – ₹3,75,000)		
	Total		82,75,000

Notes to Accounts

			₹	₹
1.	Share Capital			
	Equity share capital			
	1,10,000 Equity shares of ₹10 each			11,00,000
2.	Reserves and Surplus			
	Capital Reserve		2,00,000	
	Capital Redemption Reserve		2,50,000	
	Securities premium	2,50,000		
	Less: Utilization for share buy-back	(1,25,000)	1,25,000	
	Share Option Outstanding Account		4,00,000	
	Revenue reserves	15,00,000		
	Less: Transfer to CRR	(2,50,000)	12,50,000	
	Surplus i.e. Profit and Loss A/c		1,25,000	23,50,000
3.	Long-term borrowings			
	Secured			
	12% Debentures		18,75,000	
	Unsecured loans		10,00,000	28,75,000
4.	Short-term borrowings			
	Current maturities of long-term borrowings			16,50,000
5.	Other Current Liabilities			
	Unpaid dividend		1,00,000	
	Application money received for allotment due for refund		2,00,000	3,00,000

Q-31

(i) Can preference shares be also issued with differential rights? Explain in brief.

(ii) Explain the conditions under Companies (Shares Capital and Debentures) Rules 2014, to deal with equity shares with differential rights.

Ans.(i) No; the preference shares cannot be issued with differential rights. It is only the equity shares, which are issued. Equity shares with Differential Rights means the share with dissimilar rights as to dividend, voting or otherwise.

(ii) As per Share Capital and Debentures Rules, 2014, for equity shares with differential rights, following conditions to be compulsorily complied with:

- The articles of association of the company authorizes the issue of shares with differential rights;
- The issue of shares is authorized by an ordinary resolution passed at a general meeting of the shareholders: Provided that where the equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot;
- The voting power in respect of shares with differential rights shall not exceed seventy four percent of the total voting power including voting power in respect of equity shares with differential rights issued at any point of time;
- The company has not defaulted in filing financial statements and annual returns for three financial years immediately preceding the financial year in which it is decided to issue such shares;

- The company has no subsisting default in the payment of a declared dividend to its shareholders or repayment of its matured deposits or redemption of its preference shares or debentures that have become due for redemption or payment of interest on such deposits or debentures or payment of dividend;
- The company has not defaulted in payment of the dividend on preference shares or repayment of any term loan from a public financial institution or State level financial institution or scheduled Bank that has become repayable or interest payable thereon or dues with respect to statutory payments relating to its employees to any authority or default in crediting the amount in Investor Education and Protection Fund to the Central Government;
  Provided that a company may issue equity shares with differential rights upon expiry of five years from the end of financial year in which such default was made good.
- The company has not been penalized by Court or Tribunal during the last three years of any offence under the Reserve Bank of India Act, 1934, the Securities and Exchange Board of India Act, 1992, the Securities Contracts Regulation Act, 1956, the Foreign Exchange Management Act, 1999 or any other special Act, under which such companies being regulated by sectoral regulators.

Q-32 Mohan Ltd. furnishes the following summarised Balance Sheet on 31st March 2021.

	(₹ in Lakhs)
	Amount
Equity and Liabilities:	
Shareholders' fund	
Share Capital	
Equity Shares of ₹ 10 each fully paid up	780
6% Redeemable Preference shares of ₹ 50 each fully Paid up	240
Reserves and Surplus	
Capital Reserves	58
General Reserve	625
Securities Premium	52
Profit & Loss	148
Revaluation Reserve	34
Infrastructure Development Reserve	16
Non-current liabilities	
7% Debentures	268
Unsecured Loans	36
Current Liabilities	**395**
	2652
Assets:	
Non-current Assets	
Plant and Equipment less depreciation	725
Investment at cost	720
Current Assets	1207
	2652

Other Information :

(1) The company redeemed preference shares at a premium of 10% on 1st April,2021.

(2) It also offered to buy back the maximum permissible number of equity shares of ₹ 10 each at ₹ 30 per share on 2nd April 2021.

(3) The payment for the above was made out of available bank balance, which appeared as a part of the current assets.

(4) The company had investment in own debentures costing ₹ 60 lakhs (face value ₹ 75 lakhs). These debentures were cancelled on 2nd April 2021.

(5) On 4th April 2021 company issued one fully paid-up equity share of ₹ 10 each by way of bonus for every five equity shares held by the shareholders.

You are required to:

(a) Calculate maximum possible number of equity shares that can be bought back as per the Companies Act, 2013 and

(b) Record the Journal Entries for the above-mentioned information.

Ans.(a) (i) Statement determining the maximum number of shares to be bought back

	Number of shares (in lakhs)
Particulars	When loan fund is ₹ 304 lakhs
Shares Outstanding Test (W.N.1)	19.5
Resources Test (W.N.2)	11.175
Debt Equity Ratio Test (W.N.3)	29.725
Maximum number of shares that can be bought back [least of the above]	11.175

Thus, the company can buy 11,17,500 Equity shares at ₹ 30 each.

Working Notes:

1. Shares Outstanding Test

Particulars	**(Shares in lakh)**
Number of shares outstanding	78
25% of the shares outstanding	19.5

2. Resources Test

Particulars	
Paid up capital (₹ in lakh)	780
Free reserves (₹ in lakh) (625+52+148-24-240*)	561
Shareholders' funds (₹ in lakh)	1341
25% of Shareholders fund (₹ in lakh)	335.25
Buy-back price per share	30
Number of shares that can be bought back	11.175

*Amount transferred to CRR is excluded from free reserves.

Premium on redemption also reduced.

• Loan funds have been taken without considering current liabilities. Alternatively, If current liabilities are considered, then the maximum number of shares that can be bought back as per debt equity ratio test will be 24.7875 lakhs.

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back

	Particulars	**₹ In lakh**
(a)	Loan funds (₹)	304
(b)	Minimum equity to be maintained after buyback in the ratio of 2:1 (₹) (a/2)	152
(c)	Present equity shareholders fund (₹)	1341
(d)	Future equity shareholders fund (₹) (see W.N.4)	1043.75 (1341-297.25)

(e)	Maximum permitted buy-back of Equity (₹) [(d) – (b)]	891.75
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share	29.725
	As per the provisions of the Companies Act, 2013, company	Qualifies

Alternatively, when current liabilities are considered as part of loan funds, in that case Debt Equity Ratio Test will be done as follows:

	Particulars	₹ in lakh
(a)	Loan funds (₹)	699
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (₹) (a/2)	349.5
(c)	Present equity shareholders fund (₹)	1341
(d)	Future equity shareholders fund (₹) (see W.N.4)	1093.125 (1341-247.875)
(e)	Maximum permitted buy-back of Equity (₹) [(d) – (b)]	743.625
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share	24.7875
	As per the provisions of the Companies Act, 2013, company	Qualifies

4. Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method

Suppose amount transferred to CRR account is 'x' and maximum permitted buy - back of equity is 'y' Then

Equation 1: (Present Equity- Transfer to CRR) - Minimum Equity to be maintained = Maximum Permitted Buy-Back

= (1341 – x) – 152 = y

= 1189 – x =y (1)

Equation 2: Maximum Permitted Buy-Back x Nominal Value Per Share/Offer Price Per Share

y/30 x 10 = x or 3x = y (2)

by solving the above two equations we get

x = ₹ 297.25 and y = ₹ 891.75

Alternatively, when current liabilities are considered as part of loan funds, in that case

Equation 1: (Present Equity- Transfer to CRR)- Minimum Equity to be maintained = Maximum Permitted Buy-Back

= (1341 – x) – 349.5 = y

= 991.5 – x =y (1)

Equation 2: Maximum Permitted Buy-Back X Nominal Value Per Share/Offer Price Per Share

y/30 x 10 = x or 3x = y (2)

by solving the above two equations we get x = 247.875 and y = 743.625

(ii)

Journal Entries for Buy Back

			(₹ in lakhs)	
Date	**Particulars**		**Debit**	**Credit**
2021				
1st April	6% Redeemable preference share capital A/c	Dr.	240	
	Premium on redemption of preference shares A/c	Dr.	24	
	To Preference shareholders A/c			264
	(Being preference share capital transferred to shareholders account)			
	Preference shareholders A/c	Dr.	264	
	To Bank A/c			264
	(Being payment made to shareholders)			
	General Reserve or P&L A/c*	Dr.	24	
	To Premium on redemption of preference shares A/c			24
	(Being premium on redemption of preference shares adjusted through securities premium)			
2nd April	Equity shares buy-back A/c	Dr.	335.25	
	To Bank A/c			335.25
	(Being 11.175 lakhs equity shares of ₹ 10 each bought back @ ₹ 30 per share)			
	Equity share capital A/c	Dr.	111.75	
	Securities Premium A/c	Dr.	52	
	General Reserve or P&L A/c	Dr.	171.50	
	To Equity Shares buy-back A/c			335.25
	(Being cancellation of shares bought back)			
	General reserve A/c	Dr.	351.75	
	To Capital redemption reserve A/c			351.75
	(Being creation of capital redemption reserve account to the extent of the face value of preference shares redeemed and equity shares bought back as per the law ie. 240+ 111.75 lakhs)			
2nd April	7% Debentures A/c	Dr.	75	
	To Investment (own debentures) A/c			60
	To Profit on cancellation of own debentures A/c			15
	(Being cancellation of own debentures costing ₹ 60 lakhs, face value being ₹ 75 lakhs and the balance being profit on cancellation of debentures)			

4th April	Capital Redemption Reserve	Dr.	133.65	
	To Bonus Shares A/c			133.65
	(Being issue of one bonus equity share for every five equity shares held)			
	Bonus shares A/c	Dr.	133.65	
	To Equity share capital A/c			133.65
	(Being bonus shares issued)			

Working Note: Bonus Share to be issued =66.825 (78 - 11.175) lakh shares divided by 5 = 13.365 lakh shares.

Note: *Securities premium has not been utilized for the purpose of premium payable on redemption of preference shares assuming that the company referred in the question is governed by Section 133 of the Companies Act, 2013 and complies with the Accounting Standards prescribed for them. Alternative entry considering otherwise is also possible by utilizing securities premium amount.

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CHAPTER-5

AMALGAMATION OF COMPANIES

Q-1 P Ltd. and Q Ltd. agreed to amalgamate and form a new company called PQ Ltd. The summarized balance sheets of both the companies on the date of amalgamation stood as below:

Liabilities	P Ltd. ₹	Q Ltd. ₹	Assets	P Ltd. ₹	Q Ltd. ₹
Equity Shares (₹ 100 each)	8,20,000	3,20,000	Land & Building	4,50,000	3,40,000
9% Pref. Shares (₹ 100 each)	3,80,000	2,80,000	Furniture & Fittings	1,00,000	50,000
8% Debentures	2,00,000	1,00,000	Plant & Machinery	6,20,000	4,50,000
General Reserve	1,50,000	50,000	Trade receivables	3,25,000	1,50,000
Profit & Loss A/c	3,52,000	2,05,000	Inventory	2,33,000	1,05,000
Unsecured Loan	-	1,75,000	Cash at bank	2,08,000	1,75,000
Trade payables	88,000	1,60,000	Cash in hand	54,000	20,000
	19,90,000	**12,90,000**		**19,90,000**	**12,90,000**

PQ Ltd. took over the assets and liabilities of both the companies at book value after creating provision @ 5% on inventory and trade receivables respectively and depreciating Furniture & Fittings by @ 10%, Plant and Machinery by @ 10%. The trade receivables of P Ltd. include ₹ 25,000 due from Q Ltd.

PQ Ltd. will issue:

(i) 5 Preference shares of ₹ 20 each @ ₹ 18 paid up at a premium of ₹ 4 per share for each pref. share held in both the companies.

(ii) 6 Equity shares of ₹ 20 each @ ₹ 18 paid up a premium of ₹ 4 per share for each equity share held in both the companies.

(iii) 6% Debentures to discharge the 8% debentures of both the companies.

(iv) 20,000 new equity shares of ₹ 20 each for cash @ ₹ 18 paid up at a premium of ₹ 4 per share.

PQ Ltd. will pay cash to equity shareholders of both the companies in order to adjust their rights as per the intrinsic value of the shares of both the companies.

You are required to prepare ledger accounts in the books of P Ltd. and Q Ltd. to close their books.

Ans.

In the Books of P Ltd.

Realization Account

	₹		₹
To Land & Building	4,50,000	By 8% Debentures	2,00,000
To Plant & Machinery	6,20,000	By Trade Payables	88,000
To Furniture & Fitting	1,00,000	By PQ Ltd.	16,02,100
To Trade receivables	3,25,000	(Purchase consideration)	
To Inventory/Stock	2,33,000	By Equity Shareholders A/c	1,37,900
To Cash at Bank	2,08,000	(loss)	
To Cash in Hand	54,000		
To Preference shareholders (excess payment)	38,000		
	20,28,000		**20,28,000**

Equity Shareholders Account

	₹		₹
To Realization A/c (loss)	1,37,900	By Share capital	8,20,000
To Equity Shares in PQ Ltd.	10,82,400	By Profit & Loss A/c	3,52,000
To Cash	1,01,700	By General Reserve	1,50,000
	13,22,000		**13,22,000**

9% Preference Shareholders Account

To Preference Shares in PQ Ltd.	4,18,000	By Pref. Share capital	3,80,000
		By Realization A/c	38,000
	4,18,000		**4,18,000**

PQ Ltd. Account

To Realization A/c	16,02,100	By Shares in PQ Ltd.		
		For Equity	10,82,400	15,00,400
		For Pref.	4,18,000	
		By Cash		1,01,700
	16,02,100			**16,02,100**

8% Debentures holders Account

	₹		₹
To 6% Debentures	2,00,000	By 8% Debentures	2,00,000

Books of Q Ltd.

Realization Account

	₹		₹
To Land & Building	3,40,000	By 8% Debentures	1,00,000
To Plant & Machinery	4,50,000	By Trade payables	1,60,000
To Furniture & Fittings	50,000	By Unsecured loan	1,75,000
To Trade receivables	1,50,000	By PQ Ltd. (Purchase consideration)	7,92,250
To Inventory	1,05,000		
To Cash at bank	1,75,000	By Equity Shareholders A/c	90,750
To Cash in hand	20,000	Loss	
To Pref. shareholders	28,000		
	13,18,000		**13,18,000**

Equity Shareholders Account

	₹		₹
To Equity shares in PQ Ltd.	4,22,400	By Share Capital	3,20,000
To Realization	90,750	By Profit & Loss A/c	2,05,000
To Cash	61,850	By General Reserve	50,000
	5,75,000		**5,75,000**

9% Preference Shareholders Account

	₹		₹
To Preference Shares in PQ Ltd.	3,08,000	By Share capital	2,80,000
		By Realization A/c	28,000
	3,08,000		**3,08,000**

PQ Ltd. Account

	₹			₹
To Realization A/c	7,92,250	By Equity shares in PQ Ltd.		
		For Equity	4,22,400	
		Preference	3,08,000	7,30,400
		By Cash		61,850
	7,92,250			**7,92,250**

8% Debentures holders Account

	₹		₹
To 6% Debentures	1,00,000	By 8% Debentures	1,00,000

Working Notes:

(i) Purchase consideration

	P Ltd. ₹	Q Ltd. ₹
Payable to preference shareholders:		
Preference shares at ₹ 22 per share	4,18,000	3,08,000
Equity Shares at ₹ 22 per share	10,82,400	4,22,400
Cash [See W.N. (ii)]	1,01,700	61,850
	16,02,100	**7,92,250**

(ii) Value of Net Assets

		P Ltd. ₹		Q Ltd. ₹
Land & Building		4,50,000		3,40,000
Plant & Machinery less 10% Depreciation		5,58,000		4,05,000
Furniture & Fittings less 10% Depreciation		90,000		45,000
Trade receivables less 5%		3,08,750		1,42,500
Inventory less 5%		2,21,350		99,750
Cash at Bank		2,08,000		1,75,000
Cash in hand		54,000		20,000
		18,90,100		12,27,250
Less: Debentures	2,00,000		1,00,000	
Trade payables	88,000		1,60,000	
Secured Loans	–	(2,88,000)	1,75,000	(4,35,000)
			16,02,100	7,92,250
Payable in shares			15,00,400	7,30,400
Payable in cash*			1,01,700	(61,850)

(iii)

	P	Q
Plant &Machinery	6,20,000	4,50,000
Less: Depreciation 10%	62,000	45,000
	5,58,000	4,05,000
Furniture & Fixtures	1,00,000	50,000
Less: Depreciation 10%	10,000	5,000
	90,000	45,000

*This cash is paid to equity shareholders of both the companies for adjustment of their rights as per intrinsic value of both companies.

Q-2 The following is the summarized Balance Sheet of 'A' Ltd. as on 31.3.2019:

Liabilities	Rs.	Assets	Rs.
14,000 Equity shares of Rs. 100 each, fully paidup	14,00,000	Sundry assets	18,00,000
General reserve	10,000		
10% Debentures	2,00,000		
Trade payables	1,40,000		
Bank overdraft	50,000		
	18,00,000		**18,00,000**

B Ltd. agreed to take over the business of 'A' Ltd. Calculate purchase consideration under Net Assets method on the basis: Market value of 75% of the sundry assets is estimated to be 12% more than the book value and that of the remaining 25% at 8% less than the book value. The liabilities are taken over at book values. There is an unrecorded liability of Rs. 25,000.

Ans. **Calculation of Purchase Consideration under Net Assets Method**

	Rs.	Rs.
Sundry assets		
$18,00,000 \times \frac{75}{100} \times \frac{112}{100} =$	15,12,000	
$18,00,000 \times \frac{25}{100} \times \frac{92}{100} =$	4,14,000	19,26,000
Less: Liabilities:		
10% Debentures	2,00,000	
Trade payables	1,40,000	
Bank overdraft	50,000	
Unrecorded liability	25,000	(4,15,000)
Purchase consideration		15,11,000

Q-3 The following were the summarized Balance Sheets of P Ltd. and V Ltd. as at 31-3-20X1 :

Liabilities	P Ltd. (₹ in lakhs)	V Ltd. (₹ in lakhs)
Equity Share Capital (Fully paid shares of ₹ 10 each)	15,000	6,000
Securities Premium	3,000	–
Foreign Project Reserve	–	310
General Reserve	9,500	3,200
Profit and Loss Account	2,870	825
12% Debentures	–	1,000
Trade payables	1,200	463
Provisions	1,830	702
	33,400	12,500

Assets	P Ltd. (₹ in lakhs)	V Ltd. (₹ in lakhs)
Land and Buildings	6,000	–
Plant and Machinery	14,000	5,000
Furniture, Fixtures and Fittings	2,304	1,700
Inventory	7,862	4,041
Trade receivables	2,120	1,100
Cash at Bank	1,114	609
Cost of Issue of Debentures	—	50
	33,400	12,500

All the bills receivable held by V Ltd. were P Ltd.'s acceptances.

On 1st April 20X1, P Ltd. took over V Ltd in an amalgamation in the nature of merger. It was agreed that in discharge of consideration for the business P Ltd. would allot three fully paid equity shares of ₹ 10 each at par for every two shares held in V Ltd. It was also agreed that 12% debentures in V Ltd. would be converted into 13% debentures in P Ltd. of the same amount and denomination.

Details of trade receivables and trade payables as under:

Assets	P Ltd. (₹ in lakhs)	V Ltd. (₹ in lakhs)
Trade payables		
Bills Payable	120	-
Creditors	1,080	463
	1,200	463
Trade receivables		
Debtors	2,120	1,020
Bills Receivable	—	80
	2,120	1,100

Expenses of amalgamation amounting to ₹ 1 lakh were borne by P Ltd.

You are required to:

(i) Prepare journal entries in the books of P Ltd. and

(ii) Prepare P Ltd.'s Balance Sheet immediately after the merger considering that the cost of issue of debentures shown in the balance sheet of the V Ltd. company is not transferred to the P Ltd. company.

Ans. **Books of P Ltd.**

Journal Entries

		Dr. (₹ in Lacs)	Cr. (₹ in Lacs)
Business Purchase A/c	Dr.	9,000	
To Liquidator of V Ltd.			9,000
(Being business of V Ltd. taken over for consideration settled as per agreement)			
Plant and Machinery	Dr.	5,000	
Furniture & Fittings	Dr.	1,700	
Inventory	Dr.	4,041	
Debtors	Dr.	1,020	

Cash at Bank	Dr.	609	
Bills Receivable	Dr.	80	
To Foreign Project Reserve			310
To General Reserve (3,200 - 3,000)			200
To Profit and Loss A/c (825 – 50*)			775
To Liability for 12% Debentures			1,000
To Creditors			463
To Provisions			702
To Business Purchase			9,000
(Being assets & liabilities taken over from V Ltd.)			
Liquidator of V Ltd. A/c	Dr.	9,000	
To Equity Share Capital A/c			9,000
(Purchase consideration discharged in the form of equity shares)			
Profit & loss A/c	Dr.	1	
To Bank A/c			1
(Liquidation expenses paid by P Ltd.)			
Liability for 12% Debentures A/c	Dr.	1,000	
To 13% Debentures A/c			1,000
(12% debentures discharged by issue of 13% debentures)			
Bills Payable A/c	Dr.	80	
To Bills Receivable A/c			80
(Cancellation of mutual owing on account of bills)			

Balance Sheet of P Ltd. as at 1st April, 20X1 (after merger)

	Particulars		**Notes**	**₹ (in lakhs)**
	Equity and Liabilities			
1	Shareholders' funds			
	A	Share capital	1	24,000
	B	Reserves and Surplus	2	16,654
2	Non-current liabilities			
	A	Long-term borrowings	3	1,000
3	Current liabilities			
	A	Trade Payables (1,543 + 40)		1,583
	B	Short-term provisions		2,532
		Total		**45,769**
	Assets			
1	Non-current assets			
	A	Fixed assets		
	Tangible assets		4	29,004
2	Current assets			
	A	Inventories		11,903
	B	Trade receivables		3,140
	C	Cash and cash equivalents		1,722
		Total		**45,769**

Notes to accounts		₹
1.	Share Capital	
	Equity share capital	
	Authorised, issued, subscribed and paid up	
	24 crores equity shares of ₹ 10 each (Of the above shares,	
	9 crores shares have been issued for consideration other than cash)	24,000
	Total	24,000
2.	Reserves and Surplus	
	General Reserve	9,700
	Securities Premium	3,000
	Foreign Project Reserve	310
	Profit and Loss Account	3,644
	Total	16,654
3.	Long-term borrowings	
	Secured	
	13% Debentures	1,000
4.	Tangible assets	
	Land & Buildings	6,000
	Plant & Machinery	19,000
	Furniture & Fittings	4,004
	Total	**29,004**

Working Note:

Computation of purchase consideration

The purchase consideration was discharged in the form of three equity shares of P Ltd. for every two equity shares held in V Ltd.

Purchase consideration = ₹ 6,000 lacs × $\frac{3}{2}$ = ₹ 9,000 lacs.

* Cost of issue of debenture adjusted against P & L Account of V Ltd.

Q-4 The following is the summarized Balance Sheet of 'A' Ltd. as on 31.3.2017:

Liabilities	₹	Assets	₹
14,000 Equity shares of ₹ 100 each, fully paid up	14,00,000	Sundry assets	18,00,000
General reserve	10,000		
10% Debentures	2,00,000		
Trade payables	1,40,000		
Bank overdraft	50,000		
	18,00,000		**18,00,000**

B Ltd. agreed to take over the business of 'A' Ltd. Calculate purchase consideration under Net Assets method on the basis: Market value of 75% of the sundry assets is estimated to be 12% more than the book value and that of the remaining 25% at 8% less than the book value. The liabilities are taken over at book values. There is an unrecorded liability of ₹ 25,000.

Ans. **Calculation of Purchase Consideration under Net Assets Method**

	₹	₹
Sundry assets		
$18,00,000 \times \frac{75}{100} \times \frac{112}{100} =$	15,12,000	
$18,00,000 \times \frac{25}{100} \times \frac{92}{100} =$	4,14,000	19,26,000
Less: Liabilities:		
10% Debentures	2,00,000	
Trade payables	1,40,000	
Bank overdraft	50,000	
Unrecorded liability	25,000	(4,15,000)
Purchase consideration		15,11,000

Q-5 P Ltd. and Q Ltd. decided to amalgamate as on 01.04.2016 Their summarized Balance Sheets as on 31.03.2016 were as follows: (Rs.in '000)

Particulars	**P Ltd.**	**Q Ltd.**
Source of Funds:		
Equity share capital (Rs.10 each)	300	280
9% preference share Capital (Rs.100 each)	60	40
Investment allowance Reserve	70	60
Profit and Loss Account	8	12
10 % Debentures	100	60
Trade Payables	50	30
Tax provision	14	8
Total	602	490
Application of Funds:		
Building	120	100
Plant and Machinery	160	140
Investments	80	50
Trade receivables	90	70
Inventories	72	80
Cash and Bank	80	50
Total	602	490

From the following information, you are required to prepare the Balance Sheet as on 01.04.2016 of a new company, R Ltd., which was formed to take over the business of both the companies and took over all the assets and liabilities:

(i) 50 % Debenture are to be converted into Equity Shares of the New Company.

(ii) Investments are non - current in nature.

(iii) Fixed Assets of P Ltd. were valued at 10% above cost and that of Q Ltd. at 5% above cost.

(iv) 10 % of trade receivables were doubtful for both the companies. Inventories to be carried at cost.

(v) Preference shareholders were discharged by issuing eq ual number of 9% preference shares at par.

(vi) Equity shareholders of both the transferor companies are to be discharged by issuing Equity shares of Rs.10 each of the new company at a premium of Rs. 5 per share.

Give your answer on the basis that amalgamation is in the nature of purchase.

Ans.

M/s R Ltd.

Balance Sheet as at 1.4.2016

		Particulars	Notes	Rs. in'000
		Equity and Liabilities		
1		**Shareholders' funds**		
	a	**Share capital**	1	6,55,980
	b	Reserves and Surplus	2	2,77,990
2		**Non-current liabilities**		
	a	Long-term borrowings	3	80,000
3		**Current liabilities**		
	a	Trade Payables	4	80,000
	b	Short term provision	5	22,000
		Total		11,15,970

Assets

1		**Non-current assets**		
	a	Fixed assets		
		Tangible assets	6	5,60,000
	b	Non-current investments	7	1,30,000
2		**Current assets**		
	a	Inventory	8	1,52,000
	b	Trade receivables	9	1,44,000
	c	Cash and cash equivalents	10	1,29,970
		Total		11,15,970

Notes to accounts

		Rs. in'000
1.	**Share Capital**	
	Equity share capital	
	55,598 Equity shares of Rs.10 each, fully paid up (W.N.2)	5,55,980
	Preference share capital	
	9% Preference share capital (Share of Rs.100 each) (W.N.2)	1,00,000
		6,55,980
2.	**Reserves and Surplus**	
	Securities premium (W.N.2)	2,77,990
	Investment allowance reserve	
	(Rs.70,000+ Rs.60,000)	1,30,000
	Amalgamation adjustment reserve	(1,30,000)
		2,77,990

3.	**Long-term borrowings**	
	Secured	
	10% Debentures (50% of Rs.1,60,000)	80,000
4.	**Trade Payables** (Rs.50,000+ Rs.30,000)	80,000
5.	**Short term provisions**	
	Provision for tax (Rs.14,000+ Rs.8,000)	22,000
6.	**Tangible assets**	
	Building (Rs.1,32,000+Rs.1,05,000)	2,37,000
	Plant and machinery (Rs.1,76,000+Rs.1,47,000)	3,23,000
		5,60,000
7.	Non – current Investments (Rs.80,000+ Rs.50,000)	1,30,000
8.	**Inventory**	
	Stock (Rs. 72,000+ Rs. 80,000)	1,52,000
9.	**Trade receivables**	
	Trade receivables (90% of (Rs.90,000+ Rs.70,000)	1,44,000
10.	**Cash and cash equivalents**	
	Cash and Bank (Rs. 80,000+ Rs. 50,000 – Rs. 30)	1,29,970

Working Notes:

1. **Calculation of value of equity shares issued to transferor companies**

	P Ltd. (Rs.)	**Q Ltd. (Rs.)**
Assets taken over:		
Building	1,32,000	1,05,000
Plant and machinery	1,76,000	1,47,000
Investments	80,000	50,000
Inventories	72,000	80,000
Trade receivables	81,000	63,000
Cash & Bank	80,000	50,000
	6,21,000	4,95,000

Less: Liabilities:

10% Debentures	1,00,000		60,000	
Trade payables	50,000		30,000	
Tax Provision	14,000	1,64,000	8,000	98,000
		4,57,000		3,97,000
Less: Preference Share Capital		60,000		40,000
		3,97,000		**3,57,000**

2. Number of shares issued to equity shareholders, debenture holders and preference shareholders

	P Ltd.	**Q Ltd.**	**Total**
Equity shares issued @ Rs.15 per share (including Rs.5 premium)			
Rs.3,97,000/15	26,466 shares		
Rs.3,57,000/15		23,800shares	50,266 shares
Equity share capital @ Rs.10	Rs.2,64,660	Rs.2,38,000	Rs.5,02,660
Securities premium @ Rs.5	Rs.1,32,330	Rs.1,19,000	Rs.2,51,330
	Rs.3,96,990	Rs.3,57,000	Rs.7,53,990

50% of Debentures are converted into equity shares @ Rs. 15 per share

1,00,000/2 = 50,000/15	3,332 shares		
60,000/2 = 30,000/15		2,000 shares	5,332 shares
Equity share capital @ Rs.10	Rs.33,320	Rs.20,000	Rs.53,320
Security premium@ Rs.5	Rs.16,660	Rs.10,000	Rs.26,660
	Rs.49,980	Rs.30,000	Rs. 79,980
9% Preference share capital issued	Rs.60,000	Rs.40,000	Rs.1,00,000

Q-6 The following is the summarized Balance Sheet of A Ltd. as at 31st March, 2019 :

Liabilities	₹	**Assets**	₹
8,000 Equity shares of ₹ 100 each	8,00,000	Building	3,40,000
10% Debentures	4,00,000	Machinery	6,40,000
Loans	1,60,000	Inventory	2,20,000
Trade payables	3,20,000	Trade receivables	2,60,000
General Reserve	80,000	Bank	1,36,000
		Patent	1,30,000
		Share issue Expenses	34,000
	17,60,000		**17,60,000**

B Ltd. agreed to absorb A Ltd. on the following terms and conditions:

(1) B Ltd. would take over all assets, except bank balance and Patent at their book values less 10%. Goodwill is to be valued at 4 year's purchase of super profits, assuming that the normal rate of return be 8% on the combined amount of share capital and general reserve.

(2) B Ltd. is to take over trade payables at book value.

(3) The purchase consideration is to be paid in cash to the extent of ₹ 6,00,000 and the balance in fully paid equity shares of ₹ 100 each at ₹ 125 per share.

The average profit is ₹ 1,24,400. The liquidation expenses amounted to ₹ 16,000. B Ltd. sold prior to 31st March, 2018 goods costing ₹ 1,20,000 to A Ltd. for ₹ 1,60,000. ₹ 1,00,000 worth of goods are still in Inventory of A Ltd. on 31st March, 2018. Trade payables of A Ltd. include ₹ 40,000 still due to B Ltd.

Show the necessary Ledger Accounts to close the books of A Ltd. and prepare the Balance Sheet of B Ltd. as at 1st April, 2019 after the takeover.

Ans.

Books of A Limited

Realization Account

	₹		₹
To Building	3,40,000	By Trade payables	3,20,000
To Machinery	6,40,000	By B Ltd.	12,10,000
To Inventory	2,20,000	By Equity Shareholders (Loss)	76,000
To Trade receivables	2,60,000		
To Patent	1,30,000		
To Bank (Exp.)	16,000		
	16,06,000		**16,06,000**

Bank Account

To Balance b/d	1,36,000	By Realization (Exp.)	16,000
To B Ltd.	6,00,000	By 10% Debentures	4,00,000
		By Loan	1,60,000
		By Equity shareholders	1,60,000
	7,36,000		**7,36,000**

10% Debentures Account

To Bank	4,00,000	By Balance b/d	4,00,000
	4,00,000		4,00,000

Loan Account

To Bank	1,60,000	By Balance b/d	1,60,000
	1,60,000		1,60,000

Share Issue Expenses Account

To Balance b/d	34,000	By Equity shareholders	34,000
	34,000		34,000

General Reserve Account

To Equity shareholders	80,000	By Balance b/d	80,000
	80,000		80,000

B Ltd. Account

To Realisation A/c	12,10,000	By Bank	6,00,000
		By Equity share in B Ltd.	
		(4,880 shares at ₹ 125 each)	6,10,000
	12,10,000		12,10,000

Equity Shares in B Ltd. Account

To B Ltd.	6,10,000	By Equity shareholders	6,10,000
	6,10,000		6,10,000

Equity Share Holders Account

To Realization Account	76,000	By Equity share capital	8,00,000
To Share issue Expenses	34,000	By General reserve	80,000
To Equity shares in B Ltd.	6,10,000		
To Bank	1,60,000		
	8,80,000		8,80,000

B Ltd

Balance Sheet as on 1st April, 2019 (An extract)

	Particulars		Notes	₹
	Equity and Liabilities			
1	Shareholders' funds			
	a	Share capital	1	4,88,000
	b	Reserves and Surplus	2	1,07,000
2	Current liabilities			
	a	Trade Payables	3	2,80,000
	b	Bank overdraft		6,00,000
		Total		14,75,000
	Assets			
1	Non-current assets			
	a	Property, Plant and Equipment		
		Tangible assets	4	8,82,000
		Intangible assets	5	2,16,000

2	Current assets		
	a Inventories	6	1,83,000
	b Trade receivables	7	1,94,000
			14,75,000

Notes to Accounts

			₹
1	Share Capital		
	Equity share capital		
	4,880 Equity shares of ₹ 100 each (Shares have been issued for consideration other than cash)		4,88,000
	Total		4,88,000
2	Reserves and Surplus (an extract)		
	Securities Premium		1,22,000
	Profit and loss account	.....	
	Less: Unrealized profit	(15,000)	(15,000)
	Total		1,07,000
3	Trade payables		
	Opening balance	3,20,000	
	Less: Inter-company transaction cancelled upon amalgamation	(40,000)	2,80,000
4	Tangible assets		
	Buildings		3,06,000
	Machinery		5,76,000
	Total		8,82,000
5	Intangible assets		
	Goodwill		2,16,000
6	Inventories		
	Opening balance	1,98,000	
	Less: Cancellation of profit upon amalgamation	(15,000)	1,83,000
7	Trade receivables		
	Opening balance	2,34,000	
	Less: Intercompany transaction cancelled upon amalgamation	(40,000)	1,94,000

Working Notes :

			₹
1.	Valuation of Goodwill		
	Average profit		1,24,400
	Less: 8% of ₹ 8,80,000		(70,400)
	Super profit		54,000
	Value of Goodwill = 54,000 x 4		2,16,000
2.	Net Assets for purchase consideration		
	Goodwill as valued in W.N.1		2,16,000
	Building		3,06,000
	Machinery		5,76,000
	Inventory		1,98,000

Trade receivables (2,60,000-26,000)	2,34,000
Total Assets	15,30,000
Less: Trade payables	(3,20,000)
Net Assets	12,10,000

Out of this ₹ 6,00,000 is to be paid in cash and remaining i.e., (12,10,000 – 6,00,000) ₹ 6,10,000 in shares of ₹ 125. Thus, the number of shares to be allotted 6,10,000/125 = 4,880 shares.

3. Unrealized Profit on Inventory ₹

The Inventory of A Ltd. includes goods worth ₹ 1,00,000 which was sold by

B Ltd. on profit. Unrealized profit on this Inventory will be $\frac{40,000}{1,60,000} \times 1,00,000$ 25,000

As B Ltd purchased assets of A Ltd. at a price 10% less than the book value,
10% need to be adjusted from the Inventory i.e., 10% of ₹ 1,00,000. (10,000)

Amount of unrealized profit 15,000

Q-7 The financial position of two companies Alex Ltd. and Beta Ltd. as on 31st March, 2017 was as under:

Assets	**Alex Ltd. (₹)**	**Beta Ltd. (₹)**
Goodwill	1,40,000	70,000
Building	8,40,000	2,80,000
Machinery	14,00,000	4,20,000
Inventory	7,00,000	4,90,000
Trade receivables	5,60,000	2,80,000
Cash at Bank	1,40,000	56,000
	37,80,000	15,96,000
Liabilities	**Alex Ltd. (₹)**	**Beta Ltd. (₹)**
Share Capital:		
Equity Shares of ₹ 10 each	28,00,000	8,40,000
8% Preference Shares of ₹ 100 each	2,80,000	–
10% Preference Shares of ₹ 100 each	–	2,80,000
General Reserve	1,96,000	1,96,000
Retirement Gratuity fund	1,40,000	56,000
Trade payables	3,64,000	2,24,000
	37,80,000	15,96,000

Beta Ltd.is absorbed by Alex Ltd. on the following terms:

(a) 10% Preference Shareholders are to be paid at 10% premium by issue of 8% Preference Shares of Alex Ltd.

(b) Goodwill of Beta Ltd. is valued at ₹ 1,40,000, Buildings are valued at ₹ 4,20,000 and the Machinery at ₹ 4,48,000.

(c) Inventory to be taken over at 10% less value and Provision for Doubtful Debts to be created @ 7.5%.

(d) Equity Shareholders of Beta Ltd. will be issued Equity Shares of Alex Ltd. @ 5% premium.

You are required to:

(a) Prepare necessary Ledger Accounts to close the books of Beta Ltd.

(b) Prepare the acquisition entries in the books of Alex Ltd.

(c) Also prepare the Balance Sheet after absorption as at 31st March, 2017.

Ans. (a) **In the Books of Beta Ltd.**

Realisation Account

	₹		₹
To Sundry Assets	15,96,000	By Retirement GratuityFund	56,000
To Preference Shareholders (Premium onRedemption)	28,000	By Trade payables (PurchaseConsideration)	2,24,000
To Equity Shareholders (Profit on Realisation)	1,40,000	By Alex Ltd.	14,84,000
	17,64,000		17,64,000

Equity Shareholders Account

	₹		₹
To Equity Shares of Alex Ltd.	11,76,000	By Share Capital	8,40,000
		By General Reserve	1,96,000
		By Realisation Account (Profit onRealisation)	1,40,000
	11,76,000		11,76,000

Preference Shareholders Account

	₹		₹
To 8% Preference Sharesof Alex Ltd.	3,08,000	By Preference Share Capital	2,80,000
		By Realisation Account (Premium on Redemption of Preference Shares)	28,000
	3,08,000		3,08,000

Alex Ltd. Account

	₹		₹
To Realisation Account	14,84,000	By 8% Preference Shares	3,08,000
		By Equity Shares	11,76,000
	14,84,000		14,84,000

(b) **In the Books of Alex Ltd.**

Journal Entries

		Dr. ₹	Cr. ₹
Business Purchase A/c	Dr.	14,84,000	
To Liquidators of Beta Ltd. Account			14,84,000
(Being business of Beta Ltd. taken over)			
Goodwill Account	Dr.	1,40,000	
Building Account	Dr.	4,20,000	
Machinery Account	Dr.	4,48,000	
Inventory Account	Dr.	4,41,000	
Trade receivables Account	Dr.	2,80,000	
Bank Account	Dr.	56,000	
To Retirement Gratuity Fund Account			56,000
To Trade payables Account			2,24,000
To Provision for Doubtful Debts Account			21,000
To Business Purchase A/c			14,84,000

(Being Assets and Liabilities taken over as peragreed valuation).

Liquidators of Beta Ltd. A/c	Dr.	14,84,000	
To 8% Preference Share Capital A/c			3,08,000
To Equity Share Capital A/c			11,20,000
To Securities Premium A/c			56,000

(Being Purchase Consideration satisfied asabove).

(c) Balance Sheet of Alex Ltd. (after absorption) as at 31st March, 2017

	Particulars		Notes	₹
	Equity and Liabilities			
1	Shareholders' funds			
	A	Share capital	1	45,08,000
	B	Reserves and Surplus	2	2,52,000
2	Non-current liabilities			
	A	Long-term provisions		1,96,000
3	Current liabilities			
	A	Trade Payables		5,88,000
	B	Short term provision		21,000
		Total		55,65,000
	Assets			
1	Non-current assets			
	A	Fixed assets		
		Tangible assets	3	31,08,000
		Intangible assets		2,80,000
2	Current assets			
	A	Inventories		11,41,000
	B	Trade receivables		8,40,000
	C	Cash and cash equivalents		1,96,000
		Total		55,65,000

Notes to accounts:

		₹
1	**Share Capital**	
	Equity share capital	
	3,92,000 Equity Shares of ₹ 10 each fully paid (Out ofabove 1,12,000 Equity Shares were issued inconsideration other than for cash)	39,20,000
	Preference share capital	
	5,880 8% Preference Shares of ₹ 100 each (Out of above 3,080 Preference Shares were issued in considerationother than for cash)	5,88,000
	Total	45,08,000
2	**Reserves and Surplus**	
	Securities Premium	56,000
	General Reserve	1,96,000
	Total	2,52,000
3	**Tangible assets**	
	Buildings	12,60,000
	Machinery	18,48,000
	Total	31,08,000

Working Notes :

Purchase Consideration:	₹
Goodwill	1,40,000
Building	4,20,000
Machinery	4,48,000
Inventory	4,41,000
Trade receivables	2,59,000
Cash at Bank	56,000
Less: Liabilities:	
Retirement Gratuity	(56,000)
Trade payables	(2,24,000)
Net Assets/ Purchase Consideration	14,84,000
To be satisfied as under:	
Preference Shareholders of Beta Ltd.	2,80,000
Add: 10% Premium	28,000
Satisfied by issue of 3,080 no. of 8% Preference Shares of AlexLtd.	3,08,000
Equity Shareholders of Beta Ltd. to be satisfied by issue of 1,12,000	
Equity Shares of Alex Ltd. at 5% Premium	11,76,000
Total	14,84,000

Q-8 P Ltd. and Q Ltd. agreed to amalgamate their business. The scheme envisaged a share capital, equal to the combined capital of P Ltd. and Q Ltd. for the purpose of acquiring the assets, liabilities and undertakings of the two companies in exchange for share in PQ Ltd. The Summarized Balance Sheets of P Ltd. and Q Ltd. as on 31st March, 2017 (the date of amalgamation) are given below:

Summarized balance sheets as at 31-03-2017

Liabilities	P Ltd.₹	Q Ltd.₹	Assets	P Ltd.₹	Q Ltd.₹
Equity & liabilities:			Assets:		
Shareholders Fund			Non-current Assets:		
a. Share Capital	6,00,000	8,40,000	Fixed Assets		
b. Reserves	10,20,000	6,00,000	(excluding Goodwill)	7,20,000	10,80,000
Current Liabilities			Current Assets		
Bank Overdraft	-	5,40,000	a. Inventories	3,60,000	6,60,000
Trade payables	2,40,000	5,40,000	b. Trade receivables	4,80,000	7,80,000
			c. Cash at Bank	3,00,000	-
	18,60,000	**25,20,000**		**18,60,000**	**25,20,000**

The consideration was to be based on the net assets of the companies as shown in the above Balance Sheets, but subject to an additional payment to P Ltd. for its goodwill to be calculated as its weighted average of net profits for the three years ended 31st March, 2017. The weights for this purpose for the years 2014-15, 2015-16 and 2016-17 were agreed as 1, 2 and 3 respectively.

The profit had been:

2014-15 ₹ 3,00,000; 2015-16 ₹ 5,25,000 and 2016-17 ₹ 6,30,000.

The shares of PQ Ltd. were to be issued to P Ltd. and Q Ltd. at a premium and in proportion to the agreed net assets value of these companies.

In order to raise working capital, PQ Ltd proceeded to issue 72,000 shares of ₹ 10 each at the same rate of premium as issued for discharging purchase consideration to P Ltd. and Q Ltd.

You are required to :

(i) Calculate the number of shares issued to P Ltd. and Q Ltd; and

(ii) Prepare required journal entries in the books of PQ Ltd.; and

(iii) Prepare the Balance Sheet of PQ Ltd. as per Schedule III after recording the necessary journal entries.

(i) Calculation of number of shares issued to P Ltd. and Q Ltd.:

Amount of Share Capital as per balance sheet	₹
P Ltd.	6,00,000
Q Ltd.	8,40,000
	14,40,000

Share of P Ltd. = ₹ 14,40,000 x [21,60,000/ (21,60,000 + 14,40,000)]

= ₹ 8,64,000 or 86,400 shares

Securities premium = ₹ 21,60,000 – ₹ 8,64,000 = ₹ 12,96,000

Premium per share = ₹ 12,96,000 / ₹ 86,400 = ₹ 15

Issued 86,400 shares @ ₹ 10 each at a premium of ₹ 15 per share

Share of Q Ltd. = ₹ 14,40,000 x [14,40,000/ (21,60,000 + 14,40,000)]

= ₹ 5,76,000 or 57,600 shares

Securities premium = ₹ 14,40,000 – ₹ 5,76,000 = ₹ 8,64,000

Premium per share = ₹ 8,64,000 /₹ 57,600 = ₹ 15

Issued 57,600 shares @ ₹ 10 each at a premium of ₹ 15 per share

(ii) Journal Entries in the books of PQ Ltd.

Particulars		**Dr. Amount (₹)**	**Cr. Amount (₹)**
Business purchase account	Dr.	36,00,000	
To Liquidator of P Ltd. account			21,60,000
To Liquidator of Q Ltd. account			14,40,000
(Being the amount of purchase considerationpayable to liquidator of P Ltd. and Q Ltd. forassets taken over)			
Goodwill	Dr.	5,40,000	
Fixed assets account	Dr.	7,20,000	
Inventory account	Dr.	3,60,000	
Trade receivables account	Dr.	4,80,000	
Cash at bank	Dr.	3,00,000	
To Trade payables account			2,40,000
To Business purchase account			21,60,000
(Being assets and liabilities of P Ltd. taken over)			

Fixed assets account	Dr.	10,80,000	
Inventory account	Dr.	6,60,000	
Trade receivables account	Dr.	7,80,000	
To bank overdraft account			5,40,000
To Trade payables account			5,40,000
To Business purchase account			14,40,000
(Being assets and liabilities of Q Ltd. taken over)			
Liquidator of P Ltd. Account	Dr.	21,60,000	
To Equity share capital account(86,400 x ₹ 10)			8,64,000
To Securities premium (86,400 x ₹ 15)			12,96,000
(Being the allotment of shares as per agreementfor discharge of purchase consideration)			
Liquidator of Q Ltd. account	Dr.	14,40,000	
To Equity share capital account(57,600 x ₹ 10)			5,76,000
To Securities premium (57,600 x ₹ 15)			8,64,000
(Being the allotment of shares as per agreementfor discharge of purchase consideration)			
Bank A/c		18,00,000	
To Equity share capital account			7,20,000
To Securities premium(Equity share capital issued to raise workingcapital)			10,80,000

(iii) Balance Sheet of PQ Ltd. on 31st March, 2017 after amalgamation

	Particulars		Notes	₹
	Equity and Liabilities			
1	Shareholders' funds			
	a	Share capital	1	21,60,000
	b	Reserves and Surplus	2	32,40,000
2	Current liabilities			
	a	Trade payables (2,40,000 + 5,40,000)		7,80,000
		Total		61,80,000

	Assets			
1	Non-current assets			
	a	Fixed assets		
		Tangible assets (7,20,000 + 10,80,000)		18,00,000
		Intangible assets (goodwill)	4	5,40,000
2	Current assets			
	a	Inventories (3,60,000 + 6,60,000)		10,20,000
	b	Trade receivables (4,80,000 +7,80,000)		12,60,000
	c	Cash and cash equivalents	3	15,60,000
		Total		61,80,000

Notes to accounts

		₹
1	**Share Capital**	
	Issued, subscribed and paid up share capital	
	2,16,000 Equity shares of ₹10 each	21,60,000
	(Out of the above 1,44,000 shares issued for non-cashconsideration under scheme of amalgamation)	
2	**Reserves and Surplus**	
	Securities premium (@₹ 15 for 2,16,000 shares)	32,40,000
3	**Cash and cash equivalents**	
	Cash at Bank	15,60,000
4	**Intangible Assets**	
	Goodwill	5,40,000

Working Notes:

1. **Calculation of goodwill of P Ltd.**

Particulars	**Amount ₹**	**Weight**	**Weighted amount ₹**
2014-15	3,00,000	1	3,00,000
2015-16	5,25,000	2	10,50,000
2016-17	6,30,000	3	18,90,000
Total (a+b+c)	14,55,000	6	32,40,000
weighted Average = [Total weightedamount/ Total of weight][₹ 32,40,000/6]Goodwill			5,40,000

2. Calculation of Net assets

		P Ltd.₹	**Q Ltd. ₹**
	Assets		
	Goodwill	5,40,000	
	Fixed assets	7,20,000	10,80,000
	Inventory	3,60,000	6,60,000
	Trade receivable	4,80,000	7,80,000
	Cash at bank	3,00,000	
	Less: Liabilities		
	Bank overdraft	5,40,000	
	Trade payables	2,40,000	5,40,000
	Net assets or Purchase consideration	21,60,000	14,40,000
3.	New authorized capital		
	= ₹ 14,40,000 + ₹ 12,00 000 = ₹ 26,40,000		
4.	**Cash and Cash equivalents** ₹		
	P Ltd. Balance 3,00,000		
	Cash received from Fresh issue (72,000 x ₹ 25) 18,00,000		
	21,00,000		
	Less: Bank Overdraft 5,40,000		
	15,60,000*		

*The balance of cash and cash equivalents has been shown after setting off overdraft amount.

Q-9 The following are the summarized Balance Sheet of VT Ltd. and MG Ltd. as on 31st March, 2018:

Particulars	VT Ltd. (₹)	MG Ltd. (₹)
Equity and Liabilities		
Equity Shares of ₹ 10 each	12,00,000	6,00,000
10% Pref. Shares of ₹ 100 each	4,00,000	2,00,000
Reserve and Surplus	6,00,000	4,00,000
12% Debentures	4,00,000	3,00,000
Trade Payables	5,00,000	3,00,000
Total	31,00,000	18,00,000
Assets		
Fixed Assets	14,00,000	5,00,000
Investment	1,60,000	1,60,000
Inventory	4,80,000	6,40,000
Trade Receivables	8,40,000	4,20,000
Cash at Bank	2,20,000	80,000
Total	31,00,000	18,00,000

Details of Trade receivables and trade payables are as under:

	VT Ltd. (₹)	MG Ltd. (₹)
Trade Receivable		
Debtors	7,20,000	3,80,000
Bills Receivable	1,20,000	40,000
	8,40,000	4,20,000
Trade Payables		
Sundry Creditors	4,40,000	2,50,000
Bills Payable	60,000	50,000
	5,00,000	3,00,000

Fixed Assets of both the companies are to be revalued at 15% above book value.

Inventory in Trade and Debtors are taken over at 5% lesser than their book value.

Both the companies are to pay 10% equity dividend, Preference dividend having been already paid.

After the above transactions are given effect to, VT Ltd. will absorb MG Ltd. on the following terms:

(i) VT Ltd. will issue 16 Equity Shares of ₹ 10 each at par against 12 Shares of MG Ltd.

(ii) 10% Preference Shareholders of MG Ltd. will be paid at 10% discount by issue of 10% Preference Shares of ₹ 100 each, at par, in VT. Ltd.

(iii) 12% Debenture holders of MG Ltd. are to be paid at 8% premium, by 12% Debentures in VT Ltd., issued at a discount of 10%.

(iv) ₹ 60,000 is to be paid by VT Ltd. to MG Ltd. for Liquidation expenses.

(v) Sundry Debtors of MG Ltd. includes ₹ 20,000 due from VT Ltd.

You are required to prepare :

(1) Journal entries in the books of VT Ltd.

(2) Statement of consideration payable by VT Ltd.

Ans. (i) **Journal Entries in the Books of VT Ltd.**

		Dr. ₹	Cr. ₹
Fixed Assets	Dr.	2,10,000	
To Revaluation Reserve			2,10,000
(Revaluation of fixed assets at 15% above book value)			
Reserve and Surplus	Dr.	1,20,000	
To Equity Dividend			1,20,000
(Declaration of equity dividend @ 10%)			
Equity Dividend	Dr.	1,20,000	
To Bank Account			1,20,000
(Payment of equity dividend)			
Business Purchase Account	Dr.	9,80,000	
To Liquidator of MG Ltd.			9,80,000
(Consideration payable for the business taken over from MG Ltd.)			
Fixed Assets (115% of ₹ 5,00,000)	Dr.	5,75,000	
Inventory (95% of ₹ 6,40,000)	Dr.	6,08,000	
Debtors	Dr.	3,80,000	
Bills Receivable	Dr.	40,000	
Investment	Dr.	1,60,000	
Cash at Bank	Dr.	20,000	
(₹ 80,000 – ₹60,000 dividend paid)			
To Provision for Bad Debts (5% of ₹ 3,60,000)			18,000
To Sundry Creditors			2,50,000
To 12% Debentures in MG Ltd.			3,24,000
To Bills Payable			50,000
To Business Purchase Account			9,80,000
To Capital Reserve (Balancing figure)			1,61,000
(Incorporation of various assets and liabilities taken over from MG Ltd. at agreed values and difference of net assets and purchase consideration being credited to capital reserve)			
Liquidator of MG Ltd.	Dr.	9,80,000	
To Equity Share Capital			8,00,000
To 10% Preference Share Capital			1,80,000
(Discharge of consideration for MG Ltd.'s business)			
12% Debentures in MG Ltd. (₹ 3,00,000 × 108%)	Dr.	3,24,000	
Discount on Issue of Debentures	Dr.	36,000	
To 12% Debentures			3,60,000
(Allotment of 12% Debentures to debenture holders of MG Ltd. at a discount of 10%)			

Sundry Creditors	Dr.	20,000	
To Sundry Debtors			20,000
(Cancellation of mutual owing)			
Goodwill	Dr.	60,000	
To Bank			60,000
(Being liquidation expenses reimbursed to MG Ltd.)			
Capital Reserve/P&L A/c	Dr.	60,000	
To Goodwill			60,000
(Being goodwill set off)			

(ii) Statement of Consideration payable by VT Ltd. for 60,000 shares (payment method)

Shares to be allotted 60,000/12 x 16 = 80,000 shares of VT Ltd.

Issued 80,000 shares of ₹ 10 each i.e.	₹ 8,00,000	(i)
For 10% preference shares, to be paid at 10% discount		
₹ 2,00,000x 90/100	₹ 1,80,000	(ii)
Consideration amount [(i) + (ii)]	₹ 9,80,000	

Q-10 Distinguish between Amalgamation, Absorption and External Reconstruction of Company.

Ans. Difference between Amalgamation, Absorption and External Reconstruction

Basis	Amalgamation	Absorption	External Reconstruction
Meaning	Two or more companies are wound up and a new company is formed to take over their business.	In this case, an existing company takes over the business of one or more existing companies.	In this case, a newly formed company takes over the business of an existing company.
Minimum number of Companies involved	At least three companies are involved.	At least two companies are involved.	Only two companies are involved.
Number of new resultant companies	Only one resultant company is formed. Two companies are wound up to form a single resultant company.	No new resultant company is formed.	Only one resultant company is formed. Under this case a newly formed company takes over the business of an existing company.
Objective	Amalgamation is done to cut competition and reap the economies in large scale.	Absorption is done to cut competition and reap the economies in large scale.	External reconstruction is done to reorganise the financial structure of the company.
Example	A Ltd. and B Ltd. amalgamate to form C Ltd.	A Ltd. takes over the business of another existing company B Ltd.	B Ltd. is formed to take over the business of an existing company A Ltd.

Q-11 The financial position of X Ltd. and Y Ltd. as on 31st March, 2018 was as under:

	X Ltd. (₹)	Y Ltd. (₹)
Equity and Liabilities		
Equity Shares of ₹ 10 each	30,00,000	9,00,000
9% Preference Shares of ₹ 100 each	3,00,000	-
10% Preference Shares of ₹ 100 each	-	3,00,000
General Reserve	2,10,000	2,10,000
Retirement Gratuity Fund (long term)	1,50,000	60,000
Trade Payables	3,90,000	2,40,000
Total	40,50,000	17,10,000
Assets		
Goodwill	1,50,000	75,000
Land & Buildings	9,00,000	3,00,000
Plant & Machinery	15,00,000	4,50,000
Inventories	7,50,000	5,25,000
Trade Receivables	6,00,000	3,00,000
Cash and Bank	1,50,000	60,000
Total	40,50,000	17,10,000

X Ltd. absorbs Y Ltd. on the following terms:

(i) 10% Preference Shareholders are to be paid at 10% premium by issue of 9% PreferenceShares of X Ltd.

(ii) Goodwill of Y Ltd. on absorption is to be computed based on two times of average profits of preceding three financial years (2016-17 : ₹ 90,000; 2015-16 : ₹ 78,000 and 2014-15: ₹ 72,000). The profits of 2014 -15 included credit of an insurance claim of ₹ 25,000 (fire occurred in 2013-14 and loss by fire ₹ 30,000 was booked in Profit and Loss Account of that year). In the year 2015 -16, there was an embezzlement of cash by an employee amounting to ₹ 10,000.

(iii) Land & Buildings are valued at ₹ 5,00,000 and the Plant & Machinery at ₹ 4,00,000.

(iv) Inventories are to be taken over at 10% less value and Provision for Doubtful Debts is to be created @ 2.5%.

(v) There was an unrecorded current asset in the books of Y Ltd. whose fair value amountedto ₹ 15,000 and such asset was also taken over by X Ltd.

(vi) The trade payables of Y Ltd. included ₹ 20,000 payable to X Ltd.

(vii) Equity Shareholders of Y Ltd. will be issued Equity Shares @ 5% premium.

You are required to

(i) Prepare Realisation A/c in the books of Y Ltd.

(ii) Show journal entries in the books of X Ltd.

(iii) Prepare the Balance Sheet of X Ltd. after absorption as at 31st March,2018.

Ans. **In the Books of Y Ltd.**

Realisation Account

		₹		₹
To Sundry Assets :			By RetirementGratuity Fund	60,000
Goodwill	75,000			
Land & Building	3,00,000		By Trade payables	2,40,000
Plant & Machinery	4,50,000		By X Ltd. (Purchase	15,90,000
Inventory	5,25,000		Consideration)	
Trade receivables	3,00,000			
Bank	60,000	17,10,000		
To PreferenceShareholders		30,000		
(Premium onRedemption)				
To Equity Shareholders				
(Profit on Realisation)		1,50,000		
		18,90,000		**18,90,000**

In the Books of X Ltd.

Journal Entries

		Dr. ₹	Cr. ₹
Business Purchase A/c	Dr.	15,90,000	
To Liquidators of Y Ltd. Account			15,90,000
(Being business of Y Ltd. taken over)			
Goodwill Account	Dr.	1,50,000	
Land & Building Account	Dr.	5,00,000	
Plant & Machinery Account	Dr.	4,00,000	
Inventory Account	Dr.	4,72,500	
Trade receivables Account	Dr.	3,00,000	
Bank Account	Dr.	60,000	
Unrecorded assets Account	Dr.	15,000	
To Retirement Gratuity Fund Account			60,000
To Trade payables Account			2,40,000
To Provision for Doubtful Debts Account			7,500
To Business Purchase A/c			15,90,000
(Being Assets and Liabilities taken over as per agreedvaluation).			
Liquidators of Y Ltd. A/c	Dr.	15,90,000	
To 9% Preference Share Capital A/c			3,30,000
To Equity Share Capital A/c			12,00,000
To Securities Premium A/c			60,000
(Being Purchase Consideration satisfied as above)			

Balance Sheet of X Ltd. (after absorption)
as at 31st March, 2018

	Particulars		Notes	₹
	Equity and Liabilities			
1	Shareholders' funds			
	A	Share capital	1	48,30,000
	B	Reserves and Surplus	2	2,70,000
2	Non-current liabilities			
	A	Long-term provisions	3	2,10,000
3	Current liabilities			
	A	Trade Payables	4	6,10,000
	B	Short term provision	5	7,500
		Total		59,27,500
	Assets			
1	Non-current assets			
	A	Fixed assets		
	Tangible assets		6	33,00,000
	Intangible assets		7	3,00,000
2	Current assets			
	A	Inventories	8	12,22,500
	B	Trade receivables	9	8,80,000
	C	Other current Assets	10	15,000
	D	Cash and cash equivalents	11	2,10,000
		Total		59,27,500

Notes to accounts

		₹
1	Share Capital	
	Equity share capital	
	4,20,000 Equity Shares of ₹ 10 each fully paid (Out of above 1,20,000	
	Equity Shares were issued in consideration other thanfor cash)	42,00,000
	Preference share capital	
	6,300 9% Preference Shares of ₹ 100 each (Out of above 3,300	
	Preference Shares were issued in consideration other than forcash)	6,30,000
	Total	48,30,000
2	Reserves and Surplus	
	Securities Premium	60,000
	General Reserve	2,10,000
	Total	2,70,000
3	Long-term provisions	
	Retirement Gratuity fund	2,10,000

4	Trade payables(3,90,000 + 2,40,000 - 20,000*)* Mutual Owings eliminated.	6,10,000
5	Short term Provisions	
	Provision for Doubtful Debts	7,500
6	Tangible assets	
	Land & Buildings	14,00,000
	Plant & Machinery	19,00,000
	Total	33,00,000
7	Intangible assets	
	Goodwill (1,50,000 +1,50,000)	3,00,000
8	Inventories (7,50,000 + 4,72,500)	12,22,500
9	Trade receivables (6,00,000 + 3,00,000 - 20,000)	8,80,000
10	Other current Assets	15,000
11	Cash and cash equivalents (1,50,000 +60,000)	2,10,000

Working Notes:

1.	**Computation of goodwill**		₹
	Profit of 2016-17		90,000
	Profit of 2015-16 adjusted ₹ 78,000 + 10,000)		88,000
	Profit of 2014-15 adjusted (₹ 72,000 – 25,000)		47,000
			2,25,000
	Average profit		75,000
	Goodwill to be valued at 2 times of average profits = ₹ 75,000 x 2 = ₹ 1,50,000		
2.	**Purchase Consideration:**		₹
	Goodwill		1,50,000
	Land & Building		5,00,000
	Plant & Machinery		4,00,000
	Inventory		4,72,500
	Trade receivables		3,00,000
	Unrecorded assets		15,000
	Cash at Bank		60,000
			18,97,500
	Less: Liabilities:		
	Retirement Gratuity	60,000	
	Trade payables	2,40,000	
	Provision for doubtful debts	7,500	(3,07,500)
	Net Assets/ Purchase Consideration		15,90,000
	To be satisfied as under:		
	10% Preference Shareholders of Y Ltd.		3,00,000
	Add: 10% Premium		30,000
	9% Preference Shares of X Ltd.		3,30,000
	Equity Shareholders of Y Ltd. to be satisfied by issue of		
	1,20,000 equity Shares of X Ltd. at 5% Premium		12,60,000
	Total		**15,90,000**

Q-12 X Ltd. is a group engaged in manufacture and sale of industrial and FMCG products. One of their division also deals in Leasing of properties - Mobile Towers. The accountant showed the rent arising from the leasing of such properties as other income in the Statement of Profit and Loss.

Comment whether the classification of the rent income made by the accountant is correct or not in the light of Schedule HI to the Companies Act, 2013.

Ans. As per para 4 of the 'General Instructions for preparation of Statement of Profit and Loss' given in the Schedule III to the Companies Act, 2013, 'other income' does not include operating income.

The term "Revenue from operations" has not been defined under Schedule III to the Companies Act 2013. However, as per Guidance Note on Schedule III to the Companies Act 2013 this would include revenue arising from a company's operating activities i.e. either its principal or ancillary revenue-generating activities. Whether a particular income constitutes "Revenue from operations" or "other income" is to be decided based on the facts of each case and detailed understanding of the company's activities. The classification of income would also depend on the purpose for which the particular asset is acquired or held.

As per the information given in the question, X Ltd is a group engaged in manufacture and sale of industrial and FMCG products and its one of the division deals in leasing of properties- Mobile Towers. Since its one division is continuously engaged in leasing of properties, it shall be considered as its principal or ancillary revenue-generating activities. Therefore, the rent arising from such leasing shall be shown under the head "Revenue from operations" and not as "Other Income".

Hence the presentation of rent arising from the leasing of such properties as "other income" in the statement of Profit and Loss is not correct. It should be shown under the head "Revenue from operations".

Q-13 Two companies named Alex Ltd. and Beta Ltd. provide you the following summary of ledger balances as on 31st March, 2020:

	Alex Ltd. (₹)	**Beta Ltd. (₹)**
Goodwill	1,40,000	70,000
Building	8,40,000	2,80,000
Machinery	14,00,000	4,20,000
Inventory	7,00,000	4,90,000
Trade receivables	5,60,000	2,80,000
Cash at Bank	1,40,000	56,000
Equity Shares of ₹ 10 each	28,00,000	8,40,000
8% Preference Shares of ₹ 100 each	2,80,000	–
10% Preference Shares of ₹ 100 each	–	2,80,000
General Reserve	1,96,000	1,96,000
Retirement Gratuity fund	1,40,000	56,000
Trade payables	3,64,000	2,24,000

Beta Ltd. is absorbed by Alex Ltd. on the following terms:

(a) 10% Preference Shareholders are to be paid at 10% premium by issue of 8% Preference Shares of Alex Ltd.

(b) Goodwill of Beta Ltd. is valued at ₹1,40,000, Buildings are valued at ₹ 4,20,000 and the Machinery at ₹ 4,48,000.

(c) Inventory to be taken over at 10% less value and Provision for Doubtful Debts to be created @ 7.5%.

(d) Equity Shareholders of Beta Ltd. will be issued Equity Shares of Alex Ltd. @ 5% premium.

You are required to:

(i) Prepare necessary Ledger Accounts to close the books of Beta Ltd.

(ii) Show the acquisition entries in the books of Alex Ltd.

(iii) Also draft the Balance Sheet after absorption as at 31st March, 2020.

Ans.

(i) **In the Books of Beta Ltd.**

Realisation Account

	₹		₹
To Sundry Assets	15,96,000	By Retirement Gratuity Fund	56,000
To Preference Shareholders (Premium on Redemption)	28,000	By Trade payables (Purchase Consideration)	2,24,000
To Equity Shareholders (Profit on Realisation)	1,40,000	By Alex Ltd.	14,84,000
	17,64,000		**17,64,000**

Equity Shareholders Account

	₹		₹
To Equity Shares of Alex Ltd.	11,76,000	By Share Capital	8,40,000
		By General Reserve	1,96,000
		By Realisation Account (Profit on Realisation)	1,40,000
	11,76,000		**11,76,000**

Preference Shareholders Account

	₹		₹
To 8% Preference Shares of Alex Ltd.	3,08,000	By Preference Share Capital	2,80,000
		By Realisation Account (Premium on Redemption of Preference Shares)	28,000
	3,08,000		**3,08,000**

Alex Ltd. Account

	₹		₹
To Realisation Account	14,84,000	By 8% Preference Shares	3,08,000
		By Equity Shares	11,76,000
	14,84,000		**14,84,000**

(ii) **In the Books of Alex Ltd.**

Journal Entries

		Dr. ₹	Cr. ₹
Business Purchase A/c	Dr.	14,84,000	
To Liquidators of Beta Ltd. Account			14,84,000
(Being business of Beta Ltd. taken over)			
Goodwill Account	Dr.	1,40,000	
Building Account	Dr.	4,20,000	
Machinery Account	Dr.	4,48,000	
Inventory Account	Dr.	4,41,000	
Trade receivables Account	Dr.	2,80,000	
Bank Account	Dr.	56,000	

To Retirement Gratuity Fund Account			56,000
To Trade payables Account			2,24,000
To Provision for Doubtful Debts Account			21,000
To Business Purchase A/c			14,84,000
(Being Assets and Liabilities taken over as per agreed valuation).			
Liquidators of Beta Ltd. A/c	Dr.	14,84,000	
To 8% Preference Share Capital A/c			3,08,000
To Equity Share Capital A/c			11,20,000
To Securities Premium A/c			56,000
(Being Purchase Consideration satisfied as above).			

(iii) **Balance Sheet of Alex Ltd. (after absorption) as at 31st March, 2020**

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	45,08,000
	B	Reserves and Surplus	2	2,52,000
2		**Non-current liabilities**		
	A	Long-term provisions		1,96,000
3		**Current liabilities**		
	A	Trade Payables		5,88,000
	B	Short term provision		21,000
		Total		55,65,000
Assets				
1		**Non-current assets**		
	A	Property, Plant and Equipment (PPE)	3	31,08,000
	B	Intangible assets		2,80,000
2		**Current assets**		
	A	Inventories		11,41,000
	B	Trade receivables		8,40,000
	C	Cash and cash equivalents		1,96,000
		Total		55,65,000

Notes to accounts:

		₹
1	**Share Capital**	
	Equity share capital	
	3,92,000 Equity Shares of ₹ 10 each fully paid (Out of above 1,12,000 Equity Shares were issued in consideration other than for cash)	39,20,000
	Preference share capital	
	5,880 8% Preference Shares of ₹ 100 each (Out of above 3,080 Preference Shares were issued in consideration other than for cash)	5,88,000
	Total	**45,08,000**

2	**Reserves and Surplus**	
	Securities Premium	56,000
	General Reserve	1,96,000
	Total	2,52,000
3	**PPE**	
	Buildings	12,60,000
	Machinery	18,48,000
	Total	31,08,000

Working Notes:

Purchase Consideration:	₹
Goodwill	1,40,000
Building	4,20,000
Machinery	4,48,000
Inventory	4,41,000
Trade receivables	2,59,000
Cash at Bank	56,000
Less: Liabilities:	
Retirement Gratuity	(56,000)
Trade payables	(2,24,000)
Net Assets/ Purchase Consideration	14,84,000
To be satisfied as under:	
Preference Shareholders of Beta Ltd.	2,80,000
Add: 10% Premium	28,000
Satisfied by issue of 3,080 no. of 8% Preference Shares of Alex Ltd.	3,08,000
Equity Shareholders of Beta Ltd. to be satisfied by issue of 1,12,000 Equity Shares of Alex Ltd. at 5% Premium	11,76,000
Total	14,84,000

Q-14 Explain the difference between pooling of interest and purchase method of accounting for amalgamations.

Ans. **Pooling of Interest Method**

Under pooling of interests method, the assets, liabilities and reserves of the Transferor Company will be taken over by Transferee Company at existing carrying amounts unless any adjustment is required due to different accounting policies followed by these companies. As a result the difference between the amount recorded as share capital issued (plus any additional consideration in the form of cash or other assets) and the amount of share capital of Transferor Company should be adjusted in reserves.

Purchase Method

The assets and liabilities of the transferor company should be incorporated at their existing carrying amounts or the purchase consideration should be allocated to individual identifiable assets and liabilities on the basis of their fair values at the date of amalgamation. No reserves, other than statutory reserves, of the transferor company should be incorporated in the financial statements of transferee company.

Q-15 X Ltd. and Y Ltd. give the following information of assets, equity and liabilities as on 31st March, 2018:

	X Ltd. (₹)	Y Ltd. (₹)
Equity and Liabilities		
Equity Shares of ₹ 10 each	30,00,000	9,00,000
9% Preference Shares of ₹ 100 each	3,00,000	-
10% Preference Shares of ₹ 100 each	-	3,00,000
General Reserve	2,10,000	2,10,000
Retirement Gratuity Fund (long term)	1,50,000	60,000
Trade Payables	3,90,000	2,40,000
Assets		
Goodwill	1,50,000	75,000
Land & Buildings	9,00,000	3,00,000
Plant & Machinery	15,00,000	4,50,000
Inventories	7,50,000	5,25,000
Trade Receivables	6,00,000	3,00,000
Cash and Bank	1,50,000	60,000

X Ltd. absorbs Y Ltd. on the following terms:

(i) 10% Preference Shareholders are to be paid at 10% premium by issue of 9% Preference Shares of X Ltd.

(ii) Goodwill of Y Ltd. on absorption is to be computed based on two times of average profits of preceding three financial years (2016-17 : ₹ 90,000; 2015-16 : ₹ 78,000 and 2014-15: ₹ 72,000). The profits of 2014 -15 included credit of an insurance claim of ₹ 25,000 (fire occurred in 2013-14 and loss by fire ₹ 30,000 was booked in Profit and Loss Account of that year). In the year 2015 -16, there was an embezzlement of cash by an employee amounting to ₹ 10,000.

(iii) Land & Buildings are valued at ₹ 5,00,000 and the Plant & Machinery at ₹ 4,00,000.

(iv) Inventories are to be taken over at 10% less value and Provision for Doubtful Debts is to be created @ 2.5%.

(v) There was an unrecorded current asset in the books of Y Ltd. whose fair value amounted to ₹ 15,000 and such asset was also taken over by X Ltd.

(vi) The trade payables of Y Ltd. included ₹ 20,000 payable to X Ltd.

(vii) Equity Shareholders of Y Ltd. will be issued Equity Shares @ 5% premium.

You are required to:

(i) Prepare Realisation A/c in the books of Y Ltd.

(ii) Show journal entries in the books of X Ltd.

(iii) Prepare the Balance Sheet of X Ltd. after absorption as at 31st March,2018.

Ans.

In the Books of Y Ltd.

Realisation Account

		₹			₹
To	Sundry Assets:		By	Retirement Gratuity Fund	60,000
	Goodwill 75,000				
	Land & Building 3,00,000		By	Trade payables	2,40,000
	Plant & Machinery 4,50,000		By	X Ltd. (Purchase Consideration)	15,90,000
	Inventory 5,25,000				
	Trade receivables 3,00,000				
	Bank 60,000	17,10,000			

To	Preference Shareholders (Premium on Redemption)	30,000		
To	Equity Shareholders (Profit on Realisation)	1,50,000		
		18,90,000		**18,90,000**

In the Books of X Ltd.

Journal Entries

		Dr. ₹	Cr. ₹
Business Purchase A/c	Dr.	15,90,000	
To Liquidators of Y Ltd. Account			15,90,000
(Being business of Y Ltd. taken over)			
Goodwill Account	Dr.	1,50,000	
Land & Building Account	Dr.	5,00,000	
Plant & Machinery Account	Dr.	4,00,000	
Inventory Account	Dr.	4,72,500	
Trade receivables Account	Dr.	3,00,000	
Bank Account	Dr.	60,000	
Unrecorded assets Account	Dr.	15,000	
To Retirement Gratuity Fund Account			60,000
To Trade payables Account			2,40,000
To Provision for Doubtful Debts Account			7,500
To Business Purchase A/c			15,90,000
(Being Assets and Liabilities taken over as per agreed valuation).			
Liquidators of Y Ltd. A/c	Dr.	15,90,000	
To 9% Preference Share Capital A/c			3,30,000
To Equity Share Capital A/c			12,00,000
To Securities Premium A/c			60,000
(Being Purchase Consideration satisfied as above)			

Balance Sheet of X Ltd. (after absorption)

as at 31st March, 2018

		Particulars	**Notes**	**₹**
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	48,30,000
	B	Reserves and Surplus	2	2,70,000
2		Non-current liabilities		
	A	Long-term provisions	3	2,10,000
3		Current liabilities		
	A	Trade Payables	4	6,10,000
	B	Short term provision	5	7,500
		Total		59,27,500

		Assets		
1		Non-current assets		
		Property, Plant and Equipment	6	33,00,000
		Intangible assets	7	3,00,000
2		Current assets		
	A	Inventories	8	12,22,500
	B	Trade receivables	9	8,80,000
	C	Other current Assets	10	15,000
	D	Cash and cash equivalents	11	2,10,000
	Total			**59,27,500**

Notes to accounts ₹

1	Share Capital	
	Equity share capital	
	4,20,000 Equity Shares of ₹ 10 each fully paid (Out of above 1,20,000 Equity Shares were issued at 5% premium in consideration other than for cash)	42,00,000
	Preference share capital	
	6,300 9% Preference Shares of ₹ 100 each (Out of above 3,300 Preference Shares were issued in consideration other than for cash)	6,30,000
	Total	48,30,000
2	Reserves and Surplus	
	Securities Premium	60,000
	General Reserve	2,10,000
	Total	2,70,000
3	Long-term provisions	
	Retirement Gratuity fund	2,10,000
4	Trade payables	
	(3,90,000 + 2,40,000 - 20,000*)	6,10,000
	* Mutual Owings eliminated.	
5	Short term Provisions	
	Provision for Doubtful Debts	7,500
6	Property, Plant and Equipment	
	Land & Buildings	14,00,000
	Plant & Machinery	19,00,000
	Total	33,00,000
7	Intangible assets	
	Goodwill (1,50,000 +1,50,000)	3,00,000
8	Inventories (7,50,000 + 4,72,500)	12,22,500
9	Trade receivables (6,00,000 + 3,00,000 - 20,000)	8,80,000
10	Other current Assets	15,000
11	Cash and cash equivalents (1,50,000 +60,000)	2,10,000

Working Notes:

1.

Computation of goodwill	₹
Profit of 2016-17	90,000
Profit of 2015-16 adjusted (₹ 78,000 + 10,000)	88,000
Profit of 2014-15 adjusted (₹ 72,000 – 25,000)	47,000
	2,25,000
Average profit	75,000

Goodwill to be valued at 2 times of average profits = ₹ 75,000 x 2 = ₹ 1,50,000

2.

Purchase Consideration:		₹
Goodwill		1,50,000
Land & Building		5,00,000
Plant & Machinery		4,00,000
Inventory		4,72,500
Trade receivables		3,00,000
Unrecorded assets		15,000
Cash at Bank		60,000
		18,97,500
Less: Liabilities:		
Retirement Gratuity	60,000	
Trade payables	2,40,000	
Provision for doubtful debts	7,500	(3,07,500)
Net Assets/ Purchase Consideration		15,90,000
To be satisfied as under:		
10% Preference Shareholders of Y Ltd.		3,00,000
Add: 10% Premium		30,000
9% Preference Shares of X Ltd.		3,30,000
Equity Shareholders of Y Ltd. to be satisfied by issue of 1,20,000 equity Shares of X Ltd. at 5% Premium		12,60,000
Total		**15,90,000**

Q-16 A Ltd. gives the following information on 31st March, 2021:

	₹
8,000 Equity shares of ‘ 100 each	8,00,000
10% Debentures	4,00,000
Loans	1,60,000
Trade payables	3,20,000
General Reserve	80,000
Building	3,40,000
Machinery	6,40,000
Inventory	2,20,000
Trade receivables	2,60,000
Bank	1,36,000
Patent	1,30,000
Profit & Loss account (Dr. balance)	34,000

B Ltd. agreed to absorb A Ltd. on the following terms and conditions:

(1) B Ltd. would take over all assets, except bank balance and Patent at their book values less 10%. Goodwill is to be valued at 4 year's purchase of super profits, assuming that the normal rate of return be 8% on the combined amount of share capital and general reserve.

(2) B Ltd. is to take over trade payables at book value.

(3) The purchase consideration is to be paid in cash to the extent of ₹6,00,000 and the balance in fully paid equity shares of ₹ 100 each at ₹ 125 per share.

The average profit is ₹ 1,24,400. The liquidation expenses amounted to ₹ 16,000. B Ltd. sold prior to 31st March, 2021 goods costing ₹ 1,20,000 to A Ltd. for ₹ 1,60,000. ₹ 1,00,000 worth of goods are still in Inventory of A Ltd. on 31st March, 2021. Trade payables of A Ltd. include ₹ 40,000 still due to B Ltd.

Show the Realisation A/c, Bank A/c, B Ltd. A/c and Equity shareholders A/c to close the books of A Ltd. and prepare the Balance Sheet of B Ltd. as at 1st April, 2021 after the takeover from the available information.

Ans. **Books of A Limited**

Realization Account

	₹		₹
To Building	3,40,000	By Trade payables	3,20,000
To Machinery	6,40,000	By B Ltd.	12,10,000
To Inventory	2,20,000	By Equity Shareholders (Loss)	76,000
To Trade receivables	2,60,000		
To Patent	1,30,000		
To Bank (Exp.)	16,000		
	16,06,000		16,06,000

Bank Account

To Balance b/d	1,36,000	By Realization (Exp.)	16,000
To B Ltd.	6,00,000	By 10% Debentures	4,00,000
		By Loans	1,60,000
		By Equity shareholders	1,60,000
	7,36,000		**7,36,000**

B Ltd. Account

To Realisation A/c	12,10,000	By Bank	6,00,000
		By Equity share in B Ltd. (4,880 shares at ` 125 each)	6,10,000
	12,10,000		**12,10,000**

Equity Share Holders Account

To Realization Account	76,000	By Equity share capital	8,00,000
To Profit & Loss A/c (Dr.)	34,000	By General reserve	80,000
To Equity shares in B Ltd.	6,10,000		
To Bank	1,60,000		
	8,80,000		**8,80,000**

B Ltd

Balance Sheet as on 1st April, 2021 (An extract)1

		Particulars	Notes	₹
			Equity and Liabilities	
1		Shareholders' funds		
	a	Share capital	1	4,88,000
	b	Reserves and Surplus	2	1,07,000
2		Current liabilities		
	a	Trade Payables	3	2,80,000
	b	Bank overdraft		6,00,000
		Total		14,75,000
Assets				
1		Non-current assets		
		Property, Plant and Equipment	4	8,82,000
		Intangible assets	5	2,16,000
2		Current assets		
	a	Inventories	6	1,83,000
	b	Trade receivables	7	1,94,000
				14,75,000

Notes to Accounts

				₹
1	**Share Capital**			
	Equity share capital			4,880
	Equity shares of ₹ 100 each (Shares have been issued for consideration other than cash)			4,88,000
		Total		4,88,000
2	**Reserves and Surplus (an extract)**			
	Securities Premium			**1,22,000**
	Profit and loss account		**…..**	
	Less: Unrealized profit		(15,000)	(15,000)
		Total		1,07,000
3	**Trade payables**			
	Opening balance		3,20,000	
	Less: Inter-company transaction cancelled upon amalgamation		(40,000)	2,80,000
4	**Property, Plant and Equipment**			
	Buildings			3,06,000
	Machinery			5,76,000
		Total		**8,82,000**
5	**Intangible assets**			
	Goodwill			2,16,000
6	**Inventories**			
	Opening balance		1,98,000	
	Less: Cancellation of profit upon amalgamation		(15,000)	1,83,000
7	Trade receivables			
	Opening balance		2,34,000	
	Less: Intercompany transaction cancelled upon amalgamation		(40,000)	1,94,000

Working Notes:

1. Valuation of Goodwill

	₹
Average profit	1,24,400
Less: 8% of f 8,80,000	(70,400)
Super profit	54,000
Value of Goodwill = 54,000 x 4	2,16,000

2. Net Assets for purchase consideration

Goodwill as valued in W.N.1	2,16,000
Building	3,06,000
Machinery	5,76,000
Inventory	1,98,000
Trade receivables	2,34,000
Total Assets	15,30,000
Less: Trade payables	(3,20,000)
Net Assets	12,10,000

Out of this ₹ 6,00,000 is to be paid in cash and remaining i.e., (12,10,000 – 6,00,000) ₹ 6,10,000 in shares of ₹ 125. Thus, the number of shares to be allotted 6,10,000/125 = 4,880 shares.

3. Unrealized Profit on Inventory

	₹
The Inventory of A Ltd. includes goods worth ₹ 1,00,000 which was sold by B Ltd. on profit. Unrealized profit on this Inventory will be	
$\frac{40,000}{1,60,000} \times 1,00,000$	25,000
As B Ltd. purchased assets of A Ltd. at a price 10% less than the bookvalue, 10% need to be adjusted from the Inventory i.e., 10% of₹ 1,00,000.	(10,000)
Amount of unrealized profit	15,000

Q-17 Sun and Neptune (both companies) had been carrying on business independently. They agreed to amalgamate and form a new company Jupiter Ltd. with an authorised share capital of ₹ 4,00,000 divided into 80,000 equity shares of ₹ 5 each. On 31st March, 2021 Sun and Neptune provide the following information:

	Sun (₹)	Neptune (₹)
Fixed Assets	6,35,000	3,65,000
Current Assets	3,27,000	1,67,750
	9,62,000	5,32,750
Less: Current Liabilities	(5,97,000)	(1,80,250)
Representing Capital	3,65,000	3,52,500

Additional Information:

(a) Revalued figures of Fixed and Current assets were as follows:

	Sun (₹)	Neptune (₹)
Fixed Assets	7,10,000	3,90,000
Current Assets	2,99,500	1,57,750

(b) The debtors and creditors include ₹ 43,350 owed by Sun to Neptune.

The purchase consideration is satisfied by issue of the following shares and debentures.

(i) 60,000 equity shares of Jupiter Ltd. to Sun and Neptune in the proportion to the profitability of their respective business based on the average net profit during the last three years which were as follows:

	Sun (₹)	Neptune (₹)
2019 Profit	4,49,576	2,73,900
2020 (Loss)/Profit	(2,500)	3,42,100
2021 Profit	3,77,924	3,59,000

(ii) 15% debentures in Jupiter Ltd. at par to provide an income equivalent to 8% return business as on capital employed in their respective business as on 31st March, 2021 after revaluation of assets.

You are required to :

(1) Compute the amount of debentures and shares to be issued to Sun and Neptune.

(2) A Balance sheet of Jupiter Ltd. showing the position immediately after amalgamation.

Q-18 Explain the difference between pooling of interest and purchase method of accounting for amalgamations.

Ans.(1) Computation of Amount of Debentures and Shares to be issued:

	Sun ₹	Neptune ₹
(i) Average Net Profit		
₹ (4,49,576-2,500+3,77,924)/3	= 2,75,000	
₹ (2,73,900+,3,42,100+3,59,000)/3		= 3,25,000

(ii) Equity Shares Issued

(a) Ratio of distribution

Sun	:	Neptune
275	:	325

(b) Number

Sun	:	27,500
Neptune	:	32,500
		60,000

(c) Amount

	Sun ₹	Neptune ₹
27,500 shares of ₹ 5 each	1,37,500	
32,500 shares of ₹ 5 each		1,62,500

(iii)	Capital Employed (after revaluation of assets)	₹	₹
	Fixed Assets	7,10,000	3,90,000
	Current Assets	2,99,500	1,57,750
		10,09,500	5,47,750
	Less: Current Liabilities	-5,97,000	-1,80,250
		4,12,500	3,67,500

(iv)	Debentures Issued		
	8% Return on capital employed	33,000	29,400
	15% Debentures to be issued to provide equivalent income:		
	Sun: 33,000 × 100/15	2,20,000	
	Neptune: 29,400 × 100/15		1,96,000

(2) **Balance Sheet of Jupiter Ltd.**

As at 31st March 2021 (after amalgamation)

Particulars	Note No	₹
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Share Capital	1	3,00,000
(b) Reserves and Surplus	2	64,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	4,16,000
(3) Current Liabilities		
(a) Other current liabilities		7,33,900
Total		15,13,900
II. Assets		
(1) Non-current assets		
(a) Fixed assets		11,00,000
(2) Current assets		
(a) Other current assets		4,13,900
Total		**15,13,900**

Notes to Accounts

1	Share Capital	
	Authorized	
	80,000 Equity Shares of ₹ 5 each	4,00,000
	Issued and Subscribed	
	60,000 Equity Shares of ₹ 5 each	3,00,000
	(all the above shares are allotted as fully paid-up pursuant to a contract without payment being received in cash)	

2	Reserve and Surplus	
	Capital Reserve	64,000
3	Long-term borrowings	
	Secured Loans	
	15% Debentures	4,16,000

Working Notes:

			Sun ₹	Neptune ₹	Total ₹
(1)		Purchase Consideration			
		Equity Shares Issued	1,37,500	1,62,500	3,00,000
		15% Debentures Issued	2,20,000	1,96,000	4,16,000
			3,57,500	3,58,500	7,16,000
(2)	(a)	Capital Reserve Net Assets taken over			
		Fixed Assets	7,10,000	3,90,000	11,00,000
		Current Assets	2,99,500	1,14,400*	4,13,900
			10,09,500	5,04,400	15,13,900
		Less: Current Liabilities	(5,53,650**)	(1,80,250)	(7,33,900)
			4,55,850	3,24,150	7,80,000
	(b)	Purchase Consideration	3,57,500	3,58,500	7,16,000
	(c)	Capital Reserve [(a) - (b)]	98,350		
	(d)	Goodwill [(b) - (a)]		34,350	
	(e)	Capital Reserve [Final Figure(c) -(d)]			64,000

* 1,57,750–43,350= 1,14,400

** 5,97,000–43,350= 5,53,650

(b) Pooling of Interest Method

Under pooling of interests method, the assets, liabilities and reserves of the Transferor Company will be taken over by Transferee Company at existing carrying amounts unless any adjustment is required due to different accounting policies followed by these companies. As a result the difference between the amount recorded as share capital issued (plus any additional consideration in the form of cash or other assets) and the amount of share capital of Transferor Company should be adjusted in reserves.

Purchase Method

The assets and liabilities of the transferor company should be incorporated at their existing carrying amounts or the purchase consideration should be allocated to individual identifiable assets and liabilities on the basis of their fair values at the date of amalgamation. No reserves, other than statutory reserves, of the transferor company should be incorporated in the financial statements of transferee company.

Q-19 The summarized Balance Sheets of Black Limited and White Limited as on 31st March, 2020 is as follows:

Particulars	Notes (₹ In 000)	Black Limited	White Limited (₹ In 000)
Equity and Liabilities			
Shareholders' Funds			
(a) Share Capital	1	6,000	3,600
(b) Reserves and Surplus	2	1,080	660
Current Liabilities			
Trade payables		600	360
Total	7,680	4,620	
Assets			
Non-current assets			
Property, Plant and Equipment		3,600	2,400
Current assets			
(a) Inventories		960	720
(b) Trade receivables		1,680	1,080
(c) Cash and Cash Equivalents		1,440	420
Total		7,680	4,620

Note No.	Particulars	Black Limited (₹ in 000)	White Limited (₹ in 000)
1.	Share CapitalEquity Shares of ₹ 100 each	6,000	3,600
2.	Reserves and Surplus		
	General Reserve	360	180
	Profit and Loss Account	720	480
	Total	1,080	660

Black Limited takes over White Limited on 1st July, 2020.

No Balance Sheet of White Limited is available as on that date. It is, however estimated that White Limited earned profit of ₹ 2,40,000 after charging proportionate depreciation @ 10% p.a. on Property Plant and Equipment, during April-June, 2020.

Estimated profit of Black Limited during these 3 months was ₹ 4,80,000 after charging proportionate depreciation @ 10% p.a. on Property Plant and Equipment.

Both the companies have declared and paid 10% dividend within this 3 months' period.

Goodwill of White Limited is valued at ₹ 2,40,000 and Property Plant and Equipment are valued at ₹ 1,20,000 above the depreciated book value on the date of takeover.

Purchase consideration is to be satisfied by Black Limited by issuing shares at par.

Ignore income tax. You are required to:

(i) Compute No. of shares to be issued by Black Limited to White Limited against purchase consideration.

(ii) Calculate the balance of Net Current Assets of Black Limited and White Limited as on 1st July, 2020.

(iii) Give balance of Profit or Loss of Black Limited as on 1st July, 2020

(iv) Give balance of Property Plant and Equipment as on 1st July, 2020 after takeover.

Ans.(i) No. of shares issued by Black Ltd. to White Ltd. against purchase consideration

White Ltd.		₹	₹
Goodwill			2,40,000
Property, plant and equipment		24,00,000	
Less: Depreciation [24,00,000 **x** 10 % **x** 3/12]		(60,000)	
		23,40,000	
Add: Appreciation		1,20,000	24,60,000
Inventory			7,20,000
Trade receivables			10,80,000
Cash and Bank balances		4,20,000	
Add: Profit after depreciation	2,40,000		
Add: Depreciation (non-cash)	60,000	3,00,000	
Less: Dividend [36,00,000 x 10%]		(3,60,000)	3,60,000
			48,60,000
Less: Trade payables			(3,60,000)
Purchase Consideration			45,00,000
Number of shares to be issued by Black Ltd. @ ₹ 100 each			45,000 shares

(ii) Calculation of Net Current Assets as on 01.07.2020

		Black Ltd.		**White Ltd.**
	₹	₹		₹
Current assets:				
Inventory		9,60,000		7,20,000
Trade receivables		16,80,000		10,80,000
Cash and Bank	14,40,000		4,20,000	
Less: Dividend	(6,00,000)		(3,60,000)	
Add: Profit after depreciation	4,80,000		2,40,000	
Add: Depreciation being non cash	90,000	14,10,000	60,000	3,60,000
		40,50,000		21,60,000
Less: Trade payables		(6,00,000)		(3,60,000)
		34,50,000		18,00,000

(iii) Profit and Loss Account balance of Black Ltd. as on 1.07.2020

	₹
P & L A/c balance as on 31.03.2020	7,20,000
Less: Dividend paid	(6,00,000)

		1,20,000
Add: Estimated profit for 3 months after charging depreciation		4,80,000
		6,00,000

(iv) Property, plant and equipment as on 01.07.2020

Property, plant and equipment of Black Ltd. as on 31.03.2020		36,00,000
Less: Depreciation for 3 months [36,00,000 x 10% x 3/12]		(90,000)
		35,10,000
Property, plant and equipment of White Ltd.		
Taken over as on 31.03.2020	24,00,000	
Less: Proportionate depreciation for 3 months on fixed assets	(60,000)	
	23,40,000	
Add: Appreciation above the estimated book value	1,20,000	24,60,000
Total Property, plant and equipment as on 1.7.2020		59,70,000

Q-20 Galaxy Ltd. and Glory Ltd., are two companies engaged in the same business of chemicals. To mitigate competition, a new company Glorious Ltd, is to be formed to which the assets and liabilities of the existing companies, with certain exception, are to be transferred. The summarized Balance Sheet of Galaxy Ltd. and Glory Ltd. as at 31st March, 2020 are as follows:

	Galaxy Ltd. ₹	Glory Ltd. ₹
(I) Equity & Liabilities		
(1) Shareholders' fund		
Share Capital		
Equity shares of ₹ 10 each	8,40,000	4,55,000
Reserves & Surplus		
General Reserve	4,48,000	40,000
Profit & Loss A/c	1,12,000	72,000
(2) Non-current Liabilities		
Secured Loan		
6% Debentures	-	3,30,000
(3) Current Liabilities		
Trade Payables	4,20,000	1,83,000
Total	18,20,000	10,80,000
(II) Assets		
(1) Non-current assets		
Property, Plant & Equipment		
Freehold property, at cost	5,88,000	3,36,000
Plant & Machinery, at cost less depreciation	1,40,000	84,000
Motor vehicles, at cost less depreciation	56,000	-

(2)	**Current Assets**		
	Inventories	3,36,000	4,38,000
	Trade Receivables	4,62,000	1,18,000
	Cash at Bank	2,38,000	1,04,000
	Total	18,20,000	10,80,000

Assets and Liabilities are to be taken at book value, with the following exceptions:

(i) The Debentures of Glory Ltd. are to be discharged, by the issue of 8% Debentures of Glorious Ltd. at a premium of 10%.

(ii) Plant and Machinery of Galaxy Ltd. are to be valued at ₹ 2,52,000.

(iii) Goodwill is to be valued at:
Galaxy Ltd. ₹ 4,48,000
Glory Ltd. ₹ 1,68,000

(iv) Liquidator of Glory Ltd. is appointed for collection from trade debtors and payment to trade creditors. He retained the cash balance and collected ₹ 1,10,000 from debtors and paid ₹ 1,80,000 to trade creditors. Liquidator is entitled to receive 5% commission for collection and 2.5% for payments. The balance cash will be taken over by new company.

You are required to:

(1) Compute the number of shares to be issued to the shareholders of Galaxy Ltd. and Glory Ltd, assuming the nominal value of each share in Glorious Ltd. is ₹ 10.

(2) Prepare Balance Sheet of Glorious Ltd., as on 1st April, 2020 and also prepare notes to the accounts as per Schedule III of the Companies Act, 2013. **[Sugg.-Jan'21] (20 Marks)**

Ans. (i) Calculation of Purchase consideration (or basis for issue of shares of Glorious Ltd.

Purchase Consideration:	**Galaxy Ltd.** ₹	**Glory Ltd.** ₹
Goodwill	4,48,000	1,68,000
Freehold property	5,88,000	3,36,000
Plant and Machinery	2,52,000	84,000
Motor vehicles	56,000	-
Inventory	3,36,000	4,38,000
Trade receivables	4,62,000	-
Cash at Bank	2,38,000	24,000
	23,80,000	10,50,000
Less: Liabilities:		
6% Debentures (3,00,000 x 110%)	-	(3,30,000)
Trade payables	(4,20,000)	
Net Assets taken over	19,60,000	7,20,000
To be satisfied by issue of shares of Glorious. Ltd. @ ₹ 10 each	1,96,000	72,000

(ii) Balance Sheet of Glorious Ltd. as at 1st April, 2020

Particulars				Note No	Amount ₹
			EQUITY AND LIABILITIES		
1			Shareholders' funds		
	(a)		Share capital	1	26,80,000
	(b)		Reserves and surplus	2	30,000
2			Non-current liabilities		
	(a)		Long-term borrowings	3	3,00,000
3	(a)		Current liabilities Trade payables		4,20,000
			Total		34,30,000
ASSETS					
1	(a)	i	Non-current assets Property, plant and equipment	4	13,16,000
		ii	Intangible assets	5	6,16,000
2			Current assets		
	(a)		Inventories	6	7,74,000
	(b)		Trade receivables		4,62,000
	(c)		Cash and cash equivalents	7	2,62,000
			Total		34,30,000

Notes to accounts:

	₹	₹
1. Share Capital		
Equity share capital		
2,68,000 shares of ₹ 10 each		26,80,000
(All the above shares are issued for consideration other than cash)		
2. Reserves and surplus		
Securities Premium		
(10% premium on debentures of ₹ 3,00,000)		30,000
3. Long-term borrowings		
Secured		
8% 3,000 Debentures of ₹ 100 each		3,00,000
4. Property Plant and Equipment		
Freehold property		
Galaxy Ltd.	5,88,000	
Glory Ltd.	3,36,000	9,24,000
Plant and Machinery		
Galaxy Ltd.	2,52,000	
Glory Ltd.	84,000	3,36,000
Motor vehicles - Galaxy Ltd.		56,000
		13,16,000

5	Intangible assets		
	Goodwill		
	Galaxy Ltd.	4,48,000	
	Glory Ltd.	1,68,000	6,16,000
6	Inventories		
	Galaxy Ltd.	3,36,000	
	Glory Ltd.	4,38,000	7,74,000
7	Cash and cash equivalents		
	Galaxy Ltd.	2,38,000	
	Glory Ltd.(As per working note)	24,000	2,62,000

Working note:

Calculation of cash balance of Glory Limited to be taken over by Glorious Limited

	₹
Cash balance as at 31st March,2020	1,04,000
Add: Received from debtors	1,10,000
	2,14,000
Less: paid to creditors	(1,80,000)
	34,000
Less: Commission to liquidators	
On Debtors @ 5% 5,500	
On Creditors @ 2.5% 4,500	(10,000)
	24,000

Note:

1. It is assumed that the nominal value of debentures of Glory Ltd. is ₹ 100 each.
2. As per the information given in the question, debentures of Glory Ltd. are to be discharged by the issue of debentures of Glorious Ltd. at premium of 10%. It is assumed in the above solution that the debentures are issued at premium of ₹ 10 for discharge of debentures of ₹ 3,30,000. Alternative answer considering other reasonable assumption is also possible.

Q-21 High Ltd. and Low Ltd. were amalgamated on and from, 1st April, 2020. A new companyLittle Ltd. was formed to take over the business of the existing Companies. The summarized Balance sheets of High Ltd. and Low Ltd. as on 31st March, 2020 are as under:

(₹ in Lakhs)

Liabilities	**High Ltd.**	**Low Ltd.**	**Assets**	**High Ltd.**	**Low Ltd.**
Share Capital:			Property, Plant and Equipment:		
Equity Shares of ₹ 100 each	1000	850	Land & Building	670	385
14% Pref Shares of ₹ 100 each	320	175	Plant & Machinery	475	355
Reserves & Surplus:			Investments	95	80
Revaluation Reserve	225	110	Current Assets:		

General Reserve	360	240	Stock	415	389
Investment Allowance Reserve	80	40	Sundry Debtors	322	213
P & L Account	85	82	Bills Receivables	35	-
Non-Current Liabilities:			Cash & Bank	303	166
Secured Loans:					
13% Debentures (` 100 each)	100	56			
Unsecured Loans (Public Deposits)	50	-			
Current Liabilities & Provisions:		-			
Sundry Creditors	65	35			
Bills Payable	30	-			
TOTAL	**2315**	**1588**	**TOTAL**	**2315**	**1588**

Other Information :

(1) 13% Debenture holders of High Ltd. & Low Ltd. are discharged by Little Ltd. by issuing such number of its 15% Debentures of ₹ 100 each so as to maintain the same amount of interest.

(2) Preference Shareholders of the two companies are issued equivalent number of 15% Preference shares of Little Ltd. at a price of ₹ 125 per share (Face Value ₹ 100)

(3) Little Ltd. will issue 4 Equity Shares for each Equity Share of High Ltd. & 3 equity shares for each Equity Share of Low Ltd. The shares are to be issued at ₹ 35 each having a face value of ₹ 10 per share.

(4) Investment Allowance Reserve is to be maintained for two more years.

Prepare the Balance sheet of Little Ltd. as on 1st April, 2020 after the amalgamation has been carried out in basis of in the nature of Purchase. **[Sugg-Nov'20](15 Marks)**

Ans. **Balance Sheet of Little Ltd. as at 1st April, 2020**

Particulars			**Note No.**	**(₹ in lakhs)**
I.	Equity and Liabilities			
	(1)	Shareholder's Funds		
		(a) Share Capital	1	1,150.0
		(b) Reserves and Surplus	2	2,437.8
	(2)	Non-Current Liabilities		
		Long-term borrowings	3	135.2
		Other Borrowings- Unsecured Loans		
	(3)	Current Liabilities		50
		Trade payables	4	130.0
		Total		3,903

II. Assets

(1)	Non-current assets		
	(a) Property, Plant and Equipment	5	1,885
	(b) Non-current investment (95 + 80)		175
(2)	Current assets		
	(a) Inventory (415+389)		804
	(b) Trade receivables	6	570
	(c) Cash and bank balances (303 + 166)		469
Total			3,903

Notes to Accounts

			(₹ in lakhs)	(₹ in lakhs)
1.	**Share Capital**			
	Equity share capital (W.N.1)			
	65,50,0001 Equity shares of 10 each		655	
	4,95,0002 Preference shares of ₹ 100 each		495	
	(all the above shares are allotted as fully paid-up pursuant to contracts without payment being received in cash)		_____	1,150
2.	**Reserves and surplus**			
	Securities Premium Account (W.N.3) (1080+ 681.25)		1,761.25	
	Capital Reserve (W.N. 2)(283.33 + 393.22)		676.55	
	Investment Allowance Reserve (80 + 40)		120	2,437.8
	Amalgamation Adjustment Reserve (80 + 40) (120)			
3.	**Long-term borrowings**			
	15% Debentures			**135.2**
4.	**Trade payables**			
	Sundry Creditors: High Ltd.		**65**	
	Low Ltd.Bills			
	Payable: High Ltd.		3530	130
5.	Property, Plant and Equipment			
	Land and Building : High Ltd	670		
	Low Ltd	385	1055	
	Plant and Machinery: High Ltd.	475		
	Low Ltd.	355	830	1,885
6.	Trade receivables			
	Sundry Debtors: High Ltd.		322	
	Low Ltd.Bills		213	
	Receivables: High Ltd.		35	570

Working Notes:

(₹ in lakhs)

		High Ltd.		Low Ltd.
(1) Computation of Purchase consideration				
(a) Preference shareholders:				
$\left(\frac{3,20,00,000}{100} \text{ i.e. } 3,20,000 \text{ shares}\right)$		400		
x ` 125 each				
$\left(\frac{1,75,00,000}{100} \text{ i.e. } 1,75,000 \text{ shares}\right)$			218.75	
(b) Equity shareholder:				
$\left(\frac{10,00,00,000 \times 4}{100} \text{ i.e. } 4,00,000 \text{ shares}\right)$		1,400		
x ` 35 each				
$\left(\frac{8,50,00,000 \times 3}{100} \text{ i.e. } 25,50,000 \text{ shares}\right)$		———		892.50
Amount of Purchase Consideration		1,800		1,111,25
(2) Computation of Capital Reserve				
Assets taken over:				
Land and Building		670		385
Plant and Machinery		475		355
Investments		95		80
Inventory		415		389
Trade receivables		322		213
Bills Receivables		35		
Cash and bank		303		166
		2,315		1,588
Less: Liabilities taken over:				
Debentures	86.67			48.53
Unsecured Loan	50			
Creditors	65			
Bills Payable	30			35
		231.67		83.53
Net assets taken over		2083.33		1,504.47
Purchase consideration		1,800		1,111.25
Capital reserve		283.33		393.22

(3) Computation of securities premium		
On preference share capital		
High Ltd.- 3,20,000 x 25	80	
Low Ltd.- 1,75,000 x 25		43.75
On equity share capital		
High Ltd.- 40,00,000 x 25	1000	
Low Ltd.- 25,50,000 x 25	____	637.5
Total	1080	681.25

(4) Issue of Debentures (` In Lakhs)

High Ltd.- 15% fresh issue of debenture for 13% old debentures = 100 X 13% / 15% = 86.67(rounded off)

Low Ltd.- 15% fresh issue of debenture for 13% old debentures = 56 X 13% /15% = 48.53 (rounded off)

Total number of debentures issued = 86.67 + 48.53 = 135.20 Lakhs

Q-22 Mohan Ltd. gives you the following information as on 31st March, 2020:

	(₹)
Share capital:	
Equity shares of ₹ 10 each	3,00,000
6,000, 9% cumulative preference shares of ₹ 10 each	60,000
Profit and Loss Account (Dr. balance)	1,70,000
10% Debentures of ₹ 100 each	2,00,000
Interest payable on Debentures	20,000
Trade Payables	1,50,000
Property, Plant and Equipment	3,40,000
Goodwill	10,000
Inventory	80,000
Trade Receivables	1,10,000
Bank Balance	20,000

A new company Ravi Ltd. is formed with authorised share capital of ₹ 4,00,000 divided into 40,000 Equity Shares of ₹ 10 each. The new company will acquire the assets and liabilities of Mohan Ltd. on the following terms:

(i) (a) Mohan Ltd.'s debentures are paid by similar debentures in new company and for outstanding accrued interest on debentures, equity shares of equal amount are issued at par.

(b) The trade payables are paid by issue of 12,000 equity shares at par in full and final settlement of their claims.

(c) Preference shareholders are to get equal number of equity shares issued at par. Dividend on preference shares is in arrears for three years. Preference shareholders to forgo dividend for two years. For balance dividend, equity shares of equal amount are issued at par.

(d) Equity shareholders are issued one share at par for every three shares held in Mohan Ltd.

(ii) Current Assets are to be taken at book value (except inventory, which is to be reduced by 10%). Goodwill is to be eliminated. The Property, plant and equipment is taken over at ₹ 3,08,400.

(iii) Remaining equity shares of the new company are issued to public at par fully paid up.

(iv) Expenses of ₹ 5,000 to be met from bank balance of Mohan Ltd. This is to be adjusted from the bank balance of Mohan Ltd. before acquisition by Ravi Ltd.

You are required to prepare:

(a) Realisation account and Equity Shareholders' account in the books of Mohan Ltd.

(b) Bank Account and Balance Sheet with notes to accounts in the books of Ravi Ltd.

Ans. **In the books of Mohan Ltd.**

(i) **Realisation Account**

	₹		₹
To Goodwill	10,000	By 10% Debentures	2,00,000
To Property, plant and equipment	3,40,000	By Interest accrued on debentures	20,000
To Inventory	80,000	By Trade payables	1,50,000
To Trade receivables	1,10,000	By Ravi Ltd. (Purchase consideration) (W.N. 1)	1,65,400
To Bank (20,000 - 5,000)	15,000	By Equity shareholders A/c (loss on realization) (Bal. fig.)	25,000
To Preference share holders A/c (W.N.2)	5,400		
	5,60,400		**5,60,400**

(ii) **Equity shareholders' Account**

	₹		₹
To Profit & loss A/c	1,70,000	By Equity Share capital	3,00,000
To Expenses* 5,000			
To Equity shares in Ravi Ltd.	1,00,000		
To Realization A/c	25,000		
	3,00,000		**3,00,000**

*Alternatively, expenses may be routed through Realization account.

In the books of Ravi Ltd.

(i) **Bank Account**

	₹		₹
To Business Purchase	15,000	By Balance c/d (Bal. fig.)	1,09,600
To Equity shares application & allotment A/c (W.N. 3)	94,600		
	1,09,600		**1,09,600**

(ii) **Balance Sheet as at 31st March, 2020**

Particulars	Note No.	₹
I. Equity and Liabilities		
(1) Shareholder's Funds		
Share Capital	1	4,00,000
(2) Non-Current Liabilities		
Long-term borrowings	2	2,00,000
Total		6,00,000
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment		3,08,400
(2) Current assets		
(a) Inventories		72,000
(b) Trade receivables		1,10,000
(c) Cash and cash equivalents		1,09,600
Total		6,00,000

Notes to Accounts

	₹
1. Share Capital	
Authorised share capital	
40,000 equity shares of ₹ 10 each	4,00,000
Issued and Subscribed	
40,000 shares of ₹ 10 each fully paid up	4,00,000
(out of the above, 30,540 (W.N.3) shares have been allotted as fully paid-up pursuant to contract without payment being received in cash)	
2. **Long Term Borrowings**	
10% Debentures	2,00,000

Working Notes:

1. Calculation of Purchase consideration

	₹
Payment to preference shareholders	
6,000 equity shares @ ₹ 10	60,000
For arrears of dividend: (6,000 x ₹ 10) x 9%	5,400
Payment to equity shareholders	
(30,000 shares x 1/3) @ ₹ 10	1,00,000
Total purchase consideration	1,65,400

2. Preference shareholders' Account in books of Mohan Ltd.

	₹		₹
To Equity Shares in Ravi Ltd.	65,400	By Preference Share capital	60,000
		By Realization A/c (Bal. fig.)	5,400
	65,400		**65,400**

3. Calculation of number of Equity shares issued to public

		Number of shares
Authorized equity shares		40,000
Less: Equity shares issued for		
Interest accrued on debentures	2,000	
Trade payables of Mohan Ltd.	12,000	
Preference shareholders of Mohan Ltd.	6,000	
Arrears of preference dividend	540	
Equity shareholders of Mohan Ltd.	10,000	(30,540)
Number of equity shares issued to public at par for cash		9,460

Q-23 Heera Ltd. and Rita Ltd. agreed to amalgamate their business. The scheme envisaged a share capital, equal to the combined capital of Heera Ltd. and Rita Ltd. for the purpose of acquiring the assets, liabilities and undertakings of the two companies in exchange for share in HR Ltd.

Heera Ltd. and Rita Ltd. make available the following information as on 31st March, 2021 (the date of amalgamation):

	Heera Ltd. ₹	Rita Ltd. ₹
Property, plant and Equipment	7,20,000	10,80,000
Inventories	3,60,000	6,60,000
Trade receivables	4,80,000	7,80,000
Cash at Bank	3,00,000	-
Share Capital	6,00,000	8,40,000
Reserves	10,20,000	6,00,000
Bank Overdraft	-	5,40,000
Trade payables	2,40,000	5,40,000

The consideration was to be based on the net assets of the companies as shown above but subject to an additional payment to Heera Ltd. for its goodwill to be calculated as its weighted average of net profits for the three years ended 31st March, 2021. The weights for this purpose for the years 2018-19, 2019-20 and 2020-21 were agreed as 1, 2 and 3 respectively.

The profit had been:

2018-19 ₹ 3,00,000; 2019-20 ₹ 5,25,000 and 2020-21 ₹ 6,30,000.

The shares of HR Ltd. were to be issued to Heera Ltd. and Rita Ltd.at a premium and in proportion to the agreed net assets value of these companies.

In order to raise working capital, HR Ltd. proceeded to issue 72,000 shares of ₹ 10 each at the same rate of premium as issued for discharging purchase consideration to Heera Ltd. and Rita Ltd.

You are required to calculate the number of shares issued to Heera Ltd. and Rita Ltd. and prepare necessary journal entries in the books of HR Ltd.

Ans. Calculation of number of shares issued to Heera Ltd. and Rita Ltd.

Amount of Share Capital as per balance sheet	₹
Heera Ltd.	6,00,000
Rita Ltd.	8,40,000
	14,40,000

Share of Heera Ltd.	= ₹ 14,40,000 x [21,60,000/ (21,60,000 + 14,40,000)]
	= ₹ 8,64,000 or 86,400 shares
Securities premium	= ₹ 21,60,000 – ₹ 8,64,000 = ₹ 12,96,000
Premium per share	= ₹ 12,96,000 / ₹ 86,400 = ₹ 15
Issued 86,400 shares	@ ₹ 10 each at a premium of ₹ 15 per share
Share of Rita Ltd.	= ₹ 14,40,000 x [14,40,000/ (21,60,000 + 14,40,000)]
	= ₹ 5,76,000 or 57,600 shares
Securities premium	= ₹ 14,40,000 – ₹ 5,76,000 = ₹ 8,64,000
Premium per share	= ₹ 8,64,000 / ₹57,600 = ₹ 15
Issued 57,600 shares	@ ₹ 10 each at a premium of ₹ 15 per share

Journal Entries in the books of HR Ltd.

Particulars		Dr. Amount (₹)	Cr. Amount (₹)
Business purchase account	Dr.	36,00,000	
To Liquidator of Heera Ltd. account			21,60,000
To Liquidator of Rita Ltd. account			14,40,000
(Being the amount of purchase consideration payable to liquidator of Heera Ltd. and Rita ltd. for assets taken over)			
Goodwill	Dr.	5,40,000	
PPE account	Dr.	7,20,000	
Inventory account	Dr.	3,60,000	
Trade receivables account	Dr.	4,80,000	
Cash at bank	Dr.	3,00,000	
To Trade payables account			2,40,000
To Business purchase account			21,60,000
(Being assets and liabilities of Heera Ltd. taken over)			
PPE account	Dr.	10,80,000	
Inventory account	Dr.	6,60,000	
Trade receivables account	Dr.	7,80,000	
To bank overdraft account			5,40,000
To Trade payables account			5,40,000
To Business purchase account			14,40,000
(Being assets and liabilities of Rita Ltd. taken over)			
Liquidator of Heera Ltd. Account	Dr.	21,60,000	
To Equity share capital account (86,400 x ₹ 10)			8,64,000
To Securities premium (86,400 x ₹ 15)			12,96,000
(Being the allotment of shares as per agreement for discharge of purchase consideration)			

Liquidator of Rita Ltd. account	Dr.	14,40,000	
To Equity share capital account (57,600 x ₹ 10)			5,76,000
To Securities premium (57,600 x ₹ 15)			8,64,000
(Being the allotment of shares as per agreement for discharge of purchase consideration)			
Bank A/c		18,00,000	
To Equity share capital account (72,000 x ₹10)			7,20,000
To Securities premium (72,000 x ₹ 15)			
(Equity share capital issued to raise working capital)			10,80,000

Working Notes:

1. Calculation of goodwill of Heera Ltd.

Particulars	Amount ₹	Weight	Weighted amount ₹
2018-19	3,00,000	1	3,00,000
2019-20	5,25,000	2	10,50,000
2020-21	6,30,000	3	18,90,000
Total (a+b+c)	14,55,000	6	32,40,000
weighted Average = [Total weighted amount/Total of weight] [₹ 32,40,000/6]			
Goodwill			5,40,000

2. Calculation of Net assets

	Heera Ltd. ₹	Rita Ltd. ₹
Assets		
Goodwill	5,40,000	
PPE	7,20,000	10,80,000
Inventory	3,60,000	6,60,000
Trade receivable	4,80,000	7,80,000
Cash at bank	3,00,000	
Less: Liabilities		
Bank overdraft		5,40,000
Trade payables	2,40,000	5,40,000
Net assets or Purchase consideration	21,60,000	14,40,000

Q-24 A Ltd. had acquired 80% shares of B Ltd. for ₹ 15 lakhs at the beginning of year. During the year, A Ltd. sold the investment for ₹ 30 lakhs and net assets of B Ltd. on the date of disposal was ₹ 35 lakhs. Calculate the profit or loss on disposal of this investment to be recognized in the Financial Statements of A Ltd.

Ans. **Calculation of Profit/Loss on disposal of investment in subsidiary**

Particulars	₹
Proceeds from the sale of Investment	30,00,000
Less: A Ltd.'s share in net assets of B Ltd.	**(28,00,000)**
	2,00,000

Working Note:

A Ltd.'s share in net assets of B Ltd.

	₹
Net Assets of B Ltd. on the date of disposal	35,00,000
Less: Minority Interest (20% of ₹ 35 lakhs)	(7,00,000)
A Ltd.'s share in the net assets of B Ltd.	28,00,000

Q-25 The following are the Balance Sheets of Aakash Limited and Ganga Limited as at March 31, 2021:

Particulars	**NoteNo.**	**Aakash Limited(₹)**	**Ganga Limited(₹)**
I. Equity and Liabilities:			
(1) Shareholder's Funds:			
(a) Share Capital	1	80,00,000	20,00,000
(b) Reserves and Surplus	2	(3,24,00,000)	56,00,000
(2) Non-Current Liabilities:			
(a) Secured Loans	3	3,20,00,000	1,60,00,000
(b) Unsecured Loans	4	1,72,00,000	-
(3) Current Liabilities:			
(a) Trade Payables		56,00,000	36,00,000
(b) Other Current Liabilities Total	5	2,04,00,000	56,00,000
Total		5,08,00,000	3,28,00,000
II. Assets:			
(1) Non-Current Assets:			
Property, Plant & Equipment		68,00,000	1,36,00,000
(2) Current Assets:			
(a) Inventories		3,68,00,000	-
(b) Other Current Assets		72,00,000	1,92,00,000
Total		5,08,00,000	3,28,00,000

Notes to Accounts:

	AakashLimited (₹)	Ganga Limited(₹)
1. Share Capital		
Authorized, Issued, Subscribed & Paid up :		
6,00,000 Equity Shares of ₹10 each	60,00,000	-
20,000 Preference Shares of ₹ 100 each	20,00,000	-
2,00,000 Equity Shares of ₹ 10 each	-	20,00,000
	80,00,000	20,00,000

2.	Reserves and Surplus		
	General Reserve	8,00,000	56,00,000
	Surplus	(3,32,00,000)	-
		(3,24,00,000)	56,00,000
3.	Secured Loans		
	(Secured Loans of Aakash Limited aresecured against pledge of Inventories)	3,20,00,000	1,60,00,000
4.	Unsecured Loans	1,72,00,000	-
5.	Other Current Liabilities		
	Statutory Liabilities	1,44,00,000	20,00,000
	Liability to Employees	60,00,000	36,00,000
		2,04,00,000	56,00,000

Both the companies go into liquidation and a new company 'AakashGanga Limited' is formed to take over their business. The following information is given:

(i) All Current Assets of two companies, except pledged inventory are taken over byAakash Ganga Limited. The realizable value of all the Current Assets (including pledged inventory) is 80% of book value in case of Aakash Limited and 70% for Ganga Limited.

(ii) Property, Plant and Equipment of both the companies are taken over at book valueby AakashGanga Limited.

(iii) Secured Loans include ₹ 32,00,000 accured interest in case of Ganga Limited.

(iv) 4,00,000 Equity Shares of ₹ 10 each are allotted by AakashGanga Limited at par against cash payment of entire face value to the shareholders of Aakash Limited and Ganga Limited in the ratio of shares held by them in Aakash Limited and Ganga Limited.

(v) Preference Shareholders in Aakash Limited are issued Equity Shares inAakashGanga Ltd. worth '4,00,000 in lieu of their present holdings.

(vi) Secured Loan agree to continue the balance amount of their loans to AakashGanga Limited after adjusting realizable value of pledged asset in case of Aakash Limited and after waiving 50% of interest due in the case of Ganga Limited.

(vii) Unsecured Loans are taken over by AakashGanga Limited at 25% of loan amounts.

(viii) Employees are issued fully paid Equity Shares in AakashGanga Limited in full settlement of their dues.

(ix) Statutory Liabilities are taken over by AakashGanga Limited at full value and Trade Payables are taken over at 80% of the book value.

You are required to prepare the opening Balance Sheet of AakashGanga Limited as at 1.4.2021.

Ans. **Balance sheet of AakashGanga Ltd. as at 1st April, 2021**

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) **Shareholders' Funds**		
(a) Share Capital	1	1,40,00,000
(2) **Non-Current Liabilities**		
(a) Long term borrowings	2	2,12,60,000
(3) **Current Liabilities**		
(a) Trade Payables	3	73,60,000
(b) Other current liabilities	**4**	1,64,00,000
Total		5,90,20,000

II.	**Assets**			
	(1) **Non-current assets**			
	(a) Property, Plant & Equipment		5	2,04,00,000
	(b) Intangible assets		**6**	1,54,20,000
	(2) **Current assets**			
	(a) Cash and cash equivalents			40,00,000
	(b) Other current assets		7	1,92,00,000
		Total		5,90,20,000

Notes to Accounts

				(₹)
1.	Share Capital			
	Issued, subscribed & Paid up:			
	14,00,000 equity shares of ₹ 10 each, fully paid up (W.N.4)			1,40,00,000
	(of the above 10,00,000 shares have been issued forconsideration other than cash)			
2.	Long Term borrowings			
	Secured Loans			
	Aakash Limited	25,60,000		
	Ganga Limited	1,44,00,000	1,69,60,000	
	Unsecured Loans		43,00,000	2,12,60,000
3.	Trade Payables (W.N.1)			
	Aakash Limited		44,80,000	
	Ganga Limited		28,80,000	73,60,000
4.	Other current liabilities			
	Statutory Liabilities			
	Aakash Limited		1,44,00,000	
	Ganga Limited		20,00,000	1,64,00,000
5.	Property, Plant & Equipment			
	Aakash Limited		68,00,000	
	Ganga Limited		1,36,00,000	2,04,00,000
6.	Intangible assets			
	Goodwill (W.N.3)			1,54,20,000
7.	Other Current Assets			
	Aakash Limited		57,60,000	
	Ganga Limited		1,34,40,000	1,92,00,000

Working Notes:

1. Value of total liabilities taken over by AakashGanga Ltd. (₹)

	Aakash Limited		**Ganga Limited**	
Current liabilities				
Statutory liabilities	1,44,00,000		20,00,000	
Liability to employees	60,00,000		36,00,000	
Trade payables @ 80%	44,80,000	2,48,80,000	28,80,000	84,80,000
Secured loans				
Given in Balance Sheet	3,20,00,000		1,60,00,000	

Interest waived	-		16,00,000	1,44,00,000
Value of Inventory				
(80% of' 3,68,00,000)	2,94,40,000	25,60,000		
Unsecured Loans				
(25% of'1,72,00,000)		43,00,000		-
		3,17,40,000		2,28,80,000

2. Assets taken over by AakashGanga Ltd. (₹)

	Aakash Limited	Ganga Limited
	₹	₹
Property, Plant & Equipment	68,00,000	1,36,00,000
Current Assets		
(80% and 70% respectively of book value)	57,60,000	1,34,40,000
	1,25,60,000	2,70,40,000

3. Goodwill / Capital Reserve on amalgamation (₹)

Liabilities taken over (W.N. 1)			
Equity shares to be issued to Preference		3,17,40,000	2,28,80,000
Shareholders		4,00,000	-
	A	3,21,40,000	2,28,80,000
Less: Total assets taken over (W.N. 2)	B	(1,25,60,000)	(2,70,40,000)
	A-B	1,95,80,000	(41,60,000)
		Goodwill	Capital Reserve
Net Goodwill (1,95,80,000- 41,60,000)		1,54,20,000	

4. Equity shares issued by AakashGanga Ltd.

(i)	For Cash		40,00,000
	For consideration other than cash		
(ii)	In Discharge of Liabilities to Employees	96,00,000	
(iii)	To Preference shareholders	4,00,000	1,00,00,000
			1,40,00,000
	No. of shares @ ₹ 10		14,00,00

Q-26 Dark Ltd. and Fair Ltd. were amalgamated on and from 1st April, 2021. A new company Bright Ltd. was formed to take over the business of the existing companies. The balance Sheets of Dark Ltd. and Fair Ltd. as at 31st March, 2021 are given below:

(₹ In Lakhs)

	Particulars	**Note No.**	**Dark Ltd.**	**Fair Ltd.**
1	Equity and Liabilities			
	(1) Shareholders' Funds			
	(a) Share Capital	1	1,650	1,425
	(b) Reserves and Surplus	2	630	495
	(2) Non-Current Liabilities			
	Long Term Borrowings:			
	10% Debentures of 100 ₹ each		90	45

	(3) Current Liabilities		
	Trade Payables	630	285
	Total	3,000	2,250
II	Assets		
	(1) Non Current Assets		
	(a) Property, Plant and Equipment	1,350	975
	(b) Non Current Investments	225	75
	(2) Current Assets		
	(a) Inventories	525	375
	(b) Trade Receivables	450	525
	(c) Cash and Cash Equivalents	450	300
	Total	3,000	2,250

Notes to Accounts

		Dark Ltd. (₹ in Lakh)	Fair Ltd. (₹ in Lakh)
1	Share Capital		
	Equity Shares of ₹ 100 each	1, 200	1,125
	14% Preference Shares of ₹ 100 each	450	300
		1,650	1,425
2	Reserves and Surplus		
	Revaluation Reserve	225	150
	General Reserve	255	225
	Investment Allowance Reserve	75	75
	Profit and Loss Account	75	45
		630	**495**

Additional Information:

(i) Bright Limited will issue 5 equity shares for each equity share of Dark Limited and 4 equity shares for each equity share of Fair Limited. The shares are to be issued @ ₹ 35 each having a face value of ₹ 10 per share.

(ii) Preference shareholders of the two companies are issued equivalent number of 16% preference shares of Bright Limited at a price of ₹ 160 per share (face value ₹ 100).

(iii) 10% Debenture holders of Dark Limited and Fair Limited are discharged by Bright Limited, issuing such number of its 16% Debentures of ₹ 100 each so as to maintain the same amount of interest.

(iv) Investment allowance reserve is to be maintained for 4 more years.

(v) Liquidation expenses are for Dark Limited ₹ 6,00,000 and for Fair Limited ₹3,00,000. It is decided that these expenses would be borne by Bright Limited.

(vi) All the assets and liabilities of Dark Limited and Fair Limited are taken over at book value.

(vii) Authorized equity share capital of Bright Limited is ₹ 15,00,00,000 divided into equity share of ₹ 10 each. After issuing required number of shares to the liquidators of Dark Limited and Fair Limited, Bright Limited issued balance shares to public. The issue was fully subscribed.

You are required to prepare Balance Sheet of Bright Limited as at 1st April, 2021 after amalgamation has been carried out on the basis of Amalgamation in the nature of purchase.

Ans. **Balance Sheet of Bright Ltd. as at 1st April, 2021**

Particulars	Note No.	(₹ in lakhs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	2,250
(b) Reserves and Surplus	2	4,200
(2) Non-Current Liabilities		
Long-term borrowings	3	84.375
(3) Current Liabilities		
Trade payables	4	915
Total		7449.375
II. Assets		
(1) Non-current assets		
(a) i. Property, plant and equipment	5	2,325
ii. Intangible assets	6	633.375
(b) Non-current investments	7	300
(2) Current assets		
(a) Inventories	8	900
(b) Trade receivables	9	975
(c) Cash and cash equivalents	10	2316
Total		7449.375

Notes to Accounts

			(₹ in lakhs)	(₹ in lakhs)
1.	Share Capital			
	Authorized Share Capital			
	1,50,00,000 Equity shares of ₹10 each		1500	
	7,50,000 16% Preference Share of 100 each		750	
	Issued: 1,50,00,000 Equity shares of ₹ 10 each		1500	
	(Out of which 1,05,00,000 Shares were Issued for consideration other than cash)			
	7,50,000 16% Preference Shares of 100 each (Issued for consideration other than cash)		750	2,250
2.	Reserves and surplus			
	Securities Premium Account			
	(1,50,00,000 shares × ₹ 25)	3750		
	(7,50,000 shares × ₹ 60)	450	4,200	
	Investment Allowance Reserve		150	
	Amalgamation Adjustment Reserve		(150)	4,200
3.	Long-term borrowings			
	16% Debentures (56,25,000+28,12,500) (W.N. 3)			84.375

4.	Trade payables			
	Dark Ltd.		630	
	Fair Ltd.		285	915
5.	Property, plant & equipment			
	Land and Building		1350	
	Plant and Machinery		975	2,325
6.	Intangible assets			
	Goodwill [W.N. 2]	624.375		
	Add: liquidation exp. (6+3)	9.00		633.375
7.	Non-current Investments			
	Investments (225+75)			300
8.	Inventories			
	Dark Ltd.		525	
	Fair Ltd.		375	900
9	Trade receivables			
	Dark Ltd.		450	
	Fair Ltd.		525	975
10	Cash & cash equivalents			
	Dark Ltd.		450	
	Fair Ltd.		300	
	Liquidation Expenses (6+3)		(9)	
	Shares issued for cash (45 lakh shares x ₹35)		1575	2316

Working Notes:

			(₹ in lakhs)
		Dark Ltd.	**Fair Ltd.**
(1)	Computation of Purchase consideration		
	(a) Preference shareholders:		
	$\left(\frac{4,50,00,000}{100}\right)$		
	i.e. 4,50,000 shares × ₹ 160 each	720	
	$\left(\frac{3,00,00,000}{100}\right)$		
	i.e. 3,00,000 shares × ₹ 160 each		480
(b)	Equity shareholders:		
	$\left(\frac{12,00,00,000 \times 5}{100}\right)$		
	i.e. 60,00,000 shares x ₹ 35 each	2,100	
	$\left(\frac{11,25,00,000 \times 4}{100}\right)$		
	i.e. 45,00,000 shares × ₹ 35 each		1,575
	Amount of Purchase Consideration	**2,820**	**2,055**

(2) Net Assets Taken Over

Assets taken over:		
Property Plant & Equity	1,350	975
Non-Current Investments	225	75
Inventory	525	375
Trade receivables	450	525
Cash and bank	450	300
	3,000	2,250
Less: Liabilities taken over:		
10% Debentures	56.25	28.125
Trade payables	630 (686.25)	285 (313.125)
Net assets taken over	2,313.75	1936.875
Purchase consideration	2,820	2055.00
Goodwill	506.25	118.125
Total goodwill		624.375

(3) Issue of Debentures

Debentures	₹ 90,00,000	₹ 45,00,000
Interest 10%	₹ 9,00,000	₹ 4,50,000

$\left(\frac{9,00,000 \times 100}{16}\right) = 56,25,000 \left(\frac{4,50,000 \times 100}{16}\right) = 28,12,500$

NOTE: In the above solution ‘ 35 has been considered as the issue price of Equity shares for public issue also. Alternative considering this as ₹10 also possible. In that case, the balance of cash and cash equivalents will be ₹ 1,191 lakhs and securities premium will be ₹ 3,075 lakhs in place of the balances given in the balance sheet in the above solution.

Q-27 Sulpher Ltd. and Diamond Ltd. give the following information as at 31.03.2022:

	Sulpher Ltd. (₹ in lakhs)	**Diamond Ltd. (₹ in lakhs)**
Equity Share Capital (Fully paid shares of ₹ 10 each)	22,500	9,000
Securities Premium	4,500	-
Foreign Project Reserve	-	465
General Reserve	14,250	4,800
Profit and Loss Account	4,305	1,162.5
12% Debentures	-	1,500
Trade payables	1,800	694.5
Provisions	2,745	1,053
Land and Buildings	9,000	-
Plant and Machinery	21,000	7,500
Furniture, Fixtures and Fittings	3,456	2,550
Inventory	11,793	6,061.5
Trade receivables	3,180	1,650
Cash at Bank	1,671	913.5

All the bills receivable held by Diamond Ltd. were Sulpher Ltd.'s acceptances.

On 1st April 2022, Sulpher Ltd. took over Diamond Ltd. in an amalgamation in the nature of merger.

It was agreed that in discharge of consideration for the business, Sulpher Ltd. would allot three fully paid equity shares of ' 10 each at par for every two shares held in Diamond Ltd. It was also agreed that 12% debentures in Diamond Ltd. would be converted into 13% debentures in Sulpher Ltd. of the same amount and denomination.

Details of trade receivables and trade payables are as under:

Particulars	**Sulpher Ltd.**	**Diamond Ltd.**
		(₹ in lakhs)
Trade Payables:		
Creditors	1,620	694.5
Bills Payable	180	-
	1,800	694.5
Trade receivables:		
Debtors	3,180	1,530
Bills Receivables	-	120
	3,180	1,650

Expenses of amalgamation amounting to ₹ 1.5 lakhs were borne by Sulpher Ltd.

You are required to:

(i) Pass journal entries in the books of Sulpher Ltd. and

(ii) Prepare Sulpher Ltd.'s Balance Sheet immediately after the merger.

Ans.

Books of Sulpher Ltd.

Journal Entries

		(₹ in Lacs)	**(₹ in Lacs)**
Business Purchase A/c	Dr.	13,500	
To Liquidator of Diamond Ltd.			13,500
(Being business of Diamond Ltd. taken over for consideration settled as per agreement)			
Plant and Machinery	Dr.	7,500	
Furniture & Fittings	Dr.	2,550	
Inventory	Dr.	6,061.5	
Debtors	Dr.	1,530	
Cash at Bank	Dr.	913.5	
Bills Receivable	Dr.	120	
To Foreign Project Reserve			465
To General Reserve ₹ (4,800 - 4,500)			300
To Profit and Loss A/c			1,162.5
To Liability for 12% Debentures			1,500
To Creditors			694.5

To Provisions			1,053
To Business Purchase A/c			13,500
(Being assets & liabilities taken over from Diamond Ltd.)			
Liquidator of Diamond Ltd. A/c	Dr.	13,500	
To Equity Share Capital A/c			13,500
(Purchase consideration discharged in the form of equity shares)			
Profit & Loss A/c	Dr.	1.5	
To Bank A/c			1.5
(Liquidation expenses paid and charged to P& L A/c)			
Liability for 12% Debentures A/c	Dr.	1,500	
To 13% Debentures A/c			1500
(12% debentures discharged by issue of 13% debentures)			
Bills Payable A/c	Dr.	120	
To Bills Receivable A/c			120
(Cancellation of mutual owing on account of bills)			

Balance Sheet of Sulpher Ltd. as at 1st April, 2022 (after merger)

		Particulars	**Notes**	**₹ (in lakhs)**
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	36,000
	B	Reserves and Surplus	2	24,981
2		Non-current liabilities		
	A	Long-term borrowings	3	1,500
3		Current liabilities		
	A	Trade Payables (1,800+694.5-120)		2,374.5
	B	Short-term provisions (2,745+1,053)		3,798
		Total		68,653.5
		Assets		
1		Non-current assets		
	A	Property, Plant & Equipment	4	43,506
2		Current assets		
	A	Inventories (11,793+6,061.5)		17,854.5
	B	Trade receivables (3,180+1,650-120)		4,710
	C	Cash and cash equivalents (1,671+913.5-1.5)		2,583
		Total		68,653.5

Notes to Accounts

		₹
1.	Share Capital	

	Equity share capital	
	Authorized, issued, subscribed and paid-up: 36 crores equity shares of ₹ 10 each (out of these shares, 13.5 crores shares have been issued for consideration other than cash)	36,000
2.	Reserves and Surplus	
	General Reserve	14,550
	Securities Premium	4,500
	Foreign Project Reserve	465
	Profit and Loss Account ₹ (4,305 +1,162.5-1.5)	5,466
	Total	24,981
3.	Long-term borrowings	
	Secured	
	13% Debentures	1,500
4.	PPE	
	Land & Buildings	9,000
	Plant & Machinery	28,500
	Furniture & Fittings	6,006
	Total	43,506

Working Note:

Computation of purchase consideration

Purchase consideration was discharged in the form of three equity shares of *Sulpher* Ltd. for every two equity shares held in *Diamond* Ltd.

Purchase consideration = ₹ 9,000 lacs × 3/2 = ₹ 13,500 lacs

Q-28 Minda Financiers Ltd. is an NBFC providing Hire Purchase Solutions for acquiring consumer durables. The following information is extracted from its books for the year ended 31st March, 2022:

Assets Funded	**Interest Overdue but recognized in Profit & Loss**		**Net Book Value of Assets outstanding**
	Period Overdue	**Interest Amount (₹ In crore)**	**(₹ In crore)**
LCD Televisions	Up to 12 Months	500.00	20,000
Washing Machines	For 24 Months	100.00	2,000
Refrigerators	For 30 Months	50.00	1,250
Air Conditioners	For 45 Months	25.00	600
Mobile Phones	For 60 Months	10.00	100

You are required to calculate the amount of provision to be made.

Ans. On the basis of the information, in respect of hire purchase and leased assets, additional provision shall be made as under:

			(₹ in crore)
(a)	Where hire charges are overdue upto 12 months	Nil	-
(b)	Where hire charges are overdue for more than 12 months but upto 24 months	10% of the net book value 10% x 2,000	200

(c)	Where hire charges are overdue for more than 24 months but upto 36 months	40 percent of the net book value 40% x 1,250	500
(d)	Where hire charges or lease rentals are overdue for more than 36 months but upto 48 months	70 percent of the net book value 70% x 600	420
(e)	Where hire charges or lease rentals are overdue for more than 48 months	100% of net book value (100% x 100)	100
		Total	**1,220**

Q-29 Two companies named Alex Ltd. and Beta Ltd. provide you the following summary of ledger balances as on 31st March, 2020:

	Alex Ltd. (₹)	**Beta Ltd. (₹)**
Goodwill	1,40,000	70,000
Building	8,40,000	2,80,000
Machinery	14,00,000	4,20,000
Inventory	7,00,000	4,90,000
Trade receivables	5,60,000	2,80,000
Cash at Bank	1,40,000	56,000
Equity Shares of ₹ 10 each	28,00,000	8,40,000
8% Preference Shares of ₹ 100 each	2,80,000	–
10% Preference Shares of ₹ 100 each	–	2,80,000
General Reserve	1,96,000	1,96,000
Retirement Gratuity fund	1,40,000	56,000
Trade payables	3,64,000	2,24,000

Beta Ltd. is absorbed by Alex Ltd. on the following terms:

(a) 10% Preference Shareholders are to be paid at 10% premium by issue of 8% Preference Shares of Alex Ltd.

(b) Goodwill of Beta Ltd. is valued at ₹ 1,40,000, Buildings are valued at ₹ 4,20,000 and the Machinery at ₹ 4,48,000.

(c) Inventory to be taken over at 10% less value and Provision for Doubtful Debts to be created @ 7.5%.

(d) Equity Shareholders of Beta Ltd. will be issued Equity Shares of Alex Ltd. @ 5% premium.

You are required to:

(i) Prepare necessary Ledger Accounts to close the books of Beta Ltd.

(ii) Show the acquisition entries in the books of Alex Ltd.

(iii) Also draft the Balance Sheet after absorption as at 31st March, 2020.

Ans. **In the Books of Beta Ltd.**

Realisation Account

	₹			₹
To Sundry Assets	15,96,000	By	Retirement Gratuity Fund	56,000
To Preference Shareholders (Premium on Redemption)	28,000	By	Trade payables	2,24,000

				(Purchase Consideration)	
To	Equity Shareholders		By	Alex Ltd. 14,84,000	
	(Profit on Realisation)	1,40,000			
		17,64,000			17,64,000

Equity Shareholders Account

		₹			₹
To	Equity Shares of Alex Ltd.	11,76,000	By	Share Capital	8,40,000
			By	General Reserve	1,96,000
			By	Realisation Account (Profit on Realisation)	1,40,000
		11,76,000			**11,76,000**

Preference Shareholders Account

		₹			₹
To	8% Preference Shares of Alex Ltd.	3,08,000	By	Preference Share Capital	2,80,000
			By	Realisation Account (Premium on Redemption of Preference Shares)	28,000
		3,08,000			**3,08,000**

Alex Ltd. Account

		₹			₹
To	Realisation Account	14,84,000	By	8% Preference Shares	3,08,000
			By	Equity Shares	11,76,000
		14,84,000			**14,84,000**

(ii) **In the Books of Alex Ltd.**

Journal Entries

		Dr. ₹	Cr. ₹
Business Purchase A/c	Dr.	14,84,000	
To Liquidators of Beta Ltd. Account			14,84,000
(Being business of Beta Ltd. taken over)			
Goodwill Account	Dr.	1,40,000	
Building Account	Dr.	4,20,000	
Machinery Account	Dr.	4,48,000	
Inventory Account	Dr.	4,41,000	
Trade receivables Account	Dr.	2,80,000	
Bank Account	Dr.	56,000	
To Retirement Gratuity Fund Account			56,000
To Trade payables Account			2,24,000

To Provision for Doubtful Debts Account			21,000
To Business Purchase A/c			14,84,000
(Being Assets and Liabilities taken over as per agreed valuation).			
Liquidators of Beta Ltd. A/c	Dr.	14,84,000	
To 8% Preference Share Capital A/c			3,08,000
To Equity Share Capital A/c			11,20,000
To Securities Premium A/c			56,000
(Being Purchase Consideration satisfied as above)			

(iii) Balance Sheet of Alex Ltd. (after absorption) as at 31st March, 2020

		Particulars	**Notes**	**₹**
Equity and Liabilities				
1		**Shareholders' funds**		
	A	Share capital	1	45,08,000
	B	Reserves and Surplus	2	2,52,000
2		**Non-current liabilities**		
	A	Long-term provisions 1,96,000		
3		**Current liabilities**		
	A	Trade Payables		5,88,000
	B	Short term provision		21,000
		Total		**55,65,000**
		Assets		
1		**Non-current assets**		
	A	Property, Plant and Equipment (PPE)	3	31,08,000
	B	Intangible assets		2,80,000
2		**Current assets**		
	A	Inventories		11,41,000
	B	Trade receivables		8,40,000
	C	Cash and cash equivalents		1,96,000
		Total		**55,65,000**

Notes to accounts:

		₹
1	**Share Capital**	
	Equity share capital	
	3,92,000 Equity Shares of ₹ 10 each fully paid (Out of above 1,12,000 Equity Shares were issued in consideration other than for cash)	39,20,000
	Preference share capital	
	5,880 8% Preference Shares of ₹ 100 each (Out of above 3,080 Preference Shares were issued in consideration other than for cash)	_____
	Total	45,08,000

2	**Reserves and Surplus**	
	Securities Premium	56,000
	General Reserve	1,96,000
	Total	2,52,000
3	**PPE**	
	Buildings	12,60,000
	Machinery	18,48,000
	Total	31,08,000

Working Notes:

Purchase Consideration:	₹
Goodwill	1,40,000
Building	4,20,000
Machinery	4,48,000
Inventory	4,41,000
Trade receivables	2,59,000
Cash at Bank	56,000
Less: Liabilities:	
Retirement Gratuity	(56,000)
Trade payables	(2,24,000)
Net Assets/ Purchase Consideration	14,84,000
To be satisfied as under:	
Preference Shareholders of Beta Ltd.	2,80,000
Add: 10% Premium	28,000
Satisfied by issue of 3,080 no. of 8% Preference Shares of Alex Ltd.	3,08,000
Equity Shareholders of Beta Ltd. to be satisfied by issue of 1,12,000 Equity Shares of Alex Ltd. at 5% Premium	11,76,000
Total	14,84,000

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NOTES

CHAPTER-6

INTERNAL RECONSTRUCTION

Q-1 The following is the Balance Sheet of Star Ltd. as on 31st March, 2019:

				₹
A.	**Equity & Liabilities**			
	1.	Shareholders' Fund:		
		(a)	Share Capital:	
			9,000 7% Preference Shares of ₹ 100 each fully paid	9,00,000
			10,000 Equity Shares of ₹ 100 each fully paid	10,00,000
		(b)	Reserve & Surplus:	
			Profit & Loss Account	(2,00,000)
	2.	**Non-current liabilities:**		
			"A" 6% Debentures (Secured on Bombay Works)	3,00,000
			"B" 6% Debentures (Secured on Chennai Works)	3,50,000
	3.	**Current Liabilities and Provisions:**		
	(a)	Workmen's Compensation Fund:		
		Bombay Works		10,000
		Chennai Works		5,000
	(b)	Trade Payables		1,25,000
		Total		24,90,000
B.	**Assets:**			
	Non- current Assets:			
	1.	**PPE:**		
		Bombay Works		9,50,000
		Chennai Works		7,75,000
	2.	Investment:		
		Investments for Workman's Compensation Fund		15,000
	3.	Current Assets:		
		(a)	Inventories	4,50,000
		(b)	Trade Receivables	2,50,000
		(c)	Cash at Bank	50,000
				24,90,000

A reconstruction scheme was prepared and duly approved. The salient features of the scheme were as follows:

(i) Paid up value of 7% Preference Share to be reduced to ₹ 80, but the rate of dividend being raised to 9%.

(ii) Paid up value of Equity Shares to be reduced to ₹ 10.

(iii) The directors to refund ₹ 50,000 of the fees previously received by them.

(iv) Debenture holders forego their interest of ₹ 26,000 which is included among the trade payables.

(v) The preference shareholders agreed to waive their claims for preference share dividend, which is in arrears for the last three years.

(vi) "B" 6% Debenture holders agreed to take over the Chennai Works at ₹ 4,25,000 and to accept an allotment of 1,500 equity shares of ₹ 10 each at par, and upon their forming a company called Zia Ltd. (to take over the Chennai Works) they allotted 9,000 equity shares of ₹ 10 each fully paid at par to Star Ltd.

(vii) The Chennai Worksmen's compensation fund disclosed that there were actual liabilities of ₹ 1,000 only. As a consequence, the investments of the fund were realized to the extent of the balance. Entire investments were sold at a profit of 10% on book value and the proceeds were utilized for part payment of the creditors.

(viii) Inventory was to be written off by ₹ 1,90,000 and a provision for doubtful debts is to be made to the extent of ₹ 20,000.

(ix) Chennai works completely written off.

(x) Any balance of the Capital Reduction Account is to be applied as two-third to write off the value of Bombay Works and one-third to Capital Reserve.

Pass necessary Journal Entries in the books of Star Ltd. after the scheme has been carried into effect.

Ans. **In the books of Star Ltd.**

Journal Entries

Particulars			**Amount** ₹	**Amount** ₹
(i)	7% Preference share capital (₹ 100)	Dr.	9,00,000	
	To 9% Preference share capital (₹ 80)			7,20,000
	To Capital reduction A/c			1,80,000
	(Being preference shares reduced to ₹ 80 and also rate of dividend raised from 7% to 9%)			
(ii)	Equity share capital A/c (₹ 100 each)	Dr.	10,00,000	
	To Equity share capital A/c (₹ 10 each)			1,00,000
	To Capital reduction A/c			9,00,000
	(Being reduction of nominal value of one share of ₹ 100 each to ₹ 10 each)			
(iii)	Bank A/c	Dr.	50,000	
	To Capital reduction A/c			50,000
	(Being directors refunded the fee amount)			
(iv)	Trade payables A/c (Interest on debentures)	Dr.	26,000	
	To Capital reduction A/c			26,000
	(Being interest forgone by the debenture holders)			
(v)	No entry required			

(vi) a	'B' 6% Debentures A/c	Dr.	3,50,000	
	To Debentures holders A/c			3,50,000
	(Being amount due to Debentures holders)			
b	Debentures holders A/c	Dr.	4,40,000	
	To Chennai Works A/c			4,25,000
	To Equity share capital A/c			15,000
	(Being Chennai works taken over and equity shares issued to 'B' 6% Debenture holders)			
c	Equity share of Zia ltd. A/c	Dr.	90,000	
	To Debentures holders A/c			90,000
	(Being 9,000 equity shares of Zia Ltd. issued by Debentures holders)			
(vii) a	Chennai Works – Workmen Compensation Fund	Dr.	4,000	
	To Capital reduction A/c			4,000
	(Being difference due to reduced amount of actual liability transferred to capital reduction account)			
b	Bank A/c	Dr.	15,400	
	To Investment for Workmen Compensation Fund			14,000
	To Capital reduction A/c			1,400
	(Being investment for Workmen Compensation Fund sold @ 10% profit)			
c	Trade Payables A/c	Dr.	15,400	
	To Bank A/c			15,400
	(Being part payment made to trade payables)			
(viii)	Capital reduction A/c	Dr.	2,10,000	
	To Provision for Doubtful Debts A/c			20,000
	To Inventory A/c			1,90,000
	(Being assets revalued)			
(ix)	Capital reduction A/c	Dr.	5,50,000	
	To Profit & Loss A/c			2,00,000
	To PPE – Chennai Works			3,50,000
	(Being assets revalued and losses written off)			
(x)	Capital reduction A/c	Dr.	4,01,400	
	To PPE – Bombay Works			2,67,600
	To Capital reserve A/c			1,33,800
	(Being assets revalued and remaining amount transferred to capital reserve account)			

Q-2 M/s Xylem Limited has decided to reconstruct the Balance Sheet since it has accumulated huge losses. The following is the summarized Balance Sheet of the company as on 31st March, 2019 before reconstruction:

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
Share Capital		Land & Building	42,70,000
50,000 shares of Rs. 50		Machinery	8,50,000
each fully paid up	25,00,000	Computers	5,20,000
1,00,000 shares of Rs. 50		Inventories	3,20,000
each Rs. 40 paid up	40,00,000	Trade receivables	10,90,000
Capital Reserve	5,00,000	Cash at Bank	2,68,000
8% Debentures of Rs. 100 each	4,00,000	Profit & Loss Account	29,82,000
12% Debentures of Rs. 100 each	6,00,000		
Trade payables	12,40,000		
Outstanding Expenses	10,60,000		
	1,03,00,000		**1,03,00,000**

Following is the interest of Mr. A and Mr. B in M/s Xylem Limited:

	Mr. A	Mr. B
8% Debentures	3,00,000	1,00,000
12% Debentures	4,00,000	2,00,000
Total	7,00,000	3,00,000

The following scheme of internal reconstruction was framed and implemented, as approved by the court and concerned parties:

(1) Uncalled capital is to be called up in full and then all the shares to be converted into Equity Shares of Rs. 40 each.

(2) The existing shareholders agree to subscribe in cash, fully paid up equity shares of 40 each for Rs. 12,50,000.

(3) Trade payables are given option of either to accept fully paid equity shares of Rs. 40 each for the amount due to them or to accept 70% of the amount due to them in cash in full settlement of their claim. Trade payables for Rs. 7,50,000 accept equity shares and rest of them opted for cash towards full and final settlement of their claim.

(4) Mr. A agrees to cancel debentures amounting to Rs. 2,00,000 out of total debentures due to him and agree to accept 15% Debentures for the balance amount due. He also agree to subscribe further 15% Debentures in cash amounting to Rs. 1,00,000.

(5) Mr. B agrees to cancel debentures amounting to Rs. 50,000 out of total debentures due to him and agree to accept 15% Debentures for the balance amount due.

(6) Land & Building to be revalued at Rs. 51,84,000, Machinery at Rs. 7,20,000, Computers at Rs. 4,00,000, Inventories at Rs. 3,50,000 and Trade receivables at 10% less to as they are appearing in Balance Sheet as above.

(7) Outstanding Expenses are fully paid in cash.

(8) Profit & Loss A/c will be written off and balance, if any, of Capital Reduction A/c will be adjusted against Capital Reserve.

You are required to pass necessary Journal Entries for all the above transactions and draft the company's Balance Sheet immediately after the reconstruction.

(b) A Liquidator is entitled to receive remuneration at 2% on the assets realized, 3% on the amount distributed to Preferential Creditors and 3% on the payment made to Unsecured Creditors. The assets were realized for Rs. 25,00,000 against which payment was made as follows:

Liquidation expenses	Rs. 25,000
Secured Creditors	Rs. 10,00,000
Preferential Creditors	Rs. 75,000

The amount due to Unsecured Creditors was Rs. 15,00,000. You are asked to calculate the total Remuneration payable to Liquidator. Calculation shall be made to the nearest multiple of a rupee.

Ans. **Journal Entries**

		Rs.	Rs.
Bank A/c	Dr.	10,00,000	
To Equity share capital A/c			10,00,000
(Being money on final call received)			
Equity share capital (Rs. 50) A/c	Dr.	75,00,000	
To Equity share capital (Rs. 40) A/c			60,00,000
To Capital Reduction A/c			15,00,000
(Being conversion of equity share capital of Rs. 50 each intoRs. 40 each as per reconstruction scheme)			
Bank A/c	Dr.	12,50,000	
To Equity Share Capital A/c			12,50,000
(Being new shares allotted at Rs. 40 each)			
Trade payables A/c	Dr.	12,40,000	
To Equity share capital A/c			7,50,000
To Bank A/c (4,90,000 x 70%)			3,43,000
To Capital Reduction A/c			1,47,000
(Being payment made to trade payables in shares or cash to the extent of 70% as per reconstruction scheme)			
8% Debentures A/c	Dr.	3,00,000	
12% Debentures A/c	Dr.	4,00,000	
To A A/c			7,00,000
(Being cancellation of 8% and 12% debentures of A)			
A A/c	Dr.	8,00,000	
To 15% Debentures A/c			6,00,000
To Capital Reduction A/c			2,00,000
(Being issuance of new 15% debentures and balance transferredto capital reduction account as per reconstruction scheme)			
Bank A/c	Dr.	1,00,000	
To A A/c			1,00,000

(Being new debentures subscribed by A)			
8% Debentures A/c	Dr.	1,00,000	
12% Debentures A/c Dr.		2,00,000	
To B A/c			3,00,000
(Being cancellation of 8% and 12% debentures of B)			
B A/c	Dr.	3,00,000	
To 15% Debentures A/c			2,50,000
To Capital Reduction A/c			50,000
(Being issuance of new 15% debentures and balance transferredto capital reduction account as per reconstruction scheme)			
Land and Building	Dr		
(51,84,000 – 42,70,000)		9,14,000	
Inventories Dr.		30,000	
To Capital Reduction A/c			9,44,000
(Being value of assets appreciated)			
Outstanding expenses A/c	Dr.	10,60,000	
To Bank A/c			10,60,000
(Being outstanding expenses paid in cash)			
Capital Reduction A/c	Dr.	33,41,000	
To Machinery A/c			1,30,000
To Computers A/c			1,20,000
To Trade receivables A/c			1,09,000
To Profit and Loss A/c			29,82,000
(Being amount of Capital Reduction utilized in writing off P & L A/c(Dr.) balance and downfall in value of other assets)			
Capital Reserve A/c	Dr.	5,00,000	
To Capital Reduction A/c			5,00,000
(Being debit balance of capital reduction account adjusted against capital reserve)			

Balance Sheet of Xylem Ltd. (as reduced) as on 31.3.2019

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		Shareholders' funds		
	a	Share capital	1	80,00,000
2		**Non-current liabilities**		
	a	Long-term borrowings	2	8,50,000
		Total		**88,50,000**

Assets

1	**Non-current assets**			
	a Property, Plant and Equipment			
	Tangible assets	3	63,04,000	
2	**Current assets**			
	a Inventories			3,50,000
	b Trade receivables			9,81,000
	c Cash and cash equivalents			12,15,000
		Total		**88,50,000**

Notes to accounts

				Rs.
1.	**Share Capital**			
	2,00,000 Equity shares of Rs. 40			80,00,000
2.	**Long-term borrowings**			
	Secured			
	15% Debentures (assumed to be secured)			8,50,000
3.	**Tangible assets**			
	Land & Building	51,84,000		
	Machinery	7,20,000		
	Computers	4,00,000		63,04,000

Working Notes:

1. **Cash at Bank Account**

Particulars		Rs.	Particulars		Rs.
To	Balance b/d	2,68,000	By	Trade payables A/c	3,43,000
To	Equity Share capital A/c	10,00,000	By	Outstanding expenses A/c	10,60,000
To	Equity Share Capital A/c	12,50,000	By	Balance c/d (bal. fig.)	12,15,000
To	A A/c	1,00,000			
		26,18,000			26,18,000

2. **Capital Reduction Account**

	Particulars	Rs.	Particulars		Rs.
To	Machinery A/c	1,30,000	By	Equity Share Capital A/c	15,00,000
To	Computers A/c	1,20,000	By	Trade payables A/c	1,47,000
To	Trade receivables A/c	1,09,000	By	A A/c	2,00,000
To	Profit and Loss A/c	29,82,000	By	B A/c	50,000
By	Land & Building	9,14,000			
By	Inventories	30,000			
			By	Capital Reserve A/c	5,00,000
		33,41,000			**33,41,000**

(b) Calculation of Total Remuneration payable to Liquidator

Amount in Rs.

2% on Assets realised	25,00,000 x 2%	50,000
3% on payment made to Preferential creditors	75,000 x 3%	2,250
3% on payment made to Unsecured creditors (ReferW.N)		39,255
Total Remuneration payable to Liquidator		91,505

Working Note:

Liquidator's remuneration on payment to unsecured creditors =

Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors, preferential creditors & liquidator's remuneration

= Rs. 25,00,000 – Rs. 25,000 – Rs. 10,00,000 – Rs. 75,000 – Rs. 50,000 – Rs. 2,250 = Rs. 13,47,750.

Liquidator's remuneration on payment to unsecured creditors = 3/103 x Rs. 13,47,750 = Rs. 39,255.

Q-3 The shareholders of Lili Ltd. decided on a corporate restructuring exercise necessitated because of economic recession. From the given summarised balance sheet as on 31-3-2017 and the information supplied, you are required to prepare (i) Journal entries reflecting the scheme of reconstruction, (ii) Capital reduction account, (iii) Cash account in the books of Lili Ltd.

Summarised Balance Sheet of Lili Ltd. as on 31.3.2017

Liabilities		₹	**Assets**		₹
Share Capital			Fixed Assets		
30,000 Equity shares of ₹ 10 each		3,00,000	Trademarks and Patents		1,10,000
40,000 8% Cumulative Preference			Goodwill at cost		36,100
shares ₹ 10 each		4,00,000	Freehold Land		1,20,000
Reserves and Surplus			Freehold Premises		2,44,000
Securities Premium Account		10,000	Plant and Equipment		3,20,000
Profit and Loss Account		(1,38,400)	Investment		
Secured Borrowings			(marked to market)		64,000
9% Debentures (₹ 100)	1,20,000		Current Assets		
Accrued Interest	5,400	1,25,400	Inventories:		
Current liabilities Trade payables		1,20,000	Raw materials and packing		
			materials	60,000	
Tax payable		50,000	Finished goods	16,000	76,000
Temporary bank overdraft		2,23,100	Trade receivables		1,20,000
		10,90,100			**10,90,100**

Note: Preference dividends are in arrears for 4 years.

The scheme of reconstruction that received the permission of the Court was on the following lines:

(1) The authorized capital of the Company to be re-fixed at ₹ 10 lakhs (preference capital of ₹ 3 lakhs and equity capital of ₹ 7 lakhs). Both classes of shares are of ₹ 10 each.

(2) The preference shares are to be reduced to ₹ 5 each and equity shares reduced by ₹ 3 per share. Post reduction, both classes of shares to be re-consolidated into Rs.10 shares.

(3) Trade Investments are to be liquidated in open market.

(4) One fresh equity shares of Rs.10 to be issued for every Rs.40 of preference dividends in arrears (ignore taxation).

(5) Expenses for the scheme were ₹ 10,000.
(6) The debenture holders took over freehold land at ₹ 2,10,000 and settled the balance after adjusting their dues.
(7) Unprovided contingent liabilities were settled at ₹ 54,000 and a pending insurance claim receivable settled at ₹ 12,500.
(8) The intangible assets were all to be written off along with ₹ 10,000 worth obsolete packing material and 10% of the receivables.
(9) Remaining cash available as a result of the above transactions is to be utilized to pay off the bank overdraft to that extent.
(10) The Equity shareholders agree that they will bring in necessary cash to liquidate the balance outstanding on the overdraft account by subscribing the fresh shares. The equity shares will be issued at par for this purpose.

Ans. (i) In the books of Lili Ltd.

Journal Entries

	2017			Dr. ₹	Cr. ₹
1.	March 31	Equity Share Capital A/c (₹ 10)	Dr.	3,00,000	
		To Capital Reduction A/c			90,000
		To Equity Share Capital A/c (₹ 7)			2,10,000
		(Being reduction of equity shares of ₹ 10 each to shares of ₹ 7 each as per Reconstruction Scheme dated...)			
2.		8% Cum. Preference Share Capital A/c (₹ 10)	Dr.	4,00,000	
		To Capital Reduction A/c			2,00,000
		To Preference Share Capital A/c (₹ 5)			2,00,000
		(Being reduction of preference shares of ₹ 10 each to shares of ₹ 5 each as per reconstruction scheme)			
3.		Equity Share Capital A/c (30,000 x ₹ 7)	Dr.	2,10,000	
		Preference Share Capital A/c (40,000 x ₹ 5)	Dr.	2,00,000	
		To Equity Share Capital A/c (21,000 x ₹ 10)			2,10,000
		To Preference Share Capital A/c (20,000 x ₹ 10)			2,00,000
		(Being post reduction, both classes of shares reconsolidated into ₹ 10 each)			
4.		Cash Account	Dr.	64,000	
		To Trade Investments			64,000
		(Being trade investments liquidated in the open market)			
5.		Capital Reduction Account	Dr.	32,000	
		To Equity Share Capital Account			32,000
		(Being arrears of preference dividends of 4 years satisfied by the issue of 3,200 equity shares of ₹ 10 each)			
6.		Capital Reduction Account	Dr.	10,000	
		To Cash Account			10,000
		(Being expenses of reconstruction scheme paid in cash)			
7.		9% Debentures Account	Dr.	1,20,000	
		Accrued Interest Account	Dr.	5,400	
		To Debenture holders Account			1,25,400
		(Being amount due to debenture holders)			

8.	Debenture holders Account	Dr.	1,25,400	
	Cash Account (2,10,000 – 1,25,400)	Dr.	84,600	
	To Freehold Land			1,20,000
	To Capital Reduction Account (2,10,000 – 1,20,000)			90,000
	(Being Debenture holders took over freehold land at ₹ 2,10,000 and settled the balance)			
9.	Capital Reduction Account	Dr.	54,000	
	To Cash Account			54,000
	(Being contingent liability of ₹ 54,000 paid)			
10.	Cash Account	Dr.	12,500	
	To Capital Reduction Account			12,500
	(Being pending insurance claim received)			
11.	Capital Reduction Account	Dr.	1,68,100	
	To Trademarks and Patents			1,10,000
	To Goodwill			36,100
	To Raw materials & Packing materials			10,000
	To Trade receivables			12,000
	(Being intangible assets written off along with raw materials and packing materials worth ₹ 10,000 and 10% of trade receivables)			
12.	Cash Account	Dr.	1,26,000	
	To Equity Share Capital Account			1,26,000
	(Being 12,600 shares issued to existing shareholders)			
13.	Bank Overdraft Account	Dr.	2,23,100	
	To Cash Account			2,23,100
	(Being cash balance utilized to pay off bank overdraft)			
14.	Capital Reduction Account	Dr.	1,28,400	
	To Capital reserve Account			1,28,400
	(Being balance of capital reduction account transferred to capital reserve account)			

(ii) Capital Reduction Account

Particulars	₹	Particulars	₹
To Equity share capital	32,000	By Preference share capital	2,00,000
To Cash (contingent liability settled)	54,000	By Equity share capital	90,000
To Trademarks and Patents	1,10,000	By Freehold land	90,000
To Goodwill	36,100	By Cash	
To Raw material and		(insurance claim)	12,500
Packing materials	10,000		
To Trade receivables	12,000		
To Cash account	10,000		
To Capital reserve account	1,28,400		
	3,92,500		**3,92,500**

(iii) Cash Account

Particulars	₹	Particulars	₹
To Investment	64,000	By Capital reduction	
To 9% Debenture holders		(Contingent liability)	54,000
(2,10,000-1,25,400)	84,600	By Expenses	10,000
To Capital reduction (insurance claim)	12,500	By Temporary bank overdraft	
		- From available cash	
		(64,000+84,600+12,500	
		-54,000-10,000)	97,100
To Equity share capital 12,600		- From proceeds of equity	
shares @ ₹ 10 each	1,26,000	share capital	
		(2,23,100–97,100) 1,26,000	2,23,100
	2,87,100		**2,87,100**

Note: Shares issued to existing equity shareholders for bringing cash for payment of balance of bank overdraft = ₹ 2,23,100 – ₹ 97,100 = ₹ 1,26,000

Q-4 The Balance Sheet of Lion Limited as on 31-03-2018 is given below:

Particulars	Note No.	Amount (₹ in lakh)
Equity & Liabilities		
Shareholders' Funds		
Shares' Capital	1	1,400
Reserves & Surplus	2	(522)
Non-Current Liabilities		
Long term Borrowings	3	700
Current Liabilities		
Trade Payables	4	102
Other Liabilities	5	24
Total		**1704**
Assets		
Non-Current Assets		
Property, Plant & Equipment		
Tangible Assets	6	750
Current Assets		
Current Investments	7	200
Inventories	8	300
Trade Receivables	9	450
Cash & Cash Equivalents	10	4
Total		**1704**
Notes to Accounts :		
		₹ in Lakhs
(1) Share Capital		
Authorised :		
200 lakh shares of ₹ 10 each		2,000
8 lakh, 8% Preference Shares of ₹ 100 each		800
		2,800

	Issued, Subscribed and paid up:	
	100 lakh Equity Shares of ₹ 10 each, full paid up	1,000
	4 lakh 8% Preference Shares of ₹ 100 each, fully paid up	400
	Total	1400
(2)	Reserves and Surplus	
	Debit balance of Profit & Loss A/c	(522)
(3)	Long Term Borrowings	
	6% Debentures (Secured by Freehold Property)	400
	Directors' Loan	300
		700
(4)	Trade Payables	
	Trade payables for Goods	102
(5)	Other Current Liabilities	
	Interest Accrued and Due on 6% Debentures	24
(6)	Tangible Assets	
	Freehold Property	550
	Plant & Machinery	200
		750
(7)	Current Investment	
	Investment in Equity Instruments	200
(8)	Inventories	
	Finished Goods	300
(9)	Trade Receivables	
	Trade receivables for Goods	450
(10)	Cash and Cash Equivalents	
	Balance with Bank	4

The Board of Directors of the company decided upon the following scheme of reconstruction with the consent of respective shareholders:

(1) Preference Shares are to be written down to ₹ 80 each and Equity Shares to ₹ 2 each.

(2) Preference Shares Dividend in arrears for 3 years to be waived by 2/3rd and for balance 1/3rd, Equity Shares of ₹ 2 each to be allotted.

(3) Debenture holders agreed to take one Freehold Property at its book value of ₹ 300 lakh in part payment of their holding. Balance Debentures to remain as liability of the company.

(4) Interest accrued and due on Debentures to be paid in cash.

(5) Remaining Freehold Property to be valued at ₹ 400 lakh.

(6) All investments sold out for ₹ 250 lakh.

(7) 70% of Directors' loan to be waived and for the balance, Equity Shares of ₹ 2 each to be allowed.

(8) 40% of Trade receivables and 80% of Inventories to be written off.

(9) Company's contractual commitments amounting to ₹ 600 lakh have been settled by paying 5% penalty of contract value.

You are required to :

(a) Pass Journal Entries for all the transactions related to internal reconstruction;

(b) Prepare Reconstruction Account; and

(c) Prepare notes on Share Capital and Tangible Assets to Balance Sheet, immediately after the implementation of scheme of internal reconstruction.

Ans. **Journal Entries in the books of Lion Ltd.**

	Particulars		Debit (₹ in lakhs)	Credit (₹ in lakhs)
(i)	8% Preference share capital A/c (₹ 100 each)	Dr.	400	
	To 8% Preference share capital A/c (₹ 80 each)			320
	To Capital Reduction A/c			80
	(Being the preference shares of ₹ 100 each reduced to ₹ 80 each as per the approved scheme)			
(ii)	Equity share capital A/c (₹ 10 each)	Dr.	1,000	
	To Equity share capital A/c (₹ 2 each)			200
	To Capital Reduction A/c			800
	(Being the equity shares of ₹ 10 each reduced to ₹ 2 each)			
(iii)	Capital Reduction A/c	Dr.	32	
	To Equity share capital A/c (₹ 2 each)			32
	(Being 1/3rd arrears of preference share dividend of 3 years to be satisfied by issue of 16 lakhs equity shares of ₹ 2 each)			
(iv)	6% Debentures A/c	Dr.	300	
	To Freehold property A/c			300
	(Being claim of Debenture holders settled in part by transfer of freehold property)			
(v)	Accrued debenture interest A/c	Dr.	24	
	To Bank A/c			24
	(Being accrued debenture interest paid)			
(vi)	Freehold property A/c	Dr.	150	
	To Capital Reduction A/c			150
	(Being appreciation in the value of freehold property)			
(vii)	Bank A/c	Dr.	250	
	To Investments A/c			200
	To Capital Reduction A/c			50
	(Being investment sold at profit)			
(viii)	Director's loan A/c	Dr.	300	
	To Equity share capital A/c (₹ 2 each)			90
	To Capital Reduction A/c			210
	(Being director's loan waived by 70% and balance being discharged by issue of 45 lakhs equity shares of ₹ 2 each)			
(ix)	Capital Reduction A/c	Dr.	972	
	To Profit and loss A/c			522
	To Trade receivables A/c (450 x 40%)			180
	To Inventories-in-trade A/c (300x 80%)			240
	To Bank A/c (600 x 5%)			30
	(Being certain value of various assets, penalty on cancellation of contract, profit and loss account debit balance written of through Capital Reduction Account)			

(x)	Capital Reduction A/c To Capital reserve A/c (Being balance transferred to capital reserve account as per the scheme)	286	 286

Capital Reduction Account

Dr.	(₹ in lakhs)		Cr. (₹ in lakhs)
To Equity Share Capital	32	By Preference Share Capital	80
To Trade receivables	180	By Equity Share Capital	800
To Finished Goods	240	By Freehold Property	150
To Profit & Loss A/c	522	By Bank	50
To Bank A/c	30	By Director's Loan	210
To Capital Reserve	286		
	1,290		**1,290**

Notes to Balance Sheet

	(₹ in lakhs)	(₹ in lakhs)
1. Share Capital		
Authorised:		
200 lakhs Equity shares of ₹ 2 each		400
8 lakhs 8% Preference shares of ₹ 80 each		640
		1,040
Issued:		
161 lakhs equity shares of ₹ 2 each		322
4 lakhs Preference Shares of ₹ 80 each		320
		642
2. Tangible Assets		
Freehold Property	550	
Less: Utilized to pay Debenture holders	(300)	
	250	
Add: Appreciation	150	400
Plant and Machinery		200
		600

Q-5 Platinum Limited has decided to reconstruct the Balance Sheet since it has accumulated huge losses. The following is the draft Balance Sheet of the company as on 31st March, 2019 before reconstruction:

Liabilities	Amount (₹)	Assets	Amount (₹)
Share Capital			
50,000 shares of ₹ 50		Goodwill	22,00,000
each fully paid up	25,00,000	Land & Building	42,70,000
1,00,000 shares of ₹ 50		Machinery	8,50,000
each ₹ 40 paid up	40,00,000	Computers	5,20,000
Capital Reserve	5,00,000	Inventories	3,20,000
8% Debentures of ₹ 100 each	4,00,000	Trade receivables	10,90,000
12% Debentures of ₹ 100 each	6,00,000	Cash at Bank	2,68,000
Trade payables	12,40,000	Profit & Loss Account	7,82,000
Outstanding Expenses	10,60,000		
Total	1,03,00,000	Total	1,03,00,000

Following is the interest of Mr. Shiv and Mr. Ganesh in Platinum Limited:

	Mr. Shiv	Mr. Ganesh
8% Debentures	3,00,000	1,00,000
12% Debentures	4,00,000	2,00,000
Total	7,00,000	3,00,000

The following scheme of internal reconstruction was framed and implemented, as approved by the court and concerned parties:

(1) Uncalled capital is to be called up in full and then all the shares to be converted into Equity Shares of ₹ 40 each.

(2) The existing shareholders agree to subscribe in cash, fully paid up equity shares of 40 each for ₹ 12,50,000.

(3) Trade payables are given option of either to accept fully paid equity shares of ₹ 40 each for the amount due to them or to accept 70% of the amount due to them in cash in full settlement of their claim. Trade payables for ₹ 7,50,000 accept equity shares and rest of them opted for cash towards full and final settlement of their claim.

(4) Mr. Shiv agrees to cancel debentures amounting to ₹ 2,00,000 out of total debentures due to him and agree to accept 15% Debentures for the balance amount due. He also agrees to subscribe further 15% Debentures in cash amounting to ₹ 1,00,000.

(5) Mr. Ganesh agrees to cancel debentures amounting to ₹ 50,000 out of total debentures due to him and agree to accept 15% Debentures for the balance amount due.

(6) Land & Building to be revalued at ₹ 51,84,000, Machinery at ₹ 7,20,000, Computers at ₹ 4,00,000, Inventories at ₹ 3,50,000 and Trade receivables at 10% less to as they are appearing in Balance Sheet as above.

(7) Outstanding Expenses are fully paid in cash.

(8) Goodwill and Profit & Loss A/c will be written off and balance, if any, of Capital Reduction A/c will be adjusted against Capital Reserve.

You are required to pass necessary Journal Entries for all the above transactions and draft the company's Balance Sheet immediately after the reconstruction.

Ans. **Journal Entries in the books of Platinum Ltd.**

		₹	₹
Bank A/c (1,00,000 x ₹ 10)	Dr.	10,00,000	
To Equity share capital A/c			10,00,000
(Being money on final call received)			
Equity share capital (₹ 50) A/c	Dr.	75,00,000	
To Equity share capital (₹ 40) A/c			60,00,000
To Capital Reduction A/c			15,00,000
(Being conversion of equity share capital of ₹ 50 each into ₹ 40 each as per reconstruction scheme)			
Bank A/c	Dr.	12,50,000	
To Equity Share Capital A/c			12,50,000
(Being new shares allotted at ₹ 40 each)			
Trade payables A/c	Dr.	12,40,000	
To Equity share capital A/c			7,50,000
To Bank A/c (4,90,000 x 70%)			3,43,000
To Capital Reduction A/c			1,47,000

(Being payment made to trade payables in shares or cash to the extent of 70% as per reconstruction scheme)			
8% Debentures A/c	Dr.	3,00,000	
12% Debentures A/c	Dr.	4,00,000	
To Shiv A/c			7,00,000
(Being cancellation of 8% and 12% debentures of Shiv)			
Bank A/c	Dr.	1,00,000	
To Shiv A/c			1,00,000
(Being new debentures subscribed by Shiv)			
Shiv A/c	Dr.	8,00,000	
To 15% Debentures A/c			6,00,000
To Capital Reduction A/c			2,00,000
(Being issuance of new 15% debentures and balance transferred to capital reduction account as per reconstruction scheme)			
8% Debentures A/c	Dr.	1,00,000	
12% Debentures A/c	Dr.	2,00,000	
To Ganesh A/c			3,00,000
(Being cancellation of 8% and 12% debentures of Ganesh)			
Ganesh A/c	Dr.	3,00,000	
To 15% Debentures A/c			2,50,000
To Capital Reduction A/c			50,000
(Being issuance of new 15% debentures and balance transferred to capital reduction account as per reconstruction scheme)			
Land and Building (51,84,000 – 42,70,000)	Dr.	9,14,000	
Inventories	Dr.	30,000	
To Capital Reduction A/c			9,44,000
(Being value of assets appreciated)			
Outstanding expenses A/c	Dr.	10,60,000	
To Bank A/c			10,60,000
(Being outstanding expenses paid in cash)			
Capital Reduction A/c	Dr.	33,41,000	
To Machinery A/c			1,30,000
To Computers A/c			1,20,000
To Trade receivables A/c			1,09,000
To Goodwill A/c			22,00,000
To Profit and Loss A/c			7,82,000
(Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) balance, goodwill and downfall in value of other assets)			
Capital Reserve A/c	Dr.	5,00,000	
To Capital Reduction A/c			5,00,000
(Being debit balance of capital reduction account adjusted against capital reserve)			

Balance Sheet (as reduced) as on 31.3.2019

	Particulars		Notes	₹
	Equity and Liabilities			
1	Shareholders' funds			
	a	Share capital	1	80,00,000
2	Non-current liabilities			
	a	Long-term borrowings	2	8,50,000
		Total		88,50,000
	Assets			
1	Non-current assets			
	a	Property, Plant and Equipment		
		Tangible assets	3	63,04,000
2	Current assets			
	a	Inventories		3,50,000
	b	Trade receivables		9,81,000
	c	Cash and cash equivalents		12,15,000
		Total		88,50,000
Notes to accounts				
				₹
1.	Share Capital			
	2,00,000 Equity shares of ₹ 40			80,00,000
2.	Long-term borrowings			
	Secured			
	15% Debentures (assumed to be secured)			8,50,000
3.	Tangible assets			
	Land & Building		51,84,000	
	Machinery		7,20,000	
	Computers		4,00,000	63,04,000

Working Notes:

1. Cash at Bank Account

Particulars	₹	Particulars	₹
To Balance b/d	2,68,000	By Trade Creditors A/c	3,43,000
To Equity Share capital A/c	10,00,000	By Outstanding expenses A/c	10,60,000
To Equity Share Capital A/c	12,50,000	By Balance c/d (bal. fig.)	12,15,000
To Shiv A/c	1,00,000		
	26,18,000		26,18,000

2. Capital Reduction Account

Particulars	₹	Particulars	₹
To Machinery A/c	1,30,000	By Equity Share Capital A/c	15,00,000
To Computers A/c	1,20,000	By Trade Creditors A/c	1,47,000
To Trade receivables A/c	1,09,000	By Shiv A/c	2,00,000
To Goodwill A/c	22,00,000	By Ganesh A/c	50,000
To Profit and Loss A/c	7,82,000	By Land & Building	9,14,000
		By Inventories	30,000
		By Capital Reserve A/c	5,00,000
	33,41,000		33,41,000

Q-6 The summarized balance sheet of Z Limited as on 31st March, 2017 is as under:

Liabilities	**Amount in ₹**
Share Capital:	
5,00,000 Equity shares of ₹ 10 each fully paid up	50,00,000
9%, 20,000 Preference shares of ₹ 100 each fully paid up	20,00,000
Reserves and Surplus:	
Profit and Loss Account	(14,60,000)
Non-Current Liabilities:	
10% Secured Debentures	16,00,000
Current Liabilities:	
Interest due on Debentures	1,60,000
Trade Payables	5,00,000
Loan from Directors	1,00,000
Bank Overdraft	1,00,000
Provision for Tax	1,00,000
Total	**81,00,000**
Assets:	
Non-Current Assets:	
Fixed Assets:	
(a) Tangible Assets:	
Land & Buildings	30,00,000
Plant & Machinery	12,50,000
Furniture & Fixtures	2,50,000
(b) Intangible Assets:	
Goodwill	10,00,000
Patents	5,00,000
Current Assets:	
Trade Investments	5,00,000
Trade Receivables	5,00,000
Inventory	10,00,000
Discount on issue of debentures	1,00,000
Total	**81,00,000**

Note: Preference dividend is in arrears for last 2 years.

Mr. Y holds 60% of debentures and Mr. Z holds 40% of debentures. Moreover ₹1,00,000 and ₹ 60,000 were also payable to Mr. Y and Mr. Z respectively as trade payable.

The following scheme of reconstruction has been agreed upon and duly approved.

(i) All the equity shares to be converted into fully paid equity shares of ₹ 5.00 each.

(ii) The Preference shares be reduced to ₹ 50 each and the preference shareholders agreed to forego their arrears of preference dividends, in consideration of which 9% preference shares are to be converted into 10% preference shares.

(iii) Mr. Y and Mr. Z agreed to cancel 50% each of their respective total debt including interest on debentures. Mr. Y and Mr. Z also agreed to pay ₹ 1,00,000 and ₹ 60,000 respectively in cash and to receive new 12% debentures for the balance amount.

(iv) Persons relating to trade payables, other than Mr. Y and Mr. Z also agreed to forgo their 50% claims.

(v) Directors also waived 60% of their loans and accepted equity shares for the balance.

(vi) Capital commitments of ₹ 3.00 lacs were cancelled on payment of ₹ 15,000 as penalty.

(vii) Directors refunded ₹ 1,00,000 of the fees previously received by them.

(viii) Reconstruction expenses paid ₹ 15,000.

(ix) The taxation liability of the company was settled for ₹ 75,000 and was paid immediately.

(x) The Assets were revalued as under:

Land and Building	32,00,000
Plant and Machinery	6,00,000
Inventory	7,50,000
Trade Receivables	4,00,000
Furniture and Fixtures	1,50,000
Trade Investments	4,50,000

You are required to prepare necessary journal entries for all the above-mentioned transactions including amounts to be written off of Goodwill, Patents, Loss in Profit and Loss account arid Discount on issue of debentures. And also, prepare Bank Account and Reconstruction Account.

Ans. **Journal Entries in the Books of Z Ltd.**

			Dr. ₹	Cr. ₹
(i)	Equity Share Capital (₹ 10 each) A/c	Dr.	50,00,000	
	To Equity Share Capital (₹ 5 each) A/c			25,00,000
	To Reconstruction A/c			25,00,000
	(Being conversion of 5,00,000 equity shares of ₹ 10 each fully paid into same number of fully paidequity shares of ₹ 5 each as per scheme ofreconstruction.)			
(ii)	9% Preference Share Capital (₹ 100 each) A/c	Dr.	20,00,000	
	To 10% Preference Share Capital (₹ 50 each) A/c			10,00,000
	To Reconstruction A/c			10,00,000
	(Being conversion of 9% preference share of ₹ 100 each into same number of 10% preferenceshare of ₹ 50 each and claims of preferencedividends settled as per scheme ofreconstruction.)			
(iii)	10% Secured Debentures A/c	Dr.	9,60,000	
	Trade payables A/c	Dr.	1,00,000	
	Interest on Debentures Outstanding A/c	Dr.	96,000	
	Bank A/c	Dr.	1,00,000	
	To 12% Debentures A/c			6,78,000
	To Reconstruction A/c			5,78,000
	(Being ₹ 11,56,000 due to Y (including tradepayables)			

	cancelled and 12% debentures allottedfor the amount after waving 50% as per scheme ofreconstruction.)			
(iv)	10% Secured Debentures A/c	Dr.	6,40,000	
	Trade Payables	Dr.	60,000	
	Interest on debentures outstanding A/c	Dr.	64,000	
	Bank A/c	Dr.	60,000	
	To 12% debentures A/c			4,42,000
	To Reconstruction A/c			3,82,000
	(Being ₹ 7,64,000 due to Z (including tradepayables) cancelled and 12% debentures allottedfor the amount after waving 50% as per scheme ofreconstruction.)			
(v)	Trade payables A/c	Dr.	1,70,000	
	To Reconstruction A/c			1,70,000
	(Being remaining trade payables sacrificed 50% oftheir claim.)			
(vi)	Directors' Loan A/c	Dr.	1,00,000	
	To Equity Share Capital (₹ 5) A/c			40,000
	To Reconstruction A/c			60,000
	(Being Directors' loan claim settled by issuing 12,000 equity shares of ₹ 5 each as per schemeof reconstruction.)			
(vii)	Reconstruction A/c	Dr.	15,000	
	To Bank A/c			15,000
	(Being payment made towards penalty of 5% forcancellation of capital commitments of ₹ 3 Lakhs.)			
(viii)	Bank A/c	Dr.	1,00,000	
	To Reconstruction A/c			1,00,000
	(Being refund of fees by directors credited toreconstruction A/c)			
(ix)	Reconstruction A/c	Dr.	15,000	
	To Bank A/c			15,000
	(Being payment of reconstruction expenses)			
(x)	Provision for Tax A/c	Dr.	1,00,000	
	To Bank A/c			75,000
	To Reconstruction A/c			25,000
	(Being payment of tax liability in full settlementagainst provision for tax)			
(xi)	Land and Building A/c	Dr.	2,00,000	
	To Reconstruction A/c			2,00,000
	(Being appreciation in value of Land & Buildingrecorded)			
(xii)	Reconstruction A/c	Dr.	49,85,000	
	To Goodwill A/c			10,00,000
	To Patent A/c			5,00,000
	To Profit and Loss A/c			14,60,000
	To Discount on issue of Debentures A/c			1,00,000

To Plant and Machinery A/c		6,50,000
To Furniture & Fixture A/c		1,00,000
To Trade Investment A/c		50,000
To Inventory A/c		2,50,000
To Trade Receivables A/c		1,00,000
To Capital Reserve (bal. fig.)		7,75,000
(Being writing off of losses and reduction in thevalue of assets as per scheme of reconstruction, balance of reconstruction A/c transfer to CapitalReserve.)		

Bank Account

	₹		₹
To Reconstruction (Y)	1,00,000	By Balance b/d	1,00,000
To Reconstruction(Z)	60,000	By Reconstruction A/c	15,000
To Reconstruction A/c		(capital commitmentpenalty paid)	
(refund of earlier fees bydirectors)	1,00,000	By Reconstruction A/c	
		(reconstructionexpenses paid)	15,000
		By Provision for tax A/c(tax paid)	75,000
		By Balance c/d	55,000
	2,60,000		**2,60,000**

Reconstruction Account

	₹		₹
To Bank (penalty)	15,000	By Equity Share	
To Bank (reconstructionexpenses)	15,000	Capital A/c	25,00,000
To Goodwill	10,00,000	By 9% Pref. Share	
To Patent	5,00,000	Capital A/c	10,00,000
To P & L A/c	14,60,000	By Mr. Y (Settlement)	5,78,000
To Discount on issue ofdebentures	1,00,000	By Mr. Z (Settlement)	3,82,000
To P & M	6,50,000	By Trade Payables A/c	1,70,000
To Furniture and Fixtures	1,00,000	By Director's loan	60,000
To Trade investment	50,000	By Bank	1,00,000
To Inventory	2,50,000	By Provision for tax	25,000
To Trade Receivables	1,00,000	By Land and Building	2,00,000
To Capital Reserve (bal. fig.)	7,75,000		
	50,15,000		**50,15,000**

Q-7 The summarized Balance Sheet of SK Ltd. as on 31st March, 2018 is given below.

(₹ in '000)

	Amount
Liabilities Equity Shares of ₹ 10 each	35,000
8%, Cumulative Preference Shares of ₹ 100 each	17,500
6% Debentures of ₹ 100 each	14,000
Sundry Creditors	17,500
Provision for taxation	350
Total	84,350
Assets	

Fixed Assets	43,750
Investments (Market value ₹ 3325 thousand)	3,500
Current Assets (Including Bank Balance)	35,000
Profit and Loss Account	2,100
Total	84,350

The following Scheme of Internal Reconstruction is approved and put into effect on 31st March, 2018.

(i) Investments are to be brought to their market value.

(ii) The Taxation Liability is settled at ₹ 5,25,000 out of current Assets.

(iii) The balance of Profit and Loss Account to be written off.

(iv) All the existing equity shares are reduced to ₹ 4 each.

(v) All preference shares are reduced to ₹ 60 each.

(vi) The rate of interest on debentures is increased to 9%. The Debenture holders surrender their existing debentures of ₹ 100 each and exchange them for fresh debentures of ₹ 80 each. Each old debenture is exchanged for one new debenture.

(vii) Balance of Current Assets left after settlement of taxation liability are revalued at ₹ 1,57,50,000.

(viii) Fixed Assets are written down to 80%.

(ix) One of the creditors of the Company for ₹ 70,00,000 gives up 50% of his claim. He is allotted 8,75,000 equity shares of ₹ 4 each in full and final settlement of his claim.

Pass journal entries for the above transactions.

Ans. **Journal Entries in the books of SK Ltd.**

			₹ '000	₹ '000
(i)	Equity share capital (₹ 10) A/c	Dr.	35,000	
	To Equity Share Capital (₹ 4) A/c			14,000
	To Capital Reduction A/c			21,000
	(Being conversion of equity share capital of ₹ 10 each into ₹ 4 each as per reconstruction scheme)			
(ii)	8% Cumulative Preference Share capital (₹ 100) A/c	Dr.	17,500	
	To 8% Cumulative Preference Share Capital (₹ 60) A/c			10,500
	To Capital Reduction A/c			7,000
	(Being conversion of 6% cumulative preference shares capital of ₹ 100 each into ₹ 60 each as per reconstructionscheme)			
(iii)	6% Debentures (₹ 100) A/c	Dr.	14,000	
	To 9% Debentures (₹ 80) A/c			11,200
	To Capital Reduction A/c			2,800
	(Being 9% debentures of ₹ 80 each issued to existing 6% debenture holders. The balance transferred to capital reduction account as per reconstruction scheme)			

(iv)	Sundry Creditors A/c	Dr.	7,000	
	To Equity Share Capital (₹ 4) A/c			3,500
	To Capital Reduction A/c			3,500
	(Being a creditor of ₹ 70,00,000 agreed to surrender hisclaim by 50% and was allotted 8,75,000 equity shares of ₹ 4 each in full settlement of his dues as per reconstructionscheme)			
(v)	Provision for Taxation A/c	Dr.	350	
	Capital Reduction A/c	Dr.	175	
	To Liability for Taxation A/c		525	
	(Being conversion of the provision for taxation into liability for taxation for settlement of the amount due)			
(vi)	Liability for Taxation A/c	Dr.	525	
	To Current Assets (Bank A/c)			525
	(Being the payment of tax liability)			
(vii)	Capital Reduction A/c	Dr.	34,125	
	To P & L A/c			2,100
	To Fixed Assets A/c			8,750
	To Current Assets A/c			18,725
	To Investments A/c			175
	To Capital Reserve A/c (Bal. fig.)			4,375
	(Being amount of Capital Reduction utilized in writing off P& L A/c (Dr.) Balance, Fixed Assets, Current Assets, Investments and the Balance transferred to CapitalReserve)			

Working Note:

Capital Reduction Account

To Liability for taxation A/c	175	By Equity share capital	21,000
To P & L A/c	2,100	By 8% Cumulative preferences	7,000
To Fixed Assets	8,750	Share capital	
To Current assets	18,725	By 6% Debentures	2,800
To Investment	175	By Sundry creditors	3,500
To Capital Reserve (Bal.fig.)	4,375		
	34,300		**34,300**

Q-8 Following is the summarized Balance Sheet of Fortunate Ltd. as on 31st March, 2019.

Particulars	Amount (₹)
Liabilities	
Authorized and Issued Share Capital	
(a) 15,000 8% Preference shares of ₹ 50 each	7,50,000
(b) 18,750 Equity shares of 50 each	9,37,500
Profit and Loss Account	(5,63,750)
Loan	7,16,250
Trade Payables	2,58,750
Other Liabilities	43,750
Total :	**21,42,500**
Assets	
Building at cost less depreciation	5,00,000
Plant at cost less depreciation	3,35,000
Trademarks and goodwill at cost	3,97,5000
Inventory	5,00,000
Trade Receivables	4,10,000
Total :	**21,42,5000**

(Note: Preference shares dividend is in arrear for last five years).

The Company is running with the shortage of working capital and earnings profits. A scheme of reconstruction has been approved by both the classes of shareholders. The summarized scheme of reconstruction is as follows:

(1) The equity shareholders have agreed that their ₹ 50 shares should be reduced to ₹ 5 by cancellation of ₹ 45,00 per shares of ₹ 5.00 each for each equity share held.

(2) The preference shareholders have agreed to forego the arrears of dividends and to accept for each ₹ 50 preference share 4 new 6% preference shares of ₹ 10 each, plus 3 new equity shares of ₹ 5.00 each, all credited as fully paid.

(3) Lenders to the company for ₹ 1,87,500 have agreed to convert their loan into shares and for this purpose they will be allotted 15,000 new preference shares of ₹ 10 each and 7,500 new Equity shares of ₹ 5.00 each

(4) The directors have agreed to subscribe in cash for 25,000 new equity shares of ₹ 5.00 each in addition to any shares to be subscribed by them under (1) above.

(5) Of the cash received by the issue of new shares, ₹ 2,50,000 is to be used to reduce the loan due by the company.

(6) The equity share capital cancelled is to be applied:

   (a) To write off the debit balance in the Profit and Loss A/c and

   (b) To write off ₹ 43,750 from the value of plant.

Any balance remaining is to be used to write down the value of trademarks and goodwill. The nominal capital as reduced is to be increased to ₹ 8,12,500 for preference share capital and ₹ 9,37,500 for equity share capital.

You are required to pass Journal entries to show the effect of above scheme and prepare the Balance Sheet of the Company after reconstruction.

Ans. **In the books of Fortunate Ltd.**

Journal Entries

	Particulars		Debit (₹)	Credit (₹)
1.	Equity share capital A/c (‘ 50)	Dr.	9,37,500	
	To Equity share capital A/c (‘ 5)			93,750
	To Capital reduction A/c*			8,43,750
	(Being equity capital reduced to nominal value of ₹ 5 each)			
2.	Bank A/c	Dr.	2,81,250	
	To Equity share capital			2,81,250
	(Being 3 right shares against each share was issued and subscribed)			
3.	8% Preference share capital A/c (₹ 50)	Dr.	7,50,000	
	Capital reduction A/c	Dr.	75,000	
	To 6% Preference share capital (₹ 10)			6,00,000
	To equity share capital (₹ 50)			2,25,000
	(Being 8% preference shares of ₹ 50 each converted to 6% preference shares of ₹ 10 each and also given to them 3 equity shares for every share held)			
4.	Loan A/c	Dr.	1,87,500	
	To 6% Preference share capital A/c (15,000 x ₹ 10)			1,50,000
	To Equity share capital A/c (7,500 x ₹ 5)			37,500
	(Being loan to the extent of ₹ 1,50,000 converted into share capital)			
5.	Bank A/c (25,000 x ₹5)	Dr.	1,25,000	
	To Equity share application A/c			1,25,000
	(Being shares subscribed by the directors)			
6.	Equity share application A/c	Dr.	1,25,000	
	To Equity share capital A/c			1,25,000
	(Being application money transferred to capital A/c)			
7.	Loan A/c	Dr.	2,50,000	
	To Bank A/c			2,50,000
	(Being loan repaid)			
8.	Capital reduction A/c	Dr.	7,68,750	
	To Profit and loss A/c			5,63,750
	To Plant A/c			43,750
	To Trademarks and Goodwill A/c (Bal. fig.)			1,61,250
	(Being losses and assets written off to the extent required)			

Balance sheet of Fortunate Ltd. (and reduced)
as on 31.3.2019

Particulars	Notes	₹
Equity and Liabilities		
1 Shareholders' funds		
a Share capital	1	15,12,500
2 Non-current liabilities		
a Long-term borrowings (7,16,250 – 1,87,500 – 2,50,000)		2,78,750
3 Current liabilities		
a Trade Payables		2,58,750
b Other current liabilities		43,750
Total		**20,93,750**

Assets

1 Non-current assets		
a Property, Plant and Equipment	2	7,91,250
b Intangible assets	3	2,36,250
2 Current assets		
a Inventories		5,00,000
b Trade receivables		4,10,000
c Cash and cash equivalents	4	1,56,250
Total		**20,93,750**

Notes to accounts:

		₹
1 **Share Capital**		
Authorized capital:		
81,250 Preference shares of ₹ 10 each	8,12,500	
1,87,500 Equity shares of ₹ 5 each	9,37,500	17,50,000
Issued, subscribed and paid up:		
1,52,500 equity shares of ₹ 5 each	7,62,500	
75,000, 6% Preference shares of ₹ 10 each	7,50,000	15,12,500
2 **Property, Plant and Equipment**		
Building at cost less depreciation	5,00,000	
Plant at cost less depreciation	2,91,250	7,91,250
3. **Intangible assets**		
Trademarks and goodwill		2,36,250
4 **Cash and cash equivalents**		
Bank (2,81,250+1,25,000-2,50,000)		1,56,250

Note: *In place of Capital Reduction Account, Reconstruction Account or Internal Reconstruction Account may also be used.

Q-9 The summarised Balance Sheet of Preeti Limited as on 31st March 2019, was as follows:

Liabilities	(₹)	Assets	(₹)
Authorized and subscribed capital:		Property, plant and equipment:	
20,000 Equity shares of ₹ 100 each fully paid	20,00,000	Machineries	7,00,000
Unsecured loans:		Current Assets:	
15% Debentures	6,00,000	Inventory	5,06,000
Interest payable thereon	90,000	Trade receivables	4,60,000
Current Liabilities:		Bank	40,000
Trade payables	1,04,000	Profit & loss A/c	11,60,000
Provision for income tax	72,000		
	28,66,000		**28,66,000**

It was decided to reconstruct the company for which necessary resolution was passed and sanctions were obtained from the appropriate authorities. Accordingly, it was decided that:

(i) Each share be sub-divided into 10 fully paid up equity shares of ₹ 10 each.

(ii) After sub-division, each shareholder shall surrender to the company 50% of his holding for the purpose of reissue to debenture holders and trade payables as necessary.

(iii) Out of shares surrendered 20,000 shares of ₹ 10 each shall be converted into 10% Preference shares of ₹ 10 each fully paid up.

(iv) The claims of the debenture holders shall be reduced by 50%. In consideration of the reduction, the debenture holder shall receive Preference Shares of ₹ 2,00,000 which are converted out of shares surrendered.

(v) Trade payables claim shall be reduced by 25%. Remaining trade payables are to be settled by the issue of equity shares of ₹ 10 each out of shares surrendered.

(vi) Balance of Profit and Loss account to be written off.

(vii) The shares surrendered and not re-issued shall be cancelled.

Pass Journal Entries giving effect to the above.

Ans. **In the books of Preeti Limited**

Journal Entries

			₹	₹
(i)	Equity Share Capital (₹ 100) A/c	Dr.	20,00,000	
	To Share Surrender A/c			10,00,000
	To Equity Share Capital (₹ 10) A/c			10,00,000
	(Sub-division of 20,000 equity shares of ₹ 100 each into 2,00,000 equity shares of ₹ 10 each and surrender of 1,00,000 of such sub-divided shares as per capital reduction scheme)			
(ii)	15% Debentures A/c	Dr.	3,00,000	
	Interest payable A/c (proportionate 50%)	Dr.	45,000	
	To Reconstruction A/c			3,45,000
	(Transferred 50% of the claims of the debenture holders to Reconstruction A/c in consideration of which 10% Preference shares are being issued, out of share surrender A/c as per capital reduction scheme)			

(iii)	Trade payables A/c	Dr.	1,04,000	
	To Reconstruction A/c			1,04,000
	(Transferred claims of the trade payables to Reconstruction A/c, 25% of which is reduction and equity shares are issued in consideration of the balance amount)			
(iv)	Share Surrender A/c	Dr.	10,00,000	
	To 10% Preference Share Capital A/c			2,00,000
	To Equity Share Capital A/c			78,000
	To Reconstruction A/c			7,22,000
	(Issued preference and equity shares to discharge the claims of the debenture holders and the trade payables respectively as per scheme and the balance in share surrender account is transferred to reconstruction account)			
(v)	Reconstruction A/c	Dr.	11,71,000	
	To Profit & Loss A/c			11,60,000
	To Capital Reserve A/c			11,000
	(Adjusted debit balance of profit and loss account against reconstruction account and the balance is transferred to Capital Reserve account)			

Note: Alternative set of correct journal entries may be given for transfer of surrendered shares to trade payables and debenture holders.

Q-10 The following information pertains to Z Limited as on 31st March, 2019:

	Amount in ₹
Share Capital:	
5,00,000 Equity shares of ₹ 10 each fully paid up	50,00,000
9%, 20,000 Preference shares of ₹ 100 each fully paid up	20,00,000
Reserves and Surplus:	
Profit and Loss Account	(14,60,000)
Non-Current Liabilities:	
10% Secured Debentures	16,00,000
Current Liabilities:	
Interest due on Debentures	1,60,000
Trade Payables	5,00,000
Loan from Directors	1,00,000
Bank Overdraft	1,00,000
Provision for Tax	1,00,000
Non-Current Assets:	
(a)Property, Plant and Equipment:	
Land & Buildings	30,00,000
Plant & Machinery	12,50,000
Furniture & Fixtures	2,50,000

(b) Intangible Assets:	
Goodwill	11,00,000
Patents	5,00,000
Current Assets:	
Trade Investments	5,00,000
Trade Receivables	5,00,000
Inventory	10,00,000

Note: Preference dividend is in arrears for last 2 years.

Mr. Y holds 60% of debentures and Mr. Z holds 40% of debentures. Moreover ₹ 1,00,000 and ₹ 60,000 were also payable to Mr. Y and Mr. Z respectively as trade payable.

The following scheme of reconstruction has been agreed upon and duly approved.

(i) All the equity shares to be converted into fully paid equity shares of ₹ 5.00 each.

(ii) The Preference shares be reduced to ₹ 50 each and the preference shareholders agreed to forego their arrears of preference dividends, in consideration of which 9% preference shares are to be converted into 10% preference shares.

(iii) Mr. Y and Mr. Z agreed to cancel 50% each of their respective total debt including interest on debentures. Mr. Y and Mr. Z also agreed to pay ₹ 1,00,000 and ₹ 60,000 respectively in cash and to receive new 12% debentures for the balance amount.

(iv) Persons relating to trade payables, other than Mr. Y and Mr. Z also agreed to forgo their 50% claims.

(v) Directors also waived 60% of their loans and accepted equity shares for the balance.

(vi) Capital commitments of ₹ 3.00 lacs were cancelled on payment of ₹ 15,000 as penalty.

(vii) Directors refunded ₹ 1,00,000 of the fees previously received by them.

(viii) Reconstruction expenses paid ₹ 15,000.

(ix) The taxation liability of the company was settled for ₹ 75,000 and was paid immediately.

(x) The Assets were revalued as under:

Land and Building	32,00,000
Plant and Machinery	6,00,000
Inventory	7,50,000
Trade Receivables	4,00,000
Furniture and Fixtures	1,50,000
Trade Investments	4,50,000

You are required to pass journal entries for all the above-mentioned transactions including amounts of Goodwill, Patents, Loss in Profit and Loss account to be written off. Also prepare Bank Account and Reconstruction A/c.

Ans. **Journal Entries in the Books of Z Ltd.**

			Dr. ₹	Cr. ₹
(i)	Equity Share Capital (₹ 10 each) A/c	Dr.	50,00,000	
	To Equity Share Capital (₹ 5 each) A/c			25,00,000
	To Reconstruction A/c			25,00,000
	(Being conversion of 5,00,000 equity shares of			

	₹ 10 each fully paid into same number of fully paid equity shares of ₹ 5 each as per scheme of reconstruction.)			
(ii)	9% Preference Share Capital (₹ 100 each) A/c	Dr.	20,00,000	
	To 10% Preference Share Capital (₹ 50 each) A/c			10,00,000
	To Reconstruction A/c			10,00,000
	(Being conversion of 9% preference share of ₹ 100 each into same number of 10% preference share of ₹ 50 each and claims of preference dividends settled as per scheme of reconstruction.)			
(iii)	10% Secured Debentures A/c	Dr.	9,60,000	
	Trade payables A/c	Dr.	1,00,000	
	Interest on Debentures Outstanding A/c	Dr.	96,000	
	Bank A/c	Dr.	1,00,000	
	To 12% Debentures A/c			6,78,000
	To Reconstruction A/c			5,78,000
	(Being ₹ 11,56,000 due to Y (including trade payables) cancelled and 12% debentures allotted for the amount after waving 50% as per scheme of reconstruction.)			
(iv)	10% Secured Debentures A/c	Dr.	6,40,000	
	Trade Payables		60,000	
	Interest on debentures outstanding A/c		64,000	
	Bank A/c		60,000	
	To 12% debentures A/c			4,42,000
	To Reconstruction A/c			3,82,000
	(Being ₹ 7,64,000 due to Z (including trade payables) cancelled and 12% debentures allotted for the amount after waving 50% as per scheme of reconstruction.)			
(v)	Trade payables A/c	Dr.	1,70,000	
	To Reconstruction A/c			1,70,000
	(Being remaining trade payables sacrificed 50% of their claim.)			
(vi)	Directors' Loan A/c	Dr.	1,00,000	
	To Equity Share Capital (₹ 5) A/c			40,000
	To Reconstruction A/c			60,000
	(Being Directors' loan claim settled by issuing 12,000 equity shares of ₹ 5 each as per scheme of reconstruction.)			
(vii)	Reconstruction A/c	Dr.	15,000	
	To Bank A/c			15,000
	(Being payment made towards penalty of 5% for cancellation of capital commitments of ₹ 3 Lakhs.)			

(viii)	Bank A/c	Dr.	1,00,000	
	To Reconstruction A/c			1,00,000
	(Being refund of fees by directors credited to reconstruction A/c.)			
(ix)	Reconstruction A/c	Dr.	15,000	
	To Bank A/c			15,000
	(Being payment of reconstruction expenses.)			
(x)	Provision for Tax A/c	Dr.	1,00,000	
	To Bank A/c			75,000
	To Reconstruction A/c			25,000
	(Being payment of tax liability in full settlement against provision for tax)			
(xi)	Land and Building A/c	Dr.	2,00,000	
	To Reconstruction A/c			2,00,000
	(Being appreciation in value of Land & Building recorded)			
(xii)	Reconstruction A/c	Dr.	49,85,000	
	To Goodwill A/c			11,00,000
	To Patent A/c			5,00,000
	To Profit and Loss A/c			14,60,000
	To Plant and Machinery A/c			6,50,000
	To Furniture & Fixture A/c			1,00,000
	To Trade Investment A/c			50,000
	To Inventory A/c			2,50,000
	To Trade Receivables A/c			1,00,000
	To Capital Reserve (bal. fig.)			7,75,000
	(Being writing off of losses and reduction in the value of assets as per scheme of reconstruction, balance of reconstruction A/c transfer to Capital Reserve.)			

Bank Account

		₹			₹
To	Reconstruction (Y)	1,00,000	By	Balance b/d	1,00,000
To	Reconstruction(Z)	60,000	By	Reconstruction A/c (capital commitment penalty paid)	15,000
To	Reconstruction A/c (refund of earlier fees by directors)	1,00,000	By	Reconstruction A/c (reconstruction expenses paid)	15,000
			By	Provision for tax A/c (tax paid)	75,000
			By	Balance c/d	55,000
		2,60,000			**2,60,000**

Reconstruction Account

		₹			₹
To	Bank (penalty)	15,000	By	Equity Share	
To	Bank (reconstruction expenses)	15,000		Capital A/c	25,00,000
To	Goodwill	11,00,000	By	9% Pref. Share	
To	Patent	5,00,000		Capital A/c	10,00,000
To	P & L A/c	14,60,000	By	Mr. Y (Settlement)	5,78,000
			By	Mr. Z (Settlement)	3,82,000
To	P & M	6,50,000	By	Trade Payables A/c	1,70,000
To	Furniture and Fixtures	1,00,000	By	Director's loan	60,000
To	Trade investment	50,000	By Bank		1,00,000
To	Inventory	2,50,000	By Provision for tax		25,000
To	Trade Receivables	1,00,000	By Land and Building		2,00,000
To	Capital Reserve (bal. fig.)	7,75,000			
		50,15,000			**50,15,000**

Q-11 Shine Ltd. provides the following information as on 31st March, 2021:

	(₹ in '000) Amount
Equity Shares of ₹ 10 each	35,000
8%, Cumulative Preference Shares of ₹ 100 each	17,500
6% Debentures of ₹ 100 each	14,000
Sundry Creditors	17,500
Provision for taxation	350
Property, Plant and Equipment	43,750
Investments (Market value ₹ 3325 thousand)	3,500
Current Assets (Including Bank Balance)	35,000
Profit and Loss Account (Dr. balance)	2,100

The following Scheme of Internal Reconstruction is approved and put into effect on 31st March, 2021.

(i) All the existing equity shares are reduced to ₹ 4 each.

(ii) All preference shares are reduced to ₹ 60 each.

(iii) The rate of interest on debentures is increased to 9%. The Debenture holders surrender their existing debentures of ₹ 100 each and exchange them for fresh debentures of ₹ 80 each. Each old debenture is exchanged for one new debenture.

(iv) Investments are to be brought to their market value.

(v) The Taxation Liability is settled at ₹ 5,25,000 out of current Assets.

(vi) The balance of Profit and Loss Account to be written off and balance of Current Assets left after settlement of taxation liability are revalued at ₹ 1,57,50,000.

(vii) One of the creditors of the Company for ₹ 70,00,000 gives up 50% of his claim. He is allotted 8,75,000 equity shares of ₹ 4 each in full and final settlement of his claim.

(viii) Property, plant and equipment to be written down to 80%.

You are required to give journal entries for the above transactions and prepare capital reduction account.

Ans. **Journal Entries in the books of Shine Ltd.**

			₹ '000	₹ '000
(i)	Equity share capital (₹ 10) A/c	Dr.	35,000	
	To Equity Share Capital (₹ 4) A/c			14,000
	To Capital Reduction A/c			21,000
	(Being conversion of equity share capital of ₹ 10 each into ₹ 4 each as per reconstruction scheme)			
(ii)	8% Cumulative Preference Share capital (₹ 100) A/c	Dr.	17,500	
	To 8% Cumulative Preference Share Capital (₹ 60) A/c			10,500
	To Capital Reduction A/c			7,000
	(Being conversion of 6% cumulative preference shares capital of ₹ 100 each into ₹ 60 each as per reconstruction scheme)			
(iii)	6% Debentures (₹ 100) A/c	Dr.	14,000	
	To 9% Debentures (₹ 80) A/c			11,200
	To Capital Reduction A/c			2,800
	(Being 9% debentures of ₹ 80 each issued to existing 6% debenture holders. The balance transferred to capital reduction account as per reconstruction scheme)			
(iv)	Sundry Creditors A/c	Dr.	7,000	
	To Equity Share Capital (₹ 4) A/c			3,500
	To Capital Reduction A/c			3,500
	(Being a creditor of ₹ 70,00,000 agreed to surrender his claim by 50% and was allotted 8,75,000 equity shares of ₹ 4 each in full settlement of his dues as per reconstruction scheme)			
(v)	Provision for Taxation A/c	Dr.	350	
	Capital Reduction A/c	Dr.	175	
	To Liability for Taxation A/c			525
	(Being conversion of the provision for taxation into liability for taxation for settlement of the amount due)			
(vi)	Liability for Taxation A/c	Dr.	525	
	To Current Assets (Bank A/c)			525
	(Being the payment of tax liability)			
(vii)	Capital Reduction A/c	Dr.	34,125	
	To P & L A/c			2,100
	To PPE A/c			8,750
	To Current Assets A/c			18,725
	To Investments A/c			175
	To Capital Reserve A/c (Bal. fig.)			4,375
	(Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) Balance, Fixed Assets, Current Assets, Investments and the Balance transferred to Capital Reserve)			

Capital Reduction Account

To	Liability for taxation A/c	175	By	Equity share capital	21,000
To	P & L A/c	2,100	By	8% Cumulative preferences Share capital	7,000
To	Fixed Assets	8,750			
To	Current assets	18,725	By	6% Debentures	2,800
To	Investment	175	By	Sundry creditors	3,500
To	Capital Reserve (Bal. fig.)	4,375			
		34,300			**34,300**

Q-12 Recover Ltd decided to reorganize its capital structure owing to accumulated losses and adverse market condition. The Balance Sheet of the company as on 31st March 2020 is as follows-

		Particulars	**Notes**	**₹**
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	3,50,000
	B	Reserves and surplus	2	(70,000)
2		**Non-current liabilities**		
	A	Long-term borrowings	3	55,000
3		**Current liabilities**		
	A	Trade Payables		80,000
	B	Short term Borrowings – Bank overdraft		90,000
				5,05,000
		Assets		
1		**Non-current assets**		
	A	Property, Plant Equipment	4	3,35,000
	B	Intangible assets	5	50,000
	C	Non-current investments	6	40,000
2		**Current assets**		
	A	Inventories		30,000
	B	Trade receivables		50,000
				5,05,000

Notes to accounts:

1	**Share Capital**	**₹**
	Equity share capital:	
	20,000 Equity Shares of ₹ 10 each	2,00,000
	Preference share capital:	
	15,000 8% Cumulative Preference Shares of ₹ 10 each (preference dividend has been in arrears for 4 years)	1,50,000
		3,50,000
2	**Reserves and surplus**	
	Securities premium	10,000
	Profit and loss account (debit balance)	(80,000)
		(70,000)

3	**Long-term borrowings**	
	Secured	
	9% Debentures (secured on the freehold property	50,000
	Accrued interest on 9% debentures	5,000
		55,000
4	**Property, Plant and Equipment**	
	Freehold property	1,20,000
	Leasehold property	85,000
	Plant and machinery	1,30,000
		3,35,000
5	**Intangible assets**	
	Goodwill	50,000
		50,000
6	**Non-current investments**	
	Non-Trade investments at cost	40,000
		40,000

Subsequent to approval by court of a scheme for the reduction of capital, the following steps were taken:

i. The preference shares were reduced to ‘ 2.5 per share, and the equity shares to ₹ 1 per share.
ii. One new equity share of ‘ 1 was issued for the arrears of preferred dividend for past 4 years.
iii. The balance on Securities Premium Account was utilized and was transferred to capital reduction account.
iv. The debenture holders took over the freehold property at an agreed figure of ₹ 75,000 and paid the balance to the company after deducting the amount due to them.
v. Plant and Machinery was written down to ₹ 1,00,000.
vi. Non-trade Investments were sold for ₹ 32,000.
vii. Goodwill and obsolete stock (included in the value of inventories) of ₹ 10,000 were written off.
viii. A contingent liability of which no provision had been made was settled at ₹ 7,000 and of this amount, ₹ 6,300 was recovered from the insurance.

You are required (a) to show the Journal Entries, necessary to record the above transactions in the company’s books and (b) to prepare the Balance Sheet, after completion of the scheme.

Ans. **In the books of Recover Ltd**

Journal entries

Particulars		**Dr.** ₹	**Cr.** ₹
8% Cumulative Preference share capital (₹ 10) A/c	Dr.	1,50,000	
To 8% Cumulative Preference share capital (₹2.5) A/c			37,500
To Capital reduction (₹ 7.5) A/c			1,12,500
(Preference shares being reduced to shares of ₹ 2.5 per share and remaining transferred to capital reduction account as per capital reduction scheme)			
Equity share capital A/c (₹10)	Dr.	2,00,000	
To Equity Share capital A/c (₹ 1)			20,000
To Capital reduction A/c (₹ 9)			1,80,000

(Equity shares reduced to ₹ 1 per share with the remaining amount transferred to capital reduction A/c as a part of the internal reconstruction scheme.)			
Capital reduction A/c	Dr.	48,000	
To Equity share capital A/c			48,000
(Equity shares of ₹ 1 issued in lieu of the arrears of preference dividend for 4 years as a part of the internal reconstruction scheme)			
Securities Premium A/c	Dr.	10,000	
To Capital reduction A/c			10,000
(Amount from the securities premium utilized towards the capital reduction a/c as a part of the internal reconstruction scheme)			
9% Debentures A/c	Dr.	50,000	
Accrued interest on debentures A/c	Dr	5,000	
Bank A/c	Dr.	20,000	
Capital reduction A/c	Dr.	45,000	
To Freehold property A/c			1,20,000
(Debenture holders being paid by the sale of property, which is sold at a loss debited to the capital reduction account. Amount received in excess being refunded to company by debenture holders as a part of the internal reconstruction scheme.)			
Capital reduction A/c	Dr.	90,000	
To Plant and Machinery Ac			30,000
To Goodwill A/c			50,000
To Inventory A/c			10,000
(The assets written off as a part of the internal reconstruction scheme)			
Bank A/c	Dr.	32,000	
Capital reduction A/c	Dr.	8,000	
To Investments A/c			40,000
(Investments sold at a loss debited to capital reduction account as a part of the internal reconstruction scheme)			
Contingent Liability A/c	Dr.	7,000	
To Bank A/c			7,000
(Contingent liability paid as a part of the internal reconstruction scheme)			
Bank A/c	Dr.	6,300	
Capital reduction A/c	Dr.	700	
To Contingent Liability A/c			7,000

(The insurance company remitting part of the contingency payment amount)			
Capital reduction A/c	Dr.	80,000	
To Profit and loss A/c			80,000
(Accumulated losses written off to capital reduction account as a part of the internal reconstruction scheme).			
Capital reduction A/c	Dr.	30,800	
To Capital reserve A/c			30,800
(The balance in capital reduction account transferred to capital reserve as a part of the internal reconstruction scheme)			

Balance sheet of Recover Ltd. as at 31st March 2020 (and reduced)

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	1,05,500
	B	Reserves and surplus	2	30,800
2		**Non-current liabilities**		
	A	Long-term borrowings -		
3		**Current liabilities**		
	A	Trade Payables		80,000
	B	Bank Overdraft		90,000
				3,06,300
		Total		
		Assets		
1		**Non-current assets**		
	A	Property, Plant and Equipment	3	1,85,000
2		**Current assets**		
	A	Inventories		20,000
	B	Trade receivables		50,000
	C	Cash and cash equivalents	4	51,300
		Total		**3,06,300**

Notes to accounts:

		₹
1	**Share Capital**	
	Equity share capital	
	68,000 Equity Shares of ₹ 1 each	68,000
	Preference share capital	
	15,000 8% Cumulative Preference Shares of ₹ 2.5 each	37,500
		1,05,500
2	**Reserves and surplus**	
	Capital reserve	30,800
3	**Property, Plant and Equipment**	
	Leasehold property	85,000
	Plant and machinery	1,00,000
		1,85,000
4	**Cash and cash equivalents**	
	Bank A/c (20,000+32,000-7000+6,300)	51,300

Q-13 Sapra Limited has laid down the following terms upon the sanction of the reconstruction scheme by the court.

(i) The shareholders to receive in lieu of their present holding at 7,50,000 shares of ₹ 10 each, the following:

- New fully paid ₹ 10 Equity Shares equal to 3/5th of their holding.
- Fully paid ₹ 10, 6% Preference Shares to the extent of 2/5th of the above new equity shares.
- 7% Debentures of ₹ 250,000.

(ii) Goodwill which stood at ₹ 2,70,000 is to be completely written off.

(iii) Plant & Machinery to be reduced by ₹ 1,00,000, Furniture to be reduced by ₹ 88,000 and Building to be appreciated by ₹ 1,50,000.

(iv) Investment of ₹ 6,00,000 to be brought down to its existing market price of ₹ 1,80,000.

(v) Write off Profit & Loss Account debit balance of ₹ 2,25,000.

In case of any shortfall, the balance of General Reserve of ₹ 42,000 can be utilized to write off the losses under reconstruction scheme.

You are required to show the necessary Journal Entries in the books of Sapra Limited of the above reconstruction scheme considering that balance in General Reserve is utilized to write off the losses.

Ans. **Journal Entries**

		₹	₹
Equity Share Capital (old) A/c	Dr.	75,00,000	
To Equity Share Capital (₹ 10) A/c			45,00,000
To 6% Preference Share Capital (₹ 10) A/c			18,00,000
To 7% Debentures A/c			2,50,000
To Capital Reduction A/c			9,50,000

(Being new equity shares, 6% Preference Shares, 7% Debentures issued and the balance transferred to Reconstruction account as per the Scheme)

Building A/c	Dr.	1,50,000	
Capital Reduction A/c	Dr.	9,53,000	
To Goodwill Account			2,70,000
To Plant and Machinery Account			1,00,000
To Furniture Account			88,000
To Investment A/c			4,20,000
To Profit & Loss A/c			2,25,000

(Being Capital Reduction Account utilized for writing off of Goodwill, Plant and Machinery, furniture, investment and Profit & Loss as per the scheme)

General reserve A/c	Dr.	3,000	
To Capital Reduction A/c			3,000

(Being general reserve utilized to write off the balance in Capital reduction A/c)

Note: In place of Capital Reduction Account, Reconstruction Account or Internal Reconstruction Account may also be used in the above journal entries.

Q-14 Z Limited provides the following information as on 31st March, 2021:

Particulars	**Amount in ₹**
Share Capital:	
5,00,000 Equity shares of ₹ 10 each fully paid up	50,00,000
9%, 20,000 Preference shares of ₹ 100 each fully paid up	20,00,000
Reserves and Surplus:	
Profit and Loss Account (Dr. balance)	14,60,000
Non-Current Liabilities:	
10% Secured Debentures	16,00,000
Current Liabilities:	
Interest due on Debentures	1,60,000
Trade Payables	5,00,000
Loan from Directors	1,00,000
Bank Overdraft	1,00,000
Provision for Tax	1,00,000
Non-Current Assets:	
Property, plant and Equipment:	
Land & Buildings	30,00,000
Plant & Machinery	12,50,000
Furniture & Fixtures	2,50,000
Intangible Assets:	
Goodwill	11,00,000
Patents	5,00,000
Current Assets:	
Trade Investments	5,00,000
Trade Receivables	5,00,000
Inventory	10,00,000

Note: Preference dividend is in arrears for last 2 years.

Mr. Y holds 60% of debentures and Mr. Z holds 40% of debentures. Moreover ₹ 1,00,000 and ₹ 60,000 were also payable to Mr. Y and Mr. Z respectively as trade payable.

The following scheme of reconstruction has been agreed upon and duly approved.

(i) All the equity shares to be converted into fully paid equity shares of ₹ 5.00 each.

(ii) The Preference shares be reduced to ₹ 50 each and the preference shareholdersagreed to forego their arrears of preference dividends, in consideration of which 9%preference shares are to be converted into 10% preference shares.

(iii) Mr. Y and Mr. Z agreed to cancel 50% each of their respective total debt including interest on debentures. Mr. Y and Mr. Z also agreed to pay ₹ 1,00,000 and ₹ 60,000 respectively in cash and to receive new 12% debentures for the balance amount.

(iv) Persons relating to trade payables, other than Mr. Y and Mr. Z also agreed to forgo their 50% claims.

(v) Directors also waived 60% of their loans and accepted equity shares for the balance.

(vi) Capital commitments of ₹ 3.00 lacs were cancelled on payment of ₹ 15,000 as penalty.

(vii) Directors refunded ₹ 1,00,000 of the fees previously received by them.

(viii) Reconstruction expenses paid ₹ 15,000.

(ix) The taxation liability of the company was settled for ₹ 75,000 and was paid immediately.

(x) The Assets were revalued as under:

Land and Building	32,00,000
Plant and Machinery	6,00,000
Inventory	7,50,000
Trade Receivables	4,00,000
Furniture and Fixtures	1,50,000
Trade Investments	4,50,000

You are required to pass journal entries for all the above-mentioned transactions including amounts to be written off for Goodwill, Patents and Loss in Profit and Loss account. Also prepare Bank Account and Reconstruction A/c.

Ans. Journal Entries in the Books of Z Ltd.

			₹	₹
(i)	Equity Share Capital (₹ 10 each) A/c	Dr.	50,00,000	
	To Equity Share Capital (₹ 5 each) A/c			25,00,000
	To Reconstruction A/c			25,00,000
	(Being conversion of 5,00,000 equity shares of ₹ 10 each fully paid into same number of fully paid equity shares of ₹ 5 each as per scheme of reconstruction.)			
(ii)	9% Preference Share Capital (₹ 100 each) A/c	Dr.	20,00,000	
	To 10% Preference Share Capital (₹ 50 each) A/c			10,00,000
	To Reconstruction A/c			10,00,000
	(Being conversion of 9% preference share of ₹ 100 each into same number of 10% preferenceshare of ₹ 50 each and claims of preferencedividends settled as per scheme ofreconstruction.)			
(iii)	10% Secured Debentures A/c	Dr.	9,60,000	
	Trade payables A/c	Dr.	1,00,000	
	Interest on Debentures payable A/c	Dr.	96,000	
	Bank A/c	Dr.	1,00,000	
	To 12% Debentures A/c			6,78,000
	To Reconstruction A/c			5,78,000
	(Being ₹ 11,56,000 due to Y (including tradepayables) cancelled and 12% debenturesallotted for the amount after waving 50% as perscheme of reconstruction.)			
(iv)	10% Secured Debentures A/c	Dr.	6,40,000	
	Trade Payables		60,000	
	Interest on debentures payable A/c		64,000	

	Bank A/c		60,000	
	To 12% debentures A/c			4,42,000
	To Reconstruction A/c			3,82,000
	(Being ₹ 7,64,000 due to Z (including tradepayables) cancelled and 12% debenturesallotted for the amount after waving 50% as perscheme of reconstruction.)			
(v)	Trade payables A/c	Dr.	1,70,000	
	To Reconstruction A/c			1,70,000
	(Being remaining trade payables sacrificed 50% of their claim.)			
(vi)	Directors' Loan A/c	Dr.	1,00,000	
	To Equity Share Capital (₹ 5) A/c			40,000
	To Reconstruction A/c			60,000
	(Being Directors' loan claim settled by issuing 8,000 equity shares of ₹ 5 each as per schemeof recons truction.)			
(vii)	Reconstruction A/c	Dr.	15,000	
	To Bank A/c			15,000
	(Being payment made towards penalty of 5% forcan cellation of capital commitments of ₹ 3Lakhs.)			
(viii)	Bank A/c	Dr.	1,00,000	
	To Reconstruction A/c			1,00,000
	(Being refund of fees by directors credited to reconstruction A/c.)			
(ix)	Reconstruction A/c	Dr.	15,000	
	To Bank A/c			15,000
	(Being payment of reconstruction expenses.)			
(x)	Provision for Tax A/c	Dr.	1,00,000	
	To Bank A/c			75,000
	To Reconstruction A/c			25,000
	(Being payment of tax liability in full settlement against provision for tax)			
(xi)	Land and Building A/c	Dr.	2,00,000	
	To Reconstruction A/c			2,00,000
	(Being appreciation in value of Land & Building recorded)			
(xii)	Reconstruction A/c	Dr.	49,85,000	
	To Goodwill A/c			11,00,000
	To Patent A/c			5,00,000
	To Profit and Loss A/c			14,60,000
	To Plant and Machinery A/c			6,50,000

To	Furniture & Fixture A/c	1,00,000
To	Trade Investment A/c	50,000
To	Inventory A/c	2,50,000
To	Trade Receivables A/c	1,00,000
To	Capital Reserve (bal. fig.)	7,75,000

(Being writing off of losses and reduction in the value of assets as per scheme of reconstruction, balance of reconstruction A/c transfer to CapitalReserve.)

Bank Account

		₹			₹
To	Reconstruction (Y)	1,00,000	By	Balance b/d (overdraft)	1,00,000
To	Reconstruction(Z)	60,000	By	Reconstruction A/c (capital commitmentpenalty paid)	15,000
To	Reconstruction A/c (refund of earlier fees by directors)	1,00,000	By	Reconstruction A/c (reconstructionexpenses paid)	15,000
			By	Provision for tax A/c (tax paid)	75,000
			By	Balance c/d	55,000
		2,60,000			2,60,000

Reconstruction Account

		₹			₹
To	Bank (penalty)	15,000	By	Equity Share Capital A/c	25,00,000
To	Bank (reconstruction expenses)	15,000			
To	Goodwill	11,00,000	By	9% Pref. Share Capital A/c	10,00,000
To	Patent	5,00,000			
To	P & L A/c	14,60,000	By	Mr. Y (Settlement)	5,78,000
To	P & M	6,50,000	By	Mr. Z (Settlement)	3,82,000
To	Furniture and Fixtures	1,00,000	By	Trade Payables A/c	1,70,000
To	Trade investment	50,000	By	Director's loan	60,000
To	Inventory	2,50,000	By	Bank	1,00,000
To	Trade Receivables	1,00,000	By	Provision for tax	25,000
To	Capital Reserve (bal. fig.)	7,75,000	By	Land and Building	2,00,000
		50,15,000			**50,15,000**

Q-15 The Paid-up capital of S Limited amounted to ₹ 5,00,000 Equity Shares of ₹ 10 each. Due to continuous losses incurred by the company, the following scheme of reconstruction has been approved for S Limited on 1st April, 2022:

(i) In lieu of present holding the Equity Shareholders are to receive:

(a) Fully Paid Equity Shares equal to 3/5th of their holding.

(b) 8% Preference Shares fully paid to the extent of 20% of the above new Equity Shares.

(c) 10% Second Debentures of ₹ 40,000.

(ii) An issue of 8% Debentures First Debentures of ₹ 1,00,000 was made and fully subscribed for cash,

(iii) The Assets were reduced as follows:-

(a) Building from ₹ 2,00,000 to ₹ 1,50,000

(b) Plant & Machinery from ₹ 1,50,000 to ₹ 1,30,000

(c) Goodwill from ₹ 30,000 to Nil.

Show the Journal Entries in the books of S Limited to give effect of the scheme of Reconstruction.

Ans.

Journal Entries in the books of S Ltd.

			Dr.	Cr.
2022			**₹**	**₹**
April 1	Equity Share Capital A/c (₹ 10)	Dr.	5,00,000	
	To Equity Share Capital A/c			3,00,000
	To 8% Preference Equity Share Capital A/c			60,000
	To 10% Second Debentures A/c			40,000
	To Capital Reduction /Reconstruction A/c			1,00,000
	(Being reduction of equity shares to 3/5 shares, issue of preference shares and debentures as per Reconstruction Scheme dated...)			
	Capital Reduction / Reconstruction A/c	Dr.	1,00,000	
	To Building A/c			50,000
	To Plant and Machinery A/c			20,000
	To Goodwill A/c			30,000
	(Being value of building and plant and machinery reduced and goodwill written off completely.)			
	Bank A/c	Dr.	1,00,000	
	To 8% First Debentures A/c			1,00,000
	(Being ₹ 1,00,000 debentures issued)			

Q-16 Preeti Limited gives the following information as on 31st March 2021, was as follows:

	(₹)
Authorized and subscribed capital:	
20,000 Equity shares of ₹ 100 each fully paid	20,00,000
Unsecured loans:	
15% Debentures	6,00,000
Interest payable thereon	90,000
Current Liabilities:	
Trade payables	1,04,000
Provision for income tax	72,000
Property, plant and equipment:	

Machineries	7,00,000
Current Assets:	
Inventory	5,06,000
Trade receivables	4,60,000
Bank	40,000
Profit & loss A/c (Dr.)	11,60,000

It was decided to reconstruct the company for which necessary resolution was passed and sanctions were obtained from the appropriate authorities. Accordingly, it was decided that:

(i) Each share be sub-divided into 10 fully paid up equity shares of ₹ 10 each.

(ii) After sub-division, each shareholder shall surrender to the company 50% of his holding for the purpose of reissue to debenture holders and trade payables as necessary.

(iii) Out of shares surrendered 20,000 shares of ₹ 10 each shall be converted into 10% Preference shares of ₹ 10 each fully paid up.

(iv) The claims of the debenture holders shall be reduced by 50%. In consideration of the reduction, the debenture holder shall receive Preference Shares of ₹ 2,00,000 which are converted out of shares surrendered.

(v) Trade payables claim shall be reduced by 25%. Remaining trade payables are to be settled by the issue of equity shares of ₹ 10 each out of shares surrendered.

(vi) Balance of Profit and Loss account to be written off.

(vii) The shares surrendered and not re-issued shall be cancelled.

Pass Journal Entries giving effect to the above.

Ans. **In the books of Preeti Limited**

Journal Entries

			₹	₹
(i)	Equity Share Capital (₹ 100) A/c	Dr.	20,00,000	
	To Share Surrender A/c			10,00,000
	To Equity Share Capital (₹ 10) A/c			10,00,000
	(Sub-division of 20,000 equity shares of ₹ 100 each into 2,00,000 equity shares of ₹ 10 each and surrender of 1,00,000 of such sub-divided shares as per capital reduction scheme)			
(ii)	15% Debentures A/c	Dr.	3,00,000	
	Interest payable A/c (proportionate 50%)	Dr.	45,000	
	To Reconstruction A/c			3,45,000
	(Transferred 50% of the claims of the debenture holders to Reconstruction A/c in consideration of which 10% Preference shares are being issued, out of share surrender A/c as per capital reduction scheme)			
(iii)	Trade payables A/c	Dr.	1,04,000	
	To Reconstruction A/c			1,04,000
	(Transferred claims of the trade payables to			

	Reconstruction A/c, 25% of which is reduction and equity shares are issued in consideration of the balance amount)			
(iv)	Share Surrender A/c	Dr.	10,00,000	
	To 10% Preference Share Capital A/c			2,00,000
	To Equity Share Capital A/c			78,000
	To Reconstruction A/c			7,22,000
	(Issued preference and equity shares to discharge the claims of the debenture holders and the trade payables respectively as per scheme and the balance in share surrender account is transferred to reconstruction account)			
(v)	Reconstruction A/c	Dr.	11,71,000	
	To Profit & Loss A/c			11,60,000
	To Capital Reserve A/c			11,000
	(Adjusted debit balance of profit and loss account against reconstruction account and the balance is transferred to Capital Reserve account)			

Note: Alternative set of correct journal entries may be given for transfer of surrendered shares to trade payables and debenture holders.

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NOTES

CHAPTER-7

LIQUIDATION OF COMPANIES

Q-1 Alpha Ltd. is under the process of liquidation. Liquidator is entitled to receive remuneration at 2% on the assets realized, 3% on the amount distributed to Preferential Creditors and 3% on the payment made to Unsecured Creditors. The assets were realized for ₹ 37,50,000 against which payment was made as follows:

Liquidation Expenses	₹ 37,500
Secured Creditors	₹ 15,00,000
Preferential Creditors	₹ 1,12,500

The amount due to Unsecured Creditors was ₹ 22,50,000. You are asked to calculate the total Remuneration payable to Liquidator.

Calculation shall be made to the nearest multiple of a rupee.

Ans. **Calculation of Total Remuneration payable to Liquidator**

		Amount in ₹
2% on Assets realised	37,50,000 x 2%	75,000
3% on payment made to Preferential creditors	1,12,500 x 3%	3,375
3% on payment made to Unsecured creditors (Refer W.N)		58,882
Total Remuneration payable to Liquidator		1,37,257

Working Note:

Liquidator's remuneration on payment to unsecured creditors

Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors, preferential creditors & liquidator's remuneration = ₹ 37,50,000 – ₹ 37,500 – ₹ 15,00,000 – ₹ 1,12,500 – ₹ 75,000 – ₹ 3,375 = ₹ 20,21,625.

Liquidator's remuneration

= 3/103 x ₹ 20,21,625= ₹ 58,882

Q-2 A Liquidator is entitled to receive remuneration at 2% on the assets realized, 3% on the amount distributed to Preferential Creditors and 3% on the payment made to Unsecured Creditors. The assets were realized for Rs. 25,00,000 against which payment was made as follows:

Liquidation expenses	Rs. 25,000
Secured Creditors	Rs. 10,00,000
Preferential Creditors	Rs. 75,000

The amount due to Unsecured Creditors was Rs. 15,00,000. You are asked to calculate the total Remuneration payable to Liquidator. Calculation shall be made to the nearest multiple of a rupee.

Ans. **Calculation of Total Remuneration payable to Liquidator**

		Amount in Rs.
2% on Assets realised	25,00,000 x 2%	50,000
3% on payment made to Preferential creditors	75,000 x 3%	2,250
3% on payment made to Unsecured creditors (ReferW.N)		39,255
Total Remuneration payable to Liquidator		91,505

Working Note:

Liquidator's remuneration on payment to unsecured creditors =

Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors, preferential creditors & liquidator's remuneration

= Rs. 25,00,000 – Rs. 25,000 – Rs. 10,00,000 – Rs. 75,000 – Rs. 50,000 – Rs. 2,250 = Rs. 13,47,750.

Liquidator's remuneration on payment to unsecured creditors = 3/103 x Rs. 13,47,750 = Rs. 39,255.

Q-3 XYZ Limited is being would up by the tribunal. All the assets of the company have been charged to the company's bankers to whom the company owes ₹ 5 crores. The company owes following amounts to others:

Dues to workers – ₹ 1,25,00,000

Taxes Payable to Government – ₹ 30,00,000

Unsecured Creditors – ₹ 60,00,000

You are required to compute with the reference to the provision of the Companies Act, 2013 the amount each kind of creditors is likely to get if the amount realized by the official liquidator from the secured assets and available for distribution among creditors is only ₹ 4,00,00,000/-

Ans. Section 326 of the Companies Act, 2013 talks about the overriding preferential payments to be made from the amount realized from the assets to be distributed to various kind of creditors. According to the proviso given in the section 326 the security of every secured creditor should be deemed to be subject to a paripassu change in favor of the workman to the extent of their portion.

$$\text{Workman's Share to Secured Asset} = \frac{\text{Amount Realied X Workman}}{\text{Workman's Dues} + \text{Secured Loan}}$$

$$\text{Workman's Share to Secured Asset} = \frac{4,00,00,000 \text{ X } 1,25,00,000}{1,25,00,000 + 5,00,00,000}$$

$$4,00,00,000 \text{ x } \frac{1}{5}$$

Workman2 s Share to Secured Assets = 80,00,000

Amount available to secured creditor is ₹ 400 Lakhs – 80 Lakhs = 320 Lakhs

Hence, no amount is available for payment of government dues and unsecured creditors.

Q-4 A liquidator is entitled to receive remuneration at 2% on the assets realized, 3% on the amount distributed to Preferential Creditors and 3% on the payment made to Unsecured Creditors. The assets were realized for ₹ 45,00,000 against which payment was made as follows :

Liquidation expenses	₹ 50,000
Secured Creditors	₹ 15,00,000
Preferential Creditors	₹ 1,25,000

The amount due to Unsecured Creditors was ₹ 30,00,000.

You are asked to calculate the total remuneration payable to liquidator. Calculation shall be made to the nearest multiple of a rupee.

Ans. **Calculation of Total Remuneration payable to Liquidator**

		Amount in ₹
2% on Assets realised	(45,00,000 x 2%)	90,000
3% on payment made to Preferential creditors	1,25,000 x 3%	3,750
3% on payment made to Unsecured creditors (Refer W.N)		79,551
Total Remuneration payable to Liquidator		1,73,301

Working Note:

Liquidator's remuneration on payment to unsecured creditors =

Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors, preferential creditors & liquidator's remuneration

= ₹ 45,00,000 – ₹ 50,000 – ₹ 15,00,000 – ₹ 1,25,000 – ₹ 90,000 – ₹ 3,750

= ₹ 27,31,250

Liquidator's remuneration on payment to unsecured creditors = 3/103 x ₹ 27,31,250 = ₹ 79,551.

Q-5 Liquidation of YZ Ltd. commenced on 2nd April, 2018. Certain creditors could not receive payments out of the realisation of assets and out of the contributions from A list contributories. The following are the details of certain transfers which took place in 2017 and 2018:

Shareholders	No. of Shares transferred	Date of Ceasing to be a member	Creditors remaining unpaid and outstanding on the date of such transfer
A	2,000	1st March, 2017	₹ 5,000
P	1,500	1st May, 2017	₹ 3,300
Q	1,000	1st October, 2017	₹ 4,300
R	500	1st November, 2017	₹ 4,600
S	300	1st February, 2018	₹ 6,000

All the shares were of ₹ 10 each, ₹ 8 per share paid up. You are required to compute the amount to be realized from the various persons listed above ignoring expenses and remuneration to liquidator etc.

Ans. **Statement of liabilities of B list contributories**

Share holders	No. of shares transferred	Maximum liability (upto ₹ 2 pershare)	Division of Liability as on				
			1.5.2017	1.10.2017	1.11.2017	1.2.2018	Total
		₹	₹	₹	₹	₹	₹
P	1,500	3,000	1,500	?	?	?	1,500
Q	1,000	2,000	1,000	555	?	?	1,555
R	500	1,000	500	278	188	?	966
S	300	600	300	167	112	21	600
	3,300	6,600	3,300	1,000	300	21	4,621

Working Note:

Date	Cumulative liability	Increase in liability	Ratio of no. of sharesheld by the members
1.5.2017	3,300	?	30 : 20 : 10 : 6
1.10.2017	4,300	1,000	20 : 10 : 6
1.11.2017	4,600	300	10 : 6
1.2.2018	6,000	1,400	Only S

Liability of S has been restricted to the maximum allowable limit of ‘ 600, therefore amount payable by S is restricted to ₹ 21 only, on 1.2.2018.

Notes:

1. A will not be liable to pay to the outstanding creditors since he transferred his shares prior to one year preceding the date of winding up.
2. P will not be responsible for further debts incurred after 1st May, 2017 (from the date when he ceases to be member). Similarly, Q and R will not be responsible for the debts incurred after the date of their transfer of shares.

Q-6 The position of Careless Ltd. on its liquidation is as under:

5,000, 10% Preference Shares of ₹ 100 each ₹ 60 paid up

2,000, Equity shares of ₹ 75 each, ₹ 50 paid up

Unsecured Creditors ₹ 99,000

Liquidation Expenses ₹ 1,000

Liquidator is entitled to a commission of 2% on the amount realized from calls made on contributories

You are required to prepare Liquidator’s Final Statement of Account if the total assets realized ₹ 3,80,400.

Ans. **Liquidator’s Final Statement of Account**

Receipts	₹	Payments	₹
Assets realized	3,80,400	Liquidation Expenses	1,000
Call on contributories: 2,000 Equity Shares @ ₹ 10 per share (W.N.)	20,000	Liquidator’s Remuneration	400
		Unsecured Creditors	99,000
		Preference Shareholders	3,00,000
	4,00,400		**4,00,400**

Working Notes :

(i)

Calculation of Shortage of funds	₹
Total Amount Available	3,80,400
Less: liquidation Expenses	(1,000)
Balance	3,79,400
Less: Unsecured Creditors	(99,000)
Balance	2,80,400
Less: Pref. Shareholders	(3,00,000)
Shortage of Funds	19,600

(ii) Calculation of funds required to meet shortage and commission payable on Calls to be made (to be called from equity shareholders)

$$\text{Shortage of funds} \times \frac{100}{100 - \text{Rate of Commission}} = ₹\ 19,600 \times \frac{100}{100 - 2}$$

$$\frac{₹\ 19,600 \times 100}{98} = ₹\ 20,000$$

(iii) Uncalled Capital @ ₹ 25 on 2,000 shares = ₹ 50,000

(iv) Amount of Calls to be made (least of funds required and uncalled capital) i.e. ₹ 20,000 i.e. ₹ 10 per Share (20,000 /20)

(v) Commission on Call = ₹ 20,000 x 2/100 = ₹ 400.

Q-7 Given below is the Balance Sheet of OM Limited as on 31.3.2019:

Liabilities	**₹**	**Assets**	**₹**
Share Capital:		Fixed Assets:	
14%, 1,60,000 cumulative preference		Land	1,60,000
shares of ₹ 100 each fully paid up	16,00,000	Buildings	6,40,000
32,000 equity shares of ₹ 100 each,		Plant and Machinery	21,60,000
₹ 60 per share paid up	19,20,000	Patents	1,60,000
Reserves and Surplus	NIL	Investments	NIL
Secured Loans:		Current Assets:	
14% debentures	9,20,000	Inventory at cost	4,00,000
(Having a floating charge on all assets)		Trade receivables	9,20,000
Interest accrued on above		Cash at bank	2,40,000
debentures	1,28,800	Profit and Loss A/c	9,60,000
(Also having a floating charge as above)			
Loan on mortgage of land and building	6,00,000		
Unsecured Loan	NIL		
Current liabilities			
Trade payables	4,71,200		
	56,40,000		**56,40,000**

On 31.3.2019 the company went into voluntary liquidation. The dividend on 14% preference shares was in arrears for one year. Trade payables include preferential creditors amounting to ₹ 1,20,000.

The assets realized the following sums:

Land ₹ 3,20,000; Buildings ₹ 8,00,000; Plant and machinery ₹ 20,00,000; Patent ₹ 2,00,000; Inventory ₹ 6,40,000; Trade receivables ₹ 8,00,000.

The expenses of liquidation amounted to ₹ 1,17,736. The liquidator is entitled to a commission of 2% on all assets realized (except cash at bank) and 2% on amounts among unsecured creditors other than preferential creditors. All payments were made on 30th June, 2019. Interest on mortgage loan shall be ignored at the time of payment.

Prepare the liquidator's final statement of account.

Ans.

OM Ltd.

Liquidator's Final Statement of Account

Receipts	Value	Realised	Payments ₹	Payments ₹
Assets Realised:				
Cash at Bank	2,40,000	Liquidator's Remuneration (W.N. 1)		1,02,224
Trade receivables	8,00,000	Liquidation Expenses		1,17,736
Inventory	6,40,000	Debentureholders:		
Plant and Machinery	20,00,000	14% Debentures	9,20,000	
Patent	2,00,000	Interest Accrued (W.N. 2)	1,61,000	10,81,000
Surplus from Securities		Creditors:		
(W.N. 3)	5,20,000	Preferential	1,20,000	
		Unsecured	3,51,200	4,71,200
		Preference Shareholders:		
		Preference Share Capital	16,00,000	
		Arrears of Dividend	2,24,000	18,24,000
		Equity Shareholders (W.N.4)		
		₹ 25.12 per share on 32,000 shares		8,03,840
	44,00,000			**44,00,000**

Working Notes:

		₹
1	Liquidator's remuneration:	
	2% on assets realised (2% of ₹ 47,60,000)	95,200
	2% on payments to unsecured creditors (2% on ₹ 3,51,200)	7,024
		1,02,224
2	Interest accrued on 14% Debentures:	
	Interest accrued as on 31.3.2019	1,28,800
	Interest accrued upto the date of payment i.e. 30.6.2019	32,200
		1,61,000
3	Surplus from Securities:	
	Amount realised from Land and Buildings (₹ 3,20,000 + ₹ 8,00,000)	11,20,000
	Less: Mortgage Loan	(6,00,000)
		5,20,000
4	Amount payable to Equity Shareholders:	
	Equity share capital (paid up)	19,20,000
	Less: Amount available for equity shareholders	(8,03,840)
	Loss to be borne by equity shareholders	11,16,160
	Loss per equity share (₹ 11,16,160/32,000)	34.88
	Amount payable to equity shareholders for each equity share (60-34.88)	25.12

Q-8 The following is the summarized Balance Sheet of Shah Ltd. Co. which is in the hands of the liquidator:

Balance Sheet as at 31.3.2017

Liabilities	₹	Assets	₹
Share Capital:		Fixed assets	2,00,000
1,000, 6% Preference Shares of ₹ 100 each, fully paid	1,00,000	Inventory	1,20,000
		Book debts	2,40,000
2,000 Equity shares of ₹ 100 each, fully paid	2,00,000	Cash in hand	40,000
		Profit and loss A/c	3,00,000
2,000 Equity shares of ₹ 100 each ₹ 75 paid up	1,50,000		
Loan from bank (on security of stock)	1,00,000		
Trade Payables	3,50,000		
	9,00,000		9,00,000

The assets realized the following amounts (after all costs of realization and liquidator's commission amounting to ₹ 5,000 paid out of cash in hand).

	₹
Fixed assets	1,68,000
Inventory	1,10,000
Trade Receivables	2,30,000

Calls on partly paid shares were made but the amounts due on 200 shares were found to be irrecoverable. You are required to prepare Liquidator's Final Statement of Receipts and Payments.

Ans. **Liquidator's Final Statement of Receipts and Payments A/c**

	₹	₹		₹
To Cash in hand To Assets realised:		40,000	By Liquidator's remuneration and expenses	5,000
Fixed assets	1,68,000		By Trade Payables	3,50,000
Inventory (1,10,000 – 1,00,000) Book debts	10,000		By Preference shareholders	1,00,000
	2,30,000	4,08,000	By Equity shareholders @ ₹ 10 on 2,000 shares	20,000
To Cash - proceeds of call on 1,800 equity shares @ ₹ 15*		27,000		
		4,75,000		**4,75,000**

Working Note:

Return per equity share

	₹
Cash available before paying preference shareholders (₹ 4,48,000 – ₹ 3,55,000)	93,000
Add: Notional calls 1,800 shares (2,000-200) × ₹ 25	45,000
	1,38,000
Less: Preference share capital	(1,00,000)
Available for equity shareholders	38,000

$$\text{Return per share} = \frac{₹38,000}{38,000(4,000-200)} = ₹10$$

and Loss per Equity Share ₹ (100-10) = ₹ 90

*Calls to be made @ ₹ 15 per share (₹ 90-75) on 1,800 shares.

Q-9 BT Ltd. went into Voluntary Liquidation on 31st March, 2018, when their detailed Balance Sheet was as follows:

Liabilities	In ₹
Issued & Subscribed Capital	
10,000 12% cumulative preference shares of ₹ 100 each, fully paid	10,00,000
10,000 Equity Shares of ₹ 100 each 75 per share paid up	7,50,000
20,000 Equity Shares of ₹ 100 each 60 per share paid up	12,00,000
Profit & Loss Account	(5,25,000)
12% Debentures (Secured by a floating charge)	10,00,000
Interest outstanding on Debentures	1,20,000
Creditors	8,50,000
	43,95,000
Assets	
Land & Building	17,60,000
Plant & Machinery	12,50,000
Furniture	4,75,000
Patents	1,45,000
Stock	1,80,000
Trade Receivables	5,09,300
Cash at Bank	75,700
	43,95,000

Preference dividends were in arrear for 1 year. Creditors include preferential creditors of ₹ 75,000. Balance creditors are discharged subject to 5% discount.

Assets are realised as under:

			In ₹
Land & Building			24,50,000
Plant & Machinery			9,00,000
Furniture			2,85,000
Patents			90,000
Stock			2,80,000
Trade Receivables			3,15,000

- Expenses of liquidation amounted to ₹ 45,000.
- The liquidator is entitled to a remuneration of 3% on all assets realised (except cash at bank).
- All payments were made on 30th June, 2018.

You are required to prepare the Liquidator's Final Statement of Account as on 30th June, 2018. Working Notes should form part of the answer.

Ans.

BT Limited

Liquidator's Statement of Account

Receipts		₹	Payments		₹
To Assets realized:			By Liquidation expenses		45,000
Bank		75,700	By Preferential creditors		75,000
Other assets:			By Liquidator's		
			Remuneration (W.N.1)		1,29,600
Land & building	24,50,000		By Debenture holders:		
Plant & Machinery	9,00,000		Debentures	10,00,000	
Furniture	2,85,000		Interest accrued	1,20,000	
Patents	90,000		Interest 1-4-18		
			to 30-6-18	30,000	11,50,000
Stock	2,80,000		By Unsecured creditors		7,36,250
Trade receivables	3,15,000	43,20,000	By Preferential shareholders		
			Preference capital	10,00,000	
			Arrear of Dividend	1,20,000	11,20,000
			By Equity shareholders -		32,55,850
			₹ 32.995 on 20,000 shares		6,59,900
			₹ 47.995 on 10,000 shares		4,79,950
		43,95,700			**43,95,700**

Working Notes:

(1) Liquidator's remuneration 43,20,000 × 3/100 = ₹ 1,29,600

(2) As the company is solvent, interest on the debentures will have to be paid for the period 1-4-2018 to 30-6-2018 10,00,000 x 12% x3/12 = ₹ 30,000

(3) Total equity capital - paid up (7,50,000 +12,00,000) ₹ 19,50,000

Less: Balance available after payment to unsecured and preference shares

(43,95,700 — 32,55,850) ₹ (11,39,850)

₹ 8,10,150

Loss to be born by 30,000 equity shares

Loss per share ₹ 27.005

Hence, Refund for share on ₹ 60 paid share (60 - 27.005) ₹ 32.995

Refund for share on ₹ 75 paid (75 - 27.005) ₹ 47.995

Q-10 Virat Ltd. furnishes the following summarized Balance Sheet as at 31st March, 2018:

	Particulars	₹	₹
	Equity and Liabilities :		
(1)	Shareholders Funds:		
	Share Capital 10,000, 12% Pref. Shares of ₹ 100each fully paid up	10,00,000	
	1,00,000 Equity shares of ₹ 10 each fully paid up	10,00,000	
	50,000 Equity shares of ₹ 10 each, ₹ 8 paid up	4,00,000	24,00,000
(b)	Reserve and Surplus		
	Profit & Loss A/c. (Dr. Balance)		(3,50,000)
(2)	Non-current Liabilities:		
	12% Debentures	15,00,000	
	Loan on Mortgage	4,50,000	19,50,000
(3)	Current Liabilities:		
	Bank Overdraft	2,75,000	
	Trade Payables	7,30,000	10,05,000
	Total		50,05,000
	Assets:		
(1)	Non-current Assets:		
	Fixed Assets - Land & Buildings		6,00,000
(2)	Current Assets : Sundry Current Assets		44,05,000
	Total		50,05,000

The mortgage loan was secured against the Land & Buildings. Debentures were secured by a floating charge on all the assets of the company. The debenture holders appointed a Receiver. The company being voluntarily wound up, a liquidator was also appointed. The Receiver was entrusted with the task of realising the Land & Buildings which fetched ₹ 7,50,000 . Receiver also took charge of Sundry current assets of value ₹ 30,00,000 and sold them for ₹ 28,75,000. The Bank overdraft was secured by a personal guarantee of the directors who discharged their obligations in full from personal resources. The costs of the Receiver amounted to ₹ 10,000 and his remuneration ₹ 15,000.

The expenses of liquidator was ₹ 17,500 and his remuneration was decided at 2% on the value of the assets realised by him. The remaining assets were realised by liquidator for ₹ 12,50,000.

Preference dividend was in arrear for 2 years. Articles of Association of the company provide for payment of preference dividend arrears in priority to return of equity capital.

Prepare the accounts to be submitted by the Receiver and the Liquidator.

Ans. **Receiver's Receipts and Payments Account**

		₹		₹
Sundry Assets realized		28,75,000	Costs of the Receiver	10,000
Surplus received from			Remuneration to Receiver	15,000
Mortgage			Debentures holders	
Sale Proceeds of landand building	7,50,000		Principal*	15,00,000
Less: Applied to			Surplus transferred	
Discharge			to the Liquidator	16,50,000
of mortgage loan	(4,50,000)	3,00,000		
		31,75,000		**31,75,000**

Note : * Assumed that interest on debentures has already been paid before winding up proceedings.

Liquidator's Final Statement of Account

	₹		₹
Surplus received from		Cost of Liquidation (legal exp.)	17,500
Receiver	16,50,000	Remuneration to Liquidator	25,000
Assets Realized	12,50,000	(12,50,000 x 2%)	
Calls on partly paidShareholders:		Unsecured Creditors:	
		for Trade	7,30,000
		Directors for payment of Bank O/D	2,75,000
		Preferential Shareholders:	
		Capital	10,00,000
		Arrears of Preference Dividends	2,40,000
		Equity shareholders:	
		Return of money to contributors	
		to holders	
		1,00,000 shares at ₹ 4.75	4,75,000
		50,000 shares at ₹ 2.75	1,37,500
	29,00,000		**29,00,000**

Working Note :

Amount to be paid or received from Equity shareholders	₹
Total Equity share capital paid up	14,00,000
Less: Surplus before call from Equity Shares (29,00,000 — 22,87,500)	(6,12,500)
Loss to be borne by 1,50,000 shares	7,87,500
Loss per share = (7,87,500/ 1,50,000 shares)	5.25
Hence, Refund to Equity shareholders of 1,00,000 shares of ₹ 10 fully paid up	4.75
Refund to Equity shareholders of 50,000 shares of ₹ 8 paid up	2.75

Q-11 A liquidator is entitled to receive remuneration at 5% of the assets realised and 8% of the amount distributed among the unsecured creditors. The assets realised ₹ 13,75,000. Payment was made from realised amount as follows:

	₹
Liquidation expenses	13,000
Preferential creditors (treated as unsecured creditors)	88,500
Secured creditors	1,00,000

You are required to calculate remuneration payable to the liquidator.

Ans. **Calculation of Total Remuneration payable to Liquidator**

		Amount in ₹
5% on Assets realised	(13,75,000 x 5%)	68,750
8% on payment made to Unsecured creditors (Refer W.N)		7,080
Total Remuneration payable to Liquidator		75,830

Working Note:

Liquidator's remuneration on payment to unsecured creditors =

Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors and liquidator's remuneration

Total amount realized	₹	₹13,75,000
Less: Liquidation expenses paid	(13,000)	
Payment to secured creditors	(1,00,000)	
Liquidator's remuneration on assets realized	(68,750)	
		₹ 1,81,750
		₹ 11,93,250

Sufficient amount is available for preference creditors (treated as unsecured creditors) therefore Liquidator's remuneration on payment to unsecured creditors = 8% x ₹ 88,500 = ₹ 7,080

Note: Since the amount of unsecured creditors (other than preferential creditors) is not given in the question, the above solution is based on the assumption that there are no unsecured creditors (other than preferential creditors who are treated as unsecured creditors).

Q-12 A Liquidator is entitled to receive remuneration at 2% on the assets realized, 3% on the amount distributed to Preferential Creditors and 3% on the payment made to Unsecured Creditors. The assets were realized for ₹ 25,00,000 against which payment was made as follows:

Liquidation expenses	₹ 25,000
Secured Creditors	₹ 10,00,000
Preferential Creditors	₹ 75,000

The amount due to Unsecured Creditors was ₹ 15,00,000. You are asked to calculate the total Remuneration payable to Liquidator. Calculation shall be made to the nearest multiple of a rupee.

Ans. **Calculation of Total Remuneration payable to Liquidator**

		Amount in ₹
2% on Assets realized	25,00,000 x 2%	50,000
3% on payment made to Preferential creditors	75,000 x 3%	2,250
3% on payment made to Unsecured creditors (Refer W.N)		39,255
Total Remuneration payable to Liquidator		91,505

Working Note:

Liquidator's remuneration on payment to unsecured creditors =

Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors, preferential creditors & liquidator's remuneration

= ₹ 25,00,000 – ₹ 25,000 – ₹ 10,00,000 – ₹ 75,000 – ₹ 50,000 – ₹ 2,250 = ₹ 13,47,750.

Liquidator's remuneration on payment to unsecured creditors = 3/103 x ₹ 13,47,750 = ₹ 39,255

Q-13 M. Ltd. resolved on 31st December 2019 that the company be wound up voluntarily. The following was the trial balance extracted from its books as on that date:

	₹ Dr.	₹ Cr.
Fixed assets	2,00,000	
Inventory	1,20,000	
Book debts	2,40,000	
Cash in hand	40,000	
Profit and loss A/c	3,00,000	
1,000, 6% Preference Shares of ₹ 100 each, fully paid		1,00,000
2,000 Equity shares of ₹ 100 each, fully paid		2,00,000
2,000 Equity shares of ₹ 100 each ₹ 75 paid up		1,50,000
Loan from bank (on security of stock)		1,00,000
Trade Payables		3,50,000
	9,00,000	**9,00,000**

The assets realized the following amounts (after all costs of realization and liquidator's commission amounting to ₹ 5,000 paid out of cash in hand).

	₹
Fixed assets	1,68,000
Inventory	1,10,000
Trade Receivables	2,30,000

Calls on partly paid shares were made but the amounts due on 200 shares were found to be irrecoverable. You are required to prepare Liquidator's Final Statement of Receipts and Payments.

Ans. **Liquidator's Final Statement of Receipts and Payments A/c**

		₹	₹			₹
To	Cash in hand		40,000	By	Liquidator's remuneration and expenses	5,000
To	Assets realised:					
	Fixed assets	1,68,000		By	Trade Payables	3,50,000
	Inventory (1,10,000 – 1,00,000)	10,000		By	Preference shareholders	1,00,000
	Book debts	2,30,000	4,08,000	By	Equity shareholders @ ₹ 10 on 2,000 shares	20,000
To	Cash - proceeds of call on 1,800 equity shares @ ₹ 15*		27,000			
			4,75,000			**4,75,000**

Working Note:

Return per equity share

	₹
Cash available before paying preference shareholders (₹ 4,48,000 – ₹ 3,55,000)	93,000
Add: Notional calls 1,800 shares (2,000-200) × ₹ 25	45,000
	1,38,000
Less: Preference share capital	(1,00,000)
Available for equity shareholders	38,000

$$\text{Return per share} = \frac{₹\,38,000}{3,800\,(4,000-200)} = ₹\,10$$

and Loss per Equity Share ₹ (100-10) = ₹ 90

*Calls to be made @ ₹ 15 per share (₹ 90-75) on 1,800 shares.

Q-14 Explain B List Contributories and the liability of contributories included in the list.

Ans. **B List Contributories:**

(a) **Persons:** Shareholders who had transferred Partly Paid Shares (otherwise than by operation of law or by death) within one year, prior to the date of winding up may be called upon to pay an amount to pay off such Creditors as existed on the date of transfer of shares. These Transferors are called as B List Contributories.

(b) **Liability:** Their liability is restricted to the amount not called up when the shares were transferred. They cannot be called upon to pay more than the entire face value of the share.

For example, if Shares having Face Value ₹ 100 were paid up ₹ 60, the B List Contributory can be called up to pay a maximum of ₹ 40 only.

(c) **Conditions:** Liability of B List Contributories will crystallize only (a) when the existing assets available with the liquidator are not sufficient to cover the liabilities; (b) when the existing shareholders fail to pay the amount due on the shares to the Liquidator.

Q-15 A Liquidator is entitled to receive remuneration at 2% on the assets realized, 3% on the amount distributed to Preferential Creditors and 3% on the payment made to Unsecured Creditors. The assets were realized for ₹ 25,00,000 against which payment was made as follows:

Liquidation expenses	₹ 25,000
Secured Creditors	₹ 10,00,000
Preferential Creditors	₹ 75,000

The amount due to Unsecured Creditors was ₹ 15,00,000. You are asked to calculate the total Remuneration payable to Liquidator. Calculation shall be made to the nearest multiple of a rupee. **[MTP-Oct'21]**

Ans. Calculation of Total Remuneration payable to Liquidator

		Amount in ₹
2% on Assets realized	25,00,000 x 2%	50,000
3% on payment made to Preferential creditors	75,000 x 3%	2,250
3% on payment made to Unsecured creditors (Refer W.N)		39,255
Total Remuneration payable to Liquidator		91,505

Working Note:

Liquidator's remuneration on payment to unsecured creditors =

Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors, preferential creditors & liquidator's remuneration

= ₹ 25,00,000 – ₹ 25,000 – ₹ 10,00,000 – ₹ 75,000 – ₹ 50,000 – ₹ 2,250 = ₹ 13,47,750.

Liquidator's remuneration on payment to unsecured creditors = 3/103 x ₹ 13,47,750 = ₹ 39,255

Q-16 In the winding up of a company, certain Creditors could not receive payments out of the realization of assets and out of contribution from "A" list contributories. Liquidation started on 1st April, 2020. The following persons have transferred their holdings before winding up:

Name	**Date of Transfer**	**No. of shares transferred**	**Amount due to creditors on the date of transfer (₹)**
O	4th April, 2019	1,000	42,000
P	2nd Feb, 2019	300	25,000
Q	8th Sep, 2019	200	57,000
R	11th Nov, 2019	1,400	85,000
S	2nd Feb, 2020	800	66,000
T	1st March, 2020	1,400	95,000

The shares were of ₹ 100 each, ₹ 70 being called up and paid up on the date of transfers.

'X' was the transferee of shares held by S. 'X' paid ₹ 30 per share as calls in advance immediately on becoming a member.

Ignoring Expenses of Liquidation, Remuneration of Liquidator, etc. work out the amount to be realized from the above contributories.

Ans. Statement of Liability as Contributories of Former Members

	Creditors outstanding	Amount to be paid to creditors (Increase in creditors)	O 1,000 Shares	Q 200 Shares	R 1,400 Shares	T 1,400 Shares	Amount to be paid to the creditors
Date	₹	₹	₹	₹	₹	₹	₹
April 4	42,000	42,000	10,500	2,100	14,700	14,700	42,000
Sep 8	57,000	15,000	-	1,000	7,000	7,000	15,000
Nov 11	85,000	28,000	-	-	14,000	14,000	28,000
March 1	95,000	10,000	-	-	-	10,000	6,300*
Total (A)			10,500	3,100	35,700	45,700	
Maximum liability at ₹ 30 per shares on shares held (B)			30,000	6,000	42,000	42,000	
Amount paid [Lower of (A) and (B)]			10,500	3,100	35,700	42,000	91,300
*₹ (10,000 - 3,700 = 6,300)							

T can be called upon to pay maximum only ₹ 42,000. So T will pay only ₹ 6,300 (42,000 -14,700 - 7,000 - 14,000) out of ₹ 10,000 above. Hence incremental creditors on 1.03.2020 amounting to ₹ 3,700 (10,000 - 6,300) will not be receiving any payment.

Note:

1. P will not be liable to pay any amount as the winding up proceedings commenced after one year from the date of the transfer.
2. S also will not be liable, as the transferee X has paid the balance ₹ 30 per share as call in advance.

Q-17 In a winding up of a company creditor remain unpaid. The following persons had transferred their holdings before winding up.

Name	Date of Transfer	No of shares transferred	Amt. due to creditors on the transfer (₹)
D	1st January, 2019	1000	8,500
E	15th February, 2019	400	13,500
H	15th March, 2019	700	19,000
J	31st March, 2019	900	22,000
K	5th April, 2019	1000	31,000

The shares were of ₹ 100 each, ₹ 80 being called up and paid up on the date of transfers.

(1) A member G, who holds 200 shares died on 28th Feb., 2019 when the amount due to creditors was ₹ 16000. His shares were transmitted to his Son X.

(2) R was the transferee of shares held by J. R paid ₹ 20 per share as calls in advance immediately on becoming a member.

(3) The liquidation of the Company commenced on 1st February, 2020. Then the liquidator made a call on the present and past contributories to pay the amount.

You are required to quantify the maximum liability of the transferors of shares mentioned in the above table.

Ans. Statement of Liability as Contributories of Former Members

Date 2019	Creditors outstanding ₹	Amount paid to Creditors (Increase in Creditors) ₹	No. of shares Ratio	E 400 shares ₹	G/X 200 shares ₹	H 700 shares ₹	K 1,000 shares ₹	Amount to be paid to Creditors ₹
Feb 15	13,500	13,500	4:2:7:10	2,348	1,174	4,108	5,870	13,500
Feb 28	16,000	2,500	2:7:10	—	263	921	1,316	2,500
March 15	19,000	3,000	2:7:10	—	316	1,105	1,579	3,000
April 5	31,000	12,000	2:10	—	2,000	—	10,000	12,000
(a) Maximum amount payable tocreditors				2,348	3,753	6,134	18,765	31,000
(b) Maximum liability at ‘ 20 per shareheld				8,000	4,000	14,000	20,000	
Lower of (a) and (b)				2,348	3,753	6,134	18,765	

Working Note:

(1) The transferors are D, E, H, J and K. When the transferees pay the amount due as “present” member contributories, there will not be any liability on the transferors. It is only when the transferees do not pay as “present” member contributories then the liability would arise in the case of “past” members as contributories.

(2) D will not be liable to pay any amount as the winding up proceedings commenced after one year from the date of the transfer.

(3) J also will not be liable as the transferee R has paid the balance ₹ 20 per share as call in advance.

(4) E, G/X, H and K will be liable, as former members, to the maximum extent as indicated, provided the transferees do not pay the calls.

(5) X to whom shares were transmitted on demise of his father G would be liable as an existing member contributory. He steps into the shoes of his deceased father under section 430. His maximum liability would be at ₹ 20 per share on 200 shares received on transmission i.e. for ₹ 4,000.

Q-18 From the following Trial Balance of All Rounder Ltd., on 1st January, 2021, prepare liquidator’s final statement of account:

Particulars	Debit (₹)	Credit (₹)
9% Preference Share Capital (2,500 Preference Shares at ₹100 each, fully paid)		2,50,000
Equity Share Capital: 4,000 Equity Shares at ₹100 each, fully paid.		4,00,000
4,000 Equity Shares at ₹100 each, ₹ 50 paid up		2,00,000

Plant	6,00,000	
Stock-in-Trade	7,20,000	
Sundry Debtors	1,70,000	
Sundry Creditors		4,42,000
Bank Balance	2,40,000	
Preliminary Expenses	12,000	
6% Mortgage Loan		4,60,000
Outstanding Liabilities for Expenses	-	50,000
Profit and Loss A/c (Trading Loss for the previous accounting year)	60,000	-
Total	18,02,000	18,02,000

Following points should be kept in mind:

1. On 21st January, 2021, the Liquidator sold plant for ₹5,90,000 and stock-in-trade at 10% less than the Book Value. He realized 80% of Sundry Debtors, and incurred cost of collection of '3,700 (remaining Debtors are to be treated as bad).
2. The Loan Mortgage was discharged as on 31st January, 2021, along with interest for 6 months. Creditors were discharged subject to 5% discount. Outstanding Expenses paid at 20% less.
3. Preference Share Dividend is due for one year and paid with final payment.
4. Liquidation Expenses incurred are ₹3,600, and Liquidator's Remuneration is settled at 4% on disbursement to shareholders (preference and equity) excluding preference dividend, subject to minimum of ₹20,000. Liquidator's Remuneration to be rounded off to the multiple of ₹10.

Ans. **Liquidator's Final Statement of Account**

Receipts		**₹**	**Payments**		**₹**
Sundry Assets realized:			Liquidator's Remuneration (Working note)		25,020
Bank Balance		2,40,000	Liquidation Expenses (given)		3,600
Plant		5,90,000	Secured Creditors:		
Debtors (1,70,000 X 80%)	1,36,000		6% Mortgage Loan	4,60,000	
Less: Realization Expenses	(3,700)		Add: Interest (4,60,000 × 6% × 6/12)	13,800	4,73,800
		1,32,300			
Stock (7,20,000× 90%)		6,48,000	Unsecured Creditors:		
			Creditors (4,42,000 X 95%)	4,19,900	
			Outstanding Expenses	40,000	4,59,900
			Preference Shareholders:		
			Capital	2,50,000	
			Dividend (for 1 year @ 9%)	22,500	2,72,500
			Equity Shareholders: (Working note)		
			Fully Paid Shares (4,000×71.935)	2,87,740	
			Partly Paid Shares (4,000×21.935)	87,740	3,75,480
		16,10,300			**16,10,300**

Working Note:

Computation of Liquidations' Remuneration and Payment to Equity Shareholders

		₹
(a)	Total of Receipts (from above account)	16,10,300
(b)	Total Payments before Final Payment to Members (excluding Preference Capital) and Liquidator's Remuneration (3,600 + 4,73,800 + 4,59,900 + Pref Dividend 22,500)	(9,59,800)
(c)	Balance left for Liquidator's Remuneration, Pref. Capital and Equity Shareholders	6,50,500S
(d)	Liquidator's Remuneration (6,50,500 × 4/104 = ₹25,020 or ₹20,000 whichever is higher)	(25,020)
(e)	Refund of Capital to Preference Shareholders	(2,50,000)
(f)	Balance money before Notional Call	3,75,480
(g)	Notional Call on 4,000 Partly Paid Shares at ₹ 50 each (to make all Shares ₹100 paid up)	2,00,000
(h)	Surplus Cash balance after Notional Call	5,75,480
(i)	Number of Equity Shares deemed fully paid (4,000 + 4,000)	8,000
(j)	Hence, Refund on every ₹100 paid up Share (**h ÷ i) =** ₹5,75,480 ÷8000	₹71.935
(k)	Loss per ₹100 paid up Equity Share = Paid Up Value ₹100 – Refund as above ₹71.935	28.065
(l)	Refund per ₹ 50 Partly Paid-Up Equity Share = Paid Up Value ₹50 - loss as above ₹ 28.065	21.935

Q-19 The position of Neha Ltd. on its liquidation is as under:

5,000, 10% Preference Shares of ₹ 100 each ₹ 60 paid up

2,000, Equity shares of ₹ 75 each, ₹ 50 paid up

Unsecured Creditors ₹ 99,000

Liquidation Expenses ₹ 1,000

Liquidator is entitled to a commission of 2% on the amount realized from calls made on contributories

You are required to prepare Liquidator's Final Statement of Account if the total assets realized ₹ 3,80,400.

Ans. **Liquidator's Final Statement of Account**

Recipts	₹	**Payment**	₹
Assets realized	3,80,400	Liquidation Expenses	1,000
Call on contributories: 2,000 Equity Shares @ ₹ 10 per share (W.N.)	20,000	Liquidator's Remuneration	400
		Unsecured Creditors	99,000
		Preference Shareholders	3,00,000
	4,00,400		**4,00,400**

Working Notes:

(i)

Calculation of Shortage of funds	₹
Total Amount Available	3,80,400
Less: liquidation Expenses	(1,000)
Balance	3,79,400
Less: Unsecured Creditors	(99,000)
Balance	2,80,400
Less: Pref. Shareholders	(3,00,000)
Shortage of Funds	19,600

(ii) Calculation of funds required to meet shortage and commission payable on Calls to be made (to be called from equity shareholders)

$$\text{Shortage of funds} \times \frac{100}{100 - \text{Rate of Commission}} = ₹\ 19{,}600 \times \frac{100}{100 - 2}$$

$$\frac{₹\ 19{,}600 \times 100}{98} = ₹\ 20{,}000$$

(iii) Uncalled Capital @ ₹ 25 on 2,000 shares = ₹ 50,000

(iv) Amount of Calls to be made from equity shareholders (least of funds required and uncalled capital) i.e. ₹ 20,000 i.e. ₹ 10 per Share

(v) Commission on Call = ₹ 20,000 x 2/100 = ₹ 400

Q-20 W, X, Y and Z hold equity share capital in the proportion of 40:30:10:20. A, B, C and D hold preference share capital in the proportion of 30:40:20:10. You are required to find their voting rights in case of resolution of winding up of the company if the paid up capital of the company is Rs. 40 Lakh and Preference share capital is Rs. 20 Lakh.

Ans. W, X, Y and Z hold Equity capital is held by in the proportion of 40:30:10:20 and A, B, C and D hold preference share capital in the proportion of 30:40:20:10. As the paid up equity share capital of the company is Rs. 40 Lakhs and Preference share capital is Rs. 20 Lakh (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be

W	=	2/3X40/100	=	4/15
X	=	2/3X30/100	=	3/15
Y	=	2/3X10/100	=	1/15
Z	=	2/3X20/100	=	2/15
A	=	1/3X30/100	=	1/10
B	=	1/3X40/100	=	2/15
C	=	1/3X20/100	=	1/15
D	=	1/3X10/100	=	1/30

Q-21

(i) Explain the meaning of Equity Shares with Differential Rights.
Can Preference Shares be also issued with differential rights?

(ii) In Jugnu Limited A, B, C and D hold equity share capital in the proportion of 30:30:30: 10 and M, N, O and P hold preference share capital in proportion of 40:20:30:10.

You are required to calculate their voting rights in case of resolution of winding up of the company, if the paid up Equity Share Capital of the company is ₹100 Lakhs and Preference Share Capital is ₹50 Lakhs.

Ans. (i) As per the Companies Act 2013, companies can issue equity shares with differential rights subject to the fulfilment of certain conditions. Companies (Share Capital and Debentures) Rules, 2014 deal with equity shares with differential rights. Differentiation can be done by giving a superior dividend / Superior voting right / diluted voting right to a class of equity shareholders.

Preference shares are not issued with differential rights. It is only the equity shares, which are issued.

(ii) In the given case, the relative weight in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be

Relative weights				Voting Power	
A	=	2/3X30/100	=	2/10	20%
B	=	2/3X30/100	=	2/10	20%
C	=	2/3X30/100	=	2/10	20%
D	=	2/3X10/100	=	1/15	6.67%
M	=	1/3X40/100	=	2/15	13.33%
N	=	1/3X20/100	=	1/15	6.67%
O	=	1/3X30/100	=	1/10	10%
P	=	1/3X10/100	=	1/30	3.33%

Q-22 The different categories of shareholders of Earth Limited, who went into liquidation on 1st April, 2021 are as follows:

(i) 32,000 Equity shares of ₹100 each, ₹ 80 paid up

(ii) 48,000 Equity shares of ₹ 100 each, ₹ 35 paid up

(iii) 12,80,000 Equity shares of ₹ 10 each, ₹ 7 paid up.

You are required to distribute the surplus money among different categories of shareholders, if the surplus available with Liquidator after discharging all the liabilities is ₹ 32,00,000.

Ans.

Particulars	**I**	**II**	**III**	**Total (₹)**
No. of shares Equity	32,000	48,000	12,80,000	13,60,000
share capital	32,00,000	48,00,000	128,00,000	208,00,000
Paid up share Capital (A)	(@₹ 100)	(@₹ 100)	(@₹ 10)	
Loss due to Liquidation (B)	25,60,000	16,80,000	89,60,000	132,00,000
(₹ 100,00,000 in 2:3:8)				
Surplus/ (deficiency) amount distributed among different categories of shareholders				
(A) - (B)	10,21,538	(6,27,692)	28,06,154	32,00,000

Loss due to Liquidation ₹ 100,00,000 will be distributed in ratio in 2:3:8

Note: Shareholders of category I and III will get surplus amount, while category II shareholders will pay ₹ 6,27,692.

Alternative Answer

Particulars	I	II	III
No. of shares (A)	32,000	48,000	12,80,000
Nominal value per share	₹ 100	₹ 100	₹ 10
Paid up value per share (B)	80	35	7
Loss per share due to Liquidation (C)	48.08	48.08	4.808
Surplus/ Deficiency amount distributed among different categories of shareholders (A) x [(B) - (C)]	10,21,440	(6,27,840)	28,05,760

Calculation of loss per share

Total Paid up Share Capital	= ₹ 1,32,00,000
Surplus	= ₹ 32,00,000
Loss to Shareholders	= ₹ 1,00,00,000
No. Shares =	= 2,08,000 [32,000 + 48,000 + (12,80,000 x 10/100)]
Loss per Share=	= ₹ 48.08

Q-23 Equity Capital is held by Anu, Adi and Arun in the proportion of 30: 30: 40 and Preference Share Capital is held by Sonu, Shri and Sanaya in the proportion of 40: 10: 50. If the paid up Equity Share Capital of the company is ₹ 60 lakhs and Preference Share Capital is ₹ 30 lakhs, find the proportion and percentage of their voting right in case of resolution of winding up of the company.

Ans. Equity capital is held by Anu, Adi and Arun in the proportion of 30:30:40. Sonu, Shri and Sanaya hold preference share capital in the proportion of 40:10:50. If the paid up equity share capital of the company is ₹ 60 lakhs and Preference share capital is ₹ 30 Lakh, then relative weight in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3.

The respective voting right of various shareholders will be:

Shareholders		Relative weights	Voting Power
Anu	2/3X30/100	3/15	20.00%
Adi	2/3X30/100	3/15	20.00%
Arun	2/3 X40/100	4/15	26.67%
Sonu	1/3X40/100	4/30	13.33%
Shri	1/3X10/100	1/30	3.33%
Sanaya	1/3X50/100	5/30	16.67%

Q-24 **Answer any four of the following:**

Under what circumstances an LLP can be wound up by the tribunal?

Ans. An LLP may be wound up by the Tribunal in the following circumstances:

- If the LLP decides that it should be wound up by the Tribunal;
- If for a period of more than six months, the number of partners of the LLP is reduced below two;
- If the LLP is unable to pay its debts;
- If the LLP has acted against the interests of the integrity and sovereignty of India, the security of the state or public order;
- If the LLP has defaulted in the filing of the Statement of Account and Solvency with the Registrar for five consecutive financial years;
- If the Tribunal is of the opinion that it is just and equitable that the LLP be wound up.

Q-25 Beekey Limited is being wound up by the tribunal. All the assets of the company have been charged in favour of the company's bankers to whom the company owes ₹ 2.50 crores.

The company owes following amounts to others:

Dues to workers	- ₹ 62,50,000
Taxes payable to Government	- ₹ 15,00,000
Unsecured creditors	- ₹ 30,00,000

You are required to compute with reference to the provisions of the Companies Act, 2013, the amount each kind of creditors is likely to get if the amount realized by the official liquidator from the secured assets and available for distribution among creditors is only ₹ 2,00,00,000.

Ans. Section 326 of the Companies Act, 2013 is talks about the overriding preferential payments to be made from the amount realized from the assets to be distributed to various kind of creditors. According to the proviso given in the section 326 the security of every secured creditor should be deemed to be subject to a pari passu change in favour of the workman to the extent of their portion.

$$\text{Workman's Share to Secured Asset} = \frac{\text{Amount Realized X Workman's Dues}}{\text{Workman's Dues} + \text{Secured Loa}}$$

$$\text{Workman's Share to Secured Asset} = \frac{2,00,00,000 \times 62,50,000}{62,50,000 + 2,50,00,000}$$

= 2,00,00,000 X 1/5

Workmen's share to Secured Assets = ₹ 40,00,000

Amount available to secured creditor is ₹ 200 Lakhs – 40 Lakhs = 160 Lakhs

Hence, no amount is available for payment of government dues and unsecured creditors.

Q-26 A, B, C and D hold Equity Share Capital in the proportion of 40:30:20:10 and P, Q, R and S hold Preference Share Capital in the proportion of 30:40:20:10 in Alpha Ltd. If the paid up Equity Share Capital of Alpha Ltd. is ₹ 75 lacs and the Preference Share Capital is ₹ 25 lacs, find their voting rights in the case of resolution of winding up of the company.

Ans. A, B, C and D hold Equity capital is held by in the proportion of 40:30:20:10 and P, Q, R and S hold preference share capital in the proportion of 30:40:20:10. As the paid-up equity share capital of the company is ₹ 75 Lakhs and Preference share capital is ₹ 25 Lakh (3:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 3/4 and 1/4.

The respective voting right of various shareholders will be:

A	=	3/4X40/100	=	.3 (30%)
B	=	3/4X30/100	=	.225 (22.5%)
C	=	3/4X20/100	=	.15 (15%)
D	=	3/4X10/100	=	.075 (7.5%)
P	=	1/4X30/100	=	.075 (7.5%)
Q	=	1/4X40/100	=	0.1 (10%)
R	=	1/4X20/100	=	.05 (5%)
S	=	1/4X10/100	=	.025 (2.5%)

Q-27 What do you mean by equity shares with differential rights. Explain in brief

Ans.

(a) Equity shares with Differential Rights means the share with dissimilar rights as to dividend, voting or otherwise.

(b) E, F, G and H hold Equity Capital in Alpha Co. in the proportion of 30:30:20:20. S, T, U and V hold preference share capital in the proportion of 40:30:10:20. If the paid up capital of the company is ₹ 120 Lakh and Preference share capital is ₹ 60 Lakh, You are required to calculate their voting rights in case of resolution of winding up of the company.

(b) E, F, G and H hold Equity capital is held by in the proportion of 30:30:20:20 and S,T,U and V hold preference share capital in the proportion of 40:30:10:20. As the paid up equity share capital of the company is ₹120 Lakhs and Preference share capital is ₹ 60 Lakhs (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be

E	=	2/3X30/100	=	3/15
F	=	2/3X30/100	=	3/15
G	=	2/3X20/100	=	2/15
H	=	2/3X20/100	=	2/15
S	=	1/3X40/100	=	2/15
T	=	1/3X30/100	=	1/10
U	=	1/3X10/100	=	1/30
V	=	1/3X20/100	=	1/15

Q-28 The Balance Sheet of Cloud Ltd., as at 31st March, 2021, being the date of voluntary winding up is as under:

			Particulars	Note	Amount (₹)
I			**Equity and Liabilities**		
	1		**Shareholders' Funds:**		
		(a)	Share Capital	1	21,00,000
		(b)	Reserve and Surplus	**2**	4,00,000
	2		**Non-Current Liabilities:**		
		(a)	Long Term Borrowings	**3**	4,20,000
	3		**Current Liabilities:**		
		(a)	Short Term Borrowings	4	9,70,000
		(b)	Trade Payables		12,00,000
		(c)	Other Current Liabilities	5	2,10,000
			Total		53,00,000
II			**Assets**		
	1		**Non-Current Assets:**		
		(a)	Property, Plant and Equipment	**6**	26,00,000

2	**Current Assets:**	
(a)	Inventories	6,50,000
(b)	Trade Receivables	20,50,000
(c)	Cash and Cash Equivalents	-
	Total	53,00,000

Notes to Accounts:

	Particulars	Amount (₹)
1.	**Share Capital**	
	Authorized:	
	10,000 Equity Shares of ₹ 100 each	10,00,000
	10,000 Equity Shares of ₹ 100 each	10,00,000
	10,000, 10% Cumulative Preference Shares of ₹ 100 each	10,00,000
	Issued, Subscribed & Paid up:	
	10,000 Equity Shares of ₹ 100 each, ₹ 60 paid up.	6,00,000
	10,000 Equity Shares of ₹ 100 each, ₹ 50 paid up.	5,00,000
	10,000, 10% Cumulative Preference Shares of ₹ 100 each, fully paid up.	10,00,000
	Total	21,00,000
2.	**Reserve and Surplus**	
	(a) Securities Premium	15,00,000
	(b) Profit & Loss A/c (Dr. balance)	(11,00,000)
		4,00,000
3.	**Long Term Borrowings**	
	10% Debentures	4,20,000
4.	**Short Term borrowings**	
	Bank Overdraft (unsecured)	9,70,000
5.	**Other Current Liabilities**	
	Preferential Creditors	2,10,000
6.	**Property, Plant and Equipment**	
	(a) Land and Buildings	10,40,000
	(b) Plant and Machinery	15,60,000
		26,00,000

Preference Dividend is in arrears for three years (upto 31st March, 2021). The assets realized as follows:

Land & Building	₹ 12,40,000	Plant & Machinery	₹ 14,20,000
Inventory	₹ 6,20,000	Trade receivables	₹ 13,20,000

Expenses of Liquidation are ₹ 1,72,000. The Remuneration of the Liquidator is 2% of the realization of assets. Income Tax Payable is ₹ 1,34,000. Interest on debentures for the year ended 31st March, 2021 has not been considered in the given balance sheet and is also to be paid.

Prepare the Liquidator's Final Statement of Account.

Ans. **Liquidator's Final Statement of Account**

Receipts		₹	Payments	₹
To Sundry Assets Realized:			By Liquidator's Remuneration (46,00,000 × 2%)	92,000
Trade receivable	13,20,000		By Liquidation Expenses	1,72,000
Inventory	6,20,000		By Preferential Creditors:	
Land & Building	12,40,000		As given in Balance Sheet	2,10,000
Plant & Machinery	14,20,000	46,00,000	income Tax Liability (given)	1,34,000
To Calls from shareholders:			By Debenture holders:	
Call money on 10,000 Equity shares, ₹ 50 paid up at ₹ 2 per Share		20,000	Face Value of Debentures	4,20,000
			Debenture Interest (for 1 year at 10%)	42,000
			By Unsecured Creditors:	
			Bank Overdraft	9,70,000
			Trade payables	12,00,000
			By Preference Shareholders:	
			Preference Capital	10,00,00
			Arrears of Dividend (10,00,000 × 10% × 3 years)	3,00,000
			By Equity Shareholders: refund on 10,000 Shares ₹ 60 paid up, at ₹ 8 per Share	80,000
Total		46,20,000	Total	46,20,000

Working Note:

Calls from Holders of Partly Paid Shares

	Particulars	₹
(a)	Total of Receipts before considering Call Money (from the above account Dr. Side)	46,00,000
(b)	Total Payments before final payments to Equity Shares (92,000 +1,72,000 + 4,20,000 + 42,000 + 2,10,000 + 1,34,000 + 9,70,000 +12,00,000 + 10,00,000 + 3,00,000)	45,40,000
(c)	Surplus from above Calls made on Equity Shares (a-b)	60,000
(d)	Notional Call on 10,000 Partly Paid Shares at ₹ 10 each (to makeall Shares ₹ 60 Paid up)	1,00,000
(e)	Surplus Cash Balance after Notional Call (c + d)	1,60,000
(f)	Number of Shares deemed to be paid at ₹ 60 per Share (10,000 +10,000)	20,000
(g)	Hence, Refund on every ₹ 60 Paid up Share (e ÷ f) = ₹ 1,60,000 ÷20,000 Shares	₹ 8.00
(h)	So, Required Call on ₹ 50 Paid up Share (₹ 10 Notional Call – ₹ 8 Refund)	₹ 2

Q-29 Answer any four of the following:

(a) A liquidator is entitled to receive remuneration at 3% on the assets realized and 4% on the payment made to creditors and company's bankers. The assets were realized for ₹ 80,00,000. All the assets of the company have been charged to the company's bankers to whom the company owes ₹ 1,00,00,000. The company owes following amounts to others:

Due to workers	₹25,00,000
Other Preferential creditors	₹ 20,00,000
Unsecured creditors	₹ 10,50,000

With reference to the provisions of the Companies Act 2013, you are required to calculate the amount payable to:

1 Workers;
2. Other Preferential creditors;
3. Unsecured creditors;
4. Liquidator for remuneration and
5. Company's bankers.

(b) P, Q, R and S hold equity share capital in the proportion of 10:40:20:30. K, L, M and N hold preference share capital in the proportion of 20:10:40:30. If the paid up equity share capital of the company is ₹ 60 lakhs and Preference Share Capital is ₹ 30 lakhs, find their voting rights in case of resolution of winding up of the company.

Ans. (a) Section 326 of the Companies Act, 2013 is talks about the overriding preferential payments to be made from the amount realized from the assets to be distributed to various kind of creditors. According to the proviso given in the section 326 the security of every secured creditor should be deemed to be subject to a pari -passu charge in favour of the workman to the extent of their portion.

$$\text{Workman's Share to Secured Asset} = \frac{\text{Amount Realized* x Workman's Dues}}{\text{Workman's Dues + Secured Loan}}$$

Workmen share to secured assets = ' 80,00,000 x (25,00,000/125,00,000) = ' 80,00,000 x 1/5 i.e. ₹ 16,00,000

• Face value ₹ 10.

Amount available to secured creditor is ₹ 80,00,000 – ₹ 16,00,000 = ₹ 64,00,000

Amount payable to workers ₹ 16,00,000. Amount payable to Company's bankers = ₹ 64,00,000.

Hence, no amount is available for payment of other preferential creditors and unsecured creditors.

Calculation of Total Remuneration payable to Liquidator

		Amount in ₹
3% on Assets realized	(80,00,000 x 3%)	2,40,000
4% on payment made to company's Banker (Refer W.N)		2,36,923
Total Remuneration payable to Liquidator		4,76,923

Working Note:

Liquidator's remuneration on payment to Company's banker:

Cash available after liquidator remuneration on assets realized

= ₹ 80,00,000 – ₹ 16,00,000 - 2,40,000= ₹ 61,60,000 X4/104= ₹ 2,36,923

Thus,

1. Amount payable to workers ₹ 16,00,000.
2. No amount is available for payment of other preferential creditors

3. No amount is available for payment of unsecured creditors.
4. Liquidator for remuneration ₹ 4,76,923
5. Amount payable to Company's bankers = ₹ 59,23,077 (₹ 61,60,000 less ₹ 2,36,923).

Note: The answer given above assumes that the workers are given the full amount due towards them without any deduction for Liquidators' remuneration and amount realized from sale of asset has been considered before Liquidator's remuneration. Accordingly, liquidator's remuneration has been considered for payment to banker only in the given answer. Hence, 4% remuneration has not been provided on the payment to workers as the question states that the liquidator is entitled to receive remuneration at 4% on payment made to banker and creditors. Moreover, workers are not considered as creditors in the given answer.

Alternative answer is possible when Liquidators' remuneration for asset realization is considered for payment to Workmen. In this case, two alternative answers will be possible which can be given as follows:

Alternative 1 -If Workmen are not treated as creditors for the purpose of Liquidator's remuneration (as the question states that the liquidator is entitled to receive remuneration at 4% on payment made to banker and creditors)

Workman's Share to Secured Asset = Amount Realized X Workman's Dues / Workman's Dues + Secured Loan

Workmen share to secured assets = ₹ 80,00,000x (25,00,000/125,00,000)

= ₹ 80,00,000x1/5 i.e. ₹ 16,00,000

Banker's share to secured assets is ₹ 80,00,000 – 16,00,000 = 64,00,000

Thus the ratio of workmen share and bankers share is 1:4. (64,00,000/16,00,000)

Calculation of Total Remuneration payable to Liquidator

	Amount in ₹
3% on Assets realized (80,00,000 x 3%)	2,40,000
4% on payment made to company's Banker (Refer W.N)	2,38,769
Total Remuneration payable to Liquidator	**4,78,769**

Working Note:

Liquidator's remuneration on payment to Company's banker

Cash available after liquidator remuneration on assets realized

= ₹ 80,00,000 – ₹ 2,40,000 = ₹ 77,60,000 which will be paid to workers and Company's banker in ratio of 1:4.

Cash balance is available Company's banker = ₹ 77,60,000 less ₹ 15,52,000 = 62,08,000 x 4/104= ₹ 2,38,769.

Thus,

1. Amount payable to workers ₹ 15,52,000 (77,60,000 x 1/5).
2. No amount is available for payment of other preferential creditors
3. No amount is available for payment of unsecured creditors.
4. Liquidator for remuneration ₹ 4,78,769
5. Amount payable to Company's bankers = ₹ 59,69,231 (62,08,000 less 2,38,769).

Alternative 2 - If Workmen are treated as creditors for the purpose of Liquidator's remuneration

Ratio of workmen share and bankers share is 1:4. (64,00,000/16,00,000) as computed in Alternative 1 above.

Calculation of Total Remuneration payable to Liquidator

		Amount in ₹
3% on Assets realized	(80,00,000 x 3%)	2,40,000
4% on payment made to company's Banker (Refer W.N)		2,98,462
Total Remuneration payable to Liquidator		5,38,462

Working Note:

Liquidator's remuneration on payment to Company's banker and workmen:

Cash available after liquidator remuneration on assets realized

= ₹ 80,00,000 – ₹ 2,40,000 = ₹ 77,60,000

Liquidator remuneration = ₹ 77,60,000 X 4/104 = ₹ 2,98,462 (rounded off)

Cash balance is available for workers and Company's banker = ₹ 77,60,000 less ₹ 2,98,462 = ₹ 74,61,538.

The amount of ₹ 74,61,538 will be paid to workers and Company's banker in ratio of 1:4. Thus

1. Amount payable to workers ₹ 14,92,308 (rounded off) (74,61,538 x 1/5).
2. No amount is available for payment of other preferential creditors
3. No amount is available for payment of unsecured creditors.
4. Liquidator for remuneration ₹ 5,38,462
5. Amount payable to Company's bankers = ₹ 59,69,230 (rounded off) (74,61,538 x 4/5).

(b) P, Q, R and S hold Equity capital is held by in the proportion of 10:40:20:30 and K, L, M and N hold preference share capital in the proportion of 20:10:40:30. As the paid up equity share capital of the company is ' 60 Lakhs and Preference share capital is ₹ 30 Lakh (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3.

The respective voting right of various shareholders will be

P	=	2/3X10/100	=	1/15
Q	=	2/3X40/100	=	4/15
R	=	2/3X20/100	=	2/15
S	=	2/3X30/100	=	3/15
K	=	1/3X20/100	=	1/15
L	=	1/3X10/100	=	1/30
M	=	1/3X40/100	=	2/15
N	=	1/3X30/100	=	1/10

Hence, their relative weights are 1/15 : 4/15 : 2/15 : 3/15: 1/15 : 1/30 : 2/15 : 1/10 or 2:8:4:6:2:1:4:3.

Their respectively voting power is P (6.67%), Q (26.67%), R (13.33%), S (20%), K (6.67%), L (3.33%), M (13.33%) and N (10%).

Q-30 A machine was given on 3 years operating lease by a dealer of the machine for equal annual lease rentals to yield 30% profit margin on cost of ₹ 2,25,000. Economic life of the machine is 5 years and output from the machine is estimated as 60,000 units, 75,000 units, 90,000 units, 1,20,000 units and 1,05,000 units consecutively for 5 years. Straight line depreciation in proportion of output is considered appropriate. You are required to compute the following as per AS-19.

(i) Annual Lease Rent

(ii) Lease Rent income to be recognized in each operating year and

(iii) Depreciation for 3 years lease

Ans.(i) Annual lease rent

Total lease rent

= 130% of ₹ 2,25,000 „e Output during lease period/ Total output

= 130% of ₹ 2,25,000 x (60,000 +75,000+ 90,000)/(60,000 + 75,000 + 90,000 + 1,20,000 + 1,05,000)

= 2,92,500 x 2,25,000 units/4,50,000 units = ₹ 1,46,250

Annual lease rent = ₹ 1,46,250 / 3 = ₹ 48,750

(ii) Lease rent Income to be recognized in each operating year

Total lease rent should be recognized as income in proportion of output during lease period, i.e. in the proportion of 60,000 : 75,000 : 90,000 or 4:5:6

Hence income recognized in years 1, 2 and 3 will be as:

Year 1 ₹ 39,000,

Year 2 ₹ 48,750 and

Year 3 ₹ 58,500.

(iii) Depreciation for three years of lease

Since depreciation in proportion of output is considered appropriate, the depreciable amount ₹ 2,25,000 should be allocated over useful life 5 years in proportion of output, i.e. in proportion of 60 :75: 90 : 120 : 105 .

Depreciation for year 1 is ‘ 30,000, year 2 = 37,500 and year 3 = 45,000.

Q-31 The following information relates to Surya Ltd. Co. which is in the hands of the liquidator:

Liabilities	₹
Share Capital:	
1,000, 6% Preference Shares of ₹ 100 each, fully paid	1,00,000
2,000 Equity shares of ₹ 100 each, fully paid	2,00,000
2,000 Equity shares of ₹ 100 each ₹ 75 paid up	1,50,000
Loan from bank (on security of stock)	1,00,000
Trade Payables	3,50,000
Property, Plant and Equipment	2,00,000
Inventory	1,20,000
Book Debts	2,40,000
Cash in hand	40,000
Profit and loss A/c (Dr. Balance)	3,00,000

The assets realized the following amounts (after all costs of realization and liquidator’s commission amounting to ₹ 5,000 paid out of cash in hand):

	₹
Property, Plant and Equipment	1,68,000
Inventory	1,10,000
Trade Receivables	2,30,000

Calls on partly paid shares were made but the amounts due on 200 shares were found to be irrecoverable.

You are required to prepare Liquidator’s Final Statement of Receipts and Payments .

Ans. **Liquidator's Final Statement of Receipts and Payments**

		₹	₹			₹
To	Cash in hand		40,000	By	Liquidator's remuneration and expenses	5,000
To	Assets realised:					
	PPE		1,68,000	By	Trade Payables	3,50,000
	Inventory			By	Preference shareholders	1,00,000
	(1,10,000 – 1,00,000)	10,000		By	Equity shareholders @ ₹ 10 on 2,000 shares	20,000
	Book debts	2,30,000	4,08,000			
To	Cash - proceeds of call on 1,800 equity shares @ ₹ 15*		27,000			
			4,75,000			**4,75,000**

Working Note:

Return per equity share

	₹
Cash available before paying preference shareholders (₹ 4,48,000 – ₹ 3,55,000)	93,000
Add: Notional calls 1,800 shares (2,000-200) × ₹ 25	45,000
	1,38,000
Less: Preference share capital	(1,00,000)
Available for equity shareholders	38,000

Return per share= $\frac{₹\ 38,000}{3,800\ (4,000-200)} = ₹\ 10$

and Loss per Equity Share ₹ (100-10) = ₹ 90

*Calls to be made @ ₹ 15 per share (₹ 90-75) on 1,800 shares.

Q-32 ABC Limited went into voluntary liquidation. Details are as follows :

1,000 - 10% Preference Shares of ₹ 100 each fully paid up

Class A - 1,200 Equity shares of ₹ 100 each (₹ 80 paid up)

Class B - 800 Equity shares of ₹ 100 each (₹ 65 paid up)

Assets realized ₹ 3,50,000 and liquidation expenses is ₹ 8,000. Company has secured Bank Loan of ₹ 60,000 and salary of 3 clerks for 3 months at a rate of ₹ 500 per month are outstanding.

Creditors are ₹ 70,000.

Calculate amount receivable from / or returnable to equity shareholders.

Ans. **Amount receivable from/returnable to Equity Shareholders**

Total equity capital - paid up	₹ 1,48,000
Less: Balance available after payment to unsecured and preference shares (3,50,000 — 2,42,500)	₹ (1,07,500)

Loss to be born by 2,000 equity shares	₹ 40,500
Loss per share	₹ 20.25
Hence,	
Amount refunded on ₹ 65 paid share	65 - 20.25 per share = ₹ 44.75
Amount refunded on ₹ 80 paid share	80 - 20.25 per share= ₹ 59.75

Working note:

Liquidator's Statement of Account

		₹			₹
To	Assets realized	3,50,000	By	Liquidation Expenses	8,000
			By	Secured bank loan	60,000
			By	Preferential creditors (salary of 3 clerks at ₹ 500 per month for three months)	4,500
			By	Unsecured creditors	70,000
			By	Preference Shareholders	1,00,000
					2,42,500
			By	Equity Shareholders	
				₹ 59.75 on 1,200 shares	71,700
				₹ 44.75 on 800 shares	35,800
		3,50,000			**3,50,000**

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NOTES

CHAPTER-8

FINANCIAL STATEMENTS OF BANKING COMPANIES

Q-1 Anmol Bank Ltd. has a balance of ₹ 40 crores in "Rebate on bills discounted" account as on 31st March, 2018. The Bank provides you the following information:

(i) During the financial year ending 31st March, 2019 Anmol Bank Ltd. discounted bills of exchange of ₹ 5,000 crores charging interest @ 14% and the average period of discount being 146 days.

(ii) Bills of exchange of ₹ 500 crores were due for realization from the acceptors/customers after 31st March, 2019. The average period of outstanding after 31st March, 2019 being 73 days. These bills of exchange of ₹ 500 crores were discounted charging interest @ 14% p.a.

You are requested to give the necessary Journal Entries in the books of Anmol Bank Ltd. for the above transactions.

Ans. **In the books of Anmol bank Ltd.**

Journal Entries

Particulars		Debit	₹ in crores Credit
Rebate on bills discounted A/c	Dr.	40	
To Discount on bills A/c			40
(Being the transfer of opening balance in 'Rebate on bills discounted A/c' to 'Discount on bills A/c')			
Bills purchased and discounted A/c	Dr.	5,000	
To Discount on bills A/c			280
To Clients A/c			4,720
(Being the discounting of bills of exchange during the year)			
Discount on bills A/c	Dr.	14	
To Rebate on bills discounted A/c			14
(Being the unexpired portion of discount in respect of the discounted bills of exchange carried forward)			
Discount on bills A/c	Dr.	306	
To Profit and Loss A/c			306
(Being the amount of income for the year from discounting of bills of exchange transferred to Profit and loss A/c)			

Working Notes:

1. Discount received on the bills discounted during the year
   ₹ 5,000 crores x 14/100 x 146/365 = ₹ 280 crores
2. Calculation of rebate on bill discounted
   ₹ 500 crores x 14/100 x 73/365 = ₹14 crores
3. Income from bills discounted transferred to Profit and Loss A/c would be calculated by preparing Discount on bills A/c.

Discount on bills A/c

Date	Particulars	Amount	Date	Particulars	' in crores Amount
31.3.2019	To Rebate on bills discounted	14	1.4.2018	By Rebate on bills discounted b/d	40
"	To Profit and Loss A/c (Bal. Fig.)	306	2018-19	By Bills purchased and discounted	280
		320			**320**

Q-2 Omega Bank Statement of interest on advances in respect of Performing assets and NonPerforming Assets are as follows:- (in lakhs)

	Performing Assets	Non-Performing Assets		
	Interest earned	Interest received	Interest earned	Interest received
Cash credits and overdrafts	1800	1060	450	70
Term Loan	480	320	300	40
Bills purchased and discounted	700	550	350	36

Find out the income to be recognized for the year ended 31st March, 20X1.

OR

A fund purchased 10,000 debentures of a company on June 1, 2018 for Rs. 10.7 lakh and further 5,000 debentures on Nov 1, 2018 for Rs. 5.45 lakh. The debentures carry fixed annual coupon of 12%, payable on every 31 March and 30 September. On Feb 28, 2019 the fund sold 6,000 of these debentures for Rs. 6.78 lakh. Nominal value per debenture is Rs. 100.

Show Investment in Debentures A/c in books of the fund.

Ans. Interest on performing assets should be recognised on accrual basis, but interest on NPA should be recognised on cash basis.

			Rs. in lakhs
Interest on cash credits and overdraft :	(1800+70)	=	1,870
Interest on Term Loan	(480+40)	=	520
Income from bills purchased and discounted :	(700+36)	=	736
			3,126

OR

Investment in Debentures A/c

		Rs. Lakh			*Rs.Lakh*
June 1, 2018	To Bank	10.70	June 1, 2018	By InterestRecoverable(Note 1)	0.20
Nov 1, 2018	To Bank	5.45	Nov 1, 2018	By InterestRecoverable(Note 2)	0.05
Feb 28, 2019	To InterestRecoverable (Note 3)	0.30	Feb 28, 2019	By Bank	6.78
Feb 28, 2019	To Profit ondisposal (Note 4)	0.12	Mar 31, 2019	By Balance c/d	9.54
		16.57			**16.57**

Working Notes:

1. 10,000 x 100 x 12/100 x 2/12 = Rs. 0.20 Lakhs
2. 5,000 x 100 x 12/100 x 1/12 = Rs. 0.05 Lakhs
3. 6,000 x 100 x 12/100 x 5/12 = Rs. 0.30 Lakhs
4. Cost of investments (per unit) = [(10,70,000 -20,000)+(5,45,000– 5,000)]/15,000 units

   = [10,50,000+ 5,40,000]/15,000 = Rs. 106

   Cost of investments sold = Rs. 106 x 6,000 = Rs. 6,36,000

   Sale proceeds = Rs. 6,78,000 - Rs. 30,000(interest) = Rs. 6,48,000

   Profit = Rs. 6,48,000 - Rs. 6,36,000 = Rs. 12,000

Q-3 As on 31st March 2016, Strong Bank Ltd. has a balance of ₹ 27 crores in "rebate on bills discounted" account. The bank provides you the following further information:

(1) During the financial year ending 31st March 2017, Strong Bank Ltd. discounted bills of exchange of ₹ 4,000 crores charging interest @ 15% p.a. and the average period of discount being 146 days.

(2) Bills of exchange of ₹ 600 crores were due for realization from the acceptors/customers after 31st March 2017, the average period outstanding after 31st March 2017, being 73 days.

You are required to pass necessary journal entries in the books of Strong Bank Ltd. for the above transactions.

Ans. **In the books of Strong Bank Ltd.**

Journal Entries

Particulars		Debit (₹)	Credit (₹)
Rebate on bills discounted A/c	Dr.	27	
To Discount on bills A/c			27
(Being the transfer of opening balance in 'Rebate on bills discounted A/c' to 'Discount on bills A/c')			
Bills purchased and discounted A/c	Dr.	4,000	
To Discount on bills A/c			240
To Clients A/c			3,760
(Being the discounting of bills of exchange during the year)			
Discount on bills A/c	Dr.	18	
To Rebate on bills discounted A/c			18
(Being the unexpired portion of discount in respect of the discounted bills of exchange carried forward)			
Discount on bills A/c	Dr.	249	
To Profit and Loss A/c			249
(Being the amount of income for the year from discounting of bills of exchange transferred to Profit and loss A/c)			

Working Notes:

1. Discount received on the bills discounted during the year

   ₹ 4,000 crores x $\frac{15}{100} \times \frac{146}{365}$ = ₹ 240 crores

2. Calculation of rebate on bill discounted

   ₹ 600 crores x $\frac{15}{100} \times \frac{73}{365}$ = ₹18 crores

   (It is assumed that discounting rate of 15% is used for the bill of ₹ 600 crores also)

3. Income from bills discounted transferred to Profit and Loss A/c would be calculated by preparing Discount on bills A/c

Discount on bills A/c

Date	Particulars	Amount	Date	Particulars	₹ in crores Amount
31 March 2017	To Rebate on bills discounted	18	1st April, 2016	By Rebate on bills discounted b/f	27
”	To Profit and Loss A/c (Bal. Fig.)	249	2016-17	By Bills purchased and discounted	240
		267			267

Q-4 The following are the figures extracted from the books of TOP Bank Limited as on 31.3.2017.

	₹
Interest and discount received	59,29,180
Interest paid on deposits	32,59,920
Issued and subscribed capital	16,00,000
Salaries and allowances	3,20,000
Directors fee and allowances	48,000
Rent and taxes paid	1,44,000
Postage and telegrams	96,460
Statutory reserve fund	12,80,000
Commission, exchange and brokerage	3,04,000
Rent received	1,04,000
Profit on sale of investments	3,20,000
Depreciation on bank’s properties	48,000
Statutory expenses	44,000
Preliminary expenses	40,000
Auditor’s fee	28,000

The following further information is given:

(i) A customer to whom a sum of ₹ 16 lakhs has been advanced has become insolvent and it is expected only 40% can be recovered from his estate.

(ii) There were also other debts for which a provision of ₹ 2,10,000 was found necessary by the auditors.

(iii) Rebate on bills discounted on 31.3.2016 was ₹ 19,000 and on 31.3.2017 was ₹ 25,000.

(iv) Preliminary expenses are to be fully written off during the year.

(v) Provide ₹ 9,00,000 for Income-tax.

(vi) Profit and Loss account opening balance was Nil as on 31.3.2016.

You are required to Prepare the Profit and Loss account of TOP Bank Limited for the year ended 31.3.2017.

Ans.

TOP Bank Limited

Profit and Loss Account for the year ended 31st March, 2017

		Schedule	Year ended 31.03.2017 (₹ in ‘000s)
I.	Income:		
	Interest earned	13	5923.18
	Other income	14	728.00
	Total		6,651.18

II.	Expenditure		
	Interest expended	15	3259.92
	Operating expenses	16	768.46
	Provisions and contingencies (960+210+900)		2,070.00
	Total		6,098.38
IIII.	Profits/Losses		
	Net profit for the year		552.80
	Profit brought forward		nil
			552.80
IV.	Appropriations		
	Transfer to statutory reserve (25%)		138.20
	Balance carried over to balance sheet		414.60
			552.80

Year ended 31.3. 2017(₹ in '000s)

Schedule 13 – Interest Earned

I.	Interest/discount on advances/bills (Refer W.N.)		5923.18
			5923.18
	Schedule 14 – Other Income		
I.	Commission, exchange and brokerage		304
II.	Profit on sale of investments		320
III.	Rent received		104
			728
	Schedule 15 – Interest Expended		
I.	Interests paid on deposits		3259.92
	Schedule 16 – Operating Expenses		
I.	Payment to and provisions for employees		320
II.	Rent and taxes		144
III.	Depreciation on bank's properties		48
IV.	Director's fee, allowances and expenses		48
V.	Auditors' fee		28
VI.	Law (statutory) charges		44
VII.	Postage and telegrams		96.46
VIII.	Preliminary expenses		40
			768.46

Working Note:

	(₹ in '000s)
Interest/discount	5,929.18
Add: Rebate on bills discounted on 31.3. 2016	19.00
Less: Rebate on bills discounted on 31.3. 2017	(25.00)
	5,923.18

Q-5 Explain "Non-Performing Assets" as per NBFC Prudential Norms (RBI) directions.

Ans. **'Non-performing asset' means:**

(a) an asset, in respect of which, interest has remained overdue for a period of six months or more;

(b) a term loan inclusive of unpaid interest, when the instalment is overdue for a period of six months or more or on which interest amount remained overdue for a period of six months or more;

(c) a demand or call loan, which remained overdue for a period of six months or more from the date of demand or call or on which interest amount remained overdue for a period of six months or more;

(d) a bill which remains overdue for a period of six months or more;

(e) the interest in respect of a debt or the income on receivables under the head 'other current assets' in the nature of short term loans/advances, which facility remained overdue for a period of six months or more;

(f) any dues on account of sale of assets or services rendered or reimbursement of expenses incurred, which remained overdue for a period of six months or more;

Note: As per Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016, the above six months criteria for the assets covered under (a) to (f) is 4 months for the financial year ending March 31, 2017; and from next year ending March 31, 2018 and thereafter it will be 3 months.

(g) the lease rental and hire purchase instalment, which has become overdue for a period of twelve months or more;

Note: The above twelve months criteria for the assets covered under (g) is 6 months for the financial year ending March 31, 2017 and from next year ending March 31, 2018 and thereafter it will be 3 months.

(h) in respect of loans, advances and other credit facilities (including bills purchased and discounted), the balance outstanding under the credit facilities (including accrued interest) made available to the same borrower/beneficiary when any of the above credit facilities becomes non-performing asset

Q-6 The following facts have been taken out from the records of City Bank Ltd. as on 31st March, 2017:

	Rs.	**Rs.**
Rebate on bill discounted (not due on March 31st , 2016)		91,600
Discount received		4,05,000
Bill discounted	24,50,000	

An analysis of the bills discounted is as follows:

	Amount Rs.	**Due date 2017**	**Rate of discount**
(i)	7,50,000	April 8	12%
(ii)	3,00,000	May 5	14%
(iii)	4,40,000	June 12	14%
(iv)	9,60,000	July 15	15%

You are required to:-

(i) Calculate Rebate on Bill Discounted as on 31st March, 2017.

(ii) The amount of discount to be credited to the profit and loss account.

Ans. **(i)** **Calculation of Rebate on bills discounted**

S.No.	Amount (Rs.)	Due date 2017	Unexpired portion	Rate of discount	Rebate on bill discounted Rs.
(i)	7,50,000	April 8	8 days	12%	1,973
(ii)	3,00,000	May 5	35 days	14%	4,027
(iii)	4,40,000	June 12	73 days	14%	12,320
(iv)	9,60,000	July 15	106 days	15%	41,819
					60,139

(ii) **Amount of discount to be credited to the Profit and Loss Account**

	Rs.
Transfer from Rebate on bills discount as on 31st March, 2016	91,600
Add: Discount received during the year ended 31st March, 2017	4,05,000
	4,96,600
Less: Rebate on bills discounted as on 31st March, 2017	60,139
Discount credited to the Profit and Loss Account	4,36,461

Q-7 From the following information, calculate the amount of Provisions and Contingencies and prepare Profit and Loss Account of 'Supreme Bank Limited' for the year ending 31st March, 2018:

Income	₹ in lakhs	Expenditure	₹ in lakhs
Interest and discount	1,835	Interest expended	1,136
Interest accrued on Investments	8	Printing & stationery	18
Commission, exchange and brokerage	12	Repair & maintenance	2
Profit on sale of investments	1	Payment to and provision for employees (salaries, bonus etc.)	80
Rent received	2	Other Operating Expenses	5

Additional Information:

		₹ in lakhs
(i)	Rebate on bills discounted to be provided for	3
(ii)	Classifications of Advances:	
	Standard Assets	4,100
	Sub-Standard Assets (fully secured)	380
	Doubtful Assets not covered by security	155
	Doubtful Assets covered by security	
	For 1 year	10
	More than 1 year, but less than 2 years	18
	More than 2 year, but less than 3 years	35
	More than 3 year	22
	Loss Assets	50
(iii)	Make tax provision @ 35% of the profit.	
(iv)	Profit and Loss Account (Cr.) brought forward from the previous year	65

Ans.(a) Calculation of Provisions and Contingencies

(i) Provision on Non-Performing Assets

₹ in lakhs

Particulars	Amount	% of Provision	Provision
Standard Assets	4,100	0.4	16.40
Sub-standard Assets	380	15	57
Doubtful Assets not covered by security	155	100	155
Doubtful Assets covered by security:			
For 1 year	10	25	2.50
More than 1 year, but less than 2 years	18	40	7.20
More than 2 years & but less than 3 years	35	40	14
More than 3 years	22	100	22
Loss Assets	50	100	50
	4,770		324.10

(ii) Calculation of Provision for tax = 35% of [Total Income – Total Expenditure (excluding tax)]

= 35% of [(1,840 +15) – (1,136+105+324.10)] = ₹ 101.47 lakhs

Total Provisions and contingencies = Provisions on NPAs + Provisions for tax

= 324.10 + 101.47 = ₹ 425.57 lakhs

(b) Supreme Bank Limited

Profit and Loss Account for the year ended 31st March, 2018

	Particulars	Schedule No.	₹ in lakhs
I	Income		
	Interest Earned	13	1,840
	Other Income	14	15
			1,855
II	Expenditures		
	Interest Expended		1,136
	Operating Expenses	16	1,05
	Provisions & Contingencies		425.57
			1,666.57
III	Profit/Loss		
	Net Profit/Loss for the year		188.43
	Profit/Loss brought forward		65
			253.43
IV	Appropriations		
	Transfer to Statutory Reserve @ 25% of 188.43		47.11
	Transfer to Other Reserves		-
	Balance carried over to Balance Sheet		206.32
			253.43
	Schedule 13 – Interest earned		
I	Interest & Discount (1,835 – 3)		1,832
II	Interest on Investments		8
			1,840

Schedule 14- other income		
Commission, exchange and brokerage		12
Profit on sale of investments		1
Rent received		2
		15
Schedule 16- Operating Expenses		
Printing & stationery		18
Repair & maintenance		2
Payment to and provision for employees (salaries, bonus etc.)		80
Other Operating Expenses		5
		105

Q-8 The following is an extract from the Trial Balance of Jeevan Bank Ltd. as at 31st March, 2019:

Rebate on bills discounted as on 1-4- 2018 1,36,518 (Cr.)

Discount received 3,40,312 (Cr.)

Analysis of the bills discounted reveals as follows:

Amount (₹)	Due date
5,60,000	June 1, 2019
17,44,000	June 8,2019
11,28,000	June 21, 2019
16,24,000	July 1, 2019
12,00,000	July 5, 2019

You are required to find out the amount of discount to be credited to Profit and Loss account for the year ending 31st March, 2019 and pass Journal Entries. The rate of discount may be taken at 10% per annum.

Ans. The amount of rebate on bills discounted as on 31st March, 2019 the period which has not been expired upto that day will be calculated as follows:

Discount on ₹ 5,60,000 for 62 days @ 10%	9,512
Discount on ₹ 17,44,000 for 69 days @ 10%	32,969
Discount on ₹ 11,28,000 for 82 days @ 10%	25,341
Discount on ₹ 16,24,000 for 92 days @ 10%	40,934
Discount on ₹ 12,00,000 for 96 days @ 10%	31,562
Total	1,40,318

Note: The due date of the bills discounted is included in the number of days above.

The amount of discount to be credited to the profit and loss account will be:

		₹
Transfer from rebate on bills discounted as on 31.03. 2018		1,36,518
Add: Discount received during the year		3,40,312
		4,76,830
Less: Rebate on bills discounted as on 31.03. 2019 (as above)		(1,40,318)
		3,36,512

Journal Entries

		₹	₹
Rebate on bills discounted A/c	Dr.	1,36,518	
To Discount on bills A/c			1,36,518
(Transfer of opening unexpired discount on 31.03. 2018)			
Discount on bills A/c	Dr.	1,40,318	
To Rebate on bills discounted A/c			1,40,318
(Unexpired discount on 31.03. 2019 taken into account)			
Discount on Bills A/c	Dr.	3,36,512	
To P & L A/c			3,36,512

(Discount earned in the year, transferred to P&L A/c)

Q-9 From the following information of Wealth Bank Limited, Prepare Profit and Loss Account for the year ended 31st March, 2018:

Particulars	₹ in lakhs	Particulars	₹ in lakhs
Interest on Cash Credit	364	Interest paid on Recurring Deposits	17
Interest on Overdraft	150	Interest paid on Savings Bank Deposits	12
Interest on Term Loans	308	Auditor's Fees and Allowances	24
Income on Investments	168	Directors' Fees and Allowance	50
Interest on Balance with RBI	30	Advertisement	36
Commission on remittances and transfer	15	Salaries, allowances and bonus to employees	248
Commission on Letters of Credit	24	Payment to Provident Fund	56
Commission on Government Business	16	Printing & Stationery	28
Profit on Sale of Land & Building	5	Repairs & Maintenance	10
Loss on exchange transactions	10	Postage, courier & telephones	16
Interest paid on Fixed Deposits	25		

Other Information :

₹ in lakhs

		Earned	Collected
(i)	Interest on NPA is as follows:		
	Cash Credit	164	80
	Term Loans	90	20
	Overdraft	150	50
(ii)	Classification of Non-performing Advances:		
	Standard		60
	Sub-standard-fully secured		22
	Doubtful assets-fully unsecured		40
	Doubtful assets covered fully by security:		
	Less than 1 year		6
	More than 1 year upto 3 years		3
	More than 3 years		2
	Loss Assets		38

(iii) Provide 35% of the profits towards provision for taxation.

(iv) Transfer 25% of the profit to Statutory Reserves.

Ans.

Wealth Bank Limited

Profit and Loss Account

For the year ended 31st March, 2018

₹ in lakhs

	Particulars	**Schedule**	**Year ended 31-3-2018**
I	Income		
	Interest earned	13	766
	Other income	14	50
			816
II	Expenditure		
	Interest expended	15	54
	Operating expenses	16	468
	Provisions and Contingencies (Refer W.N.)		158.96
			680.96
III	Profit/Loss		
	Net Profit/(Loss) for the year		135.04
	Net Profit/(Loss) brought forward		Nil
			135.04
IV	Appropriations: Transfer to Statutory reserve (25% of the profits)		33.76
	Balance carried to the balance sheet		101.28
	Total		135.04

Schedule 13 - Interest Earned

Year ended 31-3-2018

(₹ in lakhs)

I	Interest/discount on advances/bills		
	Interest on cash credit (364-84)	280	
	Interest on overdraft (150-100)	50	
	Interest on term loans (308-70)	238	568
II	Income on investments		168
III	Interest on Balance with RBI		30
			766

Interest on NPA is recognized on cash basis, hence difference of accrued interest not received have been reduced from the total accrued interest.

Schedule 14 - Other Income

			Year ended 31-3-2018 (₹ in lakhs)
I	Commission, Exchange and Brokerage:		
	Commission on remittances and transfer	15	
	Commission on letter of credit	24	
	Commission on Government business	16	55
II	Profit on sale of Land and Building		5
III	Loss on Exchange Transactions		(10)
			50

Schedule 15 - Interest Expended

			Year ended 31-3-2018 (₹ in lakhs)
I	Interest on Deposits		
	Fixed deposits	25	
	Recurring deposits	17	
	Saving bank deposits	12	54

Schedule 16 - Operating Expenses

			Year Ended 31-3-2018 (₹ in lakhs)
I	Payment to and provision for employees		
	Salaries, allowances and bonus	248	
	Provident Fund Contribution	56	304
II	Printing and Stationery		28
III	Advertisement and publicity		36
IV	Directors' fees, allowances and expenses		50
V	Auditors' fees and expenses		24
VI	Postage, telegrams, telephones etc.		16
VII	Repairs and maintenance		10
			468

Working Note:

Provisions and contingencies **(₹ in lakhs)**

Provision for Advances:			
Standard	60 × 0.40%		0.24
Sub-standard	22 × 15%		3.3
Doubtful not covered by security	40× 100%		40
Doubtful covered by security:			
Less than 1 year	6 x 25%	1.5	
More than 1 year but less	3 x 40%	1.2	
than 3 years	2 x 100%	2.0	
More than 3 years			4.7

Loss Assets	(38 × 100%)	38
		86.24
Provision for tax	35% of	
	(Total Income – Total	
	Expenditure)	
	35% of [816-(54 + 468 + 86.24)]	
	35% of 207.76	72.72
		158.96

Q-10 (i) The following is an extract of Trial Balance of SM Bank, an overseas bank as on 31st March, 2018.

	Dr. ₹	**Cr. ₹**
Bill Discounted	15,16,800	
Discount Received		1,26,859
Rebate on Bills discounted not due on 31st March,17		26,592

An analysis of bill discounted is as follows :

Amount in ₹	**Due Date**	**Rate of Discount**
1,46,200	4th May, 2018	15
2,30,400	12th May, 2018	15
4,35,900	28th May, 2018	15
4,36,200	18th June, 2018	16
2,68,100	4th July, 2018	16

You are required to calculate Rebate on Bills Discounted as on 31st March, 2018 and show necessary Journal Entries.

(ii) The following information are also given for SM Bank :

Assets	₹ in Lakhs
Standard	75,00
Sub-Standard	60,00
Doubtful: for 1 Year (fully secured)	12,00
for 1 to 3 Year (fully secured)	9,00
for more than 3 Years	9,00
Loss Assets	15,00

Additional Information:

(1) Standard Assets includes ₹ 15,00 Lakhs Advances to Commercial Real Estate (CRE).

(2) Out of ₹ 60,00 Lakhs of Sub-Standard Asset ₹ 20,00 Lakhs are unsecured.
Unsecured amount includes ₹ 5,00 Lakhs in respect of Infrastructure Loan Accounts with ESCROW safeguard.

(3) Doubtful Asset for more than 3 Years includes ₹ 4,00 Lakhs, which is covered by 50% ECGC, value of security of which is ₹ 150 Lakhs.

You are required to find out the amount of provision to be shown in the Profit & Loss Account of SM Bank.

Ans. **(i) Statement showing rebate on bills discounted**

Value	Due Date	Days after 31.3.2018	Rate of discount	Discount Amount
1,46,200	4.5.18	(30+ 4) = 34	15%	2,043
2,30,400	12.5.18	(30+12) = 42	15%	3,977
4,35,900	28.5.18	(30+28) = 58	15%	10,390
4,36,200	18.6.18	(30+ 31+ 18) = 79	16%	15,106
2,68,100	4.7.18	(30+ 31+30+4) = 95	16%	11,165
15,16,800	Rebate on bills discounted on 31.3.2018			42,681

In the books of SM Bank Ltd.

Journal Entries

(i)	Rebate on bills discounted Account	Dr.	26,592	
	To Discount on bills Account			26,592
	[Being opening balance of rebate on bills discounted account transferred to discount on bills account]			
(ii)	Bills purchased & discounted Account	Dr	15,16,800	
	To Discount on bills Account			1,26,859
	To Clients Account			13,89,941
	(Being bills purchased and discounted during the year)			
(iii)	Discount on bills Account	Dr.	42,681	
	To Rebate on bills discounted Account			42,681
	[Being provision made on 31st March, 2018]			
(iv)	Discount on bills Account	Dr.	1,10,770	
	To Profit and loss Account			1,10,770
	[Being transfer of discount on bills, of the year, to profit and loss account]			
	Credit to Profit and Loss A/c will be as follows:			
	₹ (1,26,859 + 26,592 – 42,681) = ₹ 1,10,770			

(ii) Statement showing the amount of provisions on Assets

(₹ in lakhs)

Assets	Amount	% of provision	Provision
Standard:			
Advances to CRE	15,00	1	15
Others	60,00	.4	24
Sub-standard:			
Secured	40,00	15	6,00
Unsecured- Others	15,00	25	3,75
Unsecured infrastructure	5,00	20	1,00
Doubtful Secured:			
up to one year	12,00	25	3,00
For more than 1 year up to 3 years	9,00	40	3,60
More than 3 years	4,00	W.N.1	2,75
Doubtful unsecured (more than 3 years)	5,00	100	5,00
Loss	15,00	100	15,00
Total Provision Required			40,49

Working Note :

Provision required where assets are ECGC covered

	₹ In Lakhs
Outstanding balance (ECGC Covered)	4,00
Less: Value of security	1,50
Unrealised balance	2,50
Less: ECGC Cover @ 50%	1,25
Net Unsecured Balance	1,25
Provision for unsecured portion @100%	1,25
Provision for secured portion @100%	1,50
Total Provision to be made	2,75

Q-11 While closing its books of accounts on 31st March 2018, a Non-Banking Finance Company has its advances classified as follows:

	₹ (in lakhs)
Standard assets	18,400
Sub-standard assets	1,250
Secured Portion of doubtful debts:	
Upto one year	300
One year to three years	90
More than three years	30
Unsecured portions of doubtful debts	92
Loss assets	47

Calculate the amount of provision which must be made against the Advances as per -

(i) The Non-banking Financial Company - Non-systematically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016; and

(ii) Non-banking Financial Company - Systematically Important Non- Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. **Calculation of provision required on advances as on 31st March, 2018 as per the** Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016

	Amount ₹ in lakhs	**Percentage of provision**	**Provision ₹ in lakhs**
Standard assets	18,400	0.25	46.00
Sub-standard assets	1,250	10	125.00
Secured portions of doubtful debts"			
" upto one year	300	20	60.00
" one year to three years	90	30	27.00
" more than three years	30	50	15.00
Unsecured portions of doubtful debts	92	100	92.00
Loss assets	47	100	47.00
			412.00

Calculation of provision required on advances as on 31st March, 2018 as per the NonBanking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016

	Amount ₹ in lakhs	Percentage of provision	Provision ₹ in lakhs
Standard assets	18,400	0.40*	73.60
Sub-standard assets	1,250	10	125.00
Secured portions of doubtful debts"			
" upto one year	300	20	60.00
" one year to three years	90	30	27.00
" more than three years	30	50	15.00
Unsecured portions of doubtful debts	92	100	92.00
Loss assets	47	100	47.00
			439.60

***Note:** For the year ending on 31st March, 2018, the provision rate for standard assets is 0.40%.

Q-12 Forward Bank Ltd furnishes the following information as on 31st March, 2018.

	Amount in ₹
Bills Discounted	82,23,000
Rebate on bills discounted as on 1st April, 2017	1,32,960
Discount received	6,33,990

Details of bills discounted is as given below:

Value of Bills (₹)	Due Date	Rate of Discount
10,95,000	15th June, 2018	14%
30,00,000	25th June, 2018	12%
16,92,000	5th July, 2018	16%
24,36,000	15th July, 2018	16%

(i) Calculate the rebate on bills discounted as on 31st March, 2018.
(ii) Pass necessary Journal Entries.

Ans. In order to determine the amount to be credited to the Profit and Loss A/c it is necessary to first ascertain the amount attributable to the unexpired portion of the period of the respective bills. The workings are as given below:

Value (₹)	Due Date	Days after 31-03-2018	Discount %	Discount Amount ₹
10,95,000	15-06-2018	(30+31 + 15) = 76	14%	31,920
30,00,000	25-06-2018	(30 + 31 + 25) = 86	12%	84,822
16,92,000	05-07-2018	(30 + 31 + 30 + 5) = 96	16%	71,203
24,36,000	15-07-2018	(30 + 31 + 30 + 15) = 106	16%	1,13,191*
		Rebate on bills discountedas on 31.3.2018		3,01,136

The journal entries will be as follows :

		Dr. ₹	Cr. ₹
Rebate on Bills Discounted A/c	Dr.	1,32,960	
To Discount on Bills A/c			1,32,960
(Being the transfer of Rebate on Bills Discounted on 1.4.2017 to Discount on Bills Account)			
Discount on Bills A/c	Dr.	3,01,136	
To Rebate on Bills Discounted A/c			3,01,136
(Being the transfer of rebate on bills discountedrequired on 1.4.2018 from discount on Bills Account)			
Discount on Bills A/c	Dr.	4,65,814	
To Profit and Loss A/c			4,65,814
(Being the amount of discount on Bills transferred to Profit and Loss Account)			

Working Note :

The amount of discount to be credited to the Profit and Loss Account will be:

	₹
Transfer from Rebate on bills discount as on 1.4.17	1,32,960
Add: Discount received duringthe year ended 31-3-2018	6,33,990
	7,66,950
Less: Rebate on bills discountedas on 31.3.2018	(3,01,136)
	4,65,814

Q-13 Astha Bank has the following Capital Funds and Assets as at 31st March, 2018:

	₹ in crores
Capital Funds:	
Equity Share Capital	600.00
Statutory Reserve	470.00
Profit and Loss Account (Dr. Balance)	30.00
Capital Reserve (out of which ₹ 25 crores were due to revaluationof assets and balance due to sale of assets)	130.00
Assets:	
Balance with other banks	15.00
Cash balance with RBI	35.50
Claim on Banks	52.50
Other Investments	70.00
Loans and Advances:	
(i) Guaranteed by government	22.50
(ii) Guaranteed by DICGC/ECGC	110.00
(iii) Other	9,365.00
Premises, furniture and fixtures	92.50
Leased assets	40.00
Off- Balance Sheet items:	
(i) Acceptances, endorsements and letters of credit	1,100.00
(ii) Guarantees and other obligations	6,200.00

You are required to:

(i) Segregate the capital funds into Tier I and Tier II capitals.

(ii) Find out the risk-adjusted assets and risk weighted assets ratio.

Ans.

(i) Capital Funds –Tier I : ₹ in crore	
Equity Share Capital	600
Statutory Reserve	470
Capital Reserve (arising out of sale of assets)	105
Less: Profit & Loss (Dr. bal.)	(30)
	1,145
Capital Funds - Tier II :	
Capital Reserve (arising out of revaluation of assets)	25
Less: Discount to the extent of 55%	(13.75)
	11.25

(ii) Risk Adjusted Assets

Funded Risk Assets	**₹ in crore**	**Percentage weight**	**Amount ₹ in crore**
Cash Balance with RBI	35.50	0	—
Balances with other Banks	15	20	3
Claims on banks	52.50	20	10.50
Other Investments	70	100	70
Loans and Advances:			
(i) guaranteed by government	22.50	0	—
(ii) guaranteed by DICGC/ECGC	110	50	55
(iii) Others	9,365	100	9,365
Premises, furniture and fixtures	92.50	100	92.50
Leased Assets	40	100	40
			9,636

Off-Balance Sheet Item	**₹ in Crore**	**Credit Conversion Factor**	**₹ In Crore**
(i) Acceptances, Endorsements and Letters of credit	1,100	100	1,100
(ii) Guarantees and other obligations	6,200	100	6,200
			7,300

Risk Weighted Assets Ratio : $\frac{\text{Capital Funds (Tier I \& Tier II)}}{\text{Risk Adjusted Assets off Balance sheet items}} \times 100$

= (1,145 +11.25)/ (9,636 +7,300)

= (1,156.25 /16,936) x 100 = 6.83% (rounded off)

Q-14 From the following information ,you are required to prepare Profit and Loss Account of Simple Bank for the ended as on 31st March, 2019:

2017-18 (₹ in '000)	**Item**	**2018-19 (₹ in '000)**
71,35	Interest and Discount	1,02,25
5,70	Income from investment	5,60
7,75	Interest on Balances with RBI	8,85
36,10	Commission , Exchange and Brokerages	35,60
60	Profit on sale of investments	6.10

30,60	Interest on Deposits	41.10
6,35	Interest to RBI	7,35
36,35	Payment to and provision for employees	42,75
7,90	Rent, taxes and lighting	8,95
7,35	Printing and Stationery	10.60
5,60	Advertising and publicity	4,90
4,90	Depreciation	4,90
7,40	Director's fees	10,60
5,50	Auditor's feed	5,50
2,50	Law Charges	7,60
2,40	Postage, telegrams and telephones	3,10
2,10	Insurance	2,60
2,85	Repair and maintenance	3,30

Other Information:

(i) The following items are already adjusted with interest and Discount (Cr.)

Tax Provision (₹ '000)	7,40
Provision for Doubtful Debts(₹'000)	4,60
Loss on sale of investments (₹'000)	60
Rebate on Bills discounted (₹'000)	2,75

(ii) Appropriations:

25% of profit is transferred to Statutory Reserves.

5% of profit is transferred to Revenue Reserve.

You are required to give necessary Schedules also.

Ans.

Simple Bank

Profit and Loss Account for the year ended 31-3-2019

No.		Schedule	(₹ 000's) Year ended 31-3-2019	(₹ 000's) Year ended 31-3-2018
I.	Income			
	Interest Earned	13	1,29,30	84,80
	Other Income	14	41,10	36,70
	Total		**1,70,40**	**1,21,50**
II.	Expenditure			
	Interest Expended	15	48,45	36,95
	Operating Expenses	16	1,04,80	84,85
	Provisions and Contingencies		12,00	———
	Total		**1,65,25**	**1,21,80**

III.	Profit/Loss		
	Net Profit/Loss for the year	5,15	(30)
	Profit/Loss brought forward	(30)	___
	Total	**4,85**	**(30)**
IV.	Appropriations		
	Transfer to Statutory Reserve	128.75	
	Transfer to Other Reserve, Proposed Dividend	25.75	
	Balance carried over to Balance Sheet	330.5	_____
	Total	**485.0**	

Schedule 13 - Interest Earned

(₹ 000's)

		Year ended *31-3-2019*	**Year ended *31-3-2018***
I.	Interest/Discount	1,14,85	71,35
II.	Income on Investments	5,60	5,70
III.	Interest on Balances with RBI and other inter-bank fund	8,85	7,75
IV.	Others	_____	_____
	Total	**1,29,30**	**84,80**

Schedule 14 - Other Income

(₹ 000's)

		Year ended 31-3-2019	**Year ended 31-3-2018**
I.	Commission, Exchange and Brokerage	35,60	36,10
II.	Profit on Sale of Investments	6,10	60
	Less: Loss on sale of Investments	(60)	-
	Total	**41,10**	**36,70**

Schedule 15 - Interest Expended

(₹ 000's)

		Year ended 31-3-2019	**Year ended 31-3-2018**
I.	Interest on Deposits	41,10	30,60
II.	Interest on RBI/inter-bank borrowings	7,35	6,35
	Total	**48,45**	**36,95**
VII.	Auditor's fees and expenses (including branch auditors)	5,50	5,50
VIII.	Law charges	7,60	2,50
IX.	Postage, telegrams, telephones etc.	3,10	2,40
X.	Repairs and maintenance	3,30	2,85
XI.	Insurance	2,60	2,10
XII.	Other Expenditure	_____	_____
	Total	**1,04,80**	**84,85**

Q-15 The following information is furnished by ALFA Bank Ltd.

	₹in Lakhs
Margins held against letter of credit	200
Recurring accounts deposits	100
Current accounts deposits	375
Demand deposit	125
Unclaimed deposit	75
Gold deposit	235
Demand liabilities portion of saving bank deposit	1325
Time liabilities portion of saving bank deposit	722

Explain CRR and you are required to calculate the amount of Cash Reserve Ratio (CRR) as per the direction of reserve Bank of India.

Ans. **Cash Reserve Ratio (CRR):** For smoothly meeting cash payment requirement, banks are required to maintain certain minimum ready cash balances at all times. This is called as Cash Reserve Ratio (CRR).

Cash reserve can be maintained by way of either a cash reserve with itself or as balance in a current account with the Reserve Bank of India or by way of net balance in current accounts or in one or more of the aforesaid ways. Every Scheduled Commercial Bank has to maintain cash reserve ratio (i.e. CRR) as per direction of the RBI. The current Cash Reserve Ratio (CRR) is 4% of their Net Demand and Time Liabilities (NDTL).

Margins held against letters of credit	Demand Liability	200
Recurring Accounts deposits	Time Liability	100
Current deposits	Demand Liability	375
Demand deposits	Demand Liability	125
Unclaimed deposits,	Demand Liability	75
Gold deposits	Time Liability	235
Demand liabilities portion of savings bank deposits	Demand Liability	1325
Time liabilities portion of savings bank deposits	Time Liability	722
	Total	**3,157**

Cash Reserve Ratio = Net (demand + Time) liabilities x 4/100

CRR= 3,157 x 4/100 = 126.28 Lakhs

Q-16 Astha Bank has the following Capital Funds and Assets as at 31st March, 2020:

	₹ in crores
Capital Funds:	
Equity Share Capital	600.00
Statutory Reserve	470.00
Profit and Loss Account (Dr. Balance)	30.00
Capital Reserve (out of which ₹ 25 crores were due to revaluation of assets and balance due to sale of assets)	130.00
Assets:	
Balance with other banks	15.00
Cash balance with RBI	35.50
Claim on Banks	52.50

Other Investments	70.00
Loans and Advances:	
(i) Guaranteed by Government	22.50
(ii) Guaranteed by PSUs of Central Government	110.00
(iii) Other	9,365.00
Premises, furniture and fixtures	92.50
Leased assets	40.00
Off- Balance Sheet items:	
(i) Acceptances, endorsements and letters of credit	1,100.00
(ii) Guarantees and other obligations	6,200.00

You are required to: (i) Segregate the capital funds into Tier I and Tier II capitals; and (ii) Find out the risk-adjusted assets.

Ans.

(i) **Capital Funds –**

Tier I :	₹ *in crore*
Equity Share Capital	600
Statutory Reserve	470
Capital Reserve (arising out of sale of assets)	105
Less: Profit & Loss (Dr. bal.)	(30)
	1,145
Capital Funds - Tier II :	
Capital Reserve (arising out of revaluation of assets)	25
Less: Discount to the extent of 55%	(13.75)
	11.25

(ii) **Risk Adjusted Assets**

Funded Risk Assets	**₹ in crore**	**Percentage weight**	**Amount ₹ in crore**
Cash Balance with RBI	35.50	0	—
Balances with other Banks	15	20	3
Claims on banks	52.50	20	10.50
Other Investments	70	100	70
Loans and Advances:			
(i) guaranteed by government	22.50	0	—
(ii) guaranteed by PSUs	110	0	—
(iii) Others	9,365	100	9,365
Premises, furniture and fixtures	92.50	100	92.50
Leased Assets	40	100	40
			9,581

Q-17 State with reason whether the following cash credit accounts are NPA or not:

	Case-1	Case-2
Sanctioned limit	60,00,000	45,00,000
Drawing power	56,00,000	42,00,000
Amount outstanding continuously 01-01-19 to 31-03-19	48,00,000	30,00,000
Total interest debited for the above period	3,84,000	2,40,000
Total credits for the above period	Nil	3,20,000

Ans.

	Case 1 ₹	Case 2 ₹
Sanctioned limit	60,00,000	45,00,000
Drawing power	56,00,000	42,00,000
Amount outstanding continuously from 1.01.2019 to 31.03.2019	48,00,000	30,00,000
Total interest debited	3,84,000	2,40,000
Total credits	-	320,000
Is credit in the account is sufficient to cover the interest debited during the period or amount is not ₹overdue' for a continuous period of 90 days.	No	Yes
	NPA	NOT NPA

Q-18 The following is a**n** extract from the trial balance of Novel Bank Limited as on 31st March 2019:

Rebate on bills discounted as on 1st April 2018 ₹ 78,566 (Cr. bal)

Discount Received ₹ 1,60,572 (Cr. bal)

An analysis of bills discounted is as follows:

Amount ₹	Due Date
2,90,000	01 June 2019
8,75,000	08 June 2019
5,65,000	21 June 2019
8,12,000	01 July 2019
6,50,000	05 July 2019

Find out the amount of discount to be credited to Profit and Loss Account for the year ending on 31st March, 2019 and pass the necessary journal entries. The rate of discount shall be taken at 10% per annum.

Ans. The amount of rebate on bills discounted as on 31st March, 2019 the period which has not been expired upto that day will be calculated as follows:

Discount on ₹ 2,90,000 for 62 days @ 10%	4,926
Discount on ₹ 8,75,000 for 69 days @ 10%	16,541
Discount on ₹ 5,65,000 for 82 days @ 10%	12,693
Discount on ₹ 8,12,000 for 92 days @ 10%	20,467
Discount on ₹ 6,50,000 for 96 days @ 10%	17,096
Total	**71,723**

Note: The due date of the bills discounted is included in the number of days above.

The amount of discount to be credited to the profit and loss account will be:

	₹
Transfer from rebate on bills discounted as on 1.4. 2018	78,566
Add: Discount received during the year	1,60,572
	2,39,138
Less: Rebate on bills discounted as on 31.03. 2019 (as above)	(71,723)
	1,67,415

Journal Entries

		₹	₹
Rebate on bills discounted A/c	Dr.	78,566	
To Discount on bills A/c			78,566
(Transfer of opening unexpired discount on 31.03. 2018)			
Discount on bills A/c	Dr.	71,723	
To Rebate on bills discounted			71,723
(Unexpired discount on 31.03. 2019 taken into account)			
Discount on Bills A/c	Dr.	1,67,415	
To P & L A/c			1,67,415
(Discount earned in the year, transferred to P & L A/c)			

Q-19 Classify the following NPAs of the SG Banking Limited:

- Loan Assets overdue for more than 3 months but less than 12 months: ₹ 150 Lakhs, fully secured.
- Loan Assets overdue for more than 12 months: ₹ 90 Lakhs, fully secured.
- Loan Assets overdue for more than 36 months and considered uncollectible : ₹ 50 Lakhs. (This comprise of two assets worth ₹ 25 Lakhs each. One of these has a security value of ₹ 20 Lakhs).

Also, give the amount of provisioning required in each case.

Ans.

Assets	**Classification**	**Amount - (₹ in lakhs)**	**% of ₹ Provision**	**Provision (₹ in lakhs)**
Overdue for more than 3 months but less than 12 months	Sub-standard	150	15	22.50
Overdue for more than 12 months	Doubtful less than 1 year	90	25	22.50
Overdue for more than three years (fully secured-secured by ₹ 20 lakhs)	Doubtful 1 to 3 years	20	40	8
Overdue for more than three years (unsecured)	Doubtful 1 to 3 years	5	100	5
Overdue for more than three years	Loss	25	100	25
Total provision				83

Q-20 Statement of interest on advances in respect of Performing assets and Non-Performing Assets of Omega Bank is as follows:-

	Performing Interestearned	**Assets Interest** received	**Non-Performing Interest** earned	**Assets Interest** received
Cash credits and overdrafts	1800	1060	450	70
Term Loan	480	320	300	40
Bills purchased and discounted	700	550	350	36

Find out the income to be recognized for the year ended 31st March, 2020.

Ans. Interest on performing assets should be recognised on accrual basis, but interest on NPA should be recognised on cash basis.

		₹ in lakhs
Interest on cash credits and overdraft :	(1800+70)	= 1,870
Interest on Term Loan	(480+40)	= 520
Income from bills purchased and discounted :	(700+36)	= 736
		3,126

Q-21 Astha Bank has the following Capital Funds and Assets as at 31st March, 2020:

	₹ in crores
Capital Funds:	
Equity Share Capital	600.00
Statutory Reserve	470.00
Profit and Loss Account (Dr. Balance)	30.00
Capital Reserve [out of which ? 25 crores were due to revaluation of assets (on which discount of 55% is to be provided) and balance due to sale of assets]	130.00
Assets:	
Balance with other banks	15.00
Cash balance with RBI	35.50
Claim on Banks	52.50
Other Investments	70.00
Loans and Advances:	
(i) Guaranteed by Government	22.50
(ii) Guaranteed by PSUs of Central Government	110.00
(iii) Other	9,365.00
Premises, furniture and fixtures	92.50
Leased assets	40.00

You are required to:

(i) Segregate the capital funds into Tier I and Tier II capitals; and (ii) Find out the risk-adjusted assets.

Ans. (i) Capital Funds –

Tier I :	₹ *in crore*
Equity Share Capital	600
Statutory Reserve	470
Capital Reserve (arising out of sale of assets)	105
Less: Profit & Loss (Dr. bal.)	(30)
	1,145
Capital Funds - Tier II :	
Capital Reserve (arising out of revaluation of assets)	25
Less: Discount to the extent of 55%	(13.75)
	11.25

(ii) Risk Adjusted Assets

Funded Risk Assets ₹	**in crore**	**Percentage weight**	**Amount ₹ in crore**
Cash Balance with RBI	35.50	0	—
Balances with other Banks	15	20	3
Claims on banks	52.50	20	10.50
Other Investments	70	100	70
Loans and Advances:			
(i) guaranteed by government	22.50	0	—
(ii) guaranteed by PSUs	110	0	—
(iii) Others	9,365	100	9,365
Premises, furniture and fixtures	92.50	100	92.50
Leased Assets	40	100	40
			9,581

Q-22 The following are the figures extracted from the books of New Bank Limited as on 31.03.2021:

	Figure in ₹
Interest and Discount received	48,11,200
Interest paid on Deposits	22,95,920
Salaries and allowances	8,40,510
Directors fees and allowances	45,000
Issued and subscribed capital	16,00,000
Commission, Exchange and Brokerage received	1,45,000
Postage and Telegrams	60,000
Statutory Reserve Fund	8,00,000
Interest on cash credit	2,65,000
Profit on sale of Investments	1,15,800

Depreciation on Bank's Property	40,000
Interest on Overdraft	1,20,000
Rent Received	65,000
Legal Expenses	21,000
Auditors Fees	5,000
Statutory Expenses	38,000

The following information is also given:

(i) A customer to whom a sum of ₹ 5 Lakhs was advanced has become insolvent and it is expected that only 50% can be recovered from his estate.

(ii) Make necessary provisions on Risk Assets:

Standard (excluding above ₹ 5,00,000)	10,00,000
Sub-Standard (fully secured)	8,20,000
Doubtful assets covered by security for 1 year	40,000
Loss assets	1,00,000

(iii) Provide ₹ 6,50,000 for Income Tax.

(iv) The directors desire to declare 10% dividend.

(v) 25% of profit is to be transferred to Reserve fund.

(vi) Rebate on Bills discounted on 31.03.2020 was ₹ 20,000 and ₹ 15,000 on 31.03.2021.

You are required to prepare Profit & Loss A/c of New Bank Limited for the year ended 31.03.2021.

Ans.

New Bank Limited

Profit and Loss Account for the year ended 31st March, 2021

		Schedule	Year ended 31.03.2021 ₹	
I.	Income:			
	Interest earned		13	52,01,200
	Other income	Total	14	3,25,800
				55,27,000
II.	Expenditure			
	Interest expended		15	22,95,920
	Operating expenses		16	10,49,510
	Provisions and contingencies			11,37,000
	(6,50,000+2,37,000+2,50,000)	Total		44,82,430
III.	Profits/Losses			
	Net profit for the year			
	Profit brought forward			10,44,570
				Nil
				10,44,570
IV.	Appropriations			
	Transfer to statutory reserve (25% of 10,44,570)			2,61,143
	Proposed dividend			1,60,000
	Balance carried over to balance sheet			6,23,427
				10,44,570

Note: Profit & Loss Account balance of ₹ 6,23,427 will appear under the head 'Reserves and Surplus' in Schedule 2 of the Balance Sheet.

Year ended 31.3.2021 (₹)

	Schedule 13 - Interest Earned	
I.	Interest/discount on advances/bills (Refer W.N.)	48,16,200
	Interest on cash credit*	2,65,000
	Interest on overdraft *	1,20,000
		52,01,200
	Schedule 14 - Other Income	
I.	Commission, exchange and brokerage	1,45,000
II.	Profit on sale of investment	1,15,800
III.	Rent received	65,000
		3,25,800
	Schedule 15 - Interest Expended	
I.	Interests paid on deposits	22,95,920
		22,95,920
	Schedule 16 - Operating Expenses	
I.	Payment to and provisions for employees (salaries & allowances)	8,40,510
II.	Depreciation on assets	40,000
III.	Director's fee, allowances and expenses	45,000
IV.	Auditor's fee	5,000
V.	Statutory (law) expenses	38,000
VI.	Postage and telegrams	60,000
VII.	Legal expenses	21,000
		10,49,510

***Considered to be earned.**

Working Notes:

1.

	₹
Interest and discount received	48,11,200
Add: Rebate on bills discounted on 31.3. 2020	20,000
Less: Rebate on bills discounted on 31.3. 2021	(15,000)
	48,16,200

2.

Classification of Assets	Amount of Advances	% age of provision	Amount of provision
Standard assets	10,00,000	0.40	4,000
Sub-standard assets	8,20,000	15	1,23,000
Doubtful assets:			
For one year (secured)	40,000	25	10,000
Loss assets	1,00,000	100	1,00,000
Total provision required			2,37,000

Q-23 A commercial bank has the following capital funds and assets. Segregate the capital funds into Tier I and Tier II capitals. Find out the risk-adjusted asset and risk weighted assets ratio:

Capital Funds:	**(₹ in lakhs)**
Equity Share Capital	29,00
Perpetual Non-cumulative Preference Shares	8,00
Perpetual Cumulative Preference Shares (fully paid up)	5,50
Statutory Reserve	13,50
Capital Reserve (of which ₹ 13.5 lakhs were due to revaluation of Assets and the balance due to sale of assets)	45
Securities Premium	7,00
Assets:	
Cash balance with RBI	3,50
Balances with other banks	4,75
Claims on Banks	10,25
Investments in Bonds issued by other banks	78,00
Investments in venture capital funds	17,00
Other investments	121,00

Loan and Advances:

(i)	Loans guaranteed by Government	16,10
(ii)	Loans guaranteed by public sector undertakings	6,20
(iii)	Leased assets	4
(iv)	Advances against term deposits	15,00
(v)	Educational loans	12

Other Assets:

(i)	Premises, Furniture & Fixtures and other assets	150,55
(ii)	Intangible assets	18
(iii)	Deferred tax asset	0.40

Off Balance Sheet Items:

(i)	Acceptances, Endorsements & letter of credit	203,00
(ii)	Non funded exposure to real estate	19,00

Ans.

	(in lakhs)
(i) Capital Funds - Tier I:	
Equity Share Capital	29,00.00
Securities premium	7,00.00
Perpetual non-cumulative pref. shares	8,00.00
Statutory Reserve	13,50.00
Capital Reserve (arising out of sale of assets)	31.50
	57,81.50

Less: Intangible assets	(18.00)		
Deferred tax assets	(0.40)		(18.40)
Total			**57,63.10**
Capital Funds - Tier II:			
Perpetual cumulative pref. shares			5,50.00
Capital Reserve (arising out of revaluation of assets)		13.50	
Less: Discount to the extent of 55%		(7.43)*	6.07
Total			556.07
Total Capital Funds			63,19.17

*7.425 has been rounded off as 7.43.

(ii) Calculation of Risk Adjusted Assets

	₹ in lakhs	Weight in % (₹ in lakhs)	Amount
Funded Risk Assets			
Cash Balance with RBI	3,50	0	0
Balances with other Banks	4,75	20	95
Claims on banks	10,25	20	2,05
Investment in bonds issued by other banks	78,00	20	15,60
Investment in venture capital funds	17,00	150	25,50
Other Investments	121,00	100	121,00
Loans and Advances:			
(i) guaranteed by government	16,10	0	0
(ii) guaranteed by public sector undertakings	6,20	0	0
(iii) Leased assets	4	100	4
(iv) Advances against term deposits	15,00	0	0
(v) Educational Loans	12	100	12
Premises, furniture and fixtures	150,55	100	150,55
			315,81

Off-Balance Sheet Item	**₹ in lakhs**	**Credit Conversion Factor**	**₹ in lakhs**
Acceptances, Endorsements and Letters of credit	203,00	100	203,00
Non-funded exposure to real estate sector	19,00	150	28,50
			231,50

(iii) Risk Weighted Assets Ratio: $\frac{\text{Capital Funds (Tier I \& Tier II)}}{\text{Risk Adjusted Assets + off Balance sheet items}} \times 100$

Capital Adequacy Ratio = 63,19.17/315,81+231,50

= (63,19.17/547,31) x 100=11.55%

Q-24 Vasu Commercial Bank has the following capital funds and assets. Segregate the capital funds into Tier I and Tier II capitals. Find out the risk adjusted assets and risk weighted assets ratio.

Particulars	**₹ in crores**
Equity Share Capital	600.00
Statutory Reserve	250.00
Capital Reserve (of which ₹ 26 crores were due to revaluation of assets and the balance due to sale of capital assets)	87.00
Assets:	
Cash Balance with RBI	20.00
Balance with other banks	28.00
Other investments	38.00
Loans and advances :	
(i) Guaranteed by the Govt.	18.50
(ii) Others	6,625.00
Premises, Furniture and fixtures	108.00
Off-Balance Sheet Items	
(i) Guarantee and other obligations	600.00
(ii) Acceptances, endorsements and letter of credit	4,200.00

Ans.

(₹ in Crores)

(i)

Capital Funds - Tier I :	**₹**	**₹**
Equity Share Capital		600
Statutory Reserve		250
Capital Reserve (arising out of sale of assets) (87 – 26)	61	
Capital Fund Tier I	911.0	
Capital Funds - Tier II :		
Capital Reserve (arising out of revaluation of assets)	26.0	
Less: Discount to the extent of 55%	(14.3)	
Capital fund Tier II		11.7
Total Capital Fund		922.7

(ii) **Calculation of Risk Adjusted Assets**

Funded Risk Assets	**₹**	**weight in %**	**Amount ₹**
Cash Balance with RBI	20	0	0
Balances with other Banks	28	20	5.6
Other Investments	38	100	38

Loans and Advances:

(i) guaranteed by government	18.5	0	0
(ii) Others	6625	100	6625
Premises, furniture and fixtures	108	100	108
			6776.60

Off-Balance Sheet Item	**₹ in Crores**	**Credit Conversion Factor**	
Guarantees & Other Obligations	600	100	600
Acceptances, Endorsements and Letters of credit	4,200	100	4,200
			11576.60

Risk Weighted Assets Ratio: $\frac{\text{Capital Funds (Tier I Tier II)}}{\text{Risk Adjusted Assets + off Balance sheet items}} \times 100$

$= \frac{911 + 11.7}{6776.60 + 4,800}$

Capital Adequacy Ratio = 922.7/ 11576.6 = 7.97%

Q-25 Forward Bank Ltd furnishes the following information as on 31st March, 2020.

	Amount in ₹
Bills Discounted	82,23,000
Rebate on bills discounted as on 1st April, 2019	1,32,960
Discount received	6,33,990

Details of bills discounted is as given below:

Value of Bills (₹)	**Due Date**	**Rate of Discount**
10,95,000	15th June, 2020	14%
30,00,000	25th June, 2020	12%
16,92,000	5th July, 2020	16%
24,36,000	15th July, 2020	16%

(i) Calculate the rebate on bills discounted as on 31st March, 2020. Take 365 days in year.

(ii) Pass necessary Journal Entries.

Ans.

(a) In order to determine the amount to be credited to the Profit and Loss A/c it is necessary to first ascertain the amount attributable to the unexpired portion of the period of the respective bills. The workings are as given below:

Value (₹)	**Due Date**	**Days after 31-03-2020**	**Discount %**	**Discount Amount ₹**
10,95,000	15-06-2020	(30+31 + 15) = 76	14%	31,920
30,00,000	25-06-2020	(30 + 31 + 25) = 86	12%	84,822
16,92,000	05-07-2020	(30 + 31 + 30 + 5) = 96	16%	71,203
24,36,000	15-07-2020	(30 + 31 + 30 + 15) = 106	16%	1,13,191
		Rebate on bills discounted as on 31.3.2020		3,01,136

The journal entries will be as follows :

		Dr. ₹	Cr. ₹
Rebate on Bills Discounted A/c	Dr.	1,32,960	
To Discount on Bills A/c			1,32,960
(Being the transfer of Rebate on Bills Discounted on 1.4.2019 to Discount on Bills Account)			
Discount on Bills A/c	Dr.	3,01,136	
To Rebate on Bills Discounted A/c			3,01,136
(Being the transfer of rebate on bills discounted required on 1.4.2020 from discount on Bills Account)			
Discount on Bills A/c	Dr.	4,65,814	
To Profit and Loss A/c			4,65,814
(Being the amount of discount on Bills transferred to Profit and Loss Account)			

Working Note:

The amount of discount to be credited to the Profit and Loss Account will be:	
Transfer from Rebate on bills discount as on 1.4.19	1,32,960
Add: Discount received during the year ended 31-3-2020	6,33,990
	7,66,950
Less: Rebate on bills discounted as on 31.3.2020	(3,01,136)
	4,65,814

(b) State with reason whether the following cash credit account is NPA or not:

	₹
Sanctioned limit	50,00,000
Drawing power	44,00,000
Amount outstanding continuously 01-01-20 to 31-03-20	40,00,000
Total interest debited for the above period	3,20,000
Total credits for the above period	1,80,000

(b)

	₹
Sanctioned limit	50,00,000
Drawing power	44,00,000
Amount outstanding continuously from 1.01.2020 to 31.03.2020	40,00,000
Total interest debited	3,20,000
Total credits	1,80,000
Is credit in the account is sufficient to cover the interest debited during the period or	No
Amount is 'overdue' for a continuous period of 90 days.	Yes

The cash credit account is NPA because the credit in the account is not sufficient to cover the interest debited during the period and the amount is 'overdue' for a continuous period of 90 days.

Q-26 From the following information of Sun Bank Limited, Prepare Profit and Loss Account for the year ended 31st March, 2021 after providing 35% of the profits towards provision for taxation and transferring 25% of the profit to Statutory Reserves:

Particulars	₹ in lakhs	Particulars	₹ in lakhs
Interest on Cash Credit	364	Interest paid on Recurring Deposits	17
Interest on Overdraft	150	Interest paid on Savings Bank Deposits	12
Interest on Term Loans	308	Auditor's Fees and Allowances	24
Income on Investments	168	Directors' Fees and Allowance	50
Interest on Balance with RBI	30	Advertisement	36
Commission on remittances and transfer	15	Salaries, allowances and bonus to employees	248
Commission on Letters of Credit	24	Payment to Provident Fund	56
Commission on Government Business	16	Printing & Stationaery	28
Profit on Sale of Land & Building	5	Repairs & Maintenance	10
Loss on exchange	10	Postage, courier & telephones	16
Interest paid on Fixed Deposits	25		

Other Information:

₹ in lakhs

	Earned		Collected
Interest on NPA is as follows:			
Cash Credit	164		80
Term Loans	90		20
Overdraft	150		50
Classification of Non-performing Advances:			
Standard		60	
Sub-standard-fully secured		22	
Doubtful assets-fully unsecured		40	
Doubtful assets covered fully by security:			
Less than 1 year		6	
More than 1 year upto 3 years		3	
More than 3 years		2	
Loss Assets		38	

Ans.

Sun Bank Limited

Profit and Loss Account

For the year ended 31st March, 2021

₹ in lakhs

	Particulars	Schedule	Year ended 31-3-2021
I	Income		
	Interest earned	13	766
	Other income	14	50
			816

II	Expenditure		
	Interest expended	15	54
	Operating expenses	16	468
	Provisions and Contingencies (Refer W.N.)		158.96
			680.96
III	Profit/Loss		
	Net Profit/(Loss) for the year		135.04
	Net Profit/(Loss) brought forward		Nil
			135.04
IV	Appropriations:		
	Transfer to Statutory reserve (25% of the profits)		33.76
	Balance carried to the balance sheet		101.28
	Total		135.04

Schedule 13 - Interest Earned

			Year ended 31-3-2021 (₹ in lakhs)
I	Interest/discount on advances/bills		
	Interest on cash credit (364-84)	280	
	Interest on overdraft (150-100)	50	
	Interest on term loans (308-70)	238	568
II	Income on investments		168
III	Interest on Balance with RBI		30
			766

Interest on NPA is recognized on cash basis, hence difference of accrued interest not received have been reduced from the total accrued interest.

Schedule 14 - Other Income

			Year ended 31-3-2021 (₹ in lakhs)
I	Commission, Exchange and Brokerage:		
	Commission on remittances and transfer	15	
	Commission on letter of credit	24	
	Commission on Government business	16	55
II	Profit on sale of Land and Building		5
III	Loss on Exchange Transactions		(10)
			50

Schedule 15 - Interest Expended

			Year ended 31-3-2021 (₹ in lakhs)
I	Interest on Deposits		
	Fixed deposits	25	
	Recurring deposits	17	
	Saving bank deposits	12	54

Schedule 16 - Operating Expenses

			Year Ended 31-3-2021
			(₹ in lakhs)
I	Payment to and provision for employees		
	Salaries, allowances and bonus	248	
	Provident Fund Contribution	56	304
II	Printing and Stationery		28
III	Advertisement and publicity		36
IV	Directors' fees, allowances and expenses		50
V	Auditors' fees and expenses		24
VI	Postage, telegrams, telephones etc.		16
VII	Repairs and maintenance		10
			468

Working Note:

Provisions and contingencies			(₹ in lakhs)
Provision for Advances:			
Standard	60 × 0.40%		0.24
Sub-standard	22 × 15%		3.3
Doubtful not covered by security	40× 100%		40
Doubtful covered by security:			
Less than 1 year	6 x 25%	1.5	
More than 1 year but less than 3 years	3 x 40%	1.2	
More than 3 years	2 x 100%	2.0	4.7
Loss Assets	(38 × 100%)		38
			86.24
Provision for tax	35% of (Total Income – Total Expenditure)		
	35% of [816-(54+468+86.24)]		
	35% of [816 - 608.24]		
	35% of 207.76		72.72
			158.96

Q-27 The following is an extract from the Trial Balance of Jeevan Bank Ltd. as at 31st March, 2021:

Rebate on bills discounted as on 1-4- 2020 1,36,518 (Cr.)

Discount received 3,40,312 (Cr.)

Analysis of the bills discounted reveals as follows:

Amount (₹)	Due date
5,60,000	June 1, 2021
17,44,000	June 8, 2021
11,28,000	June 21, 2021
16,24,000	July 1, 2021
12,00,000	July 5, 2021

You are required to find out the amount of discount to be credited to Profit and Loss account for the year ending 31st March, 2021 and pass Journal Entries. The rate of discount may be taken at 10% per annum.

Ans. The amount of rebate on bills discounted as on 31st March, 2021 the period which has not been expired upto that day will be calculated as follows:

Discount on ₹ 5,60,000 for 62 days @ 10%	9,512
Discount on ₹ 17,44,000 for 69 days @ 10%	32,969
Discount on ₹ 11,28,000 for 82 days @ 10%	25,341
Discount on ₹ 16,24,000 for 92 days @ 10%	40,934
Discount on ₹ 12,00,000 for 96 days @ 10%	31,562
Total	1,40,318

Note: The due date of the bills discounted is included in the number of days above.

The amount of discount to be credited to the profit and loss account will be:

	₹
Transfer from rebate on bills discounted as on 1.4. 2020	1,36,518
Add: Discount received during the year	3,40,312
	4,76,830
Less: Rebate on bills discounted as on 31.03. 2021 (as above)	(1,40,318)
	3,36,512

Journal Entries

	₹	₹
Rebate on bills discounted A/c Dr.	1,36,518	
To Discount on bills A/c		1,36,518
(Transfer of opening unexpired discount on 1.4. 2020)		
Discount on bills A/c Dr.	1,40,318	
To Rebate on bills discounted A/c		1,40,318
(Unexpired discount on 31.03. 2021 taken into account)		
Discount on Bills A/c Dr.	3,36,512	
To P & L A/c		3,36,512
(Discount earned in the year, transferred to P&L A/c)		

Q-28 The following figures are available from the books of Star Bank Ltd. for the year ended 31st March, 2021.

	Amount in ₹
Interest and Discounts Received	1,52,00,640
Interest Paid on Deposits	91,81,440
Salaries and Allowances	10,00,000
Directors' Fees and Allowances	1,40,000
Rent and Taxes Paid	4,00,000
Postage	2,61,360
Statutory Reserve Fund	32,00,000
Commission, Exchange and Brokerage Earned	7,60,000
Rent Received	2,88,000
Profit on sale of Investments	9,03,200
Depreciation on Assets	1,60,000
Statutory Expenses	1,52,000
Preliminary Expenses	1,20,000
Auditors' Fees	48,000

The following further information is also available:

(i) Issued and Subscribed Capital of the Bank is ₹ 40,00,000

(ii) Preliminary Expenses to be fully written off during the year.

(iii) Rebate on Bills Discounted was ₹ 60,000 as on 31st March, 2020 and was ₹ 80,000 on 31st March, 2021.

(iv) Transfer 25% of the profits to statutory reserves.

(v) Income Tax of ₹ 8,00,000 is to be provided.

(vi) Mr. G, a customer of the bank, who had taken an advance of ₹ 40,00,000 from the bank became insolvent and only 25% was expected to be recovered from his estate.

(vii) A provision of ₹ 8,00,000 was also necessary on other debts.

(viii) There was no opening balance of Profit and Loss Account.

You are required to prepare the Profit and Loss Account and the Schedules of Profit and Loss Account of Star bank for the year ended 31st March, 2021. Also show how the Profit and Loss Account will appear in the Balance Sheet.

Ans.

Star Bank Limited

Profit and Loss Account for the year ended 31st March, 2021

		Schedule	Year ended 31.03.2021 ₹
I.	Income:		
	Interest earned	13	1,51,80,640
	Other income	14	19,51,200
	Total		1,71,31,840
II.	Expenditure		
	Interest expended	15	91,81,440

	Operating expenses	16	22,81,360
	Provisions and contingencies (W.N.1)		46,00,000
	Total		1,60,62,800
III.	Profits/Losses		
	Net profit for the year		10,69,040
	Profit brought forward		nil
			10,69,040
IV.	Appropriations		
	Transfer to statutory reserve (25% of 10,69,040)		2,67,260
	Balance carried over to balance sheet		8,01,780
			10,69,040

Profit & Loss Account balance of ₹ 8,01,780 will appear under the head 'Reserves and Surplus' in Schedule 2 of the Balance Sheet.

		Year ended 31.3.2021 (₹)
	Schedule 13 – Interest Earned	
I	Interest/discount on advances/bills (Refer W.N. 2)	1,51,80,640
		1,51,80,640
	Schedule 14 – Other Income	
I.	Commission, exchange and brokerage	7,60,000
II.	Profit on sale of investment	9,03,200
III.	Rent received	2,88,000
		19,51,200
	Schedule 15 – Interest Expended	
I.	Interests paid on deposits	91,81,440
		91,81,440
	Schedule 16 – Operating Expenses	
I.	Payment to and provisions for employees (salaries &allowances)	10,00,000
II.	Rent, taxes paid	4,00,000
III.	Depreciation on assets	1,60,000
IV.	Director's fee, allowances and expenses	1,40,000
V.	Auditor's fee	48,000
VI.	Statutory expenses	1,52,000
VII.	Postage	2,61,360
VIII.	Preliminary expenses	1,20,000
		22,81,360

Working Notes:

1. **Provisions and contingencies**

	₹
Provision on advance to Mr. G	30,00,000
Provision on other debts	8,00,000
Provision for Income tax	8,00,000
	46,00,000

2. **Interest and discount earned**

	₹
Interest and discount received	1,52,00,640
Add: Rebate on bills discounted on 31.3. 2020	60,000
Less: Rebate on bills discounted on 31.3. 2021	(80,000)
	1,51,80,640

Q-29 From the following information, you are required to prepare Profit and Loss Account of Popular Bank for the year ended 31st March 2021.

Particulars	₹
Interest on cash credit	13,65,000
Interest on overdraft	5,62,500
Interest on term loans	11,55,000
Income on investments	6,30,000
Interest on balance with RBI	1,12,500
Commission on remittances and transfer	56,250
Commission on letters of credit	88,500
Commission on government business	61,500
Profit on sale of land and building	20,250
Loss on exchange transactions	39,000
Interest paid on deposit	20,40,000
Auditor's fees and allowances	90,000
Directors's fees and allowances	1,87,500
Advertisements	1,35,000
Salaries, allowances and bonus to employees	9,30,000
Payment to Provident Fund	2,10,000
Printing and stationery	1,05,000
Repairs and maintenance	37,500
Postage, telegrams, telephones	60,000

Other information :

(i) Interest on NPA is as follows:

	Earned (₹)	Collected (₹)
Cash credit	6,15,000	3,00,000
Overdraft	3,37,500	75,000
Term loans	5,62,500	1,87,500

(ii) Classification of Non-Performing Advances:

	₹
Standard	22,50,000
Sub-standard	8,40,000
Doubtful assets not covered by security	1,50,000
Doubtful assets covered by security for one year	37,500
Loss Assets	1,50,000

(iii) Investment ₹ 20,62,500

Bank should not keep more than 25% of its investment as 'Held -to Maturity'.
The market value of its rest 75% investment is ₹ 14,81,250 as on 31st March, 2021.

Ans.

Popular Bank

Profit and Loss Account

For the year ended 31st March, 2021

	Particulars	Schedule	Year ended 31-3-2021 (₹)
I	Income		
	Interest earned	13	28,72,500
	Other income	14	1,87,500
			30,60,000
II	Expenditure		
	Interest expended	15	20,40,000
	Operating expenses	16	17,55,000
	Provisions and Contingencies (W.N)		5,10,000
			43,05,000
III	Profit/Loss		(12,45,000)
IV	Appropriations		Nil

Schedule 13 - Interest Earned

		Year ended 31-3-2021 (₹)	
I	Interest/discount on advances/bills		
	Interest on cash credit ₹ (13,65,000-3,15,000)	10,50,000	
	Interest on overdraft ₹ (5,62,500-2,62,500)	3,00,000	
	Interest on term loans ₹ (11,55,000-3,75,000)	7,80,000	21,30,000
II	Income on investments		6,30,000
III	Interest on Balance with RBI		1,12,500
			28,72,500

Interest on NPA is recognized on cash basis, hence excess reduced.

Schedule 14 - Other Income

		Year ended 31-3-2021 (₹)	
I	Commission, Exchange and Brokerage		
	Commission on remittances and transfer	56,250	
	Commission on letter of credit	88,500	
	Commission on Government business	61,500	2,06,250
II	Profit on sale of Land and Building		20,250
III	Loss on Exchange Transactions		(39,000)
			1,87,500

Schedule 15 - Interest Expended

		Year ended 31-3-2021 (₹)
I	Interest on Deposits	20,40,000

Schedule 16 - Operating Expenses

Year ended 31-3-2021 (₹)

I	Payment and provision for employees		
	Salaries, allowances and bonus	9,30,000	
	Provident Fund Contribution	2,10,000	11,40,000
II	Printing and Stationery		1,05,000
III	Advertisement and publicity		1,35,000
IV	Directors' fees and allowances		1,87,500
V	Auditors' fees and expenses		90,000
VI	Postage, telegrams, telephones etc.		60,000
VII	Repairs and maintenance		37,500
			17,55,000

Working Note:

Provisions and contingencies			(₹)
Provision for NPA:			
Standard	22,50,000 × 0.40% 9,000		
Sub-standard	8,40,000 × 15% *		1,26,000
Doubtful not covered by security	1,50,000 × 100%		1,50,000
Doubtful covered by security for one year	37,500 × 25% 9,375		
Loss Assets	1,50,000 × 100%		1,50,000
			4,44,375
Depreciation on current investments			
Cost (75% of 20,62,500)		15,46,875	
Less: Market value		(14,81,250)	65,625
			5,10,000

* It is assumed that sub-standard asset is fully secured.

Note: 25% of the total investments are held to maturity. In the case of Held to Maturity investments the valuation is done at cost and these are not marked to market value generally. Hence, depreciation on investments has been calculated only on other investments which can either be Held for Trading (HFT) or Available for Sale (AFS).

Q-30 The following is an extract of Trial Balance of a bank as on 31st March, 2022:

	Dr. (₹)	Cr. (₹)
Bill Discounted	15,16,800	
Discount Received		1,26,859
Rebate on Bills discounted not due on 31st March, 2021		26,592

An analysis of bill discounted is as follows:

Amount in '	Due Date	Rate of Discount
1,46,200	4th May, 2022	15
2,30,400	12th May, 2022	15
4,35,900	28th May, 2022	15
4,36,200	18th June, 2022	16
2,68,100	4th July, 2022	16

You are required to calculate Rebate on Bills Discounted as on 31st March, 2022 and show necessary Journal Entries.

Ans. **Statement showing rebate on bills discounted**

Value	Due Date	Days after 31.3.2021	Rate of discount	Discount Amount
1,46,200	4.5.22	(30+ 4) = 34	15%	2,043
2,30,400	12.5.22	(30+12) = 42	15%	3,977
4,35,900	28.5.22	(30+28) = 58	15%	10,390
4,36,200	18.6.22	(30+ 31+ 18) = 79	16%	15,106
2,68,100	4.7.22	(30+ 31+30+4) = 95	16%	11,165
15,16,800	Rebate on bills discounted on 31.3.2022			42,681

Note: 365 days have been considered in a year.

In the books of SM Bank Ltd. - Journal Entries

(i)	Rebate on bills discounted Account	Dr.	26,592	
	To Discount on bills Account			26,592
	[Being opening balance of rebate on bills discounted account transferred to discount on bills account]			
(ii)	Bills purchased & discounted Account	Dr.	15,16,800	
	To Discount on bills Account			1,26,859
	To Clients Account			13,89,941
	(Being bills purchased and discounted during the year)			
(iii)	Discount on bills Account	Dr.	42,681	
	To Rebate on bills discounted Account			42,681
	[Being provision made on 31st March, 2022]			
(iv)	Discount on bills Account	Dr.	1,10,770	
	To Profit and loss Account*			1,10,770
	[Being transfer of discount on bills, of the year, to profit and loss account]			

*Credit to Profit and Loss A/c will be as follows:

₹ (1,26,859 + 26,592 – 42,681) = ₹ 1,10,770

Q-31 From the following information, prepare the Profit & Loss A/c of PNG Bank Ltd. for the year ending 31st March, 2022. Also give necessary schedules.

Particulars	Figures in '000
Total Interest earned on term loans	2,550
Interest earned on term loans classified as NPA	731
Interest received on term loans classified as NPA	238
Total Interest earned on cash credits and overdrafts	5,663
Interest earned but not received on cash credit and overdrafts treated as NPA	923
Interest on deposits	4,120
Commission	201
Profit on sale of investments	1,876
Profit on revaluation of investments	342
Income from Investments	2,174
Payments to and provision for employees	2,745
Rent, Taxes and Lighting	385

Printing and Stationery	62
Director's fees, allowances and expenses	313
Repairs and Maintenance	56
Depreciation on Bank's property	99
Insurance	43

Also make necessary provision on Risk Assets as per the following details:

Particulars	**Figures in '000**
Standard	4,700
Sub-Standard (fully secured)	1,900
Doubtful Assets not covered by security	400
Doubtful Assets covered by security for 1 year	40
Loss Assets	300

Ans.

PNG Bank Limited

Profit & Loss Account for the year ended 31st March, 2022

		Schedule	₹ '000s
I.	Income		
	Interest earned	13	8,971
	Other income	14	2,419
	Total		11,390
II.	Expenditure		
	Interest expended	15	4,120
	Operating expenses	16	3,703
	Provisions (Refer W.N.)		1,013.8
	Total		8,836.8
III.	Profit/Loss		2,553.20

Schedule 13 – Interest Earned

	₹'000s
Interest / discount on advances bills	
Interest on term loans [2,550- (731-238)]	2,057
Interest on cash credits and overdrafts (5,663-923)	4,740
Income on investments	2,174
	8,971

Note: Interest on non-performing assets is recognized on receipt basis.

Schedule 14 – Other Income

	₹ '000s
Commission, exchange and brokerage	201
Profit on sale of investments	1,876
Profit on revaluation of investments	342
	2,419

Schedule 15 – Interest Expended

	₹ '000s
Interest on deposits	4120

Schedule 16 – Operating Expenses

	₹ '000s
Payments to and provision for employees - salaries, bonus and allowances	2,745
Rent, taxes and lighting	385
Printing & stationery	62
Director's fee, allowances and expenses	313
Depreciation Charges	99
Repairs & maintenance	56
Insurance	43
	3,703

Working Note:

Provisions	₹ '000s
Provision for standard and non-performing assets	
Standard (4,700 x .4%)	18.8
Sub-standard (1900 x 15%)	285
Doubtful (400 x 100%)	400
Doubtful (40 x25%)	10
Loss assets (300 x 100%)	300
	1,013.8

Q-32 State with reason whether the following cash credit accounts are NPA or not:

	Case-1	**Case-2**	**Case- 3**	**Case-4**
Sanctioned limit	50,00,000	60,00,000	55,00,000	45,00,000
Drawing power	44,00,000	56,00,000	50,00,000	42,00,000
Amount outstanding continuously 01-01-21 to 31-03-21	40,00,000	48,00,000	56,00,000	30,00,000
Total interest debited for the above period	3,20,000	3,84,000	4,48,000	2,40,000
Total credits for the above period	1,80,000	Nil	4,48,000	3,20,000

Ans.

	Case 1 ₹	**Case 2** ₹	**Case 3** ₹	**Case 4** ₹
Sanctioned limit	50,00,000	60,00,000	55,00,000	45,00,000
Drawing power	44,00,000	56,00,000	50,00,000	42,00,000
Amount outstanding continuously from 1.01.2021 to 31.03.2021	40,00,000	48,00,000	56,00,000	30,00,000
Total interest debited	3,20,000	3,84,000	4,48,000	2,40,000
Total credits	1,80,000	-	4,48,000	320,000

Is credit in the account is sufficient to cover the interest debited during the period or amount is not 'overdue' for a continuous period of 90 days.	No	No	The credit in the account is sufficient to cover the interest debited but the amount outstanding is continuously in excess of the sanctioned drawing power for a continuous period of 90 days.	**Yes**
	NPA	**NPA**	**NPA**	**NOT NPA**

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CHAPTER-9

NON-BANKING FINANCIAL COMPANIES

Q-1 Templeton Finance Ltd. is a non-banking finance company. The extracts of its balance sheet are given below:

Liabilities	Amount Rs. in 000	Assets	Amount Rs. in 000
Paid-up equity capital	100	Leased out assets	800
Free reserves	500	Investment:	
Loans	400	In shares of subsidiaries and	
Deposits	400	group companies	100
		In debentures of subsidiaries	
		and group Companies	100
		Cash and bank balances	200
		Deferred expenditure	200
	1,400		1,400

You are required to compute 'Net owned Fund' of Templeton Finance Ltd. as per Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. **Statement showing computation of 'Net Owned Fund'**

		Rs. in 000
Paid up Equity Capital		100
Free Reserves		500
		600
Less: Deferred expenditure		(200)
	A	400
Investments		
In shares of subsidiaries and group companies		100
In debentures of subsidiaries and group companies		100
	B	200
10% of A		40
Excess of Investment over 10% of A (200-40)	C	160
Net Owned Fund [(A) - (C)] (400-160)		240

Q-2 Write short note on earning value(equity share) in context of NBFC.

Ans. Earning value means the value of an equity share computed by taking the average of profits after tax as reduced by the preference dividend and adjusted for extra-ordinary and non-recurring items, for the immediately preceding three years and further divided by the number of equity shares of the investee company and capitalized at the following rate:

(a) in case of predominantly manufacturing com pany, eight per cent;

(b) in case of predominantly trading company, ten per cent; and

(c) in case of any other company, including non -banking financial company, twelve per cent;

Note: If an investee company is a loss making company the earning value will be taken at zero.

Q-3 While closing its books of account on 31st March, 2018 a Non-Banking Finance Company has its advances classified as follows:

	₹ in lakhs
Standard assets	13,400
Sub-standard assets	670
Secured portions of doubtful debts:	
- Up to one year	160
- one year to three years	45
- more than three years	20
Unsecured portions of doubtful debts	48
Loss assets	24

You are required to Calculate the amount of provision, which must be made against the Advances as per the Non-Banking Financial Company –Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. **Calculation of provision required on advances as on 31st March, 2018:**

	Amount ₹ in lakhs	Percentage of provision	Provision ₹ in lakhs
Standard assets	13,400	.40	53.60
Sub-standard assets	670	10	670
Secured portions of doubtful debts			
. up to one year	160	20	32
. one year to three years	45	30	13.5
. more than three years	20	50	10
Unsecured portions of doubtful debts	48	100	48
Loss assets	24	100	24
			851.10

Q-4 LK Finance Ltd. is a non-banking financial company. It provides you with the following information regarding its outstanding amount, ₹ 400 lakhs of which installments are overdue on 400 accounts for last two months (amount overdue ₹ 80 lakhs), on 24 accounts for three months (amount overdue ₹ 48 lakhs), on 10 accounts for more than 30 months (amount overdue ₹ 40 lakhs) and on 4 accounts for more

than three years (amount over due ₹ 40 lakhs-already identified as sub-standard assets) and one account of ₹ 20 lakhs which has been identified as non-recoverable by the management. Out of 10 accounts overdue for more than 30 months, 6 accounts are already identified as sub-standard (amount ₹ 12 lakhs) for more than fourteen months and other are identified as sub-standard asset for a period of less than fourteen months.

Classify the assets of the company in line with Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. **Statement showing classification as per Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016**

(₹ in lakhs)

Standard Assets		
Accounts (Balancing figure)	172.00	
400 accounts overdue for a period for 2 months	80.00	
24 accounts overdue for a period by 3 months	48.00	300.00
Sub-Standard Assets		
4 accounts identified as sub-standard asset for a period less than 14 months		28.00
Doubtful Debts		
6 accounts identified as sub-standard for a period more than 14 months		12.00
4 accounts identified as sub-standard for a period more than 3 years		40.00
Loss Assets		
1 account identified by management as loss asset		20.00
Total overdue		400.00

Q-5 Lokraj Financiers Ltd. is an NBFC providing Hire Purchase Solutions for acquiring consumer durables. The following information is extracted from its books for the year ended 31st March, 2017:

Asset Funded	**Interest Overdue but recognized in Profit & loss A/c**		**Net Book Value of Assets outstanding**
	Period Overdue	**Interest Amount (₹ in crore)**	**(₹ in crore)**
Washing Machines	Upto 12 months	450.00	20,550.00
Air Conditioners	For 24 months	25.25	675.00
Music systems	For 30 months	15.25	225.00
Refrigerators	For 21 months	60.15	1,050.00
Air purifiers	Upto 12 months	18.25	980.00
LCD Televisions	For 45 months	420.00	21,200.00

You are required to calculate the amount of additional provision to be made.

Ans. On the basis of the information given, in respect of hire purchase and leased assets, additional provision shall be made as under:

(₹ in crore)

(a) Where hire charges areoverdue upto 12 months	Nil	-
(b) Where hire charges areoverdue for more than 12months but upto 24 months	10% of the net book value 10% x (675+1,050)	172.50
(c) Where hire charges areoverdue for more than 24months but upto 36 months	40 percent of the net book value 40% x 225	90
(d) Where hire charges or leaserentals are overdue for morethan 36 months but upto 48 months	70 percent of the net book value 70% x 21,200	14,840
Total		15,102.50

Q-6 While closing its books of account on 31st March, 2017 a Non-Banking Finance Company has its advances classified as follows:

	₹ in lakhs
Standard assets	53,600
Sub-standard assets	2,680
Secured portions of doubtful debts:	
- Up to one year	640
- one year to three years	180
- more than three years	60
Unsecured portions of doubtful debts	194
Loss assets	96

Calculate the amount of provision, which must be made against the Advances as per the Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. **Calculation of provision required on advances as on 31st March, 2017:**

	Amount ₹ in lakhs	Percentage of provision	Provision ₹ in lakhs
Standard assets	53,600	25	134.00
Sub-standard assets	2,680	10	268.00
Secured portions of doubtful debts			
- up to one year	640	20	128.00
- one year to three years	180	30	54.00
- more than three years	60	50	30.00
Unsecured portions of doubtful debts	194	100	194.00
Loss assets	96	100	96.00
			904.00

Q-7 Babu Bhai Financiers Ltd. is an NBFC providing Hire Purchase Solutions for acquiring consumer durables. The following information is extracted from its books for the year ended 31st March, 2018:

Assets Funded	Interest Overdue but recognized in Profit & Loss		Net Book Value of Assets Outstanding
	Period Overdue	Interest Amount (₹ In crore)	(₹ In crore)
LCD Televisions	Up to 12 Months	500.00	20,000
Washing Machines	For 24 Months	100.00	2,000
Refrigerators	For 30 Months	50.00	1,250
Air Conditioners	For 45 Months	25.00	600
Mobile Phones	For 60 Months	10.00	100

You are required to calculate the amount of provision to be made.

Ans. On the basis of the information, in respect of hire purchase and leased assets, additional provision shall be made as under:

(₹ in crore)

(a)	Where hire charges are overdue upto 12 months	Nil	-
(b)	Where hire charges are overdue for more than 12 months but upto 24 months	10% of the net book value 10% x 2,000	200
(c)	Where hire charges are overdue for more than 24 months but upto 36 months	40 percent of the net book value 40% x 1,250	500
(d)	Where hire charges or lease rentals are overdue for more than 36 months but upto 48 months	70 percent of the net book value 70% x 600	420
(e)	Where hire charges or lease rentals are overdue for more than 48 months	100% of net book value (100% x 100)	100
		Total	1,220

Q-8 ABC Financiers Ltd. is an NBFC providing Hire Purchase Solutions for acquiring consumer durables. The following information is extracted from its books for the year ending 31st March, 2017:

Assets Funded	Interest Overdue but recognised in Profit& Loss		Net book value of Assets outstanding
	Paid Overdue	Interest (₹ In lakhs)	(₹ In lakhs)
Computers	Upto 12 months	960.00	40,812.00
Televisions	For 20 months	205.00	4,950.00
Washing Machines	For 32 months	104.20	2,530.00
Refrigerators	For 45 months	53.50	1328.00
Air-conditioners	For 52 months	13.85	305.00

You are required to calculate the amount of provision to be made.

Ans. **Amount of provision to be made is as under:**

Asset Funded **(₹ in crore)**

Computers	(a) Where hire charges are overdue upto 12 months	Nil	-
Televisions	(b) Where hire charges are overdue for more than 12 months but upto 24 months	10% of the net book value 10% x 4,950	495
Washing Machines	(c) Where hire charges are overdue for more than 24 months but upto 36 months	40 percent of the net book value 40% x 2,530	1,012
Refrigerators	(d) Where hire charges or lease rentals are overdue for more than 36 months but upto 48 months	70 percent of the net book value 70% x 1,328	929.60
Air Conditioners	(e) where hire charges or lease rentals are overdue for more than 48 months	100 percent of the net book value 305 x 100%	305
		Total	2,741.60

Q-9 Explain the criterion of income recognition in the case of Non-Banking Financial Companies.

Ans. **Income Recognition in case of NBFC**

(1) The income recognition shall be based on recognised accounting principles.

(2) Income including interest/ discount or any other charges on NPA shall be recognised only when it is actually realised. Any such income recognised before the asset became non-performing and remaining unrealised shall be reversed.

(3) In respect of hire purchase assets, where instalments are overdue for more than 12 months, income shall be recognised only when hire charges are actually received. Any such income taken to the credit of profit and loss account before the asset became nonperforming and remaining unrealized, shall be reversed.

(4) In respect of lease assets, where lease rentals are overdue for more than 12 months, the income shall be recognised only when lease rentals are actually received. The net lease rentals* taken to the credit of profit and loss account before the asset became non-performing and remaining unrealised shall be reversed.

*'Net lease rentals' mean gross lease rentals as adjusted by the lease adjustment account debited/ credited to the profit and loss account and as reduced by depreciation at the rate applicable under Schedule XIV of the Companies Act, 1956 (1 of 1956)/ 2013.

Q-10 A non-banking finance company provides the extract of its balance sheet as given below:

Equity and Liabilities	Amount	Assets	Amount
	₹ in 000		₹ in 000
Paid-up equity capital	400	Leased out assets	3,200
Free reserves	2,000	Investment:	
Loans	1,600	In shares of subsidiaries and	
Deposits	1,600	group companies	400
		In debentures of subsidiaries and	
		group Companies	400
		Cash and bank balances	800
		Deferred expenditure	800
	5,600		**5,600**

You are required to compute 'Net owned Fund' of this NBFC as per Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. **Statement showing computation of 'Net Owned Fund'**

		₹ in 000
Paid up Equity Capital		400
Free Reserves		2,000
		2,400
Less: Deferred expenditure		(800)
	A	1,600
Investments		
In shares of subsidiaries and group companies		400
In debentures of subsidiaries and group companies		400
	B	800
10% of A		160
Excess of Investment over 10% of A (800-160)	C	640
Net Owned Fund [(A) - (C)] (1,600-640)		960

Q-11 Write short note on Earning value (Equity share) as per NBFC Prudential Norms (RBI) directions.

Ans. Earning value means the value of an equity share computed by taking the average of profits after tax as reduced by the preference dividend and adjusted for extra-ordinary and non-recurring items, for the immediately preceding three years and further divided by the number of equity shares of the investee company and capitalized at the following rate:

- in case of predominantly manufacturing company, eight per cent;
- in case of predominantly trading company, ten per cent; and
- in case of any other company, including non-banking financial company, twelve per cent;

Note: If an investee company is a loss making company the earning value will be taken at zero.

Q-12 While closing its books of account on 31st March, 2019 a Non-Banking Finance Company has its advances classified as follows:

	₹ in lakhs
Sub-standard assets	2,680
Secured portions of doubtful debts:	
- Up to one year	640
- one year to three years	180
- more than three years	60
Unsecured portions of doubtful debts	194
Loss assets	96

You are required to calculate the amount of provision, which must be made against the above advances as per the Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions 2016.

Ans. Calculation of provision required on advances as on 31st March, 2019:

	Amount ₹ in lakhs	Percentage of provision	Provision ₹ in lakhs
Sub-standard assets	2,680	10	268.00
Secured portions of doubtful debts			
- up to one year	640	20	128.00
- one year to three years	180	30	54.00
- more than three years	60	50	30.00
Unsecured portions of doubtful debts	194	100	194.00
Loss assets	96	100	96.00
			770.00

Q-13 While closing its books of account on 31st March, 2021 a Non-Banking Finance Company has classified its advances as follows:

	₹ in lakhs
Standard assets	13,400
Sub-standard assets	670
Secured portions of doubtful debts:	
" Up to one year	160
" one year to three years	45
" more than three years	20
Unsecured portions of doubtful debts	48
Loss assets	24

You are required to calculate the amount of provision, which must be made against the advances as per the Non-Banking Financial Company –Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. **Calculation of provision required on advances as on 31st March, 2021:**

	Amount ₹ in lakhs	Percentage of provision	Provision ₹ in lakhs
Standard assets	13,400	.40	53.60
Sub-standard assets	670	10	670
Secured portions of doubtful debts			
-up to one year	160	20	32
-one year to three years	45	30	13.5
-more than three years	20	50	10
Unsecured portions of doubtful debts	48	100	48
Loss assets	24	100	24
			851.10

Q-14 XYZ Finance Ltd. is a non-banking finance company. It provides the following information :

	(₹ in lakhs) Amount
Equity and Liabilities	
Paid-up equity capital	200
General Reserve	600
Non-Current Liabilities	
Loans	500
Deposits	600
Assets	
Non-current assets	
Property Plant and Equipment	900
Investments:	
In shares of subsidiaries	250
In debentures of group companies	400
Current Assets	
Cash and bank balances	350

You are required to compute 'Net Owned Fund' of XYZ Finance Ltd. as per Non-Banking Financial Company – Systemically Important Non-Deposit taking company and Deposit taking company (Reserve Bank) Directions, 2016.

Ans. **Statement showing computation of 'Net Owned Fund'**

S. No		₹ in lakhs
Paid up Equity Capital		200
Free Reserves		600
(i)	A	800
Investments		
In shares of subsidiaries		250
In debentures of group companies		400

(ii)		B	650
(iii)	10% of A		80
(iv)	Excess of Investment over 10% of A (650 - 80)	C	570
(v)	Net Owned Fund [(A) - (C)] (800 - 570)		230

Q-15 Siddharth Auto Financiers Limited is a NBFC providing Finance for purchasing of Auto Rickshaws. The following information is extracted from its books for the year 31st March, 2021:

Interest Overdue but recognized in Profit and Loss Account **Net Book Value of Assets Outstanding**

Period Overdue	Interest Amount (₹ In Crore)	(₹ In crores)
Up to 12 Months	750.00	30,000
For 24 Months	200.00	4,000
For 30 Months	200.00	3,750
For 45 Months	250.00	3,000
For 60 Months	500.00	10,000

You are required to calculate the amount of provision be made.

Ans. On the basis of the information, in respect of financed assets, provision shall be made as under:

(₹ in crore)

(a)	Where hire charges are overdue up to 12 months	Nil	-
(b)	Where hire charges are overdue for more than 12 months but up to 24 months	10% of the net book value 10% x 4,000	400
(c)	Where hire charges are overdue for more than 24 months but up to 36 months	40 percent of the net book value 40% x 3,750	1,500
(d)	Where hire charges or lease rentals are overdue for more than 36 months but up to 48 months	70 percent of the net book value 70% x 3,000	2,100
(e)	Where hire charges or lease rentals are overdue for more than 48 months	100% of net book value (100% x 100)	10,000
		Total	**14,000**

Q-16 Universal Financers Ltd. is a Non-Banking Financial Company.

It provides you the following information regarding its advances of ₹ 440 lakhs, of which instalments are overdue on:

- 550 accounts for last 3 months (amount overdue ₹ 105 lakhs)
- 75 accounts for 4 months (amount overdue ₹ 64 lakhs)
- 25 accounts for more than 30 months (amount overdue ₹ 66 lakhs)
- 15 accounts already identified as sub-standard for more than 3 years (unsecured) (amount overdue ₹ 82 lakhs)
- 8 accounts of ₹ 33 lakhs have been identified as non-recoverable by the management. (Out of 25 accounts overdue for more than 30 months, 17 accounts are already identified as substandard for more than 12 months (amount overdue ₹ 19 lakhs) and others are identified as substandard asset for a period of less than 12 months.

Classify the assets of the company In line with the Non-Banking Financial Company -Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. Statement showing classification as per Non-Banking Financial Company -Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016

(₹ in lakhs)

Standard Assets		
Accounts (Balancing figure)	90	
550 accounts overdue for a period of 3 months	105	
75 accounts overdue for a period of 4 months	64	259
Sub-Standard Assets		
8 accounts identified as sub-standard asset for a period less than 12 months	47	
Doubtful Debts		
17 accounts identified as sub-standard for a period more than 12 months	19	
15 accounts identified as sub-standard for a period more than 3 years		82
Loss Assets		
8 accounts identified by management as loss asset		33
Total overdue		440

Q-17 PGL Finance Ltd. is a non-banking financial company. The following information is provided by the company regarding its outstanding amounts: ₹ 600 Lakhs, of which instalments are overdue on 300 accounts for last two months (amount overdue ₹ 150 Lakhs), on 48 accounts for three months (amount overdue ₹ 64 Lakhs), on 20 accounts for more than 30 months (amount overdue ₹ 120 Lakhs) and in 4 accounts for more than three years (amount overdue ₹ 60 Lakhs - already identified as sub-standard asset) and one account of ₹ 40 Lakhs which has been identified as non-recoverable by the management. Out of 20 accounts overdue for more than 30 months, 16 accounts are already identified as sub-standard (amount ₹ 28 Lakhs) for more than fourteen months and others are identified as sub-standard asset for a period of less than fourteen months.

Classify the assets of the company in line with Non-Banking Financial CompanySystematically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. Statement showing classification as per Non-Banking Financial Company -Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016

		(₹ in lakhs)
Standard Assets		
Accounts (Balancing figure)	166.00	
300 accounts overdue for a period for 2 months	150.00	
48 accounts overdue for a period by 3 months	64.00	380.00
Sub-Standard Assets		
4 accounts identified as sub-standard asset for a period less than 14months		92.00
Doubtful Debts		
16 accounts identified as sub-standard for a period more than 14 months		28.00
4 accounts identified as sub-standard for a period more than 3 years		60.00
Loss Assets		
One account identified by management as loss asset		40.00
Total overdue		600.00

Q-18 Vikas Finance Ltd. is a Non Banking Finance Company. The extracts of its Balance Sheet are as under :

Liabilities	(₹ in ₹000)	Assets	(₹ in ₹000)
Paid up Equity Capital	250	Leased out Assets	2,000
Free Reserves	1,250	Investments:	
Loans	1,000	- In shares of subsidiaries and Group Companies	275
Deposits	1,000	- In debentures of subsidiaries and Group Companies	225
Cash & Bank Balances	500		
Deferred Expenditure	500		
TOTAL	**3,500**	**TOTAL**	**3,500**

You are requested to compute the "Net Owned Funds" of Vikas Finance Ltd. as per Non Banking Finance Company - Systematically Important Non-Deposit taking company and Deposit taking company (Reserve Bank) Directions, 2016.

Ans. **Statement showing computation of 'Net Owned Fund'**

		₹ in 000
Paid up Equity Capital		250
Free Reserves		1,250
		1,500
Less: Deferred expenditure		(500)
	A	1,000
Investments		
In shares of subsidiaries and group companies		275
In debentures of subsidiaries and group companies		225
	B	500
10% of A		100
Excess of Investment over 10% of A (500-100)	C	400
Net Owned Fund [(A) - (C)] (1,000-400)		600

Q-19 Calculate 'Owned Fund' of a NBFC based on the following facts:

Paid up share capital: ₹ 400 lakhs

Free reserves: ₹ 200 lakhs

Securities Premium: ₹ 50 lakhs

Capital Reserves (surplus arising due to sale of assets): ₹100 lakhs

Compulsory convertible preference shares (CCPS): ₹ 50 lakhs

Revaluation Reserve: ₹ 100 lakhs

Ans. **Owned fund calculation:**

Paid up share capital: ₹ 400 lakhs

Free reserves: ₹ 200 lakhs

Compulsory convertible preference shares (CCPS): ₹ 50 lakhs

Securities Premium: ₹ 50 lakhs

Capital reserve: ₹ 100 lakhs

Total Owned fund: ₹ 800 lakhs ie. ₹ (400+200+50+50+100) lakhs

Q-20 Omega Financiers Ltd. is an NBFC providing Hire Purchase Solutions for acquiring consumer durables. The following information is extracted from its books for the year ended 31st March, 2020:

Assets Funded	Interest Overdue but recognized in Profit & Loss		Net Book Value of Assets Outstanding
	Period Overdue	Interest Amount (₹ In crore)	(₹ In crore)
LCD Televisions	Up to 12 Months	100.00	4,000
Washing Machines	For 24 Months	20.00	400
Refrigerators	For 30 Months	10.00	250
Air Conditioners	For 45 Months	5.00	120
Mobile Phones	For 60 Months	1.00	10

You are required to calculate the amount of provision to be made.

Ans. On the basis of the information, in respect of hire purchase and leased assets, additional provision shall be made as under:

			(₹ in crore)
(a)	Where hire charges are overdue upto 12 months	Nil	-
(b)	Where hire charges are overdue for more than 12 months but upto 24 months	10% of the net book value (10% x 400)	40
(c)	Where hire charges are overdue for more than 24 months but upto 36 months	40 percent of the net book value (40% x 250)	100
(d)	Where hire charges or lease rentals are overdue for more than 36 months but upto 48 months	70 percent of the net book value (70% x 120)	84
(e)	Where hire charges or lease rentals are overdue for more than 48 months	100% of net book value (100% x 10)	10
		Total	234

Q-21 Gaur Finance Ltd. is a non-banking finance company. It provides the following information:

	₹ in crores
Leased out assets	600
Investment:	
In shares of subsidiaries and group companies	150
In debentures of subsidiaries and group Companies	50
Cash and bank balances	200
Deferred expenditure	100
Paid-up equity capital	100
Free reserves	400
Loans	400
Deposits	400

You are required to compute 'Net owned Fund' of Gaur Finance Ltd. as per Non- Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. **Statement showing computation of 'Net Owned Fund'**

		₹ in crores
Paid up Equity Capital		100
Free Reserves		400
		500
Less: Deferred expenditure		(100)
	A	400
Investments		
In shares of subsidiaries and group companies		150
In debentures of subsidiaries and group companies		50
	B	200
10% of A		40
Excess of Investment over 10% of A (200-40)	C	160
Net Owned Fund [(A) - (C)] (400-160)		240

Q-22 Financiers Ltd. is an NBFC providing Hire Purchase Solutions for acquiring consumer durables. The following information is extracted from its books for the year ended 31st March, 2020:

Assets Funded	Interest Overdue but recognized inNet Profit & Loss Period Overdue	Interest Amount (₹ In crore)	Book Value of Assets Outstanding (₹ In crore)
LEDs	Up to 12 Months	500.00	18,000
Air purifiers For	24 Months	100.00	2,000
R.O. For	30 Months	50.00	1,250
Air Conditioners For	45 Months	25.00	600
Microwaves For	60 Months	10.00	150

You are required to calculate the amount of provision to be made.

Ans. **On the basis of the information, in respect of hire purchase and leased assets, additional provision shall be made as under:**

		(₹ in crore)
(a) Where hire charges are overdue upto 12 months	Nil	-
(b) Where hire charges are overdue for more than 12 months but upto 24 months	10% of the net book value 10% x 2,000	200
(c) Where hire charges are overdue for more than 24 months but upto 36 months	40 percent of the net book value 40% x 1,250	500
(d) Where hire charges or lease rentals are overdue for more than 36 months but upto 48 months	70 percent of the net book value 70% x 600	420
(e) Where hire charges or lease rentals are overdue for more than 48 months	100% of net book value 100% x 150	150
	Total	**1,270**

Q-23 Calculate 'Owned Fund' of an NBFC based on the following information:
Paid up share capital: ₹ 200 lakhs
Free reserves: ₹ 150 lakhs
Compulsory convertible preference shares (CCPS): ₹ 50 lakhs
Revaluation reserve: ₹ 50 lakhs (created by revaluation of assets)
Securities premium: ₹ 25 lakhs
Book value of intangible assets: ₹ 10 lakhs
Capital reserves (surplus arising out of sale proceeds of assets): ₹ 15 lakhs

Ans. **Owned fund calculation:**
Paid up share capital: ₹ 200 lakhs
Free reserves: ₹ 150 lakhs
Compulsory convertible preference shares (CCPS): ₹ 50 lakhs
Securities premium: ₹ 25 lakhs
Capital Reserves : 15 lakhs
Total of all above items : ₹ 440 lakhs reduced by the value of intangible assets ₹ 10 lakhs ie. owned fund is computed as ₹ 430 lakhs.
Note: Revaluation reserve to be excluded while computing owned fund.

Q-24 While closing its books of account at year end, a Non-Banking Finance Company has its advances classified as follows:

	₹ in lakhs
Standard assets	1,26,000
Sub-standard assets	10,050
Secured portions of doubtful debts:	
- up to one year	2,400
- one year to three years	675
- more than three years	225
Unsecured portions of doubtful debts	727
Loss assets	360

Calculate the amount of provision, which must be made against the advances as per the Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016.

Ans. Calculation of provision required on advances as at year end, as per the Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016

	Amount ₹ in lakhs	**Percentage of provision**	**Provision ₹ in lakhs**
Standard assets	1,26,000	0.25	315.00
Sub-standard assets	10,050	10	1,050.00
Secured portions of doubtful debts			
- upto one year	2,400	20	480.00
- one year to three years	675	30	202.50
- more than three years	225	50	112.50
Unsecured portions of doubtful debts	727	100	727.00
Loss assets	360	100	360.00
			3,247.00

Q-25 GEM Ltd. is a NBFC providing Hire Purchaser Solutions for acquiring consumer durables. The following information is extracted from its books for the year ended 31st March 2021.

	₹ in Lakhs
Paid up Equity Capital	2520
Compulsory convertible preference shares	1035
Free Reserve	243
Securities premium	56
Capital Reserve	
(₹ 220 Lakhs surplus arising out of sale of Building)	319
Deferred revenue expenditure	54
Debenture issued	702
Cash & Bank Balances	243
Investments in debentures of subsidiaries	171
Investments in shares of other NBFC	945

You are required to calculate Owned Fund and Net Owned Fund.

Ans. **Statement showing computation of 'Owned Fund' and 'Net Owned Fund'**

		₹ in lakhs
Paid up Equity Capital		2,520
Free Reserves		243
Compulsory convertible preference shares		1035
Securities Premium		56
Capital Reserve (arising out of sale of building)		220
		4074
Less: Deferred revenue expenditure		(54)
Owned Fund	A	4020
Investments		
In shares of other NBFC		945
In debentures of subsidiaries and group companies		171
	B	1116
10% of A		402
Excess of Investment over 10% of A (1116-402)	C	714
Net Owned Fund [(A) - (C)] (4020-714)		3306

Q-26 A non-banking finance company provides the extract of its balance sheet as given below:

Equity and Liabilities	**Amount ₹ in 000**	**Assets**	**Amount ₹ in 000**
Paid-up equity capital	400	Leased out assets	3,200
Free reserves	2,000	Investment:	
Loans	1,600	In shares of subsidiaries and group companies	400
Deposits	1,600	n debentures of subsidiaries and group Companies	400
		Cash and bank balances	800
		Deferred expenditure	800
	5,600		**5,600**

You are required to compute 'Net owned Fund' of this NBFC as per Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

Ans.

		₹ in 000
Paid up Equity Capital		400
Free Reserves		2,000
		2,400
Less: Deferred expenditure		(800)
	A	1,600
Investments		
In shares of subsidiaries and group companies		400
In debentures of subsidiaries and group companies		400
	B	800
10% of A		160
Excess of Investment over 10% of A (800-160)	C	640
Net Owned Fund [(A) - (C)] (1,600-640)		960

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NOTES

CHAPTER-10

CONSOLIDATED FINANCIAL STATEMENTS

Q-1 From the following summarized balance sheets of Kedar Ltd. and its subsidiary Vijay Ltd. drawn up at 31st March, 2019, prepare a consolidated balance sheet as at that date, having regard to the following:

(i) Reserves and Profit and Loss Account of Vijay Ltd. stood at ₹ 62,500 and ₹ 37,500 respectively on the date of acquisition of its 80% shares by Kedar Ltd. on 1st April, 2018.

(ii) Machinery (Book-value ₹ 2,50,000) and Furniture (Book value ₹ 50,000) of Vijay Ltd. were revalued at ₹ 3,75,000 and ₹ 37,500 respectively on 1st April, 2018 for the purpose of fixing the price of its shares. [Rates of depreciation computed on the basis of useful lives: Machinery 10%, Furniture 15%.]

Summarised Balance Sheet of Kedar Ltd. and Vijay Ltd. as on 31st March, 2019

Liabilities	**Kedar Ltd.** ₹	**Vijay Ltd.** ₹	**Assets**	**Kedar Ltd.** ₹	**Vijay Ltd.** ₹
Equity and Liabilities			Non-currentassets		
Shareholders'funds			Fixed assets		
Share Capital			Machinery	7,50,000	2,25,000
Shares of ₹ 100each	15,00,000	2,50,000	Furniture	3,75,000	42,500
Reserves	5,00,000	1,87,500	Other noncurrent assets	11,00,000	3,75,000
Profit and Loss Account	2,50,000	62,500	Non-current Investments		
Trade Payables	3,75,000	1,42,500	Shares in VijayLtd.: 2,000 shares at ₹ 200 each	4,00,000	—
	26,25,000	**6,42,500**		**26,25,000**	**6,42,500**

Ans. **Consolidated Balance Sheet of Kedar Ltd. and its Subsidiary Vijay Ltd. as at 31st March, 2019**

Particulars	**Note No.**		**(₹)**
I. Equity and Liabilities			
(1) Shareholder's Funds			
(a) Share Capital			15,00,000
(b) Reserves and Surplus		1	8,61,500
(2) Minority Interest (W.N.5)			1,20,375
(3) Current Liabilities			
(a) Trade Payables		2	5,17,500
Total			29,99,375

II. Assets		
(1) Non-current assets		
(a) (i) Property, Plant & Equipment	3	14,94,375
(ii) Intangible assets	4	30,000
(b) Other non- current assets	5	14,75,000
Total		29,99,375

Notes to Accounts

			₹
1. Reserves and Surplus			
Reserves		5,00,000	
Add: 4/5th share of Vijay Ltd.'s postacquisition reserves (W.N.3)		1,00,000	6,00,000
Profit and Loss Account		2,50,000	
Add: 4/5th share of Vijay Ltd.'s postacquisition profits (W.N.4)		11,500	2,61,500
			8,61,500
2. Trade Payables			
Kedar Ltd.		3,75,000	
Vijay Ltd.		1,42,500	5,17,500
3. Property, Plant & Equipment			
Machinery			
Kedar Ltd.		7,50,000	
Vijay Ltd.	2,50,000		
Add: Appreciation	1,25,000		
	3,75,000		
Less: Depreciation	(37,500)	3,37,500	
Furniture	-		
Kedar Ltd.	-	3,75,000	
Vijay Ltd.	50,000		
Less: Decrease in value	(12,500)		
	37,500		
Less: Depreciation	(5,625)	31,875	14,94,375
4. Intangible assets			
Goodwill [WN 6]			30,000
5. Other non-current assets			
Kedar Ltd.		11,00,000	
Vijay Ltd.		3,75,000	14,75,000

Working Notes:

1.	**Pre-acquisition profits and reserves of Vijay Ltd.**		₹
	Reserves		62,500
	Profit and Loss Account		37,500
			1,00,000
	Kedar Ltd.'s = 4/5 × 1,00,000		80,000
	Minority Interest = 1/5 × 1,00,000		20,000
2.	**Profit on revaluation of assets of Vijay Ltd.**		-
	Profit on Machinery ₹ (3,75,000 – 2,50,000)		1,25,000
	Less: Loss on Furniture ₹ (50,000 – 37,500)		12,500
	Net Profit on revaluation		1,12,500
	Kedar Ltd.'s share 4/5 × 1,12,500		90,000
	Minority Interest 1/5 × 1,12,500		22,500
3.	**Post-acquisition reserves of Vijay Ltd.**		-
	Post-acquisition reserves (Total reserves less pre-acquisition		
	reserves = ₹ 1,87,500 – 62,500)		1,25,000
	Kedar Ltd.'s share 4/5 × 1,25,000		1,00,000
	Minority interest 1/5 × 25,000		25,000
4.	**Post -acquisition profits of Vijay Ltd.**		-
	Post-acquisition profits (Profit & loss account balance		
	lesspre-acquisition		
	profits = ₹ 62,500 – 37,500)		25,000
	Add: Excess depreciation charged on furniture @ 15%		-
	on ₹ 12,500 i.e. (50,000 – 37,500)		1,875
			26,875
	Less: Under depreciation on machinery @ 10%		-
	on ₹ 1,25,000 i.e. (3,75,000 – 2,50,000)		(12,500)
	Adjusted post-acquisition profits		14,375
	Kedar Ltd.'s share 4/5 × 14,375		11,500
	Minority Interest 1/5 × 14,375		2,875
5.	**Minority Interest**		-
	Paid-up value of (2,500 – 2,000) = 500 shares		-
	held by outsiders i.e. 500 × ₹ 100		50,000
	Add: 1/5th share of pre-acquisition profits and reserves		20,000
	1/5th share of profit on revaluation		22,500
	1/5th share of post-acquisition reserves		25,000
	1/5th share of post-acquisition profit		2,875
			1,20,375

6.	**Cost of Control or Goodwill**	
	Paid-up value of 2,000 shares held by Kedar Ltd. i.e. 2,000 × ₹ 100	2,00,000
	Add: 4/5th share of pre-acquisition profits and reserves	80,000
	4/5th share of profit on the revaluation	90,000
	Intrinsic value of shares on the date of acquisition	3,70,000
	Price paid by Kedar Ltd. for 2,000 shares	4,00,000
	Less: Intrinsic value of the shares	(3,70,000)
	Cost of control or Goodwill	30,000

Q-2 A Ltd. acquired 70% of equity shares of B Ltd. on 1.4.2010 at cost of Rs. 10,00,000 when B Ltd. had an equity share capital of Rs. 10,00,000 and reserves and surplus of Rs. 80,000. In the four consecutive years, B Ltd. fared badly and suffered losses of Rs. 2,50,000, Rs. 4,00,000, Rs. 5,00,000 and Rs. 1,20,000 respectively. Thereafter in 2014-15, B Ltd. experienced turnaround and registered an annual profit of Rs. 50,000. In the next two years i.e. 2015-16 and 2016-17, B Ltd. recorded annual profits of Rs. 1,00,000 and Rs. 1,50,000 respectively. Show the minority interests and cost of control at the end of each year for the purpose of consolidation.

Ans. The losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. The excess, and any further losses applicable to the minority, are adjusted against the majority interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses. If the subsidiary subsequently reports profits, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered. Accordingly, the minority interests will be computed as follows:

Year	Profit/(Loss) Interest (30%)	Minority P& L (Dr.) Cr.	Additional Consolidated	Minority's Share of losses borne by A Ltd. Rs.	Balance	Cost ofControl
At the time of acquisition in 2010		3,24,000 (W.N.)	-			
2010-11	(2,50,000)	(75,000)	(1,75,000)			2,44,000 (W.N.)
Balance 2011-12	(4,00,000)	2,49,000 (1,20,000)	(2,80,000)			2,44,000
Balance 2012-13	(5,00,000)	1,29,000 (1,50,000)	(3,50,000)			2,44,000
	Loss of minority borne by Holding Co.	(21,000) 21,000	(21,000)	21,000	21,000	

Balance		Nil	(3,71,000)			
2013-14	(1,20,000)	(36,000)	(84,000)			2,44,000
	Loss of minority borne by Holding Co.	36,000	(36,000)	36,000	57,000	
Balance		Nil	(1,20,000)			
2014-15	50,000	15,000	35,000			2,44,000
	Profit share of minority adjusted against losses of minority absorbed by Holding Co.	(15,000)	15,000	(15,000)	42,000	
		Nil	50,000			
2015-16	1,00,000	30,000	70,000			
	Profit share of minority adjusted against losses of minority absorbed by Holding Co.	(30,000)	30,000	(30,000)	12,000	2,44,000
Balance		Nil	100,000			
2016-17	1,50,000	45,000	1,05,000	(12,000)	Nil	2,44,000
		(12,000)	12,000			
Balance		33,000	1,17,000			

Working Note:

		Share of Holding Co.	Minority Interest
	100%	**70%**	**30%**
	(Rs.)	**(Rs.)**	**(Rs.)**
Share Capital	10,00,000	7,00,000	3,00,000
Reserve	80,000	56,000	24,000
		7,56,000	3,24,000
Less: Cost of investment		(10,00,000)	
Goodwill		2,44,000	

Q-3 From the following data, determine the amount of holding company's profit in the consolidated Balance Sheet assuming holding company's own Profit & Loss Account to be ₹ 2,00,000 in each case:

Case	Subsidiary Company	% shares owned	Cost	Date of acquisition 1.1.2018		Consolidation Date 31.12.2018	
				Share Capital	Profit & Loss Account	Share Capital	Profit & Loss Account
			₹	₹	₹	₹	₹
Case 1	A	90%	1,40,000	1,00,000	50,000	1,00,000	70,000
Case 2	B	85%	1,04,000	1,00,000	30,000	1,00,000	20,000
Case 3	C	80%	56,000	50,000	20,000	50,000	20,000
Case 4	D	100%	1,00,000	50,000	40,000	50,000	55,000

Ans. The balance in the Profit & Loss Account on the date of acquisition (1.1.2018) is Capital profit, as such the balance of Consolidated Profit & Loss Account shall be equal to Holding Co.'s profit.

On 31.12.2018 in each case the following amount shall be added or deducted from the balance of holding Co.'s Profit & Loss account.

	% Share holding [K]	P & L as on 31.12.2018	P & L as on consolidation [L]	P & L post acquisition date [M] [N] = [M]-[L]	Amount to be added / (deducted) from holding's P & L [O] = [K] x [N]
1	90 %	50,000	70,000	20,000	18,000
2	85 %	30,000	20,000	(10,000)	(8,500)
3	80 %	20,000	20,000	NIL	NIL
4	100 %	40,000	55,000	15,000	15,000

Q-4 Consider the following summarized balance sheets of subsidiary Neel Ltd.:

	2015 ₹	2016 ₹		2015 ₹	2016 ₹
Share-Capital			Fixed Assets		
Issued & subscribed			Cost	1,60,000	1,60,000
2,500 equity shares			*Less*: Accumulated		
of ₹ 100 each	2,50,000	2,50,000	depreciation	(24,000)	(48,000)
Reserves & Surplus				1,36,000	1,12,000
Revenue reserves	1,43,000	3,57,000	Investments at cost		
Current Liabilities			Current Assets:	—	2,00,000
& Provisions:					
Trade Payables	2,45,000	2,47,000	Inventory	2,98,500	3,71,000
Bank overdraft	—	85,000	Trade Receivables	2,97,000	4,45,500
Provision for taxation	1,55,000	2,15,000	Prepaid Expenses	36,000	24,000
			Cash at Bank	25,500	1,500
	7,93,000	**11,54,000**		**7,93,000**	**11,54,000**

Also consider the following information:

(i) Neel Ltd. is a subsidiary of Sky Ltd. Both the companies follow calendar year as the accounting year.

(ii) Sky Ltd. values inventory on LIFO basis while Neel Ltd. used FIFO basis. To bring Neel Ltd.'s values in line with those of Sky Ltd. its value of inventory is required to be reduced by ₹ 6,000 at the end of 2015 and ₹ 17,000 at the end of 2016.

(iii) Neel Ltd. deducts 1% from Trade Receivables as a general provision against doubtful debts.

(iv) Prepaid expenses in Neel Ltd. include advertising expenditure carried forward of ₹ 30,000 in 2015 and ₹ 15,000 in 2016, being part of initial advertising expenditure of ₹ 45,000 in 2015 which is being written off over three years. Similar amount of advertising expenditure of Sky Ltd. has been fully written off in 2015.

You are required to restate the balance sheet of Neel Ltd. as on 31st December, 2016 after considering the above information, for the purpose of consolidation. Make the necessary restatement which is necessary to make the accounting policies adopted by Sky Ltd. and Neel Ltd. uniform.

Ans. Adjusted revenue reserves of Neel Ltd.

	₹	₹
Revenue reserves as given		3,57,000
Add: Provision for doubtful debts [4,45,500 / 99 x 1]		4,500
		3,61,500
Less: Reduction in value of Inventory	17,000	
Advertising expenditure to be written off	15,000	(32,000)
Adjusted revenue reserve		3,29,500

Note: Since Neel Ltd. follows FIFO basis, it is assumed that opening inventory has been sold out during the year 2015. Therefore, reduction in inventory would have been taken care of by sale value. Hence no adjustment has been made for the same.

Restated Balance Sheet of Neel Ltd.
as at 31st December, 2016

	Particulars	Note No.	(₹)
I.	Equity and Liabilities		
(1)	Shareholder's Funds		
	(a) Share Capital		2,50,000
	(b) Reserves and Surplus	1	3,29,500
(2)	Current Liabilities		
	(a) Short term borrowings	2	85,000
	(b) Trade Payables		2,47,000
	(c) Short-term provision	3	2,15,000
	Total		11,26,500
II.	Assets		
(1)	Non-current assets		
	(a) Fixed assets		
	Tangible assets	4	1,12,000
	(b) Non-current Investment		2,00,000
(2)	Current assets		
	(a) Inventories		3,54,000
	(b) Trade Receivables		4,50,000
	(c) Cash & Cash Equivalents		1,500
	(d) Other current assets	5	9,000
	Total		11,26,500

Notes to Accounts

			₹
1.	Reserves and Surplus		
	Revenue Reserve (refer computation of adjusted revenue reserves of Neel Ltd)		3,29,500
2.	Short term borrowings		
	Bank overdraft		85,000
3.	Short-term provision		
	Provision for taxation		2,15,000
4.	Tangible Assets		
	Cost	1,60,000	
	Less: Depreciation to date	(48,000)	1,12,000
5.	Other current assets		
	Prepaid expenses (After adjusting advertising expenditure to be written off each year)		9,000

Q-5 XYZ Ltd. purchased 80% shares of ABC Ltd. on 1st January, 2016 for ₹ 2,80,000. The issued capital of ABC Ltd., on 1st January, 2016 was ₹ 2,00,000 and the balance in the Profit & Loss Account was ₹ 1,20,000.

During the year ended 31st December, 2016, ABC Ltd. earned a profit of ₹ 40,000 and at year end, declared and paid a dividend of ₹ 60,000.

Show by an entry how the dividend should be recorded in the books of XYZ Ltd.

What is the amount of minority interest as on 1st January, 2016 and 31st December, 2016?

Ans. Total dividend paid = ₹ 60,000

Out of post-acquisition profit = ₹ 40,000

Out of pre-acquisition profit = ₹ 20,000

Hence, 2/3rd of dividend received by XYZ will be credited to P & L and 1/3rd will be credited to Investment.

XYZ Ltd.'s share of dividend = ₹ 60,000 X 80% = ₹ 48,000

In the books of XYZ Ltd.

		₹	₹
Bank A/c	Dr.	48,000	
To Profit & Loss A/c			32,000
To Investments in ABC Ltd.			16,000
(Dividend received from ABC Ltd. 1/3 credited to investment A/c being out of capital profits – as explained above)			
Goodwill on Consolidation:			₹
Cost of shares less dividend out of capital profits			2,64,000
Less: Face value of capital i.e. 80% of capital		1,60,000	
Add: Share of capital profits [1,20,000-20,000 (dividend portion out of pre-acquisition profits)] X 80 %		80,000	2,40,000
Goodwill			24,000
Minority interest on: 1st January, 2016: 20% of ₹ 3,20,000 [2,00,000 + 1,20,000]			64,000
31st December, 2016: 20% of ₹ 3,00,000 [2,00,000 + 1,20,000 + 40,000 – 60,000]			60,000

Q-6 Given below are the Profit & Loss Accounts of H Ltd. and its subsidiary Ltd. for the year ended 31st March, 2017:

	H Ltd. (₹ in lacs)	S Ltd. (₹ in lacs)
Incomes:		
Sales and other income	5,000	1,000
Increase in Inventory	1,000	200
	6,000	1,200
Expenses:		
Raw material consumed	800	200
Wages and Salaries	800	150
Production expenses	200	100
Administrative Expenses	200	100
Selling and Distribution Expenses	200	50
Interest	100	50
Depreciation	100	50
	2,400	700
Profit before tax	3,600	500
Provision for tax	1,200	200
Profit after tax	2,400	300
Dividend paid	1,200	150
Balance of Profit	1,200	150
Other Information:		

H Ltd. sold goods to S Ltd. of ₹ 120 lacs at cost plus 20%. Inventory of S Ltd. includes such goods valuing ₹ 24 lacs. Administrative expenses of S Ltd. include ₹ 5 lacs paid to H Ltd. as consultancy fees. Selling and distribution expenses of H Ltd. include ₹ 10 lacs paid to S Ltd. as commission.

H Ltd. holds 80% of equity share capital of ₹1,000 lacs in S Ltd. prior to 2015-2016. H Ltd. took credit to its Profit and Loss Account, the proportionate amount of dividend declared and paid by S Ltd. for the year 2015-2016.

You are required to prepare a consolidated profit and loss account of H Ltd. and its subsidiary S Ltd. for the year ended on 31st March, 2017.

Ans. **Consolidated Profit & Loss Account of H Ltd. and its subsidiary S Ltd. for the year ended on 31st March, 2017**

	Particulars	Note No.	₹ in Lacs
I.	Revenue from operations	1	5,865
II.	Total revenue		5,865
III.	Expenses		
	Cost of Material purchased/Consumed	3	1,180
	Changes of Inventories of finished goods	2	(1,196)
	Employee benefit expense	4	950
	Finance cost	6	150
	Depreciation and amortization expense	7	150
	Other expenses	5	535
	Total expenses		1,769

IV.	Profit before Tax(II-III)		4,096
	V. Tax Expenses	8	1,400
VI.	Profit After Tax		2,696
	Profit transferred to Consolidated Balance Sheet		
	Profit After Tax		2,696
	Dividend paid		
	H Ltd.	1,200	
	S Ltd.	150	
		1,350	
	Less: Share of H Ltd. in dividend of S Ltd.		
	80% of ₹ 150 lacs	(120)	(1,230)
	Profit to be transferred to consolidated balance sheet		1,466

Notes to Accounts

		₹ in Lacs	₹ in Lacs
1.	Revenue from Operations		
	Sales and other income		
	H Ltd.	5,000	
	S Ltd.	1,000	
		6,000	
	Less: Inter-company Sales	(120)	
	Consultancy fees received by H Ltd. from S Ltd.	(5)	
	Commission received by S Ltd. from H Ltd.	(10)	5,865
2.	Increase in Inventory		
	H Ltd.	1,000	
	S Ltd.	200	
		1,200	
	Less: Unrealized profits ₹ 24 lacs × $\frac{20}{120}$	(4)	1,196
			7,061
3.	Cost of Material purchased/consumed		
	H Ltd.	800	
	S Ltd.	200	
		1,000	
	Less: Purchases by S Ltd. from H Ltd.	(120)	880
	Direct Expenses		
	H Ltd.	200	
	S Ltd.	100	300
			1,180
4.	Employee benefits and expenses		
	Wages and Salaries:		
	H Ltd.	800	
	S Ltd.	150	950
5.	Other Expenses		
	Administrative Expenses		
	H Ltd.	200	
	S Ltd.	100	
		300	
	Less: Consultancy fees received by H Ltd. from S Ltd.	(5)	295
	Selling and Distribution Expenses:		
	H Ltd.	200	

	S Ltd.	50	
		250	
	Less: Commission received from S Ltd. from H Ltd.	(10)	240
			535
6.	Finance Cost		
	Interest:		
	H Ltd.	100	
	S Ltd.	50	150
7.	Depreciation and Amortisation		
	Depreciation:		
	H Ltd.	100	
	S Ltd.	50	150
8.	Provision for tax		
	H Ltd.	1,200	
	S. Ltd.	200	1,400

Q-7 XYZ Ltd. purchased 80% shares of ABC Ltd. on 1st January, 2016 for ₹ 2,80,000. The issued capital of ABC Ltd., on 1st January, 2016 was ₹ 2,00,000 and the balance in the Profit & Loss Account was ₹ 1,20,000. During the year ended 31st December, 2016, ABC Ltd. earned a profit of ₹ 40,000 and at year end, declared and paid a dividend of ₹ 60,000.
Show by an entry how the dividend should be recorded in the books of XYZ Ltd.
What is the amount of minority interest as on 1st January, 2016 and 31st December, 2016?

Ans. Total dividend paid = ₹ 60,000
Out of post-acquisition profit = ₹ 40,000
Out of pre-acquisition profit = ₹ 20,000
Hence, 2/3rd of dividend received by XYZ will be credited to P & L and 1/3rd will be credited to Investment.
XYZ Ltd.'s share of dividend = ₹ 60,000 X 80% = ₹ 48,000

In the books of XYZ Ltd.

		₹	₹
Bank A/c	Dr.	48,000	
To Profit & Loss A/c			32,000
To Investments in ABC Ltd.			16,000
(Dividend received from ABC Ltd. 1/3 credited to investment A/c being out of capital profits – as explained above)			
Goodwill on Consolidation:			₹
Cost of shares less dividend out of capital profits			2,64,000
Less: Face value of capital i.e. 80% of capital		1,60,000	
Add: Share of capital profits [1,20,000-20,000 (dividend portion out of pre-acquisition profits)] x 80 %		80,000	2,40,000
Goodwill			24,000
Minority interest on: 1st January, 2016: 20% of ₹ 3,20,000 [2,00,000 + 1,20,000]			64,000
31st December, 2016: 20% of ₹ 3,00,000 [2,00,000 + 1,20,000 + 40,000 – 60,000]			60,000

Q-8 Given below are the Profit & Loss Accounts of Hello Ltd. and its subsidiary Sun Ltd. for the year ended 31st March, 2017:

	Hello Ltd. (₹ in lacs)	Sun Ltd. (₹ in lacs)
Incomes:		
Sales and other income	10,000	2,000
Increase in Inventory	2,000	400
	12,000	2,400
Expenses :		
Raw material consumed	1,600	400
Wages and Salaries	1,600	300
Production expenses	400	200
Administrative Expenses	400	200
Selling and Distribution Expenses	400	100
Interest	200	100
Depreciation	200	100
	4,800	1,400
Profit before tax	7,200	1,000
Provision for tax	2,400	400
Profit after tax	4,800	600
Dividend paid	2,400	300
Balance of Profit	2,400	300

Other Information:

Hello Ltd. sold goods to Sun Ltd. of ₹ 240 lacs at cost plus 20%. Inventory of Sun Ltd. includes such goods valuing ₹ 48 lacs. Administrative expenses of Sun Ltd. include ₹10 lacs paid to Hello Ltd. as consultancy fees. Selling and distribution expenses of Hello Ltd. include ₹ 20 lacs paid to Sun Ltd. as commission. Hello Ltd. holds 80% of equity share capital of ₹ 2,000 lacs in Sun Ltd. prior to 2015-2016. Hello Ltd. took credit to its Profit and Loss Account, the proportionate amount of dividend declared and paid by Sun Ltd. for the year 2015-2016.

You are required to prepare a consolidated profit and loss account of Hello Ltd. and its subsidiary Sun Ltd. for the year ended 31st March, 2017.

Ans. **Consolidated Profit & Loss Account of Hello Ltd. and its subsidiary Sun Ltd. for the year ended on 31st March, 2017**

	Particulars	Note No.	₹ in Lacs
I.	Revenue from operations	1	11,730
II.	Total revenue		11,730
III.	Expenses		
	Cost of Material purchased/Consumed	3	2,360
	Changes of Inventories of finished goods	2	(2,392)
	Employee benefit expense	4	1,900
	Finance cost	6	300
	Depreciation and amortization expense	7	300
	Other expenses	5	1,070
	Total expenses		3,538

IV.	Profit before Tax(II-III)		8,192
V.	Tax Expenses	8	2,800
VI.	Profit After Tax		5,392
	Profit transferred to Consolidated Balance Sheet		
	Profit After Tax		5,392
	Dividend paid		
	Hello Ltd.	2,400	
	Sun Ltd.	300	
		2,700	
	Less: Share of Hello Ltd. in dividend of Sun Ltd.		
	80% of ₹ 300 lacs	(240)	(2,460)
	Profit to be transferred to consolidated balance sheet		2,932

Notes to Accounts

		₹ in Lacs	₹ in Lacs
1.	Revenue from Operations		
	Sales and other income		
	Hello Ltd.	10,000	
	Sun Ltd.	2,000	
		12,000	
	Less: Inter-company Sales	(240)	
	Consultancy fees received by Hello Ltd. from SunLtd.	(10)	
	Commission received by Sun Ltd. from Hello Ltd.	(20)	11,730
2.	Increase in Inventory		
	Hello Ltd.	2,000	
	Sun Ltd.	400	
		2,400	
	Less: Unrealized profits ₹ 48 lacs × $\frac{20}{120}$	(8)	2,392
			14,122
3.	Cost of Material purchased/consumed		
	Hello Ltd.	1,600	
	Sun Ltd.	400	
		2,000	
	Less: Purchases by Sun Ltd. from Hello Ltd.	(240)	1,760
	Direct Expenses		
	Hello Ltd.	400	
	Sun Ltd.	200	600
			2,360
4.	Employee benefits and expenses		
	Wages and Salaries:		
	Hello Ltd.	1,600	
	Sun Ltd.	300	1,900
5.	Other Expenses		
	Administrative Expenses		

	Hello Ltd.	400	
	Sun Ltd.	200	
		600	
	Less: Consultancy fees received by Hello Ltd. from SunLtd.	(10)	590
	Selling and Distribution Expenses:		
	Hello Ltd.	400	
	Sun Ltd.	100	
		500	
	Less: Commission received from Sun Ltd. from Hello Ltd.	(20)	480
			1,070
6.	Finance Cost		
	Interest:		
	Hello Ltd.	200	
	Sun Ltd.	100	300
7.	Depreciation and Amortization		
	Depreciation:		
	Hello Ltd.	200	
	Sun Ltd.	100	300
8.	Provision for tax		
	Hello Ltd.	2,400	
	Sun Ltd.	400	2,800

Note: Since the amount of dividend received by Hello Ltd. for the year 2015-2016 is not given, it has not been deducted from 'sales and other income' in consolidated profit and loss account and not added to consolidated opening retained earnings (which is also not given).

Q-9 Exe Ltd. acquires 70% of equity shares of Zed Ltd. as on 31st March, 2017 at a cost of Rs. 70 lakhs. The following information is available from the balance sheet of Zed Ltd. as on 31st March, 2017:

	Rs. in lakhs
Fixed Assets	120
Investments	55
Current Assets	70
Loans & Advances	15
15% Debentures	90
Current Liabilities	50

The following revaluations have been agreed upon (not included in the above figures):

Fixed Assets	Up by 20%
Investments	Down by 10%

Zed Ltd. declared and paid dividend @ 20% on its equity shares as on 31st March, 2017. Exe Ltd. purchased the shares of Zed Ltd. @ Rs.20 per share.

Calculate the amount of goodwill/capital reserve on acqu isition of shares of Zed Ltd.

Ans. Revalued net assets of Zed Ltd. as on 31st March, 2017

	Rs. in lakhs	Rs. in lakhs
Fixed Assets [120 x 120%]		144.0
Investments [55 x 90%]		49.5
Current Assets		70.0
Loans and Advances		15.0
Total Assets after revaluation		278.5
Less: 15% Debentures	90.0	
Current Liabilities	50.0	(140.0)
Equity / Net Worth		138.5
Exe Ltd.'s share of net assets (70% of 138.5)		96.95
Exe Ltd.'s cost of acquisition of shares of Zed Ltd. (Rs.70 lakhs – Rs.7 lakhs*)		63.00
Capital reserve		33.95

* Total Cost of 70 % Equity of Zed Ltd	Rs. 70 lakhs
Purchase Price of each share	Rs. 20
Number of shares purchased [70 lakhs / Rs. 20]	3.5 lakhs
Dividend @ 20 % i.e. Rs. 2 per share	Rs. 7 lakhs

Since dividend received is for pre-acquisition period, it has been reduced from the cost of investment in the subsidiary company.

Q-10 The following summarised Balance Sheets of H Ltd. and its subsidiary S Ltd. were prepared as on 31st March, 2019:

	H Ltd. (₹)	S Ltd. (₹)
Equity and Liabilities		
Shareholders' Funds		
Equity Share Capital (fully paid up shares of ₹ 10 each)	12,00,000	2,00,000
Reserves and Surplus		
General Reserve	4,35,000	1,55,000
Profit and Loss Account	2,80,000	65,000
Current Liabilities		
Trade Payables	3,25,000	1,25,000
Total	22,40,000	5,45,000
	H Ltd. (₹)	S Ltd. (₹)
Assets		
Non-Current Assets		
Property, Plant and Equipment		
Machinery	6,40,000	1,80,000
Furniture	3,75,000	34,000
Non-Current Investments		
Shares in S Ltd. - 16,000 shares @ ₹ 20 each	3,20,000	-
Current Assets		
Inventories	2,68,000	62,000
Trade Receivables	4,73,000	2,37,000
Cash and Bank	1,64,000	32,000
Total	**22,40,000**	**5,45,000**

H Ltd. acquired the 80% shares of S Ltd. on 1st April, 2018. On the date of acquisition, General Reserve and Profit Loss Account of S Ltd. stood at ₹ 50,000 and ₹ 30,000 respectively.

Machinery (book value ₹ 2,00,000) and Furniture (book value ₹ 40,000) of S Ltd. were revalued at ₹ 3,00,000 and ₹ 30,000 respectively on 1st April,2018 for the purpose of fixing the price of its shares (rates of depreciation computed on the basis of useful lives: Machinery 10% and Furniture 15%). Trade Payables of H Ltd. include ₹ 40,000 due to S Ltd. for goods supplied since the acquisition of the shares. These goods are charged at 10% above cost. The inventories of H Ltd. includes goods costing ₹ 55,000 (cost to H Ltd.) purchased from S Ltd.

You are required to prepare the Consolidated Balance Sheet of H Ltd. with its subsidiary S Ltd. as at 31st March, 2019.

Ans. **Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 2019**

	Particulars	Note No.	(₹)
I.	Equity and Liabilities		
(1)	Shareholder's Funds		
	(a) Share Capital (1,20,000 equity shares of ₹ 10 each)		12,00,000
	(b) Reserves and Surplus	1	8,16,200
(2)	Minority Interest (W.N.4)		99,300
(3)	Current Liabilities		
	(a) Trade Payables	2	4,10,000
	Total		25,25,500
II.	Assets		
(1)	Non-current assets		
	(a) Property, Plant and Equipment		
	(i) Tangible assets	3	13,10,500
	(ii) Intangible assets	4	24,000
	(b) Current assets		
	(i) Inventories	5	3,25,000
	(ii) Trade Receivables	6	6,70,000
	(iii) Cash at Bank	7	1,96,000
	Total		25,25,500

Notes to Accounts

				₹
1.	Reserves and Surplus			
	General Reserves		4,35,000	
	Add: 80% share of S Ltd.'s post- acquisition reserves (W.N.3)		84,000	5,19,000
	Profit and Loss Account		2,80,000	
	Add: 80% share of S Ltd.'s post- acquisition profits (W.N.3)	21,200		
	Less: Unrealised gain	(4,000)	17,200	2,97,200
				8,16,200

2.	Trade Payables			
	H Ltd.		3,25,000	
	S Ltd.		1,25,000	
	Less: Mutual transaction		(40,000)	4,10,000
3.	Tangible Assets			
	Machinery			
	H Ltd.		6,40,000	
	S Ltd.	2,00,000		
	Add: Appreciation	1,00,000		
		3,00,000		
	Less: Depreciation	(30,000)	2,70,000	9,10,000
	Furniture			
	H. Ltd.		3,75,000	
	S Ltd.	40,000		
	Less: Decrease in value	(10,000)		
		30,000		
	Less: Depreciation	(4,500)	25,500	4,00,500
				13,10,500
4.	Intangible assets			
	Goodwill [WN 5]			24,000
5.	Inventories			
	H Ltd.		2,68,000	
	S Ltd.		62,000	3,30,000
	Less: Inventory reserve			(5,000)
				3,25,000
6.	Trade Receivables			
	H Ltd.		4,73,000	
	S Ltd.		2,37,000	
				7,10,000
	Less: Mutual transaction			(40,000)
				6,70,000
7.	Cash and Bank			
	H Ltd.		1,64,000	
	S Ltd.		32,000	1,96,000

Working Notes:

1. Profit or loss on revaluation of assets in the books of S Ltd. and their book values as on 1.4.2018

	₹
Machinery	
Revaluation as on 1.4.2018	3,00,000
Less: Book value as on 1.4.2018	(2,00,000)
Profit on revaluation	1,00,000
Furniture	
Revaluation as on 1.4.2018	30,000
Less: Book value as on 1.4.2018	(40,000)
Loss on revaluation	(10,000)

2. Calculation of short/excess depreciation

	Machinery	Furniture
Upward/ (Downward) Revaluation (W.N. 4)	1,00,000	(10,000)
Rate of depreciation	10% p.a.	15% p.a.
Difference [(short)/excess]	(10,000)	1,500

3. Analysis of reserves and profits of S Ltd. as on 31.03.2019

	Pre-acquisition profit upto 1.4.2018 (Capital profits)	Post-acquisition profits (1.4.2018 – 31.3.2019)	
		General Reserve	Profit and loss account
General reserve as on 31.3.2019	50,000	1,05,000	
Profit and loss account as on 31.3.2019	30,000		35,000
Upward Revaluation of machinery as on 1.4.2018	1,00,000		
Downward Revaluation of Furniture as on 1.4.2018	(10,000)		
Short depreciation on machinery (W.N. 5)			(10,000)
Excess depreciation on furniture (W.N. 5)			1,500
Total	1,70,000	1,05,000	26,500

4. Minority Interest

	₹
Paid-up value of (2,00,000 x 20%)	40,000
Add: 20% share of pre-acquisition profits and reserves [(20% of (50,000 + 30,000)]	16,000
20% share of profit on revaluation	18,000
20% share of post-acquisition reserves	21,000
20% share of post-acquisition profit	5,300
	1,00,300
Less: Unrealised Profit on Inventory (55,000 x 10/110) x 20%	(1,000)
	99,300

5. Cost of Control or Goodwill

Cost of Investment		3,20,000
Less: Paid-up value of 80% shares	1,60,000	
80% share of pre-acquisition profits and reserves (₹ 64,000 + ₹ 72,000)	1,36,000	(2,96,000)
Cost of control or Goodwill		24,000

Q-11 The following data is provided to you:

Case	Subsidiary Company	% shares owned	Cost	Date of acquisition 1.1.2018		Consolidation Date 31.12.2018	
				Share Capital	Profit & Loss Account	Share Capital	Profit & Loss Account
			₹	₹	₹	₹	₹
Case 1	A	90%	1,40,000	1,00,000	50,000	1,00,000	70,000
Case 2	B	85%	1,04,000	1,00,000	30,000	1,00,000	20,000
Case 3	C	80%	56,000	50,000	20,000	50,000	20,000
Case 4	D	100%	1,00,000	50,000	40,000	50,000	55,000

Determine in each case:

(1) Minority interest at the date of acquisition and at the date of consolidation.

(2) Goodwill or Capital Reserve.

Ans. (1) Minority Interest = Equity attributable to minorities

Equity is the residual interest in the assets of an enterprise after deducting all its liabilities i.e. in this case it should be equal to Share Capital + Profit & Loss A/c.

	Minority % Shares Owned [E]	Minority interest as at the date of acquisition [E] x [A + B] ₹	Minority interest as at the date of consolidation [E] X [C + D] ₹
Case 1 [100-90]	10 %	15,000	17,000
Case 2 [100-85]	15 %	19,500	18,000
Case 3 [100-80]	20 %	14,000	14,000
Case 4 [100-100]	NIL	Nil	Nil
A = Share capital on 1.1.2018			
B = Profit & loss account balance on 1.1.2018			
C = Share capital on 31.12.2018			
D = Profit & loss account balance on 1.1.2018			

(2) Calculation of Goodwill or Capital Reserve

	Shareholding % [F]	Cost [G]	Total Equity [A] + [B] = [H]	Parent's Portion of equity [F] x [H]	Goodwill ₹ [G] – [H]	Capital Reserve ₹ [H] – [G]
Case 1	90 %	1,40,000	1,50,000	1,35,000	5,000	—
Case 2	85 %	1,04,000	1,30,000	1,10,500	—	6,500
Case 3	80 %	56,000	70,000	56,000	Nil	Nil
Case 4	100 %	1,00,000	90,000	90,000	10,000	—

Q-12 The Summarised Balance Sheet of X Ltd. and its subsidiary Y Ltd. as on 31st March, 2017 are as follows:

Particulars	Amounts as at 31st March, 2017	
	X Ltd. (₹ in lakhs)	Y Ltd. (₹ in lakhs)
LIABILITIES		
Share Capital:		
Authorised	20,000	8,000
Issues and subscribed:		
Equity share of ₹ 10 each, fully paid up	15,000	6,000
15% preference shares of ₹ 10 each, fully paid up	4,000	1,000
General Reserves	2,500	1,450
Profit & Loss Account	2,750	1,250
Trade payables	1,646	1,027
	25,896	**10,727**
ASSESTS		
Land & Building	3,550	1,510
Plant & Machinery	5,275	3,600
Furniture & Fittings	1,945	655
Investment in Y Ltd.: 450 Lakh Equity share in Y Ltd. purchased on 1st April, 2016	6,800	
Inventory	4,142	2,520
Trade Receivables	3,010	1,882
Cash and Bank Balance	1,174	560
	25,896	**10,727**

The following information is also given to you

(a) 10% dividend on Equity shares was declared by Y Ltd. on 31st March, 2016 for the year ended 31st March, 2016. X Ltd. credited the dividend received to its Profit & Loss Account.

(b) Credit Balance of Profit & Loss account of Y Ltd. as on 1st April, 2016 was ₹ 650 Lakhs.

(c) General Reserve of Y Ltd. stood at same ₹ 1,450 Lakhs as on 1st April, 2016.

(d) Y Ltd.'s Plant & machinery showed a balance of ₹ 4,000 Lakh on 1st April 2016. At the time of purchase of shares in Y Ltd., X Ltd. revalued Y's Ltd. Plant & Machinery upward by ₹ 1,000 Lakh.

(e) Included in Trade Payables of Y Ltd. are ₹ 50 Lakh for goods supplied by X Ltd.

(f) On 31st March, 2017, Y's ltd. inventory included goods for ₹ 150 lakhs which it had purchased from X Ltd. X Ltd. sold goods to Y Ltd. at cost plus 25%.

You are required to prepare a Consolidated Balance Sheet of X Ltd. and its subsidiary Y Ltd. as on 31st March, 2017 giving working notes. (Ignoring dividend on preference shares).

Ans. **Consolidated Balance Sheet of X Ltd. and its subsidiary Y Ltd.as on 31st March, 2017**

	Particulars	Note No.	₹ in lakhs
I	Equity and Liabilities		
1	Shareholders' Funds		
	(a) Share Capital	1	19,000
	(b) Reserves and Surplus	2	5,620
2.	**Minority interest**	3	3,400
3.	**Current Liabilities**		
	(a) Trade payables	4	2,623
	Total		30,643
II	**Assets**		
1	**Non Current Assets**		
	Fixed Assets		
	(i) Tangible Assets	5	17,435
2	**Current Assets**		
	(a) Inventories	6	6,632
	(b) Trade Receivables	7	4,842
	(c) Cash and Cash equivalents	8	1,734
			30,643

Notes to Accounts

			₹ in lakhs
1.	Share Capital		
	Issued, Subscribed and Paid up (1,500 lakh Equity Shares of ₹ 10 each fully paid up)		15,000
	400 lakh Preference Shares of ₹ 10 each fully paid up		4,000
			19,000
2.	**Reserves and Surplus**		
	Credit Balance of Profit & Loss Account	2,750	
	Less: Capital Receipt wrongly credited (Dividend @ 10% on ₹ 4500 Lakh Equity Shares)	450	
		2,300	
	Add: Share in Y Ltd. Revenue Profit (Working Note i)	825	
		3,125	
	Less: Unrealised Profit (Working Note iv)	30	3,095
	Capital Reserve (Working Note iii)	25	
	General Reserve	2,500	2,525
			5,620
3.	**Minority interest**		
	100 Lakh Preference Shares of ₹ 10 fully paid up	1,000	
	150 Lakh Equity Shares of ₹ 10 each fully paid up	1,500	2,500
	Share in Revenue Profits (Working Note i)	275	
	Share in Capital Profit (working Note ii)	625	900
			3,400

4.	**Trade payables**		
	X Ltd.	1,646	
	Y Ltd.	1,027	
		2,673	
	Less: Mutual owing	50	2,623
5.	**Tangible Assets**		
	Land & Building		
	X Ltd.	3,550	
	Y Ltd	1,510	5,060
	Plant & Machinery		
	X Ltd.	5,275	
	Y Ltd (Working note v)	4,500	9,775
	Furniture & Fixtures		
	X Ltd.	1,945	
	Y Ltd	655	2,600
			17,435
6.	**Inventories**		
	X Ltd.	4,142	
	Y Ltd	2,520	
		6,662	
	Less: Unrealized Profit	(30)	6,632
7.	**Trade Receivables**		
	X Ltd.	3,010	
	Y Ltd	1,882	
		4,892	
	Less: Mutual Owing	50	4,842
8.	**Cash & cash Equivalents**		
	X Ltd.	1,174	
	Y Ltd	560	1,734

Working Notes :

(i) Calculation of Revenue Profits Y's Ltd Profit & Loss Account

	₹ in lakh		₹ in lakh
To Equity Dividend		By Balance b/d	650
10 % of 6,000 lakh	600	By Net profit for theyear (Bal Fig.)	1,200
To balance c/d	1,250		
	1,850		**1,850**

Depreciation provided on Plant & Machinery

Balance as on 1st April, 2016	4,000
Less Balance as 31st March 2017	3,600
	400
Hence rate of Depreciation = 400/4000 x 100	10%
Net Profit for the year ended 31st March 2017	1,200
Less: Additional Depreciation	100
Revenue Profit	1,100
X Ltd's share- 1100 x 450/600	825
Y Ltd's share = 1100 x150/600	275

(ii) Calculation of Capital Profits

Profit & Loss Balance as on 1st April, 2016	650
Less: Dividend Paid	600
	50
Add: General Reserve as on 1st April, 2016	1,450
Add: Profit on Revaluation of Plant & machinery	1,000
Capital Profit	2,500
X Ltd's Share in Capital Profit = 2,500 x 450/600	1,875
Y Ltd's Share in Capital Profit = 2,500 x 150/600	625

(iii) Calculation of Capital Reserve

Paid up value of 450 Lakh equity shares	4,500
Add: Share in Capital Profits	1,875
	6,375
Amount Paid to acquire the 450 Lakh Equity Shares	6,800
Less: Dividend received out of Pre acquisition profits	450
	6,350
Capital Reserve = 6,375-6,350	25

(iv) Unrealised Profit

₹ 150 Lakh x 25/125* = 30 lakh

(v) Plant & Machinery of Y Ltd.

Balance as on 31st March, 2017		3,600
Add: Addition due to revaluation	1,000	
Less: Depreciation on additional Value of Plant & Machinery@ 10 %	100	900
		4,500

* ₹ 150 lakh considered as cost to Y Ltd.

Q-13 H Ltd. acquire 70% of equity share of S Ltd. as on 1st January, 2011 at a cost of ₹ 5,00,000 when S Ltd. had an equity share capital of ₹ 5,00,000 and reserves and surplus of ₹ 40,000.

Both the companies follow calendar year as the accounting year.

In the four consecutive years, S Ltd. performed badly and suffered losses of ₹ 1,25,000, ₹ 2,00,000,₹ 2,50,000 and ₹ 60,000 respectively.

Thereafter in 2015, S Ltd. experienced turnaround and registered an annual profit of ₹ 25,000. In the next two years i.e. 2016 and 2017, S Ltd. recorded annual profits of ₹ 50,000 and ₹ 75,000 respectively.

Show the Minority Interests and Cost of Control at the end of each year for the purpose of consolidation.

Ans. The losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. The excess, and any further losses applicable to the minority, are adjusted against the majority interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses. If the subsidiary subsequently reports profits, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered.Accordingly,

Year	Profit / (Loss)	Minority Interest (30%)	Additional Consolidated P & L (Dr.) or Cr.	Minority's Share of losses borne by H Ltd.		Cost of Control
				₹	Balance	
At the time of acquisition on 1.1.2011		1,62,000 (W.N.)	-			
2011	(1,25,000)	(37,500)	(87,500)			1,22,000 (W.N.)
Balance		1,24,500				
2012	(2,00,000)	(60,000)	(1,40,000)			1,22,000
Balance		64,500				
2013	(2,50,000)	(75,000)	(1,75,000)			1,22,000
		(10,500)				
	Loss of minority borne by Holding Co.	10,500	(10,500)	10,500	10,500	
Balance		Nil	(1,85,500)			
2014	(60,000)	(18,000)	(42,000)			1,22,000
	Loss of minority borne by Holding Co.	18,000	(18,000)	18,000	28,500	
Balance		Nil	(60,000)			
2015	25,000	7,500	17,500			1,22,000
	Profit share of minority adjusted against losses of minority absorbed by Holding Co.	(7,500)	7,500	(7,500)	21,000	
Balance		Nil	25,000			
2016	50,000	15,000	35,000	(15,000)	6,000	1,22,000
		(15,000)	15,000			
Balance		Nil	50,000			
2017	75,000	22,500	52,500	(6,000)	Nil	1,22,000
		(6,000)	6,000			
Balance		16,500	58,500			

Working Note :

Calculation of Minority interest and Cost of control on 1.1.2011

		Share of Holding Co.	Minority Interest
	100%	70%	30%
	(₹)	(₹)	(₹)
Share Capital	5,00,000	3,50,000	1,50,000
Reserve	40,000	28,000	12,000
		3,78,000	1,62,000
Less: Cost of investment		(5,00,000)	
Goodwill		1,22,000	

Q-14 The Profit and Loss Accounts of A Ltd. and its subsidiary B Ltd. for the year ended 31st March, 2018 are given below :

		₹ in Lakhs
Incomes	**A Ltd.**	**B Ltd.**
Sales and other income	7,500	1,500
Increase in Inventory	1,500	300
Total	9,000	1,800
Expenses		
Raw material consumed	1,200	300
Wages and Salaries	1,200	225
Production expenses	300	150
Administrative expenses	300	150
Selling and distribution expenses	300	75
Interest	150	75
Depreciation	150	75
Total	3,600	1,050
Profit before tax	5,400	750
Provision for tax	1,800	300
Profit after tax	3,600	450
Dividend paid	1,800	225
Balance of Profit	1,800	225

The following information is also given:

(i) A Ltd sold goods of ₹ 180 Lakhs to B Ltd at cost plus 25%. (1/6 of such goods were still in inventory of B Ltd at the end of the year)

(ii) Administrative expenses of B Ltd include ₹ 8 Lakhs paid to A Ltd as consultancy fees.

(iii) Selling and distribution expenses of A Ltd include ₹ 15 Lakhs paid to B Ltd as commission.

(iv) A Ltd holds 72% of the Equity Capital of B Ltd. The Equity Capital of B Ltd prior to 2016-17 is ₹ 1,500 Lakhs

Prepare a consolidated Profit and Loss Account for the year ended 31st March, 2018.

Ans. **Consolidated Profit & Loss Account of A Ltd. and its subsidiary B Ltd. for the year ended on 31st March, 2018**

	Particulars	Note No.	₹ in Lacs
I.	Revenue from operations	1	8,797
II.	Total revenue		8,797
III.	Expenses		
	Cost of Material purchased/Consumed	3	1,770
	Changes of Inventories of finished goods	2	(1,794)
	Employee benefit expense	4	1,425
	Finance cost	6	225
	Depreciation and amortization expense	7	225
	Other expenses	5	802
	Total expenses		2,653
IV.	Profit before Tax(II-III)		6,144
V.	Tax Expenses	8	2,100
VI.	Profit After Tax		4,044

Notes to Accounts

		₹ in Lacs	₹ in Lacs
1.	Revenue from Operations		
	Sales and other income		
	A Ltd.	7,500	
	B Ltd.	1,500	
		9,000	
	Less: Inter-company Sales	(180)	
	Consultancy fees received by A Ltd. from B Ltd.	(8)	
	Commission received by B Ltd. from A Ltd.	(15)	8,797
2.	Increase in Inventory		
	A Ltd.	1,500	
	B Ltd.	300	
		1,800	
	Less: Unrealised profits ₹ 180×1/6 x 25/125	(6)	1,794
3.	Cost of Material purchased/consumed		
	A Ltd.	1,200	
	BLtd.	300	
		1,500	
	Less: Purchases by B Ltd. from A Ltd.	(180)	1,320
	Direct Expenses		
	A Ltd.	300	
	BLtd.	150	450
			1,770
4.	Employee benefits and expenses		
	Wages and Salaries:		
	A Ltd.	1,200	
	B Ltd.	225	1,425

5.	Other Expenses		
	Administrative Expenses		
	A Ltd.	300	
	B Ltd.	150	
		450	
	Less: Consultancy fees received by A Ltd. from BLtd.	(8)	442
	Selling and Distribution Expenses:		
	A Ltd.	300	
	B Ltd.	75	
		375	
	Less: Commission received from B Ltd. from A Ltd.	(15)	360
			802
6.	Finance Cost		
	Interest:		
	A Ltd.	150	
	B Ltd.	75	225
7.	Depreciation and Amortisation		
	Depreciation:		
	A Ltd.	150	
	B Ltd.	75	225
8.	Provision for tax		
	A Ltd.	1800	
	B Ltd.	300	2100

Note: it is assumed that dividend adjustment has not be done in sales & other income of A Ltd i.e. dividend received from B Ltd is not included in other income of A Ltd. Alternative answer is possible considering is otherwise.

Q-15 The following summarised Balance Sheets of H Ltd. and its subsidiary S Ltd. were prepared as on 31st March, 2017:

	H Ltd. (₹)	**S Ltd. (₹)**
Equity and Liabilities		
Shareholders' Funds		
Equity Share Capital (fully paid up shares of ' 10 each)	12,00,000	2,00,000
Reserves and Surplus		
General Reserve	4,35,000	1,55,000
Profit and Loss Account	2,80,000	65,000
Current Liabilities		
Trade Payables	3,22,000	1,23,000
Total	22,37,000	5,43,000
Assets		
Non-Current Assets		
Fixed Assets		
Machinery	6,40,000	1,80,000
Furniture	3,75,000	34,000
Non-Current Investments		

Shares in S Ltd. - 16,000 shares @ ₹ 20 each	3,20,000	-
Current Assets		
Inventories	2,68,000	62,000
Trade Receivables	4,70,000	2,35,000
Cash and Bank	1,64,000	32,000
Total	22,37,000	5,43,000

H Ltd. acquired the 80% shares of S Ltd. on 1st April, 2016. On the date of acquisition, General Reserve and Profit Loss Account of S Ltd. stood at ₹ 50,000 and ₹ 30,000 respectively.

Machinery (book value ₹ 2,00,000) and Furniture (book value ₹ 40,000) of S Ltd. were revalued at ₹ 3,00,000 and ₹ 30,000 respectively on 1st April,2016 for the purpose of fixing the price of its shares (rates of depreciation computed on the basis of useful lives : Machinery 10% and Furniture 15%). Trade Payables of H Ltd. include ₹ 35,000 due to S Ltd. for goods supplied since the acquisition of the shares. These goods are charged at 10% above cost. The inventories of H Ltd. includes goods costing ₹ 55,000 purchased from S Ltd.

You are required to prepare the Consolidated Balance Sheet as at 31st March, 2017.

Ans. Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd.

as at 31st March, 2017

	Particulars	Note No.	(₹)
I.	Equity and Liabilities		
	(1) Shareholder's Funds		
	(a) Share Capital		
	(1,20,000 equity shares of ₹ 10 each)		12,00,000
	(b) Reserves and Surplus	1	8,16,200
	(2) Minority Interest (W.N.4)		99,300
	(3) Current Liabilities		
	(a) Trade Payables	2	4,10,000
	Total		25,25,500
II.	Assets		
	(1) Non-current assets		
	(a) Fixed assets		
	(i) Tangible assets	3	13,10,500
	(ii) Intangible assets	4	24,000
	(b) Current assets		
	(i) Inventories	5	3,25,000
	(ii) Trade Receivables	6	6,70,000
	(iii) Cash at Bank	7	1,96,000
	Total		25,25,500

Notes to Accounts

				₹
1.	Reserves and Surplus			
	General Reserves		4,35,000	
	Add: 80% share of S Ltd.'s post-acquisition reserves (W.N.3)		84,000	5,19,000
	Profit and Loss Account		2,80,000	
	Add: 80% share of S Ltd.'s post-acquisition profits (W.N.3)	21,200		
	Less: Unrealised gain	(4,000)	17,200	2,97,200
				8,16,200
2.	Trade Payables			
	H Ltd.		3,22,000	
	S Ltd.		1,23,000	
	Less: Mutual transaction		(35,000)	4,10,000
3.	Tangible Assets			
	Machinery			
	H. Ltd.		6,40,000	
	S Ltd.	2,00,000		
	Add: Appreciation	1,00,000		
		3,00,000		
	Less: Depreciation	(30,000)	2,70,000	9,10,000
	Furniture			
	H. Ltd.		3,75,000	
	S Ltd.	40,000		
	Less: Decrease in value	(10,000)		
		30,000		
	Less: Depreciation	(4,500)	25,500	4,00,500
				13,10,500
4.	Intangible assets			
	Goodwill [WN 5]			24,000
5.	Inventories			
	H Ltd.		2,68,000	
	S Ltd.		62,000	3,30,000
	Less: Inventory reserve			(5,000)
				3,25,000
6.	Trade Receivables			
	H. Ltd.		4,70,000	
	S Ltd.		2,35,000	
				7,05,000
	Less: Mutual transaction			(35,000)
				6,70,000
7.	Cash and Bank			
	H. Ltd.		1,64,000	
	S Ltd.		32,000	1,96,000

Working Notes:

1. Profit or loss on revaluation of assets in the books of S Ltd. and their book values as on 1.4.2016

	₹
Machinery	
Revaluation as on 1.4.2016	3,00,000
Less: Book value as on 1.4.2016	(2,00,000)
Profit on revaluation	1,00,000
Furniture	
Revaluation as on 1.4.2016	30,000
Less: Book value as on 1.4.2016	(40,000)
Loss on revaluation	(10,000)

2. Calculation of short/excess depreciation

	Machinery	Furniture
Upward/ (Downward) Revaluation (W.N. 4)	1,00,000	(10,000)
Rate of depreciation	10% p.a.	15% p.a.
Difference [(short)/excess]	(10,000)	1,500

3. Analysis of reserves and profits of S Ltd. as on 31.03.2017

	Pre-acquisition profit upto 1.4.2016 (Capital profits)	Post-acquisition profits (1.4.2016 – 31.3.2017)	
		General Reserve	Profit and loss account
General reserve as on 31.3.2017	50,000	1,05,000	
Profit and loss account as on 31.3.2017	30,000		35,000
Upward Revaluation of machinery as on 1.4.2016	1,00,000		
Downward Revaluation of Furniture as on 1.4.2016	(10,000)		
Short depreciation on machinery (W.N. 5)			(10,000)
Excess depreciation on furniture (W.N. 5)			1,500
Total	1,70,000	1,05,000	26,500

4. Minority Interest

	₹
Paid-up value of (2,00,000 x 20%)	40,000
Add: 20% share of pre-acquisition profits and reserves [(20% of (50,000 + 30,000)]	16,000
20% share of profit on revaluation	18,000
20% share of post-acquisition reserves	21,000
20% share of post-acquisition profit	5,300
	1,00,300
Less: Unrealised Profit on Inventory (55,000 x 10/110)* x 20%	(1,000)
	99,300

* considered that ₹ 55,000 is cost to H Ltd. Alternative solution considering it as cost to S Ltd. is also possible

5. Cost of Control or Goodwill

Cost of Investment		3,20,000
Less: Paid-up value of 80% shares	1,60,000	
80% share of pre-acquisition profits and reserves (₹ 64,000 + ₹ 72,000)	1,36,000	(2,96,000)
Cost of control or Goodwill		24,000

Q-16 In a liquidation which commenced on 11th November, 2017 certain creditors could not receive payments out of the realization of assets and out of the contributions from "A" list contributories.

The following are the details of certain transfer, which took place in 2016 and 2017:

Share holders	Number of shares transferred at the date of ceasing to be member	Date of ceasing to be member	Creditors remaining unpaid and outstanding (₹)
C	2,500	1st September, 2016	5,000
P	1,500	1st January, 2017	9,000
D	2,000	1st April, 2017	12,000
B	700	1st August, 2017	13,500
S	300	15th September, 2017	14,500

All the shares were ₹ 10 each, ₹ 5 paid up.

Ignoring expenses of and remuneration to liquidators show the amount to be realised from various persons listed above.

Ans. **Statement of Liabilities of B list contributors (showing the amount realized)**

Creditors Outstanding on the date of ceasing to be member	P 1,500 Shares ₹	D 2,000 Shares ₹	B 700 Shares ₹	S 300 Shares ₹	Amount to be paid to the Creditors ₹
(1) 9,000	3,000	4,000	1,400	600	9,000
(2) 3,000	-	2,000	700	300	3,000
(3) 1,500	-	-	1,050	450	1,500
(4) 1,000	-	-	-	1,000	150
Total (a)	3,000	6,000	3,150	2,350	
(b) maximum liability on shares held	7,500	10,000	3,500	1,500	
(c) Amount to be realized (a) or (b) whichever is lower	3,000	6,000	3,150	1,500	

Working Notes:

1. C will not be liable since he transferred his shares prior to one year preceding the date of winding up.
2. P will not be responsible for further debts incurred after 01.01.2017 (from the date when he ceases to be a member). Similarly, D & B will not be liable for the debts incurred after the date of their transfer of shares.
3. The increase between 1st August 2017 and 15th September 2017, is solely the responsibility of S. Liability of S has been restricted to the maximum allowable limit of ₹ 1,500. Therefore, amount payable by S on 15.09.2017 is ₹ 150 only.
4. Ratio of discharge of liability will be in the ratio of no. of shares held by B List Contributories which is as follows:

Calculation of Ratio for discharge of Liabilities

Date	Cumulative liability ₹	Increase in liabilities ₹	Ratio of no. of shares held by L, M, N, O
01.01.2017	9,000	-	15:20:7:3
01.04.2017	12,000	3,000	20:7:3
01.08.2017	13,500	1,500	7:3
15.09.2017	14,500	1,000	Only S

Q-17 Consider the following summarized Balance Sheets of subsidiary MNT Ltd. **[10 Marks]**

Liabilities	2017-18 Amount in ₹	2018-19 Amount in ₹
Share Capital		
Issued and subscribed 7500 Equity Shares of ₹100 each	7,50,000	7,50,000
Reserve and Surplus		
Revenue Reserve	2,14,000	5,05,000
Securities Premium	72,000	2,07,000
Current Liabilities and Provisions		
Trade Payables	2,90,000	2,46,000
Bank Overdraft	-	1,70,000
Provision for Taxation	2,62,000	4,30,000
	15,88,000	**23,08,000**
Assets		
Fixed Assets (Cost)	9,20,000	9,20,000
Less : Accumulated Depreciation	(1,70,000)	(2,82,500)
	7,50,000	6,37,500
Investment Cost	-	5,30,000
Current Assets		
Inventory	4,12,300	6,90,000
Trade Receivable	2,95,000	3,43,000
Prepaid expenses	78,000	65,000
Cash at Bank	52,700	42,500
	1,88,000	**23,08,000**

Other information:

(1) MNT Ltd, values inventory on FIFO basis. while MNT Ltd. used LIFO basis. To bring MNT Ltd's inventories values in the with those of LTC Ltd. its value of inventory is required to be reduced by ₹5,000 at the end of 2017- 2018 and increased by ₹ 12,000 at the end of 2018-2019. (Inventory of 2017-18, has been sold out during the year 2018-19)

(3) MNT Ltd. deducts 2% from Trade Receivables as a general provision against doubtful debts.

(4) Prepaid expenses in MNT Ltd. include Sales Promotion expenditure carried forward of ₹ 25,000 in 2017-18 and ₹12,500 in 2018-19 being part of initial Sales Promotion expenditure of ₹ 37,500 in 2017-18. Which is being written off over three years.

Similar nature of Sales Promotion expenditure of LTC Ltd. has been fully written off in 2018-18.

Restate the balance sheet of MNT Ltd. as on 31st March, 2019 after considering the above information for the purpose of consolidation. Such restatement is necessary to make the accounting policies adopted by LTC Ltd. and MNT Ltd. uniform.

Q-18 From the following data determine in each case :

Minority Interest at the date of acquisition and at the date of consolidation.

Case	Subsidiary Company	% of Share Owned	Cost	Date of Acquisition		Consolidation date	
				01-01-2018		31-12-2018	
				Share Capital ₹	Profit and Loss a/c ₹	Share Capital ₹	Profit and Loss a/c ₹
Case - A	X	90%	2,00,000	1,50,000	75,000	1,50,000	85,000
Case -B	Y	75%	1,75,000	1,40,000	60,000	1,40,000	20,000
Case-C	Z	70%	98,000	40,000	20,000	40,000	20,000
Case-D	M	95%	75,000	60,000	35,000	60,000	55,000
Case - E	N	100%	1,00,000	40,000	40,000	40,000	65,000

Ans. Minority Interest = Equity attributable to minorities

Equity is the residual interest in the assets of an enterprise after deducting all its liabilities i.e. in this case, it should be equal to Share Capital + Profit & Loss A/c

A = Share capital on 1.1.2018

B = Profit & loss account balance on 1.1.2018

C = Share capital on 31.12.2018

D = Profit & loss account balance on 31.12.2018

	Minority % Shares Owned [E]	Minority interest as at the date of acquisition [E] x [A + B] ₹	Minority interest as at the date of consolidation [E] X [C + D] ₹
Case A [100-90]	10 %	22,500	23,500
Case B [100-75]	25 %	50,000	40,000
Case C [100-70]	30 %	18,000	18,000
Case D [100-95]	5%	4,750	5,750
Case E [100-100]	NIL	NIL	NIL

Q-19 Hemant Ltd. purchased 80% shares of Power Ltd. on 1st January, 2019 for ₹ 2,10,000. The issued capital of Power Ltd., on 1st January, 2019 was ₹ 1,50,000 and the balance in the Profit & Loss Account was ₹ 90,000. During the year ended 31st December, 2019, Power Ltd. earned a profit of ₹ 30,000 and at year end, declared and paid a dividend of ₹ 22,500. What is the amount of minority interest as on 1st January, 2019 and 31st December, 2019? Also compute goodwill/ capital reserve at the date of acquisition.

Ans. Total dividend paid is ₹ 22,500 (out of post-acquisition profits), hence dividend received by Hemant will be credited to P & L account.

Hemant Ltd.'s share of dividend = ₹ 22,500 x 80% = ₹ 18,000

Goodwill on consolidation (at the date of acquisition):	₹	₹
Cost of shares		2,10,000
Less: Face value of capital i.e. 80% of capital	1,20,000	
Add: Share of capital profits [90,000 X 80 %]	72,000	(1,92,000)
Goodwill		18,000
Minority interest on:		
- **1st January, 2019:**		
20% of ₹ 2,40,000 [1,50,000 + 90,000]		48,000
- **31st December, 2019:**		
20% of ₹ 2,47,500 [1,50,000 + 90,000 + 30,000 – 22,500]		49,500

Q-20 King Ltd. acquires 70% of equity shares of Queen Ltd. as on 31st March, 2020 at a cost of ₹ 140 lakhs. The following information is available from the balance sheet of Queen Ltd. as on 31st March, 2020:

	₹ in lakhs
Property, plant and equipment	240
Investments	110
Current Assets	140
Loans & Advances	30
15% Debentures	180
Current Liabilities	100

The following revaluations have been agreed upon (not included in the above figures):

Property, plant and equipment Up by 20%

Investments Down by 10%

Queen Ltd. declared and paid dividend @ 20% on its equity shares as on 31st March, 2020 (Face value - ₹10 per share). King Ltd. purchased the shares of Queen Ltd. @ ₹20 per share.

Calculate the amount of goodwill/capital reserve on acquisition of shares of Queen Ltd.

Ans. **Revalued net assets of *Queen* Ltd. as on 31st March, 2020**

	₹ in lakhs	*₹ in lakhs*
PPE [240 x 120%]		288
Investments [110 x 90%]		99
Current Assets		140
Loans and Advances		30
Total Assets after revaluation		557
Less: 15% Debentures	180.00	
Current Liabilities	100.0	(280)

Equity / Net Worth	277
King Ltd.'s share of net assets (70% of 277)	193.9
King Ltd.'s cost of acquisition of shares of Queen Ltd.	0
(₹140 lakhs – ₹14 lakhs*)	126
Capital reserve	67.9

* Total Cost of 70 % Equity of *Queen* Ltd ₹ 140 lakhs

Purchase Price of each share	₹ 20
Number of shares purchased [140 lakhs /₹ 20]	₹ 7 lakhs
Dividend @ 20 % i.e. ₹ 2 per share	₹ 14 lakhs

Since dividend received is for pre-acquisition period, it has been reduced from the cost of investment in the subsidiary company.

Q-21 A Ltd holds 75% of the equity capital and voting power in B Ltd. A Ltd purchases inventories costing ₹ 150 lacs from B Ltd at a price of ₹ 200 lacs. The entire inventories remain unsold with A Ltd at the financial year end i.e. 31 March 2019.

Suggest the accounting treatment for this transaction in the consolidated financial statements of A Ltd giving reference of the relevant accounting standard.

Ans. As per para provisions of AS 21, Intragroup balances and intragroup transactions and resulting unrealized profits should be eliminated in full. Unrealized losses resulting from intragroup transactions should also be eliminated unless cost cannot be recovered.

Intragroup balances and intragroup transactions, including sales, expenses and dividends, are eliminated in full. Unrealised profits resulting from intragroup transactions that are included in the carrying amount of assets, such as inventory and fixed assets, are eliminated in full. Unrealised losses resulting from intragroup transactions that are deducted in arriving at the carrying amount of assets are also eliminated unless cost cannot be recovered. One also needs to see whether the intragroup transaction is "upstream" or "down-stream". Upstream transaction is a transaction in which the subsidiary company sells goods to holding company. While in the downstream transaction, holding company is the seller and subsidiary company is the buyer.

Q-22 From the following data, determine Minority Interest on the date of acquisition and on the date of consolidation in each case:

Case	Subsidiary Company	% of Share Owned	Cost	Date of Acquisition		Consolidation date	
				Share Capital ₹	01-01-2019 Profit and Loss A/c ₹	Share Capital ₹	31-12-2019 Profit and Loss A/c ₹
Case-A	X	90%	2,00,000	1,50,000	75,000	1,50,000	85,000
Case-B	Y	75%	1,75,000	1,40,000	60,000	1,40,000	20,000
Case-C	Z	70%	98,000	40,000	20,000	40,000	20,000
Case-D	M	95%	75,000	60,000	35,000	60,000	55,000
Case-E	N	100%	1,00,000	40,000	40,000	40,000	65,000

Ans. Minority Interest = Equity attributable to minorities

Equity is the residual interest in the assets of an enterprise after deducting all its liabilities i.e. in this case, it should be equal to Share Capital + Profit & Loss A/c

A = Share capital on 1.1.2019

B = Profit & loss account balance on 1.1.2019

C = Share capital on 31.12.2019

D = Profit & loss account balance on 31.12.2019

	Minority % Shares Owned [E]	Minority interest as at the date of acquisition [E] x [A + B] ₹	Minority interest as at the date of consolidation [E] x [C + D] ₹
Case A [100-90]	10 %	22,500	23,500
Case B [100-75]	25 %	50,000	40,000
Case C [100-70]	30 %	18,000	18,000
Case D [100-95]	5%	4,750	5,750
Case E [100-100]	NIL	NIL	NIL

Q-23 On 31st March, 2020 H Ltd. and its subsidiary S Ltd. give the following information:

	H Ltd. ₹	S Ltd. ₹
Shareholders' Fund:		
Equity shares of ₹ 10 each	13,40,000	2,40,000
Reserves and Surplus	4,80,000	1,80,000
Profit & Loss Account	2,40,000	60,000
Secured Loans:		
12% Debentures	1,00,000	-
Current Liabilities:		
Creditors	2,00,000	1,22,000
Bank Overdraft	1,00,000	-
Bills Payable	60,000	14,800
Property, Plant & Equipment:		
Machinery	7,20,000	2,16,000
Furniture	3,60,000	40,800
Investments:		
Investments in S Ltd. (19,200 shares at ₹ 20 each)	3,84,000	-
Current Assets:		
Inventories	6,00,000	2,00,000
Trade Receivables	3,00,000	90,000
Bill Receivables	1,00,000	30,000
Cash at Bank	56,000	40,000

The following information is also provided to you:

(a) H Ltd. purchased 19,200 shares of S Ltd. on 1st April, 2019, when the balances of Reserves & Surplus and Profit & Loss Account of S Ltd. stood at ₹ 60,000 and ₹ 36,000 respectively.

(b) Machinery (Book value ₹ 2,40,000) and Furniture (Book value ₹ 48,000) of S Ltd were revalued at ₹ 3,60,000 and ₹ 36,000 respectively on 1st April, 2019, for the purpose of fixing the price of its shares. (Rates of depreciation computed on the basis of useful lives:

Machinery 10%, Furniture 15%).

(c) On 31st March, 2020, Bills payable of ₹ 12,000 shown in S Ltd.'s Balance Sheet had been accepted in favour of H Ltd.

You are required to prepare Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 2020.

Ans. Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 2020

Particulars	Note No.	(₹)
1. Equity and Liabilities		
1. Shareholder's Funds		
(a) Share Capital	1	13,40,000
(b) Reserves and Surplus	2	8,27,040
2. Minority interest		1,15,560
3. Non- Current Liabilities		
(a) 12% Debentures		1 ,00,000
(4) Current Liabilities		
(a) Trade Payables	3	3,84,800
(b) Short term Borrowings (Bank overdraft)		1,00,000
Total		28,67,400
II Assets		
(1) Non-Current Assets		
(a)		
(i) Property, Plant and Equipment	4	14,34,600
(ii) Intangible assets	5	28,800
(2) Current assets		
(a) Inventory (6,00,000+2,00,000)		8,00,000
(b) Trade Receivables	6	5,08,000
(c) Cash and Cash equivalents		96,000
Total		**28,67,400**

Notes to Accounts

1. Share Capital		
Equity share capital		13,40,000
1,34,000 shares of ₹ 10 each fully paid up		
2. Reserves and Surplus		
Reserves	4,80,000	

	Add: 4/5th share of S Ltd.'s post-acquisition reserves (W.N.3)		96,000	5,76,000
	Profit and Loss Account		2,40,000	
	Add: 4/5th share of S Ltd.'s post-acquisition profits (W.N.4)		11,040	2,51,040
				8,27,040
3.	Trade Payables			
	Creditors			
	H Ltd.	2,00,000		
	S Ltd.	1,22,000	3,22,000	
	Bills Payables			
	H Ltd.	60,000		
	S Ltd.	14,800	74,800	
			3,96,800	
	Less: Mutual Owings		(12,000)	3,84,800
4.	Property Plant and Equipment			
	Machinery			
	H. Ltd.		7,20,000	
	S Ltd.	2,40,000		
	Add: Appreciation	1,20,000		
		3,60,000		
	Less: Depreciation (3,60,000 X 10%)	(36,000)	3,24,000	
	Furniture			
	H. Ltd.		3,60,000	
	S Ltd.	48,000		
	Less: Decrease in value	(12,000)		
		36,000		
	Less: Depreciation (36,000 X 15%)	5,400	30,600	14,34,600
5.	Intangible assets			
	Goodwill [WN 6]			28,800
6.	Trade receivables			
	H Ltd.	3,00,000		
	S Ltd.	90,000	3,90,000	
	Bills Receivables			
	H Ltd.	1,00,000		
	S Ltd.	30,000	1,30,000	
			5,20,000	
	Less: Mutual Owings		(12,000)	5,08,000

Working Notes:

1.	Pre-acquisition profits and reserves of S Ltd.	₹
	Reserves	60,000
	Profit and Loss Account	36,000
		96,000
	H Ltd.'s = 4/5 (or 80%) x 96,000	76,800
	Minority Interest= 1/5 (or 20%) x 96,000	19,200
2.	Profit on revaluation of assets of S Ltd.	
	Profit on Machinery ₹ (3,60,000 - 2,40,000)	1,20,000
	Less: Loss on Furniture ₹ (48,000 -36,000)	(12,000)
	Net Profit on revaluation	1,08,000
	H Ltd.'s share 4/5 x 1,08,000	86,400
	Minority Interest 1/5 x 1,08,000	21,600
3.	Post-acquisition reserves of S Ltd.	
	Total reserves	1,80,000
	Less: Pre- acquisition reserves	(60,000)
	Post-acquisition reserves	1,20,000
	H Ltd.'s share 4/5 x 1,20,000	96,000
	Minority interest 1/5 x 1,20,000	24,000
4.	Post -acquisition profits of S Ltd.	
	Post-acquisition profits (Profit & loss account balance less	
	pre-acquisition profits = 60,000 - 36,000)	24,000
	Add: Excess depreciation charged on furniture @ 15%	
	on x 12,000 i.e. (48,000 - 36,000)	1,800 25,800
	Less: Under depreciation on machinery @ 10%	
	on ₹ 1,20,000 i.e. (3,60,000 - 2,40,000)	(12,000)
	Adjusted post-acquisition profits	13,800
	H Ltd.'s share 4/5 x 13,800	11,040
	Minority Interest 1/5 x 13,800	2,760
5.	Minority Interest	
	Paid-up value of (24,000 - 19,200) = 4,800 shares	
	held by outsiders i.e. 2,40,000 X 20%	48,000
	Add: 1/5th share of pre-acquisition profits and reserves	19,200
	1/5th share of profit on revaluation	21,600
	1/5th share of post-acquisition reserves	24,000
	1/5th share of post-acquisition profit	2,760 1,15,560
6.	Cost of Control or Goodwill	
	Price paid by H Ltd. for 19,200 shares (A)	3,84,000
	Less: Intrinsic value of the shares	
	Paid-up value of shares held by H Ltd. i.e. 2,40,000 X 80%	1,92,000
	Add: 4/5th share of pre-acquisition profits and reserves	76,800
	4/5th share of profit on the revaluation	86,400
	Intrinsic value of shares on the date of acquisition (B)	3,55,200
	Cost of control or Goodwill (A -B)	28,800

Q-24 Consider the following information of subsidiary MNT Ltd.-

Liabilities	2019-20 Amount in ₹	2020-21 Amount in ₹
Issued and subscribed: 7,500 Equity Shares of ₹ 100 each	7,50,000	7,50,000
Revenue Reserve	2,14,000	5,05,000
Securities Premium	72,000	2,07,000
Trade Payables	2,90,000	2,46,000
Bank Overdraft	-	1,70,000
Provision for Taxation	2,62,000	4,30,000
Property, plant and equipment (Cost)	9,20,000	9,20,000
Less: Accumulated Depreciation	(1,70,000)	(2,82,500)
	7,50,000	**6,37,500**
Investment (at cost)	-	5,30,000
Inventory	4,12,300	6,90,000
Trade Receivable	2,95,000	3,43,000
Prepaid expenses	78,000	65,000
Cash at Bank	52,700	42,500

Other Information:

(1) MNT Ltd. is a subsidiary of LTC Ltd.

(2) LTC Ltd. values inventory on FIFO basis, while MNT Ltd. used LIFO basis. To bring MNT Ltd.'s inventories values in line with those of LTC Ltd., its value of inventory is required to be reduced by ₹ 5,000 at the end of 2019-2020 and increased by ₹ 12,000 at the end of 2020-2021. (Inventory of 2019-20 has been sold out during the year 2020-21)

(3) MNT Ltd. deducts 2% from Trade Receivables as a general provision against doubtful debts.

(4) Prepaid expenses in MNT Ltd. include Sales Promotion expenditure carried forward of ₹ 25,000 in 2019-20 and ₹ 12,500 in 2020-21 being part of initial Sales Promotion expenditure of ₹ 37,500 in 2019-20, which is being written off over three years. Similar nature of Sales Promotion expenditure of LTC Ltd. has been fully written off in 2019-20.

Restate the balance sheet of MNT Ltd. as on 31st March, 2021 after considering the above information for the purpose of consolidation. Such restatement is necessary to make the accounting policies adopted by LTC Ltd. and MNT Ltd. uniform.

Ans.

Restated Balance Sheet of MNT Ltd.

as at 31st March 2021

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		7,50,000
(b) Reserves and Surplus	1	7,18,500
(2) Current Liabilities		
(a) Short term borrowings	2	1,70,000

	(b) Trade Payables		2,46,000
	(c) Short-term provision	3	4,30,000
	Total		23,14,500
II.	Assets		
(1)	Non-current assets		
(a)	Property, Plant & Equipment	4	6,37,500
(b)	Non-current Investment		5,30,000
(2)	Current assets		
(a)	Inventories (6,90,000 +12,000)	5	7,02,000
(b)	Trade Receivables		3,50,000
	`$\left(\frac{3,43,000}{98}\times 100\right)$		
(c)	Cash & Cash Equivalents		42,500
(d)	Other current assets	6	52,500
	Total		**23,14,500**

Notes to Accounts

			₹
1.	Reserves and Surplus Revenue Reserve (refer W.N.)	5,11,500	
	Securities Premium	2,07,000	7,18,500
2.	**Short term borrowings**Bank overdraft		1,70,000
3.	Short-term provision Provision for taxation		4,30,000
4.	Property, Plant and Equipment Cost	9,20,000	
	Less: Depreciation to date	(2,82,500)	6,37,500
5.	**Inventories**	6,90,000	
	Increase in value as per FIFO	12,000	7,02,000
6.	**Other current assets**Prepaid expenses (After adjusting sales promotion expenses to be written off each year) (65,000 -12,500)		52,500

Working Note:

Adjusted revenue reserves of MNT Ltd.:

	₹	₹
Revenue reserves as given	5,05,000	
Add: Provision for doubtful debts [3,43,000 X 2/98)	7,000	
Add: Increase in value of inventory	12,000	19,000
		5,24,000
Less: Sales Promotion expenditure to be written off		(12,500)
Adjusted revenue reserve		5,11,500

Q-25 The Trial Balances of X Limited and Y Limited as on 31st March, 2021 were as under:

	X Limited (₹ In 000)		Y Limited (₹ In 000)	
	Dr.	**Cr.**	**Dr.**	**Cr.**
Equity Share capital (Share of ₹ 100 each)		2,000		400
7% Preference share capital		-		400
Reserves		600		200
6% Debentures		400		400
Trade Receivables/Trade Payables	160	180	100	120
Profit & Loss A/c balance		40		30
Purchases /Sales	1,000	1,800	1,200	1,900
Wages and Salaries	200		300	
Debenture Interest	24		24	
General Expenses	160		120	
Preference share dividend up to 30.09.2020		7	14	
Inventory (as on 31.03.2021)	200		100	
Cash at Bank	27		12	
Investment in Y Limited	1,056		-	
Fixed Assets	2,200		1,580	
Total	**5,027**	**5,027**	**3,450**	**3,450**

Investment in Y Limited was acquired on 1st July, 2020 and consisted of 80% of Equity Share Capital and 50% of Preference Share Capital.

- After acquiring control over Y Limited, X Limited supplied to Y Limited goods at cost plus 25%, the total invoice value of such goods being ₹ 1,20,000, one fourth of such goods were still lying in inventory at the end of the year.
- Depreciation to be charged @ 10% in X Limited and @ 15% in Y Limited on Fixed Assets.

You are required to prepare the Consolidated Statement of Profit and Loss for the year ended on 31st March, 2021.

Ans. **Consolidated Statement of Profit & Loss Account of X Ltd. and Y Ltd.**
For the year ended 31st March, 2021

Particulars	**Note No.**	**₹**
I. Revenue from operations	1	35,80,000
II. Total revenue		35,80,000
III. Expenses		
Cost of Material purchased/Consumed	2	20,80,000
Changes of Inventories of finished goods		-
Employee benefit expense	3	5,00,000
Finance cost	4	48,000
Depreciation and amortization expense	5	4,57,000
Other expenses	6	2,80,000
Total expenses		33,65,000

IV. Profit before Tax (II-III)		2,15,000
Profit transferred to Consolidated Balance Sheet		
Profit After Tax		2,15,000
Preference dividend	7,000	
Preference dividend payable	7,000	(14,000)
	2,01,000	
Share in pre-acquisition loss (WN 3)		1,800
Share of Minority interest in losses (WN 1)		1,800
Less: Investment Account- dividend for 3 months (prior to acquisition)		(3,500)
Inventory reserve (WN 2)		(6,000)
Profit to be transferred to consolidated balance sheet		1,95,100

Notes to Accounts

		₹	₹
1	Revenue from Operations		
	X Ltd.	18,00,000	
	Y Ltd.	19,00,000	
	Total	37,00,000	
	Less: Intra-group sales (X sold to Y)	(1,20,000)	35,80,000
2	Cost of Materials Purchased/Consumed		
	X Ltd.	10,00,000	
	Y Ltd.	12,00,000	
	Total	22,00,000	
	Less: Intra-group sales (X sold to Y)	(1,20,000)	20,80,000
3	Employee benefit and expenses		
	Wages and salaries		
	H Ltd.	2,00,000	
	S Ltd.	3,00,000	5,00,000
4	Finance cost		
	Interest		
	H Ltd.	24,000	
	S Ltd.	24,000	48,000
5	Depreciation		
	H Ltd.	2,20,000	
	S Ltd.	2,37,000	4,57,000
6	Other expenses		
	H Ltd.	1,60,000	
	S Ltd.	1,20,000	2,80,000

Working Notes:

1.

Profit of Subsidiary		₹
Revenue from Operations		19,00,000
Less: Expenses		
Cost of Material purchased/Consumed	12,00,000	
Changes of Inventories of finished goods	-	
Employee benefit expense	3,00,000	
Finance cost	24,000	
Depreciation and amortization expense	2,37,000	
Other expenses	1,20,000	
Total expenses		(18,81,000)
Profit Before Tax		19,000
Less: Preference Dividend	14,000	
Less: Preference Dividend Payable	14,000	(28,000)
Profit available for shareholders		(9,000)
Minority Share (20% of loss ₹ 9,000)		(1,800)

2. **Inventory reserve** = $\left[\frac{120,000}{4} \times \frac{25}{125}\right]$ = ₹ 6,000

3. **Pre-acquisition loss=** 80% of 3 month's profit up to 30th June, 2020 i.e. 80 % of % of loss ₹ 9,000. Hence, Pre-acquisition loss = ₹ 1,800

4. Investment account includes Preference dividend for 3 months prior to acquisition i.e. ₹ 4,00,000 x 50% x 7% x 1/4 = ₹ 3,500

Q-26 Long Limited acquired 60% stake in Short Limited for a consideration of ₹ 112 lakhs. On the date of acquisition Short Limited's Equity Share Capital was ₹ 100 lakhs, Revenue Reserve was ₹ 40 lakhs and balance in Profit & Loss Account was ₹ 30 lakhs. From the above information you are required to calculate Goodwill / Capital Reserve in the following situations:

(i) On consolidation of Balance Sheet.

(ii) If Long Limited showed the investment in subsidiary at a carrying amount of ₹ 104 lakhs.

(iii) If the consideration paid for acquiring the 60% stake was ₹ 92 lakhs.

Ans.

	₹
60% of the Equity Share Capital ₹ 100 Lakhs	60
60% of Accumulated Reserve ₹ 70 Lakhs (40+30) Lakhs	42
Book value of shares of Short Ltd.	102

(i) Goodwill / Capital Reserve computation on consolidation of balance sheet Long Ltd. paid a positive differential of ₹ 10 Lakhs (112 - 102). This differential ₹ 10 Lakhs is called goodwill and is shown in the balance sheet under the head intangibles.

(ii) If Long Ltd. showed the investment in Short Ltd. at carrying amount of ₹ 104 Lakhs, then the goodwill will be ₹ 2 Lakhs.

(iii) If the consideration paid is ₹ 92 lakhs, then there would have been capital reserve amounting ₹ 10 Lakhs (102- 92).

Q-27 On 31st March, 2020 the summarized Balance Sheets of H Ltd. and its subsidiary S Ltd. stood as follows:

	H Ltd. ₹	S Ltd. ₹
Shareholders' Fund		
Issued and subscribed		
Equity shares of ₹ 10 each	13,40,000	2,40,000
Reserves and Surplus	4,80,000	1,80,000
Profit & Loss Account	2,40,000	60,000
Secured Loans		
12% Debentures	1,00,000	-
Current Liabilities		
Trade Payables	2,00,000	1,22,000
Bank Overdraft	1,00,000	-
Bills Payable	60,000	14,800
Total	**25,20,000**	**6,16,800**
Assets		
Non-Current Assets		
(a) Property, Plant & Equipment		
Machinery	7,20,000	2,16,000
Furniture	3,60,000	40,800
(b) Investments		
Investments in S Ltd. (19,200 shares at ₹ 20 each)	3,84,000	-
Current Assets		
Inventories	6,00,000	2,00,000
Trade Receivables	3,00,000	90,000
Bill Receivables	1,00,000	30,000
Cash at Bank	56,000	40,000
Total	**25,20,000**	**6,16,800**

The following information is also provided to you:

(a) H Ltd. purchased 19,200 shares of S Ltd. on 1st April, 2019, when the balances of Reserves & Surplus and Profit & Loss Account of S Ltd. stood at ₹ 60,000 and ₹ 36,000 respectively.

(b) Machinery (Book value ₹ 2,40,000) and Furniture (Book value ₹ 48,000) of S Ltd were revalued at ₹ 3,60,000 and X 36,000 respectively on 1st April, 2019, for the purpose of fixing the price of its shares. (Rates of depreciation computed on the basis of useful lives:

Machinery 10%, Furniture 15%).

(c) On 31st March, 2020, Bills payable of ₹ 12,000 shown in S Ltd.'s Balance Sheet had been accepted in favor of H Ltd.

You are required to prepare Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 2020.

Ans. Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 2020

Particulars	Note No.		(₹)
I. Equity and Liabilities			
(1) Shareholder's Funds			
(a) Share Capital		1	13,40,000
(b) Reserves and Surplus		2	8,27,040
(2) Minority Interest			1,15,560
(3) Non- Current Liabilities			
(a) 12% Debentures			1,00,000
(4) Current Liabilities			
(a) Trade Payables		3	3,84,800
(b) Short term Borrowings (Bank overdraft)			1,00,000
	Total		**28,67,400**

II. Assets

(1) Non-current assets			
(a)			
(i) Property, Plant and Equipment		4	14,34,600
(ii) Intangible assets		5	28,800
(2) Current assets			
(a) Inventory (6,00,000+2,00,000)			8,00,000
(b) Trade Receivables		6	5,08,000
(c) Cash and Cash equivalents			96,000
	Total		**28,67,400**

Notes to Accounts

		₹
1. Share Capital		
Equity share capital		13,40,000
1,34,000 shares of ₹ 10 each fully paid up		
2. Reserves and Surplus		
Reserves	4,80,000	
Add: 4/5th share of S Ltd.'s post-acquisition reserves (W.N.3)	96,000	5,76,000
Profit and Loss Account	2,40,000	
Add: 4/5th share of S Ltd.'s post-acquisition profits (W.N.4)	11,040	2,51,040
		8,27,040

3.	Trade Payables			
	H Ltd.	2,00,000		
	S Ltd.	1,22,000	3,22,000	
	Bills Payables			
	H Ltd.	60,000		
	S Ltd.	14,800	74,800	
			3,96,800	
	Less: Mutual Owings		(12,000)	3,84,800
4.	Property Plant and Equipment			
	Machinery			
	H. Ltd.		7,20,000	
	S Ltd.	2,40,000		
	Add: Appreciation	1,20,000		
		3,60,000		
	Less: Depreciation (3,60,000 X 10%)	(36,000)	3,24,000	
	Furniture			
	H. Ltd.		3,60,000	
	S Ltd.	48,000		
	Less: Decrease in value	(12,000)	36,000	
	Less: Depreciation (36,000 X 15%)	5,400	30,600	14,34,600
5.	Intangible assets Goodwill [WN 6]			28,800
6.	Trade receivables H Ltd.	3,00,000		
	S Ltd.	90,000	3,90,000	
	Bills Receivables			
	H Ltd.	1,00,000		
	S Ltd.	30,000	1,30,000	
			5,20,000	
	Less: Mutual Owings		(12,000)	5,08,000

Working Notes:

1.	Pre-acquisition profits and reserves of S Ltd.	₹
	Reserves	60,000
	Profit and Loss Account	36,000
		96,000
	H Ltd.'s = 4/5 (or 80%) x 96,000	76,800
	Minority Interest= 1/5 (or 20%) x 96,000	19,200
2.	Profit on revaluation of assets of S Ltd.	
	Profit on Machinery ₹ (3,60,000 - 2,40,000)	1,20,000
	Less: Loss on Furniture ₹ (48,000 -36,000)	(12,000)
	Net Profit on revaluation	1,08,000
	H Ltd.'s share 4/5 x 1,08,000	86,400
	Minority Interest 1/5 x 1,08,000	21,600

3.	Post-acquisition reserves of S Ltd.	
	Total reserves	1,80,000
	Less: Pre- acquisition reserves	(60,000)
	Post-acquisition reserves	1,20,000
	H Ltd.'s share 4/5 x 1,20,000	96,000
	Minority interest 1/5 x 1,20,000	24,000
4.	Post -acquisition profits of S Ltd.	
	Post-acquisition profits (Profit &	
	loss account balance less	
	pre-acquisition profits = ₹ 60,000 - 36,000)	24,000
	Add: Excess depreciation charged on furniture @ 15%	
	on ₹ 12,000 i.e. (48,000 - 36,000)	1,800 25,800
	Less: Under depreciation on machinery @ 10%	
	on ₹ 1,20,000 i.e. (3,60,000 - 2,40,000)	(12,000)
	Adjusted post-acquisition profits	13,800
	H Ltd.'s share 4/5 x 13,800	11,040
	Minority Interest 1/5 x 13,800	2,760
5.	Minority InterestPaid-up value of (24,000 - 19,200) = 4,800 shares	
	held by outsiders i.e. 2,40,000 X 20%	48,000
	Add: 1/5th share of pre-acquisition profits and reserves	19,200
	1/5th share of profit on revaluation	21,600
	1/5th share of post-acquisition reserves	24,000
	1/5th share of post-acquisition profit	2,760
		1,15,560
6.	Cost of Control or Goodwill	
	Price paid by H Ltd. for 19,200 shares (A)	
	Less: Intrinsic value of the shares	
	Paid-up value of shares held by H Ltd. i.e. 2,40,000 X 80% 3,84,000	1,92,000
	Add: 4/5th share of pre-acquisition profits and reserves	76,800
	4/5th share of profit on the revaluation	86,400
	Intrinsic value of shares on the date of acquisition (B)	3,55,200
	Cost of control or Goodwil (A - B)	28,800

Q-28 H Limited acquired 64000 Equity Shares of ₹ 10 each in S Ltd. as on 1st October, 2019.The Balance Sheets of the two companies as on 31st March, 2020 were as under:

Particulars	H Ltd. (₹)	S Ltd. (₹)
Equities and Liabilities:		
Equity Share Capital: Shares of ₹ 10 each	20,00,000	8,00,000
General Reserve (1st April, 2019)	9,60,000	4,20,000
Profit & Loss Account	2,28,800	3,28,000
Preliminary Expenses (1st April, 2019)	-	(20,000)

Bank Overdraft	3,00,000	-
Bills Payable	-	52,000
Trade Payables	1,66,400	80,000
Total	36,55,200	16,60,000
Assets:		
Land and Building	7,20,000	7,60,000
Plant & Machinery	9,60,000	5,40,000
Investment in Equity Shares of S Ltd.	12,27,200	-
Inventories	4,56,000	1,68,000
Trade Receivables	1,76,000	1,60,000
Bills Receivable	59,200	-
Cash in Hand	56,800	32,000
Total	36,55,200	16,60,000

Additional Information:

(1) The Profit & Loss Account of S Ltd. showed credit balance of ₹ 1,20,000 on 1st April, 2019. S Ltd. paid a dividend of 10% out of the same on 1st November, 2019 for the year 2018-19. The dividend was correctly accounted for by H Ltd.

(2) The Plant & Machinery of S Ltd. which stood at ₹ 6,00,000 on 1st April, 2019 was considered worth ₹ 5,20,000 on the date of acquisition by H Ltd. S Ltd. charges depreciation @ 10% per annum on Plant & Machinery.

Prepare consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as on 31st March, 2020 as per Schedule III of the Companies Act, 2013.

Ans. **Consolidated Balance Sheet of H Ltd. and its subsidiary, S Ltd. as at 31st March, 2020**

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	20,00,000
(b) Reserves and Surplus	2	13,07,200
(2) Minority Interest (W.N 4)		2,96,400
(3) Current Liabilities		
(a) Trade Payables	3	2,98,400
(b) Short term borrowings		3,00,000
	Total	**42,02,000**
II. Assets		
(1) Non-current assets		
(i) Property, Plant and Equipment	4	29,34,000
(ii) Intangible assets (W.N.5)		1,60,000
(2) Current assets		
(a) Inventories	5	6,24,000
(b) Trade receivables	6	3,95,200
(c) Cash & Cash equivalents (Cash)	7	88,800
	Total	**42,02,000**

Notes to Accounts

			₹	₹
1.	Share Capital			
	2,00,000 equity shares of ₹ 10 each			20,00,000
2.	Reserves and Surplus			
	Reserves		9,60,000	
	Profit & loss			
	H Ltd.	2,28,800		
	S Ltd. (As per W.N. 3)	1,18,400	3,47,200	13,07,200
3.	Trade Payables			
	H Ltd.	1,66,400		
	S Ltd. (80,000+52,000)		1,32,000	2,98,400
4.	Property, Plant and Equipment			
	Land and building			
	H Ltd.	7,20,000		
	S Ltd.	7,60,000	14,80,000	
	Plant & Machinery			
	H Ltd.	9,60,000		
	S Ltd. (As per W.N. 7)	4,94,000	14,54,000	29,34,000
5.	Inventories			
	H Ltd.		4,56,000	
	S Ltd.		1,68,000	6,24,000
6.	Trade Receivables			
	H Ltd.	1,76,000		
	S Ltd.	1,60,000	3,36,000	
	Bills receivable: H Ltd.		59,200	3,95,200
7.	Cash & Cash equivalents			
	Cash			
	H Ltd.		56,800	
	S Ltd.		32,000	88,800

Working Notes:

1. Share holding pattern

Total Shares of S Ltd 80,000 shares

Shares held by H Ltd 64,000 shares i.e. 80 %;

Minority Shareholding 16,000 shares i.e. 20 %

2. Capital profits of S Ltd.

	₹	₹
Reserve on 1st October, 2019 (Assumed there is nomovement in reserves during the year and hence balanceas on 1st October, 2019 is same as of 31st March 2020)		4,20,000
Profit & Loss Account Balance on 1st April, 2019	1,20,000	
Less: Dividend paid	(80,000)	40,000
Profit for year:		
Total		₹ 3,28,000
Less: ₹ 40,000 (opening balance)		
		₹ 2,88,000
Proportionate up to 1st October, 2019 on time basis		1,44,000
		(₹ 2,88,000/2)
Reduction in value of Plant & Machinery (WN 6)		(50,000)
		5,54,000
Less: Preliminary expenses written off		(20,000)
Total Capital Profit 5,34,000		
Holding company's share (5,34,000 x 80%)		4,27,200
Minority Interest (5,34,000 x 20%)		1,06,800

Note: Preliminary expenses as on 1st April, 2019 amounting ₹ 20,000 have been written off.

3. Revenue profits of S Ltd.

Profit after 1st October, 2019 (3,28,000 - 40,000)/2	1,44,000	
Less 10% depreciation on ₹5,20,000 for 6 months	(26,000)	
Add: Depreciation already charged for 2nd half year on 6,00,000	30,000	4,000
		1,48,000
Holding company's share (1,48,000 X 80%)		1,18,400
Minority Interest (1,48,000 x 20%)		29,600

4. Minority interest

Par value of 16,000 shares (8,00,000 X 20%)	1,60,000
Add: 1/5 Capital Profits [WN 2]	1,06,800
1/5 Revenue Profits [WN 3]	29,600
	2,96,400

5. Cost of Control

Amount paid for 64,000 shares		12,27,200
Less:		
Par value of shares (8,00,000 X 80%)	6,40,000	
Capital Profits – share of H Ltd. [WN 2]	4,27,200	(10,67,200)
Cost of Control or Goodwill		1,60,000

6. Calculation of revaluation loss on Plant and Machinery of S Ltd. on 1st October, 2019

	₹
Value of plant and machinery as on 1st April,2019	6,00,000
Less: Depreciation for the six months	(30,000)
Value of plant and machinery as on 1st October, 2019	5,70,000
Less: Plant and machinery valued by H Ltd. on 1st October,2019	(5,20,000)
Revaluation Loss	50,000

7. Value of plant & Machinery of S Ltd. On 31st March,2020

Value of machinery on 1st October, 2019	5,20,000
Less: depreciation for next six month	(26,000)
	4,94,000

Q-29 A Ltd. acquired 70% equity shares of B Ltd. @ ₹20 per share (Face value - ₹10) on 31st March, 2021 at a cost of ₹ 140 lakhs. Calculate the amount of share of A Ltd. and minority interest in the net assets of B Ltd. on this date. Also compute goodwill/capital reserve for A Ltd. on acquisition of shares of B Ltd. from the following information available from the balance sheet of B Ltd. as on 31st March, 2021:

	₹ in lakhs
Property, plant and equipment	360
Investments	90
Current Assets	140
Loans & Advances	30
15% Debentures	180
Current Liabilities	100

Ans. Net assets of B Ltd. as on 31st March, 2021

	₹ in lakhs	**₹ in lakhs**
Property, plant and equipment		360
Investments		90
Current Assets		140
Loans and Advances		30
Total Assets		620
Less: 15% Debentures	180.0	
Current Liabilities	100.0	(280)
Equity / Net Worth		340
Share of Minority Interest in net assets (30% of 340)		102
A Ltd.'s share in net assets (70% of 340)		238
A Ltd.'s cost of acquisition of shares of B Ltd. (₹140 lakhs)		(140)
Capital reserve		98

Q-30 On 31st March, 2015, P Ltd. acquired 1,05,000 shares of Q Ltd. for ₹ 12,00,000. The position of Q Ltd. on that date was as under:

	₹
Property, plant and equipment	10,50,000
Current Assets	6,45,000
1,50,000 equity shares of ₹ 10 each fully paid	15,00,000
Pre-incorporation profits	30,000
Profit and Loss Account	60,000
Trade payables	1,05,000

P Ltd. and Q Ltd. give the following information on 31st March, 2021:

	P Ltd. ₹	**Q Ltd.** ₹
Equity shares of ₹ 10 each fully paid (before bonus issue)	45,00,000	15,00,000
Securities Premium	9,00,000	–
Pre-incorporation profits	–	30,000
General Reserve	60,00,000	19,05,000
Profit and Loss Account	15,75,000	4,20,000
Trade payables	5,55,000	2,10,000
Property, plant and equipment	79,20,000	23,10,000
Investment: 1,05,000 Equity shares in Q Ltd. at cost	12,00,000	–
Current Assets	44,10,000	17,55,000

Directors of Q Ltd. made bonus issue on 31.3.2021 in the ratio of one equity share of ₹ 10 each fully paid for every two equity shares held on that date. Bonus shares were issued out of post-acquisition profits by using General Reserve.

Calculate as on 31st March, 2021 (i) Cost of Control/Capital Reserve; (ii) Minority Interest;

(iii) Consolidated Profit and Loss Account in each of the following cases:

(a) Before issue of bonus shares.

(b) Immediately after issue of bonus shares.

Ans. **Shareholding pattern**

Particulars			**Number of Shares**	**% of holding**
a.	P Ltd.			
	(i)	Purchased on 31.03.2015	1,05,000	
	(ii)	Bonus Issue (1,05,000/2)	52,500	
		Total	1,57,500	70%
b.	Minority Interest		67,500	30%

Calculations of (i) Cost of Control/Capital Reserve; (ii) Minority Interest; (iii) Consolidated Profit and Loss Account as on 31st March, 2021:

(a) Before issue of bonus shares

(i)

	₹	₹
Cost of control/capital reserve		
Investment in Q Ltd.		12,00,000
Less: Face value of investments	10,50,000	
Capital profits (W.N.)	63,000	(11,13,000)
Cost of control		87,000

(ii)	Minority Interest	₹
	Share Capital	4,50,000
	Capital profits (W.N.)	27,000
	Revenue profits (W.N.)	6,79,500
		11,56,500
(iii)	Consolidated profit and loss account – P Ltd.	₹
	Balance	15,75,000
	Add: Share in revenue profits of Q Ltd. (W.N.)	15,85,500
		31,60,500

(b) Immediately after issue of bonus shares

(i)	Cost of control/capital reserve	₹	₹
	Face value of investments (₹ 10,50,000 + ₹5,25,000)	15,75,000	
	Capital Profits (W.N.)	63,000	16,38,000
	Less: Investment in		

Q-31 From the following information of Beta Ltd. and its subsidiary Gamma Ltd. drawn up at 31st March, 2021, prepare a consolidated balance sheet as at that date:

	Beta Ltd. ₹	Gamma Ltd. ₹
Share Capital:		
Shares of ₹ 100 each	15,00,000	2,50,000
Reserves	5,00,000	1,87,500
Profit and Loss Account	2,50,000	62,500
Trade Payables	3,75,000	1,42,500
Property, plant and Equipment:		
Machinery	7,50,000	2,25,000
Furniture	3,75,000	42,500
Other non-current assets	11,00,000	3,75,000
Non-current Investments:		
Shares in Gamma Ltd.: 2,000 shares at ₹ 200 each	4,00,000	

Other information:

Reserves and Profit and Loss Account of Gamma Ltd. stood at ₹ 62,500 and ₹ 37,500 respectively on the date of acquisition of its 80% shares by Beta Ltd. on 1st April, 2020.

Machinery (Book-value ₹ 2,50,000) and Furniture (Book value ₹ 50,000) of Gamma Ltd. were revalued at ₹ 3,75,000 and ₹ 37,500 respectively on 1st April, 2020 for the purpose of fixing the price of its shares. [Rates of depreciation computed on the basis of useful lives: Machinery 10%, Furniture 15%.]

Ans. **Consolidated Balance Sheet of Beta Ltd. and its Subsidiary Gamma Ltd. as at 31st March, 2021**

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital 15,00,000		

	(b) Reserves and Surplus		1	8,61,500
	(2) Minority Interest (W.N.5)			1,20,375
	(3) Current Liabilities			
	(a) Trade Payables		2	5,17,500
		Total		**29,99,375**
II.	**Assets**			
	(1) Non-current assets			
	(a) (i) Property, Plant & Equipment		3	14,94,375
	(ii) Intangible assets		4	30,000
	(b) Other non- current assets		5	14,75,000
		Total		29,99,375

Notes to Accounts

				₹
1.	**Reserves and Surplus**			
	Reserves		5,00,000	
	Add: 4/5th share of Gamma Ltd.'s postacquisition reserves (W.N.3)		1,00,000	6,00,000
	Profit and Loss Account 2,50,000			
	Add: 4/5th share of Gamma Ltd.'s post acquisition profits (W.N.4)		11,500	2,61,500
				8,61,500
2.	**Trade Payables**			
	Beta Ltd.		3,75,000	
	Gamma Ltd.		1,42,500	5,17,500
3.	**Property, Plant & Equipment**			
	Machinery			
	Beta Ltd.		7,50,000	
	Gamma Ltd.	2,50,000		
	Add: Appreciation	1,25,000		
		3,75,000		
	Less: Depreciation	(37,500)	3,37,500	
	Furniture			
	Beta Ltd.	3,75,000		
	Gamma Ltd.	50,000		
	Less: Decrease in value	(12,500)		
		37,500		
	Less: Depreciation	(5,625)	31,875	14,94,37

4.	**Intangible assets**		
	Goodwill [WN 6]		30,000
5.	**Other non-current assets**		
	Beta Ltd.	11,00,000	
	Gamma Ltd.	3,75,000	14,75,00

Working Notes:

1.	**Pre-acquisition profits and reserves of Gamma Ltd.**	₹
	Reserves	62,500
	Profit and Loss Account	37,500
		1,00,000
	Beta Ltd.'s = 4/5 × 1,00,000	80,000
	Minority Interest = 1/5 × 1,00,000	20,000
2.	**Profit on revaluation of assets of Gamma Ltd.**	
	Profit on Machinery ₹ (3,75,000 – 2,50,000)	1,25,000
	Less: Loss on Furniture ₹ (50,000 – 37,500)	12,500
	Net Profit on revaluation	1,12,500
	Beta Ltd.'s share 4/5 × 1,12,500	90,000
	Minority Interest 1/5 × 1,12,500	22,500
3.	**Post-acquisition reserves of Gamma Ltd.**	
	Post-acquisition reserves (Total reserves less pre-acquisition reserves = ₹ 1,87,500 – 62,500)	1,25,000
	Beta Ltd.'s share 4/5 × 1,25,000	1,00,000
	Minority interest 1/5 × 25,000 25,000	
4.	**Post -acquisition profits of Gamma Ltd.**	
	Post-acquisition profits (Profit & loss account balance less preacquisition profits = ₹ 62,500 – 37,500)	25,000
	Add: Excess depreciation charged on furniture @ 15% on ₹ 12,500 i.e. (50,000 – 37,500)	1,875
		26,875
	Less: Under depreciation on machinery @ 10% on ₹ 1,25,000 i.e. (3,75,000 – 2,50,000)	(12,500)
	Adjusted post-acquisition profits	14,375
	Beta Ltd.'s share 4/5 × 14,375	11,500
	Minority Interest 1/5 × 14,375	2,875
5.	**Minority Interest**	
	Paid-up value of (2,500 – 2,000) = 500 shares held by outsiders i.e. 500 × ₹ 100	50,000

Add: 1/5th share of pre-acquisition profits and reserves	20,000
1/5th share of profit on revaluation	22,500
1/5th share of post-acquisition reserves	25,000
1/5th share of post-acquisition profit	2,875
	1,20,375

6. Cost of Control or Goodwill

Paid-up value of 2,000 shares held by Beta Ltd. i.e. 2,000 × ₹ 100	2,00,000
Add: 4/5th share of pre-acquisition profits and reserves	80,000
4/5th share of profit on the revaluation	90,000
Intrinsic value of shares on the date of acquisition	3,70,000
Price paid by Beta Ltd. for 2,000 shares	4,00,000
Less: Intrinsic value of the shares	(3,70,000)
Cost of control or Goodwill	30,000

Q-32 Moon Ltd. and its subsidiary Star Ltd. provided the following information for the year ended 31st March, 2021:

Particulars	Moon Ltd (₹)	Star Ltd. (₹)
Equity Share Capital	20,000,000	6,000,000
Finished Goods Inventory as on 01.04.2020	4,200,000	3,010,000
Finished Goods Inventory as on 31.03.2021	8,575,000	3,762,500
Dividend Income	1,680,000	437,500
Other non-operating Income	350,000	105,000
Raw material consumed	13,930,000	4,725,000
Selling and Distribution Expenses	3,325,000	1,575,000
Production Expenses	3,150,000	1,400,000
Loss on sale of investments	262,500	Nil
Sales and other operating income	33,250,000	19,075,000
Wages and Salaries	13,300,000	2,450,000
General and Administrative Expenses	2,800,000	1,225,000
Royalty paid	Nil	50,000
Depreciation	315,000	140,000
Interest expense	175,000	52,500

Other information

- On 1st September 2018 Moon Ltd., acquired 50,000 equity shares of ₹ 100 each fully paid up in Star Ltd.
- Star Ltd. paid a dividend of 10% for the year ended 31st March 2020. The dividend was correctly accounted for by Moon Ltd.
- Moon Ltd. sold goods of ₹ 17,50,000 to Star Ltd. at a profit of 20% on selling price.
  Inventory of Star Ltd. includes goods of ‘ 7,00,000 received from Moon Ltd.
- Selling and Distribution expenses of Star Ltd. include ₹ 2,12,500 paid to Moon Ltd. as brokerage fees.
- General and Administrative expenses of Moon Ltd. include ₹ 2,80,000 paid to Star Ltd. as consultancy fees.

- Star Ltd. used some resources of Moon Ltd., and Star Ltd. paid ₹ 50,000 to Moon Ltd. as royalty.

Prepare Consolidated Statement of Profit and Loss of Moon Ltd. and its subsidiary Star Ltd. for the year ended 31st March, 2021 as per Schedule III to the Companies Act, 2013.

Ans. Consolidated statement of profit and loss of Moon Ltd. and its subsidiary Star Ltd. for the year ended on 31st March, 2021

Particulars	Note No.	₹
Revenue from operations	1	5,00,32,500
Other Income	2	23,10,000
Total revenue (I)		5,23,42,500
Expenses:		
Cost of material purchased/consumed	3	2,14,55,000
Changes (Increase) in inventories of finished goods	4	(49,87,500)
Employee benefit expense	5	1,57,50,000
Finance cost	6	2,27,500
Depreciation and amortization expense	7	4,55,000
Other expenses	8	84,32,500
Total expenses (II)		4,13,32,500
Profit before tax (II-III)		1,10,10,000

Notes to Accounts:

			₹	₹
1.	Revenue from operations			
	Sales and other operating revenues1			
	Moon Ltd.		3,32,50,000	
	Star Ltd.		190,75,000	
			523,25,000	
	Less: Inter-company sales		(17,50,000)	
	Consultancy fees received by Star Ltd. from Moon Ltd.		(2,80,000)	
	Royalty received by Moon Ltd. from Star Ltd.		(50,000)	
	Brokage received by Moon Ltd. from Star Ltd.		(2,12,500)	5,00,32,500
2.	Other Income			
	Dividend income:			
	Moon Ltd.	16,80,000		
	Star Ltd.	4,37,500	21,17,500	
	Loss on sale of investments Star Ltd.		(2,62,500)	
	Other Non-operating Income			
	Moon Ltd.	3,50,000		
	Star Ltd.	1,05,000	4,55,000	23,10,000
3.	Cost of material purchased/consumed			
	Moon Ltd.	1,39,30,000		

	Star Ltd.	47,25,000		
		1,86,55,000		
	Less: Purchases by Star Ltd. From Moon Ltd.	(17,50,000)	1,69,05,000	
	Direct expenses (Production)			
	Moon Ltd.	31,50,000		
	Star Ltd.	14,00,000	45,50,000	2,14,55,000
4.	Changes (Increase) in inventories of finished goods			
	Moon Ltd.		43,75,000	
	Star Ltd.		7,52,500	
			51,27,500	
	Less: Unrealized profits ₹ 7,00,000 × 20/100		(1,40,000)	49,87,500
5.	Employee benefits and expenses			
	Wages and salaries:			
	Moon Ltd.		1,33,00,000	
	Star Ltd.		24,50,000	1,57,50,000
6	Finance cost			
	Interest:			
	Moon Ltd.		1,75,000	
	Star Ltd.		52,500	2,27,500
7.	Depreciation			
	Moon Ltd.		3,15,000	
	Star Ltd.		1,40,000	4,55,000
8.	Other expenses			
	General & Administrative expenses:			
	Moon Ltd.	28,00,000		
	Star Ltd.	12,25,000		
		40,25,000		
	Less: Consultancy fees received by Star Ltd. from Moon Ltd.	(280,000)	37,45,000	
	Royalty:			
	Star Ltd.	50,000		
	Less: Received by Moon Ltd.	(50,000)	Nil	
	Selling and distribution Expenses:			
	Moon Ltd.	33,25,000		
	Star Ltd.	15,75,000		
		49,00,000		
	Less: Brokerage received by Moon Ltd. from Star Ltd.	(2,12,500)	46,87,500	84,32,500

Q-33 A Ltd. and its subsidiary B Ltd. give the following information for the year ended 31st March, 2022:

₹ in Lakhs

	A Ltd.	B Ltd.
Sales and other income	7,500	1,500
Increase in Inventory	1,500	300
Raw material consumed	1,200	300
Wages and Salaries	1,200	225
Production expenses	300	150
Administrative expenses	300	150
Selling and distribution expenses	300	75
Interest	150	75
Depreciation	150	75

The following information is also given:

(i) A Ltd sold goods of ₹ 180 Lakhs to B Ltd at cost plus 25% (1/6 of such goods were still in inventory of B Ltd at the end of the year).

(ii) A Ltd. holds 72% of the Equity Capital of B Ltd and the Equity Capital of B Ltd is ₹ 1,500 Lakhs on 1.4.2021 (date of acquisition of shares).

(iii) Administrative expenses of B Ltd include ₹ 8 Lakhs paid to A Ltd as consultancy fees.

Moreover, selling and distribution expenses of A Ltd include ₹ 15 Lakhs paid to B Ltd as commission.

You are required to prepare a consolidated Statement of Profit and Loss of A Ltd. with its subsidiary B Ltd. for the year ended 31st March, 2022.

Ans. **Consolidated Statement of Profit & Loss of A Ltd. and its subsidiary B Ltd. for the year ended on 31st March, 2022**

Particulars		Note No.	₹ in Lacs
I.	Revenue from operations	1	8,797
II.	Total revenue		8,797
III.	Expenses		
	Cost of Material purchased/consumed	3	1,770
	Changes of Inventories of finished goods 2 (1,794)		
	Employee benefit expense	4	1,425
	Finance cost	6	225
	Depreciation and amortization expense	7	225
	Other expenses	5	802
	Total expenses		2,653
IV.	Profit before Tax(II-III)		6,144

Notes to Accounts

		₹ in Lacs	₹ in Lacs
1.	Revenue from Operations		
	Sales and other income		
	A Ltd.	7,500	

	B Ltd.	1,500	
		9,000	
	Less: Inter-company Sales	(180)	
	Consultancy fees received by A Ltd. from B Ltd.	(8)	
	Commission received by B Ltd. from A Ltd.	(15)	8,797
2.	Increase in Inventory		
	A Ltd.	1,500	
	B Ltd.	300	
		1,800	
	Less: Unrealized profits ‘ 180×1/6 x 25/125	(6)	1,794
3.	Cost of Material purchased/consumed		
	A Ltd.	1,200	
	B Ltd.	300	
		1,500	
	Less: Purchases by B Ltd. from A Ltd.	(180)	1,320
	Direct Expenses		
	A Ltd.	300	
	B Ltd.	150	450
			1,770
4.	Employee benefits and expenses		
	Wages and Salaries:		
	A Ltd.	1,200	
	B Ltd.	225	1,425
5.	Other Expenses		
	Administrative Expenses		
	A Ltd.	300	
	B Ltd.	150	
		450	
	Less: Consultancy fees received by A Ltd. from B Ltd.	(8)	442
	Selling and Distribution Expenses:		
	A Ltd.	300	
	B Ltd.	75	
		375	
	Less: Commission received from B Ltd. from A Ltd.	(15)	360
			802
6.	Finance Cost		
	Interest:		
	A Ltd.	150	
	B Ltd.	75	225
7.	Depreciation and Amortization		
	Depreciation:		
	A Ltd.	150	
	B Ltd.	75	225

Q-34 H Ltd. and its subsidiary S Ltd. give the following information as on 31st March, 2021:

	H Ltd. (₹)	S Ltd. (₹)
Share Capital		
Equity Share Capital (fully paid up shares of ‘ 10 each)	12,00,000	2,00,000
Reserves and Surplus		
General Reserve	4,35,000	1,55,000
Cr. Balance in Profit and Loss Account	2,80,000	65,000
Current Liabilities		
Trade Payables	3,22,000	1,23,000
Non-Current Assets		
Property, Plant and Equipment		
Machinery	6,40,000	1,80,000
Furniture	3,75,000	34,000
Non-Current Investments		
Shares in S Ltd. - 16,000 shares @ ₹ 20 each	3,20,000	-
Current Assets		
Inventories	2,68,000	62,000
Trade Receivables	4,70,000	2,35,000
Cash and Bank	1,64,000	32,000

H Ltd. acquired the 80% shares of S Ltd. on 1st April, 2020. On the date of acquisition, General Reserve and Profit Loss Account of S Ltd. stood at ₹ 50,000 and ₹ 30,000 respectively.

Machinery (book value ₹ 2,00,000) and Furniture (book value ₹ 40,000) of S Ltd. were revalued at ₹ 3,00,000 and ₹ 30,000 respectively on 1st April,2020 for the purpose of fixing the price of its shares (rates of depreciation on W.D.V basis: Machinery 10% and Furniture 15%). Trade Payables of H Ltd. include ₹ 35,000 due to S Ltd. for goods supplied since the acquisition of the shares.

These goods are charged at 10% above cost. The inventories of H Ltd. includes goods costing ₹ 55,000 (cost to H Ltd.) purchased from S Ltd.

You are required to prepare the Consolidated Balance Sheet of H Ltd. with its subsidiary as at 31st March, 2021.

Ans. **Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd.**
as at 31st March, 2021

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		12,00,000
(1,20,000 equity shares of ₹ 10 each)		
(b) Reserves and Surplus	1	8,16,200
(2) Minority Interest (W.N.4)		99,300
(3) Current Liabilities		
(a) Trade Payables	2	4,10,000
Total		**25,25,500**

II.	**Assets**			
	(1) Non-current assets			
	(i) Property, plant and equipment		3	13,10,500
	(ii) Intangible assets		4	24,000
	(2) Current assets			
	(i) Inventories		5	3,25,000
	(ii) Trade Receivables		6	6,70,000
	(iii) Cash at Bank		7	**1,96,000**
		Total		**25,25,500**

Notes to Accounts

				₹
1.	Reserves and Surplus			
	General Reserves		4,35,000	
	Add: 80% share of S Ltd.'s post-acquisition reserves (W.N.3)		84,000	5,19,000
	Profit and Loss Account 2,80,000			
	Add: 80% share of S Ltd.'s post-acquisition profits (W.N.3)	21,200		
	Less: Unrealised gain	(4,000)	17,200	2,97,200
				8,16,200
2.	Trade Payables			
	H Ltd.		3,22,000	
	S Ltd.		1,23,000	
	Less: Mutual transaction		(35,000)	4,10,000
3.	Property, plant and equipment			
	Machinery			
	H Ltd.		6,40,000	
	S Ltd.	2,00,000		
	Add: Appreciation	1,00,000		
		3,00,000		
	Less: Depreciation	(30,000)	2,70,000	9,10,000
	Furniture			
	H. Ltd.		3,75,000	
	S Ltd.	40,000		
	Less: Decrease in value	(10,000)		
		30,000		
	Less: Depreciation	(4,500)	25,500	4,00,500
				13,10,500

4.	Intangible assets		
	Goodwill [WN 5]		24,000
5.	Inventories		
	H Ltd.	2,68,000	
	S Ltd.	62,000	3,30,000
	Less: Inventory reserve		(5,000)
			3,25,000
6.	Trade Receivables		
	H Ltd.	4,70,000	
	S Ltd.	2,35,000	
			7,05,000
	Less: Mutual transaction		(35,000)
			6,70,000
7.	Cash and Bank		
	H Ltd.	1,64,000	
	S Ltd.	32,000	1,96,000

Working Notes:

1. Profit or loss on revaluation of assets in the books of S Ltd. and their book values as on 1.4.2020

	₹
Machinery	
Revaluation as on 1.4.2020	3,00,000
Less: Book value as on 1.4.2020	(2,00,000)
Profit on revaluation	1,00,000
Furniture	
Revaluation as on 1.4.2020	30,000
Less: Book value as on 1.4.2020	(40,000)
Loss on revaluation	(10,000)

2. Calculation of short/excess depreciation

	Machinery	**Furniture**
Upward/ (Downward) Revaluation	1,00,000	(10,000)
Rate of depreciation	10% p.a.	15% p.a.
Difference [(short)/excess]	(10,000)	1,500

3. Analysis of reserves and profits of S Ltd. as on 31.03.2021

	Pre-acquisition profit upto 1.4.2020 (Capital profits)	Post-acquisition profits (1.4.2020 – 31.3.2021) General Reserve	Profit and loss account
General reserve as on 31.3.2021	50,000	1,05,000	
Profit and loss account as on 31.3.2021	30,000		35,000
Upward Revaluation of machinery as on 1.4.2020	1,00,000		
Downward Revaluation of Furniture as on 1.4.2020	(10,000)		
Short depreciation on machinery			(10,000)
Excess depreciation on furniture	_____	_____	1,500
Total	**1,70,000**	**1,05,000**	**26,500**

4. Minority Interest

	₹
Paid-up value of (2,00,000 x 20%)	40,000
Add: 20% share of pre-acquisition profits and reserves [(20% of (50,000 + 30,000)]	16,000
20% share of profit on revaluation	18,000
20% share of post-acquisition reserves	21,000
20% share of post-acquisition profit	5,300
	1,00,300
Less: Unrealised Profit on Inventory (55,000 x 10/110) x 20%	(1,000)
	99,300

5. Cost of Control or Goodwill

Cost of Investment		3,20,000
Less: Paid-up value of 80% shares	1,60,000	
80% share of pre-acquisition profits and reserves (₹ 64,000 + ₹ 72,000)	1,36,000	(2,96,000)
Cost of control or Goodwill		24,000

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