Star Rating

On the basis of Maximum marks from a chapter ☆☆☆☆

On the basis of Questions included every year from a chapter ☆☆☆☆☆

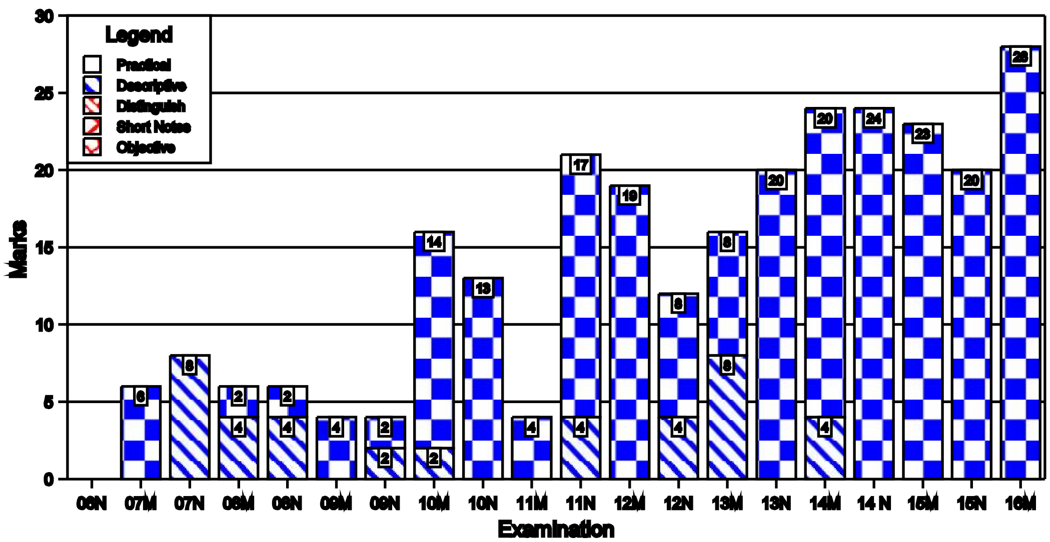
On the basis of Compulsory questions from a chapter ☆☆☆☆☆

CHAPTER	
1	**Accounting Standards**

THIS CHAPTER COMPRISES OF

☞ Working knowledge of : AS 1, AS 2, AS 3, AS 6, AS 7, AS 9, AS 10, AS 13, AS 14.

Marks of Objective, Short Notes, Distinguish Between, Descriptive & Practical Questions



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* Questions of November - 2006 are from PE-II Gr. I and from May - 2007 onwards are from PCC Gr. I

◗ DESCRIPTIVE QUESTIONS

Question Based on AS - 5

2007 - Nov [6] Answer the following:

(a) Mention six areas in which different accounting policies are followed by Companies. (4 marks)

Answer :

(a) Areas in which different accounting policy can be adopted

1. Method of depreciation, *depletion and amortisation.*
2. Valuation of investment
3. Valuation of fixed asset
4. Treatment of goodwill
5. Treatment of retirement benefit
6. Conversion of foreign currency.

KZ - 1	Knowledge Zone

Other areas in which accounting policy can be adopted

1. Treatment of expenditure during construction.
2. Valuation of inventories.
3. Treatment of contingent liabilities.
4. Recognition of profit on long term contract.

Question Based on Basic

2007 - Nov [6] Answer the following:

(e) List the criteria to be applied for rating an enterprise as Level-I enterprise for the purpose of Compliance of Accounting Standards in India. (4 marks)

Answer :

Enterprises which fall in any one or more of following categories are classified as level I Enterprise–

1. Enterprises, whose equity or debt securities are either listed or are in the process to be listed in India or outside India.
2. Banks, Insurance Companies and Financial institutions.

3. All commercial, industrial and other reporting business enterprises, whose **total turnover** during the previous year **exceeds ₹ 50 crores** (as per the audited financial statement).
4. All commercial, industrial and other reporting business enterprises, whose **total borrowings including public deposits** during the previous year **exceeds ₹ 10 crores** (as per audited financial statement).
5. Holding or subsidiary company of any of the above enterprises any time during the year.

KZ - 2 **Knowledge Zone**

Level II Enterprise:

1. All commercial, industrial and other reporting business enterprises, whose **total turnover** during the previous year **exceeding ₹ 1 crore but does not exceed ₹ 50 crores (as per the audited financial statement).**
2. All commercial, industrial and other reporting business enterprises, whose **total borrowings including public deposits** during the previous year **exceeds ₹ 1 crore but not exceeds ₹ 10 crores** (as per the audited financial statement).
3. Holding or subsidiary company of any of the above enterprises any time during the year.

Level III Enterprises:

All the enterprises not covered in two levels (i.e. Level I & II Enterprises) come under this level.

Do you know ?

Applicability of AS : There are Two classifications made by two different acts/statute.

1. By Companies Accounting Standard Rules 2006 (CASR) i.e. SMC's (Small and medium companies) and Non SMC's.
2. By ICAI - i.e. (i) Level I, (ii) Level II & (iii) Level III Enterprises

2008 - May [6] Answer the following :

(f) What are the items that are to be excluded in determination of the cost of inventories as per AS-2? (4 marks)

Answer :

Para 13 of AS-2 lists down the specific costs which are to be excluded from cost of inventories The list is as follows :

1. **Abnormal amounts** of wasted materials, labour or other production cost.
2. **Storage costs,** unless those costs are necessary in the production process prior to a further production stage.
3. **Administrative overheads** that do not contribute to bringing the inventories to their present location and condition; and
4. **Selling and distribution costs**.

As per Para 12, Interest and other borrowing costs are usually considered as not related to bringing the inventories to their present location and condition and are therefore usually not included in the cost of inventory.

Note: For Practical aspect you should go through 2010 - Nov [1] {C} (b) on page no. 30

KZ - 3 **Knowledge Zone**

Cost of Inventories

1. **Cost of Purchase**: **Includes** Purchase Price + Taxes & Duties (which are not subsequently recoverable) + other expenditure directly attributable to acquisition (like freight inward)
   BUT EXCLUDES Trade Discount, Rebates, Duty Drawbacks, Subsidiaries and Taxes (which are subsequently recoverable)
2. **Cost of Conversion**: **Includes** Direct Labour, Direct Expenses, Sub Contracted work and Production Overheads absorbed on the basis of Normal Capacity.
3. **Other Costs** incurred in bringing the inventories to their present location and condition. e.g. cost incurred in designing products for specific customers.

2008 - Nov [5] Answer the following :

(ii) Mention four Assets, where AS 6 (revised) is not applicable.

(iv) Mention two categories of investments defined by AS 13 and also State their valuation principles. (2 marks each)

Answer :

(ii) AS-6 deals with "Depreciation Accounting" of fixed assets. The AS is applicable to all assets except:

1. Forests, plantations and similar regenerative natural resources;
2. Wasting assets including expenditure on the exploration for and extraction of minerals, oils, natural gas and similar non-regenerative resources;
3. Expenditure on research and development;
4. Goodwill
5. Live stock

Note: AS - 6 does not apply to land unless it has a limited useful life for the enterprise.

Answer:

(iv) As per AS 13 'Accounting for Investments', there are two categories of investments, viz. Current Investments and Long Term Investments. According to Para 14 of the standard, the carrying amount for **Current Investments** is the lower of cost and fair value whereas **Long Terms Investments** are valued at cost less permanent diminutions in value of investment. For current investments, according to this standard any reduction to fair value and any reversals of such reductions are included in the profit and loss statement.

KZ - 4	Knowledge Zone
Investment also include one another type of Investment, that is Investment properties and it should be treated as Long term investment.	

2009 - Nov [1] (viii) Explain contract costs as per Accounting Standard-7 related to 'Construction Contracts'. (2 marks)

Answer :

According to AS 7 "Construction Contracts (revised 2002)", contract cost should comprise:

1. costs that relate directly to the specific contract;
2. costs that are attributable to contract activity in general and can be allocated to the contract;

3. other costs as are specifically chargeable to the customer under the terms of the contract.

2010 - May [1] (viii) According to Accounting Standard-9, when revenue from sales should be recognised ? (2 marks)

Answer :

According to AS 9 'Revenue Recognition', revenue from sales should be recognised only when requirements as to performance are satisfied provided that at the time of performance it is not unreasonable to expect ultimate collection. These requirements can be given as follows:

(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.

2011 - Nov [7] Answer the following:

(e) M/s. Son Ltd. charged depreciation on its assets on SLM basis. In the year ended 31st March, 2011 it changed to WDV basis. The impact of the change when computed from the date of the assets putting into use amounts to ₹ 18 lakhs being additional depreciation. Discuss, when should an enterprise change method of charging depreciation and how it should be dealt with in Profit and Loss A/c (4 marks)

Answer :

According to AS 6 'Depreciation Accounting', an enterprise can change one method of depreciation to another method only if the adoption of the new method is required by statue or for compliance with an accounting standard or if it is considered that the change would result in a more appropriate preparation or presentation of the financial statements of the enterprise.

When such a change in the method of depreciation is made, depreciation should be recalculated in accordance with the new method from the date of the asset coming into use. The deficiency or surplus arising from retrospective re-computation of depreciation in accordance with the new method should be adjusted in the accounts through statement of profit and loss in the year in which the method of depreciation is changed. In case the change in the method results in deficiency in depreciation in respect of past years, the deficiency should be charged in the statement of profit and loss.

2012 - Nov [7] Answer the following:

(d) "In determining the cost of inventories, it is appropriate to exclude certain costs and recognize them as expenses in the period in which they are incurred." Provide example of such costs as per AS-2: Valuation of Inventories. (4 marks)

Answer:

As per AS- 2 'Valuation of Inventories', cost of inventories includes all costs of purchase, cost of conversion and other costs incurred in bringing the inventories to their present location and condition. However, certain costs are excluded from the cost of the inventories and are recognised as expenses in the period in which incurred. Following are some of the examples of such cost:

(i) Selling and distribution costs.
(ii) Administrative overheads that do not contribute to bringing the inventories to their present location and condition; and
(iii) Abnormal amount of wasted materials, labour, or other production costs.
(iv) Storage costs, unless those costs are necessary in the production process prior to a further production stage.

2013 - May [7] Answer the following:

(b) What are the three fundamental accounting assumptions recognised by Accounting Standard (AS) 1? Briefly describe each one of them. (4 marks)

Answer:

Accounting Standard (AS) 1 recognizes three fundamental accounting assumptions. These are as follows:

(i) Going Concern: The financial statements are normally prepared on the assumption that an enterprise will continue its operations in the foreseeable future and neither there is intention, nor there is need to materially curtail the scale of operations.

(ii) Consistency: The principle of consistency refers to the practice of using same accounting policies for similar transactions in all accounting periods unless the change is required (i) by a statute, (ii) by an accounting standard or (iii) for more appropriate presentation of financial statements.

(iii) **Accrual basis of accounting:** Under this basis of accounting, transactions are recognised as soon as they occur, whether or not cash or cash equivalent is actually received or paid.

KZ - 5	Knowledge Zone

Disclosure requirements as to Fundamental Accounting Assumptions (FAA)

1. If All FAA are followed: No specific disclosure is required
2. If any of FAA is not followed: The fact that accounting assumption is not followed must be disclosed.

2013 - May [7] Answer the following:

(e) What are the issues, with which Accounting Standards deal?

(4 marks)

Answer :

Accounting Standards deal with the issues of:

1. **Recognition** of events and transactions in the financial statements,
2. **Measurement** of these transactions and events,
3. **Presentation** of these transactions and events in the financial statements in a manner that is meaningful and understandable to the reader, and
4. **Disclosure** requirements which should be there to enable the public at large and the stakeholders and the potential investors in particular, to get an insight into what these financial statements are trying to reflect and thereby facilitating them to take prudent and informed business decisions.

KZ - 6 **Knowledge Zone**

You should also know the basic OBJECTIVE of AS:

The main objective of AS is **to harmonise the diverse accounting policies and practices.** However, harmonisation does not mean that AS should become very rigid. In fact, harmonisation of AS permits flexibility to make the necessary adjustments to suit their purpose.

2014 - May [7] Answer the following:

(d) What are depreciable assets as per Accounting Standard-6 ? Explain why AS 6 does not apply to Land. (4 marks)

Answer:

Meaning of Depreciable Assets as per AS - 6

Depreciable Assets are assets which:

(i) are expected to be used during more than one accounting period;

(ii) have a limited useful life;

(iii) are held by an enterprise for use in the production or supply of goods and services, for rental to others or for administrative purpose and not for the purpose of sale in the ordinary course of business.

Land is not depreciated as per the accounting standard, because it does not fulfil all requirements of depreciable asset under accounting standard i.e. its useful life is unlimited.

◗ PRACTICAL QUESTIONS

Question based on AS - 6

2007 - May [5] Answer the following :

(ii) A machinery costing ₹10 lakhs has useful life of 5 years. After the end of 5 years, its scrap value would be ₹ 1 lakh. How much depreciation is to be charged in the books of the company as per Accounting Standard-6? (2 marks)

Answer :

Provision:

As per AS - 6 'Depreciation Accounting' the depreciable amount of a depreciable asset should be allocated on a systematic basis to each accounting period during the useful life of the asset.

Analysis and Conclusion

In this problem, the depreciation amount can be determined as follows:-

	₹
Cost of machinery	10,00,000
Less: Scrap value at the end	1,00,000
Value to be written off	9,00,000

$\therefore$ Depreciation per year = $\dfrac{\textbf{Amount to be written off}}{\textbf{Useful life of the asset}} = \dfrac{\textbf{₹ 9,00,000}}{\textbf{5 year}}$

= ₹ 1,80,000

Question based on AS - 10

2007 - May [5] Answer the following :

(ix) ABC Ltd. gave 50,000 equity shares of ₹ 10 each (fully paid up) in consideration for supply of certain machinery by X & Co. The shares exchanged for machinery are quoted on Bombay Stock Exchange (BSE) at ₹ 15 per share, at the time of transaction. In the absence of fair market value of the machinery acquired, how the value of machinery would be recorded in the books of the company?

(2 marks)

Answer :

Provision:

According to AS - 10 'Accounting for Fixed Assets', when fixed assets are acquired in exchange of share or other securities, they should be recorded at their fair market value or the fair market value of the securities issued, whichever is more clearly evident.

Analysis and Conclusion:

In this case, the market value of the securities exchanged for the asset is more clearly evident, the company should record the asset is more clearly evident. The company should record the value of machinery at ₹ 7,50,000 (50,000 shares @ ₹ 15 i.e. market price of the share)

Question based on AS - 7

2007 - May [5] Answer the following :

(x) A company took a construction contract for ₹ 100 lakhs in January, 2006. It was found that 80% of the contract was completed at a cost of ₹ 92 lakhs on the closing date i.e. on 31.3.2007. The company estimates further expenditure of ₹ 23 lakhs for completing the contract. The expected loss would be ₹ 15 lakhs. Can the company recognise the loss in the financial statements prepared for the year ended 31.3.2007 ? (2 marks)

Answer :

According to AS - 7, 'Accounting for construction contract' an expected loss on the construction contract should be recognised as an expense immediately irrespective of :

(i) The amount of profit expected to arise in other contracts; or
(ii) Whether or not the work has commenced on the contract; or
(iii) The stage of completion of the contract.

Hence, the company must recognize the loss immediately.

Question based on AS - 10

2008 - May [5] Answer the following :

(v) What is the accounting entry to be passed as per AS-10 for the following situations :
  (a) Increase in value of fixed asset by ₹ 50,00,000 on account of revaluation.
  (b) Decrease in the value of fixed asset by ₹ 30,00,000 on account of revaluation. (2 marks)

Answer :

	Particulars	L/ F	Dr. (₹)	Cr. (₹)
a.	Fixed Asset A/c Dr. To Revaluation Reserve A/c (Being the increase in value of fixed asset due to upward revaluation)		50,00,000	50,00,000
b.	Profit and Loss A/c Dr. To Fixed Asset A/c (Being the decrease in net book value of		30,00,000	30,00,000

	fixed asset due to downward revaluation)			

Note: It has been assumed that both the above instances are independent of each other and revaluation is done for first time.

2008 - Nov [5] Answer the following :

(iii) Y Ltd. used certain resources of X Ltd. In return X Ltd. receives ₹ 10 lakhs and ₹ 15 lakhs as interest and royalties respectively, from Y Ltd. during the year 2007-08. State on what basis X Ltd. should recognize their revenue, as per AS 9. (2 marks)

Answer :

According to AS 9 on 'Revenue Recognition', interest of ₹ 10 lakhs received in the year 2007-08 should be recognized on the time proportion basis taking into account the amount outstanding and the rate applicable; whereas royalty of ₹ 15 lakhs received in the same year should be recognized on accrual basis as per the terms of relevant agreement.

Question based on AS - 2

2009 - May [6] Answer the following :

(a) Sony Pharma ordered 12,000 kg. of certain material at ₹ 80 per unit. The purchase price includes excise duty ₹ 4 per kg in respect of which full CENVAT credit is admissible. Freight incurred amounted to ₹ 77,400. Normal transit loss is 3%. The company actually received 11,600 kg. and consumed 10,100 kg. of material. Compute cost of inventory under AS-2 and abnormal loss. (4 marks)

Answer:

Computation of Cost of Inventory

	₹
Purchase price (12,000 kg × ₹ 80)	9,60,000
Less: CENVAT credit (12,000 kg. × ₹ 4)	48,000
	9,12,000
Add: Freight	77,400
Total material cost	9,89,400
Number of units after normal loss = 97% of 12,000 kgs.	11,640 kgs.

Avg./Normal cost per kg. $\left(\frac{9,89,400}{11,640}\right)$ = ₹ 85

Value of closing stock under AS 2 = (11,600 kgs. –10,100 kgs.) × ₹ 85
= ₹ 1,27,500

Abnormal loss = (11,640 kgs. – 11,600 kgs.) × ₹ 85 = ₹ 3,400

Question based on AS - 2

2009 - Nov [1] (vii) From the following data, find out value of inventory as on 30.04.2009 using (a) LIFO method, and (b) FIFO method :

(1) 01.04.2009 Purchased 10 units @ ₹ 70 per unit
(2) 06.04.2009 Sold 6 units @ ₹ 90 per unit
(3) 09.04.2009 Purchased 20 units @ ₹ 75 per unit
(4) 18.04.2009 Sold 14 units @ ₹ 100 per unit.

(2 marks)

Answer :

(a) Statement showing valuation of closing inventory by LIFO method

Date	Receipts			Issue			Balance		
	Unit	Cost/unit	Amount	Unit	Cost/unit	Amount	Unit	Cost/unit	Amount
1.4.09	10	70	700				10	70	700
6.4.09				6	70	420	4	70	280
9.4.09	20	75	1,500				4	70	280
							20	75	1,500
18.4.09				14	75	1,050	4	70	280
							6	75	450

Value of closing inventory as per LIFO method:

Unit	Rate	Total
4	₹ 70	₹ 280
6	₹ 75	₹ 450
	Total	₹ 730

(b) Statement showing valuation of closing inventory by FIFO method

Date	Receipts			Issue			Balance		
	Unit	Cost/Unit	Amount	Unit	Cost/Unit	Amount	Unit	Cost/Unit	Amount
1.4.09	10	70	700				10	70	700
6.4.09				6	70	420	4	70	280
9.4.09	20	75	1,500				4	70	280
							20	75	1,500
				4	70	280	10	75	750
18.4.09				10	75	750			

Value of closing inventory as per FIFO method:

Unit	Rate	Total
10	₹ 75	₹ 750

Question based on AS - 6

2010 - May [1] (v) A company acquired a machine on 1.4.2006 for ₹ 5,00,000. The company charged depreciation upto 2008-09 on straight line basis with estimated working life of 10 years and scrap value of ₹ 50,000. From 2009 -10, the company decided to change depreciation method at 20% on reducing balance method. Compute the amount of depreciation to be debited to Profits and Loss A/c for the year 2009 - 10. (2 marks)

Answer :

Annual depreciation charged by the company up to 2008-09

$$= \frac{\textbf{Cost price of the machine} - \textbf{Scrap value}}{\textbf{Useful life of the machine}}$$

$$= \frac{\textbf{₹ 5,00,000} - \textbf{₹ 50,000}}{\textbf{10}} = ₹\ 45,000$$

WDV of machine at the end of 2008-09 by Straight Line Method (SLM)

$= ₹\ 5,00,000 - (₹\ 45,000 \times 3) = ₹\ 3,65,000$

(i) Depreciation by Reducing Balance Method (RBM)

Year	Cost/WDV at the beginning of the year ₹	Depreciation ₹	WDV at the end of the year ₹
2006-07	5,00,000	5,00,000 × 20% = 1,00,000	4,00,000

2007-08	4,00,000	4,00,000 × 20% = 80,000	3,20,000
2008-09	3,20,000	3,20,000 × 20% = 64,000	2,56,000
		2,44,000	
2009-10	2,56,000	2,56,000 × 20% = 51,200	2,04,800

(ii) Depreciation to be charged in 2009-2010

Particulars	₹
Book value of the machine as per SLM as on 2008-09	3,65,000
Less : Book value of the machine as per RBM as on 2008-09	(2,56,000)
	1,09,000
Add : Depreciation for the year 2009-10 as per RBM	51,200
Total depreciation debited to Profit and Loss Account in the year 2009-10	1,60,200

Question based on AS - 12

2010 - May [6] Answer the following :

(a) Weak Ltd. acquired the fixed assets of ₹ 100 lakhs on which it received the grant of ₹ 10 lakhs. What will be the cost of the fixed assets as per AS-12 and how it will be disclosed in the financial statements.

(4 marks)

Answer :

Provision:

According to AS 12 'Accounting for Government Grants' deal with the presentation of Government grants related to specific fixed assets. According to AS 12 there are two different methods for recognition of a Government grant.

1. **Deductive Method:** Government grants related to specific fixed assets should be presented in the balance sheet by showing the grant as a deduction from the gross value of the assets concerned in arriving at their book value. Therefore, in the given case, fixed assets should be presented at ₹ 90 lakhs (₹ 100 lakhs less ₹ 10 lakhs) in the balance sheet of Weak Ltd.
2. **Additive Method:** Government grants related to depreciable fixed assets may be treated as deferred income which should be recognised in the profit and loss statement on a systematic and rational basis over

the useful life of the asset, i.e., such grants should be allocated to income over the periods and in the proportions in which depreciation on those assets is charged.

Analysis and Conclusion:

In this case, fixed assets will be shown at ₹ 100 lakhs in the balance sheet of Weak Ltd. and the corresponding grant amounting ₹ 10 lakhs will be treated as deferred income to be recognized over useful life of the fixed assets.

Question based on AS - 10

2010 - May [6] Answer the following :

(b) During the current year 2009 - 10 M/s L & C Ltd. made the following expenditure relating to its plant and machinery :

	₹
General repairs	4,00,000
Repairing of Electric Motors	1,00,000
Partial Replacement of parts of Machinery	50,000
Substantial improvements to the electrical wiring system which will increase efficiency of the plant and machinery	10,00,000

What amount should be capitalised according to AS-10 ?

(4 marks)

Answer :

Provision:

According to AS 10 'Accounting for Fixed Assets', expenditure that increases the future benefits from the existing asset beyond its previously assessed standard of performance is included in the gross book value, e.g., an increase in capacity.

Analysis and Conclusion:

Therefore, in the given case, repairs amounting ₹ 5 lakhs and partial replacement of parts of machinery worth ₹ 50,000 should be charged to profit & loss account. ₹ 10 lakhs incurred for substantial improvement to the electrical wiring system which will increase efficiency should be capitalized.

Question based on AS - 2

2010 - May [6] Answer the following :

(d) Raw materials inventory of a company includes certain material purchased at ₹ 100 per kg. The price of the material is on decline and replacement cost of the inventory at the year end is ₹ 75 per kg. It is possible to convert the material into finished product at conversion cost of ₹ 125.

Decide whether to make the product or not to make the product, if selling price is (i) ₹ 175 and (ii) ₹ 225. Also find out the value of inventory in each case. (4 marks)

Answer :

Provision:

According to AS 2 'Valuation of Inventories', materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost. But when there has been a decline in the price of materials and it is estimated that the cost of the finished products will exceed net realizable value, the materials are written down to net realisable value.

Analysis and Conclusion:

In such circumstances, the replacement cost of the materials may be the best available measure of their net realisable value.

(i) When the selling price be ₹ 175
Incremental Profit= ₹ 175 - ₹ 125 = ₹50
Current price of the material = ₹ 75
Therefore, it is better not to make the product. Raw material inventory would be valued at net realisable value i.e. ₹ 75 because the selling price of the finished product is less than ₹ 225 (100 + 125) per kg.

(ii) When the selling price be ₹ 225
Incremental Profit = ₹ 225 - ₹ 125 = ₹ 100
Current price of the raw material = ₹ 75
Therefore, it is better to make the product.
Raw material inventory would be valued at ₹ 100 per kg because the selling price of the finished product is not less than ₹ 225.

Question based on AS - 2

2010 - Nov [1] {C} (b) HP is a leading distributor of petrol. A detail inventory of petrol in hand is taken when the books are closed at the end of each month. At the end of month following information is available :

Sales	₹	47,25,000
General overheads cost	₹	1,25,000
Inventory at beginning		1,00,000 litres @ 15/- per litre
Purchases		
June 1 two lakh litres @ 14.25		
June 30 one lakh litres @ 15.15		
Closing inventory 1.30 lakh litres		

Compute the following by the FIFO as per AS-2 :

(i) Value of Inventory on June 30.

(ii) Amount of cost of goods sold for June.

(iii) Profit/Loss for the month of June. (5 marks)

Answer :

(i) **Cost of closing inventory for 1,30,000 litres as on 30th June**

Particulars	**₹**
1,00,000 litres @ 15.15	15,15,000
30,000 litres @ 14.25	4,27,500
Total	19,42,500

(ii) **Computation of cost of goods sold**

Particulars	**₹**
Opening inventories (1,00,000 litres @ 15)	15,00,000
Purchases June-1 (2,00,000 litres @ 14.25)	28,50,000
June-30 (1,00,000 litres @ 15.15)	15,15,000
	58,65,000
Less : Closing inventories	(19,42,500)
Cost of goods sold	39,22,500

(iii) **Computation of profit**

Particulars	₹
Sales (Given) (A)	47,25,000
Cost of goods sold	39,22,500
Add: General overheads	1,25,000
Total cost (B)	40,47,500
Profit (A–B)	6,77,500

Question based on AS - 6

2010 - Nov [7] Answer the following :

(a) A company installed a plant at a cost of ₹ 20 lacs with estimated useful life of 10 years and decided to depreciate on straight line method. In the fifth year company decided to switch over from straight line method to written down value method. Compute the resultant surplus/deficiency if any, and state how will you treat the same in the accounts.

(4 marks)

Answer :

Table showing depreciation under Straight Line Method (SLM) and depreciation under Written Down Value Method (WDV)

	Depreciation	**₹ in lacs**
Year	**SLM**	**WDV**
I	2.00 (Note–1)	2.00 (Note–2)
II	2.00	1.80
III	2.00	1.62
IV	2.00	1.46
Total	8.00	6.88

Resultant surplus on change in method of depreciation from SLM to WDV = (8.00 – 6.88) ₹ 1.12 lakhs.

Provision:

- **According to AS 6 'Depreciation Accounting'**, when a change in the method of depreciation is made, depreciation should be re-calculated in accordance with the new method from the date of the asset put to use.
- The deficiency or surplus arising from retrospective re-computation of depreciation in accordance with the new method should be adjusted in the accounts in the year in which the method of depreciation is changed.

Analysis and Conclusion:

- In the given question, surplus amounting ₹ 1.12 lakhs (8.00 – 6.88) should be credited to profit and loss statement in the fifth year. Such a change should be treated as a change in accounting policy and its effect should be quantified and disclosed as per AS 5. “Net Profit loss for the period, prior period items and changes in Accounting Policies.

Note 1 : Depreciation as per SLM ₹ 20 lakhs/10 years = 2 lakhs.
Note 2 : Depreciation rate under SLM is 10% (2,00,000/20,00,000 × 100). It is assumed that depreciation rate will remain same under WDV method also.

Question based on AS - 7

2010 - Nov [7] Answer the following :

(c) An amount of ₹ 9,90,000 was incurred on a contract work upto 31-3-2010. Certificates have been received to date to the value of ₹ 12,00,000 against which ₹ 10,80,000 has been received in cash. The cost of work done but not certified amounted to ₹ 22,500. It is estimated that by spending an additional amount of ₹ 60,000 (including provision for contingencies) the work can be completed in all respects in another two months. The agreed contract price of work is ₹ 12,50,000. Compute a conservative estimate of the profit to be taken to the Profit and Loss Account as per AS-7. (4 marks)

Answer :

Computation of Estimated Profit as per AS 7

Particulars	**₹**
Expenditure incurred upto 31.3.2010	9,90,000
Estimated additional expenses (including provision for contingency)	60,000
Estimated cost (A)	10,50,000
Contract price (B)	12,50,000
Total estimated profit [(B-A)]	2,00,000
Percentage of completion (9,90,000/10,50,000) × 100	94.29%
Computation of estimate of the profit to be taken to Profit and Loss Account :	

$$= \text{Total estimated profit} \times \frac{\textbf{Expenses incurred till 31.3.2010}}{\textbf{Total estimated cost}}$$

$$= 2{,}00{,}000 \times \frac{\mathbf{9{,}90{,}000}}{\mathbf{10{,}50{,}000}} = 1{,}88{,}571$$

Provision:

According to AS 7 'Construction Contracts', when the outcome of a construction contract can be estimated reliably, contract revenue and contract costs associated with the construction contract should be recognised as revenue and expenses respectively by reference to stage of completion of the contract activity at the reporting date.

Analysis and Conclusion:

Therefore estimated profit amounting ₹ 1,88,571 should be recognised as revenue in the statement of profit and loss.

Question based on AS - 2

2011 - May [7] Answer the following :

(b) Best Ltd. deals in five products, P, Q, R, S, and T which are neither similar nor interchangeable. At the time of closing of its accounts for the year ending 31st March 2011, the historical cost and net realisable value of the items of the closing stock are determined as follows :

Items	Historical Cost	Net realizable value
	₹	₹
P	5,70,000	4,75,000
Q	9,80,000	10,32,000
R	3,16,000	2,89,000
S	4,25,000	4,25,000
T	1,60,000	2,15,000

What will be the value of closing stock for the year ending 31st March, 2011 as per AS-2 "Valuation of inventories"? (4 marks)

Answer :

According to para 5 of AS 2 "Valuation of Inventories, inventories should be valued at the lower of cost and net realizable value. Inventories should be written down to net realizable value on an item-by-item basis.

Valuation of inventory (item wise) for the year ending 31st March 2011

Item	*Historical Cost*	*Net realizable Value*	*Valuation of closing* **stock**
	(₹)	**(₹)**	**(₹)**
P	5,70,000	4,75,000	4,75,000
Q	9,80,000	10,32,000	9,80,000
R	3,16,000	2,89,000	2,89,000
S	4,25,000	4,25,000	4,25,000
T	1,60,000	2,15,000	1,60,000
			23,29,000

The value of inventory for the year ending 31st March 2011 = ₹ 23,29,000

Do you know ?

AS - 2 (Rev) is not applicable to WIP of service companies, but any unconsumed material attracts AS - 2 e.g. Services of Saloon/Beauty Parlour is service industry but material kept for use is inventory.

Question based on AS - 6

2011 - Nov [1] {C} Answer the following question :

(c) In the Trial Balance of M/s Sun Ltd. as on 31-3-2011, balance of machinery appears ₹ 5,60,000. The company follows rate of depreciation on machinery @ 10% p.a. on Straight Line Method. On scrutiny it was found that a machine appearing in the books on 1-4-2010 at ₹ 1,60,000 was disposed of on 30-9-2010 at ₹ 1,35,000 in part exchange of a new machine costing ₹ 1,50,000.

You are required to calculate :

(i) Total depreciation to be charged in the Profit and Loss Account.
(ii) Loss on exchange of machine.
(iii) Book value of machinery in the Balance Sheet as on 31-3-2011.

(5 marks)

Answer :

Assumption: The question has been solved on the basis of written down value method due to absence of related information regarding straight line method.

(i) **Total Depreciation to be charged in the Profit and Loss Account**

	₹
Depreciation on old machinery in use [10% of (5,60,000 - 1,60,000)]	40,000
Add: Depreciation on new machine @ 10% for six months $\left(1,50,000 \times 10\% \times \frac{6}{12}\right)$	7,500
Total depreciation on machinery in use	47,500
Add: Depreciation on machine disposed of (10% for 6 months) $\left(1,60,000 \times 10\% \times \frac{6}{12}\right)$	8,000
So, total depreciation to be charged in Profit and Loss A/c	55,500

(ii) **Loss on Exchange of Machine**

Particulars	₹
Book value of machine as on 1.4.2010	1,60,000
Less: Depreciation for 6 months @ 10%	(8,000)
Written Down Value as on 30.9.2010	1,52,000
Less: Exchange value	(1,35,000)
Loss on exchange of machine	17,000

(iii) **Book Value of Machinery in the Balance Sheet as on 31.03.2011**

	₹
Balance as per trial balance	5,60,000
Less: Book value of machine sold	(1,60,000)
	4,00,000
Add: Purchase of new machine	1,50,000
	5,50,000
Less: Depreciation on machinery in use	(47,500)
	5,02,500

KZ - 7 **Knowledge Zone**

The Effects of Change in Historical Cost and Estimated Life of the Asset on Depreciation

Change in estimated useful life/salvage value changes the amount of depreciation charged. However, such revised amount of depreciation is charged prospectively. The written down value of the asset is apportioned over the remaining estimated revised useful life.

Change in the cost of the asset

If the historical cost of an asset changes due to changes in foreign exchange rates/price fluctuation, its revised amount of depreciation will be charged from the date of such change, i.e., prospectively.

Change in depreciation due to change in either estimated life or scrap value will be disclosed as per AS - 5.

Question based on AS - 10

2011 - Nov [7] Answer the following:

(a) M/s. Tiger Ltd. allotted 7500 equity shares of ₹ 100 each fully paid up to Lion Ltd. in consideration for supply of a special machinery. The shares exchanged for machinery are quoted at National Stock Exchange (NSE) at ₹ 95 per share, at the time of transaction. In the absence of fair market value of the machinery acquired, how the value of the machinery would be recorded in the books of Tiger Ltd ? (4 marks)

Answer :

Provision:

According to para 11 of AS 10 "Accounting for Fixed Assets", fixed asset acquired in exchange for shares or other securities in the enterprise should be recorded at its fair market value, or the fair market value of the securities issued, whichever is more clearly evident.

Analysis and Conclusion:

In the given case the market value of the shares exchanged for the asset is more clearly evident therefore the company should record the value of machinery at ₹ 7,12,500 (i.e., 7,500 shares × ₹ 95 per share) being the market price of the shares issued in exchange.

Question based on AS - 9

2011 - Nov [7] Answer the following:

(b) M/s. SEA Ltd. recognized ₹ 5.00 lakhs on accrual basis income from dividend during the year 2010-11, on shares of the face value of ₹ 25.00 lakhs held by it in Rock Ltd. as at 31st March, 2011. Rock Ltd. proposed dividend @ 20% on 10th April, 2011. However, dividend was declared on 30th June, 2011. Please state with reference to relevant Accounting Standard, whether the treatment accorded by SEA Ltd. is in order.

(4 marks)

Answer :

Provision:

According to para 8.4 of AS 9 "Revenue Recognition", dividends from investments in shares are not recognized in the statement of Profit and Loss until the right to receive dividends is established.

Analysis and Conclusion:

In the given situation the dividend is proposed on 10th April, 2011, while it was declared on 30th June, 2011. Hence, the right to receive dividend is established on 30th June, 2011 only. Therefore, on applying the provisions stated in the standard, income from dividend on shares should be recognized by Sea Ltd. in the financial year 2011-2012 only.

Therefore, the recognition of income from dividend of ₹ 5 lakhs, on accrual basis, in the financial year 2010-11 is not in accordance with AS 9.

Question based on AS - 7

2011 - Nov [7] Answer the following:

(d) From the following data, show. Profit and Loss A/c (Extract) as would appear in the books of a contractor following Accounting Standard - 7 :

	(₹ in lakhs)
Contract Price (fixed)	480.00
Cost incurred to date	300.00
Estimated cost to complete	200.00

(4 marks)

Answer :

Calculation of Estimated Total Cost

Particulars	(₹ in lakhs)
Cost incurred to date	300
Estimate of cost completion	200
Estimated total cost in completing the contract	500

Percentage of completion (300/500) × 100 = 60%

Revenue recognised as a percentage to contract price

= 60% of ₹ 480 lakhs = ₹ 288 lakhs

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 recognised as an expense immediately. Accordingly, expenses to be recognized in the Profit and Loss Account will be

	(₹ in lakhs)
Total foreseeable loss (500 - 480)	20
Less: Loss for the current year (300 - 288)	(12)
Expected loss to be recognized immediately as per para 35 of AS 7	8

Profit and Loss A/c (An Extract)

	(₹ in lakhs)		(₹ in lakhs)
To Construction cost	300	By Contract price	288
To Estimated loss on completion of contract	8		
	?		?

Question based on AS - 7

2012 - May [1] {C} (a) M/s Excellent Construction Company Limited undertook a contract to construct a building for ₹ 3 Crore on 1st September, 2011. On 31st March, 2012 the company found that it had already spent ₹ 1 Crore 80 Lakhs on the construction. Prudent estimate of additional cost for completion was ₹ 1 Crore 40 Lakhs. What amount should be charged, to revenue in the final accounts for the year ended on 31st March, 2012, as per the provisions of Accounting Standard 7 "Construction Contracts (Revised)"? (5 marks)

Answer:

Computation of Estimated Cost of Construction:

Particulars	₹ in crores
Cost of construction incurred till date	1.80
Add: Estimated future cost	1.40
Total estimated cost of construction	3.20

Percentage of completion of contract till date to total estimated cost of construction = ₹ (1.80/3.20) × 100 = 56.25%

Proportion of total contract price considered as revenue as per AS 7 (Revised)

= Contract price × percentage of completion

= ₹ 3 crores × 56.25% = ₹ 1.6875 crores

Question based on AS - 13

2012 - May [1] {C} (b) M/s Innovative Garments Manufacturing Company Limited invested in the shares of another company on 1st October, 2011 at a cost of ₹ 2,50,000. It also earlier purchased Gold of ₹ 4,00,000 and Silver of ₹ 2,00,000 on 1st March, 2009. Market value as on 31st March, 2012 of above investments are as follows:

	₹
Shares	2,25,000
Gold	6,00,000
Silver	3,50,000

How above investments will be shown in the books of accounts of M/s Innovative Garments Manufacturing Company Limited for the year ending 31st March, 2012 as per the provisions of Accounting Standard 13 "Accounting for Investments"? (5 marks)

Answer :

Provision:

According to AS 13, Accounting for Investments, for investment in shares:

- If shares are purchased with an intention to hold for short-term period then it will be shown at the realizable value of ₹ 2,25,000 as on 31st March, 2012.
- However, if equity shares are acquired with an intention to hold for long term period then it will be shown at cost of ₹ 2,50,000 in the Balance Sheet of the company.
- However, provision for diminution shall be made to recognize a decline, if other than temporary, in the value of shares.
- According to the standard, investment acquired for long term period shall be shown at cost. Gold and silver are generally purchased with an intention to hold it for long term period until and unless given otherwise.

Analysis and Conclusion:

The investment in Gold and Silver (purchased on 1st March, 2009) shall continue to be shown at cost as on 31st March, 2012 i.e., ₹ 4,00,000 and ₹ 2,00,000 respectively, though their realizable values have increased.

Question based on AS - 6 & 10

2012 - May [1] {C} (c) M/s Progressive Company Limited has not charged depreciation for the year ended on 31st March, 2012, in respect of a spare bus purchased during the financial year 2011-12 and kept ready by the company for use as a stand-by , on the ground that, it was not actually used during the year. State your views with reference to Accounting Standard 6 "Depreciation Accounting".

Further during the year company made additions to its factory by using its own workforce, at a cost of ₹ 4,50,000 as wages and materials. The lowest estimate from an outside contractor to carry out the same work was ₹ 6,00,000. The directors contend that, since they are fully entitled to employ an outside contractor, it is reasonable to debit the Factory Building Account with ₹ 6,00,000. Comment whether the directors' contention is right in view of the provisions of Accounting Standard 10 "Accounting for Fixed Assets"? (5 marks)

Answer :

Provisions:

According to AS 6, 'Depreciation Accounting':

- Depreciation is a measure of wearing out, consumption or other loss of value of a depreciable asset arising from use, effluxion of time or obsolescence through technology and market changes.

- Accordingly, depreciation may arise even when asset has not been used in the current year but was ready for use in that year.
- The need for using the stand by bus may not have arisen during the year but that does not imply that the useful life of the bus has not been affected. Therefore, non-provision of depreciation on the ground that the bus was not used during the year is not tenable.
- As per AS 10, 'Accounting for Fixed Assets', the gross book value of the self constructed fixed asset includes the costs of construction that relate directly to the specific asset and the costs that are attributable to the construction activity in general can be allocated to the specific asset. If any internal profit is there it should be eliminated. Saving of ₹ 1,50,000 on account of using its own workforce is an unrealized/internal profit, which should not be capitalized/recorded as per the standard.

Analysis and Conclusion:

Therefore only ₹ 4,50,000 should be debited to the factory building account and not ₹ 6,00,000.

Hence, the contention of the directors of the company to capitalize ₹ 6,00,000 as cost of factory building, on the ground that the company is fully entitled to employ an outside contractor is not justifiable.

Question based on AS - 6

2012 - May [7] Answer the following :

(c) A computer costing ₹ 60,000 is depreciated on straight line basis, assuming 10 years working life and Nil residual value, for three years. The estimate of remaining useful life after third year was reassessed at 5 years. Calculate depreciation as per the provisions of Accounting Standard 6 "Depreciation Accounting". (4 marks)

Answer:

Depreciation per year = ₹ 60,000/10 = ₹ 6,000

Depreciation on SLM charged for three years = ₹ 6,000 × 3 years = ₹ 18,000

Book value of the computer at the end of third year = ₹ 60,000 - ₹ 18,000 = ₹ 42,000

Remaining useful life as per previous estimate = 7 years

Remaining useful life as per revised estimate = 5 years

Depreciation from the fourth year onwards = ₹ 42,000/5 = ₹ 8,400 per annum

Question based on AS - 2

2012- Nov - [7] Answer the following:

(b) From the following information ascertain the value of stock as on 31st March, 2012:

	₹
Stock as on 01.04.2011	28,500
Purchases	1,52,500
Manufacturing Expenses	30,000
Selling Expenses	12,100
Administration Expenses	6,000
Financial Expenses	4,300
Sales	2,49,000

At the time of valuing stock as on 31st March, 2011 a sum of ₹ 3,500 was written off on a particular item, which was originally purchased for ₹ 10,000 and was sold during the year of ₹ 9,000. Barring the transaction relating to this item, the gross profit earned during the year was 20% on sales. (4 marks)

Answer:

Statement showing valuation of stock as on 31.3.2012

Particulars	₹	₹
Stock as on 01.04.2011	28,500	
Less : Book value of abnormal stock (₹ 10,000 – ₹ 3,500)	(6,500)	22,000
Add : Purchases		1,52,500
Manufacturing Expenses		30,000
		2,04,500
Less : Cost of Sales :		
Sales as per Books	2,49,000	
Less : Sales of Abnormal item	(9,000)	
Less : Gross Profit @ 20%	2,40,000	
Value of Stock as on 31st March, 2012	(48,000)	
		(1,92,000)
		12,500

Question based on AS - 10

2012 - Nov [7] Answer the following:

(c) PQR Ltd. constructed a fixed asset and incurred the following expenses on its construction:

	₹
Materials	16,00,000
Direct Expenses	3,00,000
Total Direct Labour	6,00,000
(1/15th of the total labour time was chargeable to the construction)	
Total Office & Administrative Expenses	9,00,000
(4% is chargeable to the construction)	
Depreciation on assets used for the construction of this asset	15,000

Calculate the cost of the fixed asset. (4 marks)

Answer :

Calculation of cost of fixed assets

Particulars	₹
Materials	16,00,000
Direct expenses	3,00,000
Direct labour (1/15th of ₹ 6,00,000)	40,000
Office and administrative expenses (4% ₹ 9,00,000)	36,000
Depreciation on assets	15,000
Cost of fixed asset	19,91,000

Note: It is assumed that 4% of office and administrative expenses are specifically attributable to construction of a fixed asset. Alternatively, it may be assumed that 4% of office and administrative expenses are only allocated to construction project and is not specifically attributable to it. In such a case, the cost of fixed assets will be ₹ 19,55,000.

Question based on AS - 2

2013 - May [7] Answer the following:

(c) On 31st March 2013 a business firm finds that cost of a partly finished unit on that date is ₹ 530. The unit can be finished in 2013-14 by an additional expenditure of ₹ 310. The finished unit can be sold for ₹ 750 subject to payment of 4% brokerage on selling price. The firm seeks your advice regarding:-

(i) the amount at which the unfinished unit should be valued as at 31st March, 2013 for preparation of final accounts and

(ii) the desirability or otherwise of producing the finished unit.

(4 marks)

Answer:

Valuation of unfinished unit:

	₹
Net selling price	750
Less: Estimated cost of completion	(310)
	440
Less: Brokerage(4% of 750)	30
Net Realisable Value	410
Cost of inventory	530
Value of inventory (Lower of cost and net realisable value)	410

Incremental cost ₹ 310 (cost to complete) is less than incremental revenue ₹ 720 (₹ 750 - ₹ 30). The enterprise will therefore decide to finish the unit for sale at ₹ 750.

Note: The aforesaid solution is based on assumption that partly finished unit cannot be sold in semi finished form and its NRV is zero without processing it further.

Question based on AS - 9

2013 - May [7] Answer the following:

(d) M/s. Moon Ltd. sold goods worth ₹ 6,50,000 to Mr. Star. Mr. Star asked for a trade discount amounting to ₹ 53,000 and same was agreed to by M/s. Moon Ltd. The sales was effected and goods were dispatched. On receipt of goods, Mr. Star has found that goods worth ₹ 67,000 are defective. Mr. Star returned defective goods to M/s. Moon Ltd. and made payment due amounting to ₹ 5,30,000. The accountant of M/s. Moon Ltd. booked the sale for ₹ 5,30,000. Discuss the contention of the accountant with reference to Accounting Standard (AS) 9.

(4 marks)

Answer :

Provisions

- **As per AS 9 'Revenue Recognition',** revenue is the gross inflow of cash, receivable or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods.
- However, trade discounts and volume rebates given in the ordinary course of business should be deducted in determining revenue.
- Revenue from sales should be recognized at the time of transfer of significant risks and rewards.
- If the delivery of the sales is not subject to approval from customers, then the transfer of significant risks and rewards would take place when the sale is affected and goods are dispatched.

Analysis and Conclusion:

- In the given case, if trade discounts allowed by M/s. Moon Ltd. are given in the ordinary course of business, M/s. Moon Ltd. should record the sales at ₹ 5,97,000 (i.e. ₹ 6,50,000 − ₹ 53,000) and goods returned worth ₹ 67,000 are to be recorded in the form of sales return.
- However, when trade discount allowed by M/s. Moon Ltd. is not in the ordinary course of business, M/s. Moon Ltd. should record the sales at gross value of ₹ 6,50,000. Discount of ₹ 53,000 in price and return of goods worth ₹ 67,000 are to be adjusted by suitable provisions.
- M/s Moon Ltd. might have sent the credit note of ₹ 1,20,000 to Mr. Star to account for these adjustments. In both the cases, the contention of the accountant to book the sales for ₹ 5,30,000 is not correct.

Question based on AS - 10

2013 - Nov [1] {C} (a) Amna Ltd. contracted with a supplier to purchase a specific machinery to be installed in Department A in two months time. Special foundations were required for the plant, which were to be prepared within this supply lead time. The cost of site preparation and laying foundations were ₹ 47,290. These activities were supervised by a technician during the entire period, who is employed for this purpose of ₹ 15,000 per month. The Technician's services were given to Department A by Department B, which billed the services at ₹ 16,500 per month after adding 10% profit margin.

The machine was purchased at ₹ 52,78,000. Sales Tax was charged at 4% on the invoice. ₹ 18,590 transportation charges were incurred to bring the machine to the factory. An Architect was engaged at a fee of ₹ 10,000 to supervise machinery installation at the factory premises. Also, payment under the invoice was due in 3 months. However, the Company made the payment in 2nd month. The company operates on Bank Overdraft @ 11%. Ascertain the amount at which the asset should be capitalized under AS 10.

(5 marks)

Answer:

Cost of machinery is calculated as under :

Particulars	**Amount (₹)**
Purchase Price (given)	52,78,000
Add : Sales tax at 4% (Note 1)	2,11,120
Site preparation Cost (given)	47,290
Technician's Salary for 2 months	30,000
Initial Delivery Cost (transportation)	18,590
Professional Fees for Installation	10,000
Total Cost	**55,95,000**

Note:

1. 4% of 52,78,000 = 2,11,120

2. Interest on Bank overdraft for earlier payment of invoice is not relevant under AS - 10.

3. Internally booked profits should be eliminated in arriving at the cost of Fixed Assets.

4. It has been assumed that the purchase price of ₹ 52,78,000 excludes amount of sales tax.

Question based on AS - 6

2013 - Nov [1] {C} (b) Narmada Ltd. purchased an existing bottling unit from Kaveri Ltd. Kaveri Ltd. followed straight line method of charging depreciation on machinery of the sold unit whereas Narmada Ltd. followed written down value method in its other units. The directors of Narmada Ltd. want to continue to charge depreciation for the acquired unit in Straight Line Method which is not consistent with the WDV method followed in other units. Discuss the contention of the directors with reference to the Accounting Standard 6. Further during the year, Narmada Ltd. set up a new plant on coastal land. In view of the corrosive climate, the Company felt that its machine life is reducing faster. Can the Company charge a higher rate of depreciation?

(5 marks)

Answer :

As per AS 6 'Depreciation Accounting', there are several methods of allocating depreciation over the useful life of the assets. The management of a business selects the most appropriate method(s) based on various important factors.

For Example:

(i) type of asset,

(ii) the nature of the use of such asset and

(iii) circumstances prevailing in the business. A combination of more than one method is sometimes used.

- A company may adopt different methods of depreciation for different types of assets, provided the same methods are followed consistently. Thus Narmada Ltd. can continue to charge depreciation for the acquired unit as per straight line method.
- The statute governing an enterprise may provide the basis for computation of the depreciation.
- Therefore, in the given case, the company can charge higher rates of depreciation based on its estimate of the useful life of machinery.

- So, such higher depreciation rates and /or the reduced useful lives of the assets should be disclosed by way of notes to the accounts in the Financial Statements.

Question based on AS - 9

2013 - Nov [1] {C} (c) A Ltd. entered into a contract with B Ltd. to despatch goods valuing ₹ 25,000 every month for 4 months upon receipt of entire payment. B Ltd. accordingly made the payment of ₹ 1,00,000 and A Ltd. started despatching the goods. In third month, due to a natural calamity, B Ltd. requested A Ltd. not to despatch goods until further notice though A Ltd. is holding the remaining goods worth ₹ 50,000 ready for despatch. A Ltd. accounted ₹ 50,000 as sales and transferred the balance to Advance Received against Sales. Comment upon the treatment of balance amount with reference to the provisions of Accounting Standard 9. (5 marks)

Answer :

Analysis:

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 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.

Conclusion:

In the given problem 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. A Ltd. should recognize the entire sale of ₹ 1,00,000 (₹ 25,000 x 4) and no part of the same is to be treated as Advance Receipt against Sales.

Question based on AS - 14

2013 - Nov [1] {C} (d) A Ltd. is amalgamating with B Ltd. They are undecided on the method of accounting to be followed. You are required to advice the management of B Ltd. on the method of accounting that can be adopted under AS-14. (5 marks)

Answer :

- An amalgamation may be either – an amalgamation in the nature of merger, or an amalgamation in the nature of purchase.
- The selection of method of accounting for amalgamation (pooling of interests or purchase method) is to be judged after considering the intentions of the both the companies.
- If genuine pooling of all assets, liabilities, shareholders' interest is intended; separate businesses of both the companies are continued and their amalgamation scheme satisfies all the conditions necessary for merger as specified in AS 14 Accounting for Amalgamations, pooling of interests method is adopted.
- If B Ltd. or A Ltd. wants to acquire the other company, then purchase method needs to be adopted. In that case, the shareholders of the acquired company don't continue to have proportional share in equity of the combined company and the business of the acquired company is not intended to be continued.
- The object of the purchase method is to account for the amalgamation by applying the same principles as are applied in the normal purchase of assets.
- Thus choice of accounting method depends on the fact whether B Ltd. wants to continue its business or not.

2014 - May [1] {C} (a) Calculate the value of raw materials and closing stock based on the following information :

Raw material X	
Closing balance	500 units
	₹ per unit
Cost price including excise duty	200
Excise duty	10

(Cenvat credit is receivable on the excise duty paid.)

Freight inward	20
Unloading charges	10
Replacement cost	150
Finished goods Y	
Closing Balance	1200 units
	₹ per unit
Material consumed	220
Direct labour	60
Direct overhead	40

Total Fixed overhead for the year was ₹ 2,00,000 on normal capacity of 20,000 units.

Calculate the value of the closing stock, when

(i) Net Realizable Value of the Finished Goods Y is ₹ 400.

(ii) Net Realizable Value of the Finished Goods Y is ₹ 300. (5 marks)

Answer:

If NRV of the Finished Goods (y) is ₹ 400

Finished Goods = Cost or NRV whichever is less.

$$\text{Cost} = \left[220 + 60 + 40 + \frac{2,00,000}{20,000}\right] \times 1,200$$

$$\left.\begin{array}{l}\text{Cost} = 330 \times 1,200 = 3,96,000 \\ \text{NRV} = 400 \times 1,200 = 4,80,000\end{array}\right] \Rightarrow \text{Whichever is less} = 3,96,000$$

Raw Material = Since FG is sold at or above cost, hence cost of R.M. has to be considered and not the replacement cost.

Working Notes:

Raw Material X	₹
Cost price	200
Less: Cenvat Credit	(10)
	190
Add: Freight Inward	20
Unloading charges	10

Cost	220
Finished goods Y	₹
Materials consumed	220
Direct Labour	60
Direct overhead	40
Fixed overheads (₹ 2,00,000/20,000 units)	10
Cost	330

Cost = [200 − 10 + 20 + 10] × 500
= 220 × 500 = 1,10,000

Closing stock = FG +RM = 3,96,000 +1,10,000 = ₹ 5,06,000

If NRV of the Finished Goods (y) is ₹ 300

Finished Goods = Cost or NRV whichever is less

Cost = 330
NRV = 300 ⇒ whichever is less = 300 × 1,200 = ₹ 3,60,000

Raw Material = If FG is sold at/above cost then RM is considered at cost. If FG is sold below cost then RM should be valued at replacement cost.
= 500 units × 150 = ₹ 75,000

Closing St = FG + RM = 3,60,000 + 75,000 = ₹ 4,35,000

2014 - May [1] {C} (b) On 01.04.2010 a machine was acquired at ₹ 4,00,000. The machine was expected to have a useful life of 10 years. The residual value was estimated at 10% of the original cost. At the end of the 3rd year, an attachment was made to the machine at a cost of ₹ 1,80,000 to enhance its capacity. The attachment was expected to have a useful life of 10 years and zero terminal value. During the same time the original machine was revalued upwards by ₹ 90,000 and remaining useful life was reassessed at 9 years and residual value was reassessed at NIL.

Find depreciation for the year, if

(i) attachment retains its separate identity.

(ii) attachment becomes integral part of the machine. (5 marks)

Answer :

(i) **If attachment retains its Separate Identify**

Cost of Machine on 1.4.10	= 4,00,000	
Less: Residual Value 10%	= 40,000	
Depreciable Value	= 3,60,000	
Estimated Useful life	=10 years	
Dep. p.a.	= 3,60,000 ÷ 10	= ₹ 36,000
Total Dep. in 3 years	= 36,000 × 3	= ₹ 1,08,000
WDV for 4th year	= 4,00,000 −1,08,000	= 2,92,000

Upward Revaluation of Original Machine = 90,000

∴ WDV for 4th year after revaluation = 2,92,000 + 90,000 = 3,82,000

Remaining useful life	= 9 years	
Dep. in 4th year	= 3,82,000 ÷ 9	= ₹ 42,444
Dep. on attachment	= 1,80,000 ÷ 10	= ₹ 18,000
Total Depreciation	= 42,444 + 18,000	= ₹ 60,444.

Note:

1. Since, upward revaluation of the machine and reassessment of remaining useful life had been made at the end of the 3rd year, it is implied that depreciation for the 3rd year has been charged on the basis of old calculation & remaining useful life of 9 years is to be calculated from the beginning of the 4th year onwards.
2. Depreciation for the 4th year i.e. 2013-14 has been given in the solution.

(ii) If attachment becomes integral part of Machine

In this case it will be added to the value of machine and depreciated alongwith machine over the life of machine.

Value of Machine after Revaluation	= 3,82,000
Add: Cost of Attachment	= 1,80,000
Total Value	= 5,62,000
Life	= 9 years
Depreciation	= 5,62,000 ÷ 9 = ₹ 62,444

2014 - May [1] {C} (c) Ascertain the value at which various items of Fixed Assets are to be shown in the Financial Statements of Velvet Ltd. and amount to be debited to the Profit and Loss Account in the context of the relevant Accounting Standard.

Narrations for the adjustments made should form part of the answer :

(i) Goodwill was valued at ₹ 1,20,000 by independent valuers and no consideration was paid. The Company has not yet recorded the same.

(ii) Balance of Office Equipment as on 01.04.2013 is ₹ 1,20,000. On 01.04.2013, out of the above office equipment having book value ₹ 20,000 has been retired from use and held for disposal. The net realizable value of the same is ₹ 2,000. Rate of depreciation is 15% p.a. on WDV basis.

(iii) Book Value of Plant and Machinery as on 01.04.2013 was ₹ 7,20,000. On 01.08.2013 an item of machinery was purchased in exchange for 500 equity shares of face value ₹ 10. The Fair Market value of the equity shares on 01.08.2013 was ₹ 120. Rate of depreciation is 10% p.a. on WDV basis. (5 marks)

Answer :

Statement showing treatment and value of various items of Fixed Assets

	Item of Fixed Assets	**Amount ₹**	**Amount Debited to P&L in 2013-14**	**Narra-tion**	**Book Value as on 31.3.2014 to be shown in the Financial Statements**
(i)	Goodwill Book value as on 1.4.2013 Balancing as on 31.3.2014 (See Note 1)	 0			 0

(ii)	Office Equipment				
	Balance as on 1.4.2013	1,20,000			
	Less: Retired from use (Book value on 1.4.2013)	20,000			
		1,00,000			
	Less: Depreciation for 2013-14 @15% WDV	15,000	15,000	Depreciation	85,000
	Balance as on 31.3.2014	85,000			85,000
	Office Equipment (Retired from use) Book Value as on 1.4.2013	20,000			
	Less: Book value as on 31.3.2014 (at NRV) (See Note 2)	2,000			2,000
	Loss on retirement charged to P&L	18,000	18,000	Loss on retirement of asset	
(iii)	Plant and Machinery				
	Book Value as on 1.4.2013	7,20,000			
	Add: Machine purchased on 01.08.2013(See Note 3)	60,000			
		7,80,000			
	Less: Depreciation Original machine for whole year 72,000				
	New machine for 8 months 4,000	76,000	76,000	Depreciation	
	Balance as on 31.3.2014	7,04,000			7,04,000
			1,09,000		7,91,000

Note:

1. As per para 16 of AS 10 'Accounting for Fixed Assets' goodwill is to be recorded only when some consideration in money or money's worth has been paid for it. Since the goodwill is self generated and no money or

money's worth has been paid for the same, therefore, it is not to be recorded in the books.

2. Office equipment having book value of ₹ 20,000 as on 1.4.2013 has been retired from use. It has been recorded at Net Realisable Value (NRV) as the NRV is lower than the book value and shown separately in the financial statements. This is in consonance with the provisions stated in para 14 of AS 10.
3. As per para 11 of the standard, the new machine has been recorded at the Fair Market Value of the securities issued as it is more clearly evident.

2014 - May [1] {C} (d) M/s. Highway Constructions undertook the construction of a highway on 01.04.2013. The contract was to be completed in 2 years. The contract price was estimated at ₹ 150 crores. Up to 31.03.2014 the company incurred ₹ 120 crores on the construction. The engineers involved in the project estimated that a further ₹ 45 crores would be incurred for completing the work.

What amount should be charged to revenue for the year 2013-14 as per the provisions of Accounting Standard 7 "Construction Contracts"? Show the extract of the Profit & Loss A/c in the books of M/s. Highway Constructions. (5 marks)

Answer :

Statement showing the amount to be charged to Revenue as per AS 7

	₹ in crores
Cost of construction incurred upto 31.03.2014	120
Add: Estimated future cost	45
Total estimated cost of construction	165
Degree of completion (120/165x100)	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	4

Profit and Loss Account (Extract)

	₹ in crores		**₹ in crores**
To Construction Costs	120	By Contract Price	109
To Provision for loss	4	By Net loss	15
	124		124

2014 - Nov [1] {C} (a) In the books of Optic Fiber Ltd., plant and machinery stood at ₹ 6,32,000 on 1.4.2013. However on scrutiny it was found that machinery worth ₹ 1,20,000 was included in the purchases on 1.6.2013. On 30.6.2013 the company disposed a machine having book value of ₹ 1,89,000 on 1.4.2013 at ₹ 1,75,000 in part exchange of a new machine costing ₹ 2,56,000. The company charges depreciation @ 20% WDV on plant and machinery.

You are required to calculate:

(i) Depreciation to be charged to P/L

(ii) Book value of Plant and Machinery A/c as on 31.3.2014

(iii) Loss on exchange of machinery. (5 marks)

Answer :

(i) Depreciation to be charged in the Profit and Loss Account

Particulars	(₹)
Depreciation on old Machinery	31,600
[20% on ₹ 6,32,000 for 3 months]	
Add: Depreciation machinery acquired on 01.06.2013 (₹ 1,20,000 × 20% ×10/12)	20,000
Depreciation on Machinery after adjustment of Exchange [20% of ₹ (6,32,000 - 1,89,000 + 2,56,000) for 9 months]	1,04,850
Total Depreciation to be charged in Profit and Loss A/c	1,56,450

(ii) Book Value of Plant and Machinery A/c as on 31.03.2014

Particulars	₹	₹
Balances as per books on 01.04.2013		6,32,000
Add: Included in purchases on 01.06.2013	1,20,000	
Add: Purchase on 30.06.2013	2,56,000	3,76,000
		10,08,000
Less: Book value of Machine sold on 30.06.2013		(1,89,000)
		8,19,000
Less: Depreciation on machinery in use (1,56,450-9,450)		(1,47,000)
Book Value as on 31.03.2014		6,72,000

(iii) Loss on exchange of Machinery

Particulars	₹
Book value of machinery as on 01.04.2013	1,89,000
Less: Depreciation for 3 months	9,450
WDV as on 30.06.2013	1,79,550
Less: Exchange value	1,75,000
Loss on exchange of machinery	4,550

Question based on AS - 9

2014 - Nov [1] {C} (b) Sarita Publications publishes a monthly magazine on the 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 2014 issue was made in February 2014. The magazine was published on its scheduled date. It received ₹ 2,40,000 on 10.3.2014 and ₹ 60,000 on 10.4.2014 for the March 2014 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 31.3.2014. What will be the treatment if the publication is delayed till 2.4.2014? (5 marks)

Answer :

According to 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 this case, income accrues when the related advertisement appears before public.

The advertisement service would be considered as performed on the day the advertisement is seen by public and hence revenue is recognized on that date, so in this case, it is 15.03.2014, the date of publication of the magazine.

Therefore, ₹ 3,00,000 (₹ 2,40,000 + ₹ 60,000) is recognized as income in March, 2014. The terms of payment are not relevant for considering the date on which revenue is to be recognized. ₹ 60,000 is treated as amount due from advertisers as on 31.03.2014 and ₹ 2,40,000 will be treated as payment received against the sale.

Whereas, if the publication is delayed till 02.04.2014 revenue recognition will also be delayed till the advertisements get published in the magazine. In such case revenue of ₹ 3,00,000 will be recognized for the year ended 31.03.2015 after the magazine is published on 02.04.2014. The amount received from sale of advertising space on 10.03.2014 of ₹ 2,40,000 will be considered as an advance from advertisers as on 31.03.2014.

Question based on AS - 2

2014 - Nov [1] {C} (c) Capital Cables Ltd., has a normal wastage of 4% in the production process. During the year 2013-14 the Company used 12,000 MT of raw material costing ₹ 150 per MT.

At the end of the year 630 MT of wastage was in stock. The accountant wants to know how this wastage is to be treated in the books.

Explain in the context of AS 2 the treatment of normal loss and abnormal loss and also find out the amount of abnormal loss if any. (5 marks)

Answer :

According to AS-2, (Revised) 'Valuation of Inventories', abnormal amounts of wasted materials, labour and other production costs are excluded from cost of inventories and such costs are recognised as expenses in the period in which they are incurred.

The amount of normal loss will be included in computing the cost of inventories (finished goods) at the year end.

Amount of Abnormal Loss:

Material used	12,000 MT @ ₹ 150 = ₹ 18,00,000
Normal Loss (12,000 MT 4%)	480 MT
Net quantity of material	11,520 MT
Abnormal Loss in quantity	150 MT
Abnormal Loss	₹ 23,437.50
[150 units @ ₹156.25 (₹ 18,00,000/11,520)]	

Therefore, ₹ 23,437.50 will be charged to the Profit and Loss Statement.

Question based on AS - 13

2014 - Nov [1] {C} (d) Blue-chip Equity Investments Ltd., wants to re-classify its investments in accordance with AS 13.

(i) Long term investments in Company A, costing ₹ 8.5 lakhs are to be re-classified as current. The company had reduced the value of these investments to ₹ 6.5 lakhs to recognize a permanent decline in value. The fair value on date of transfer is ₹ 6.8 lakhs.

(ii) Long term investments in Company B, costing ₹ 7 lakhs are to be re-classified as current. The fair value on date of transfer is ₹ 8 lakhs and book value is ₹ 7 lakhs.

(iii) Current investment in Company C, costing ₹ 10 lakhs are to be re-classified as long term as the company wants to retain them. The market value on date of transfer is ₹ 12 lakhs.

(iv) Current investment in Company D, costing ₹ 15 lakhs are to be re-classified as long term. The market value on date of transfer is ₹ 14 lakhs. (5 marks)

Answer :

(i) **As per provisions of AS-13, 'Accounting for investments' whenever** there is re-classification of investment, as long term investments are re-classified as current investments then transfer are made at lower of cost and carrying amount at the date of transfer.

⇒ Here, cost of investment is ₹ 8.5 lakhs and carrying value as on date of transfer is ₹ 6.5 lakhs. Then, investment is valued at ₹ 6.5 lakhs on re-classification.

(ii) As, on re-classification from long term investment to current investment than it is recognised lower of cost and carrying value on transfer date.

⇒ Here, long term investment in Company B to be re-classified as current cost of investment is ₹ 7 lakhs and carrying value is ₹ 7 lakhs. Then investment is re-classified as ₹ 7 lakhs which is lower of cost and fair value.

(iii) As per AS-13, when there is re-classification of investment from current to long term investments then valuation is to be done lower of cost and fair value at the date of transfer.

⇒ Here, investment in Company C shall be re-classified as long term. The cost of investment is ₹ 10 and fair value on transfer date is ₹ 12 lakhs. Then investment is valued at ₹ 10 lakhs which is lower of cost and fair value.

(iv) As per AS-13, when there is re-classification of investment from current to long term investments then valuation is to be done on lower of cost and fair value at the date of transfer.

⇒ Here investment in Company D shall be re-classified as long term. The cost of investment is ₹ 15 lakhs and fair value on transfer date is ₹ 14 lakhs. Then investment is valued of ₹ 14 lakhs which is lower of cost and fair value.

Note: This question states that Blue Chip Equity Investment Ltd. wants to reclassify its investments in accordance with AS 13. The values, at which the investments have to be reclassified, have been given in the above answer.

Question based on AS - 10

2014 - Nov [7] Answer the following:

(a) From the following information state the amount to be capitalized as per AS 10. Give the explanations for your answers.
₹ 5 lakhs as routine repairs and ₹ 1 lakh on partial replacement of a part of a machine.
₹ 10 lakhs on replacement of part of a machinery which will improve the efficiency of a machine. (4 marks)

Answer :

As per AS 10 "Accounting for Fixed Assets", only those expenditures that increase the future benefits from the existing assets, beyond its previously assessed standard of performance, are to be included in the gross book value.

Hence, in the given case, amount of ₹ 5 lakhs spent on routine repairs and ₹ 1 lakh on partial replacement of a part of the machinery should be charged to Profit and Loss Account as these amounts will help in maintaining the capacity but will not improve the efficiency of the machine.

However, ₹ 10 lakhs incurred on replacement of a part of the machinery, which will increase the efficiency of a machine, should be capitalized by inclusion in the gross book value of machinery.

Question based on AS - 7

2015 - May [1] {C} (b) 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	2093	6168*	8100**
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 Statement of Profit and Loss as per AS-7 (revised). (5 marks)

Answer :

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

(Amount in ₹ lakhs)

	Upto the reporting date	**Recognized in prior 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 consider 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	8,200
		(6,168-100)	(8,100+100)
Degree of completion (B/A)	26%	74%	100%

Question based on AS - 2

2015 - May [1] {C} (c) Mr. Mehul gives the following information relating to items forming part of inventory as on 31-3-2015. His factory produces Product X using Raw material A.

(i) 600 units of Raw material A (purchased @ ₹ 120). Replacement cost of raw material A as on 31-3-2015 is ₹ 90 per unit.

(ii) 500 units of partly finished goods in the process of producing X and cost incurred till date ₹ 260 per unit. These units can be finished next year by incurring additional cost of ₹ 60 per unit.

(iii) 1500 units of finished Product X and total cost incurred ₹ 320 per unit.

Expected selling price of Product X is ₹ 300 per unit.

Determine how each item of inventory will be valued as on 31-3-2015.

Also calculate the value of total inventory as on 31-3-2015. (5 marks)

Answer:

(i) **Valuation of Raw Material:** If finished product is expected to be sold below cost then raw material should be valued at NRV if there is decline in price of material. In such circumstances, the replacement cost of materials may be best available measure of their net realizable value.

Here product x is expected to be sold at ₹ 300 per unit which is below than total cost per unit which is ₹ 320. Then raw material is to be valued at replacement cost.

So, valuation of raw material is done as follows:

No. of units × Replacement Cost/unit = 600 × 90 = ₹ 54,000

Raw material is to be valued at ₹ 54,000

(ii) **Valuation of WIP :** 500 units of partly finished goods will be valued at ₹ 240 per unit i.e. lower of cost ₹ 320 (₹ 260 + additional cost ₹ 60) or Net estimated selling price ₹ 240 (Estimated selling price ₹ 300 per unit less additional cost of ₹ 60).

(iii) **Cost of Finished Goods:** As per AS-2, inventory is to be valued at cost or realizable value which ever is lower. Here the cost of finished good is ₹ 320 per unit and finished good is expected to be sold at ₹ 300 which is less than the cost of finished goods. So, finished good is valued at expected selling price, as calculated follows:

1500 units × ₹ 300 per unit = ₹ **4,50,000**

So, finished good is valued at ₹ 4,50,000 to the year end.

- **Valuation of total inventory as on 31.3.2015**

	Particulars	Amount (₹)
(i)	Valuation of raw material	54,000
(ii)	Valuation of partly finished goods	1,20,000
(iii)	Valuation of finished goods	4,50,000
	Total valuation of inventory as on 31.3.2015	6,24,000

Question based on AS - 6

2015 - May [1] {C} (d) M/s. Laghu Udyog Limited has been charging depreciation on an item of Plant and Machinery on straight line basis. The machine was purchased on 1-4-2012 at ₹ 3,25,000. It is expected to have a total useful life of 5 years from the date of purchase and residual value of ₹ 25,000. Calculate the book value of the machine as on 1-4-2014 and the total depreciation charged till 31-3-2014 under SLM. The company wants to change the method of depreciation and charge depreciation @ 20% on WDV from 2014-15.

Is it valid to change the method of depreciation? Explain the treatment required to be done in the books of accounts in the context of AS-6.

Ascertain the amount of depreciation to be charged for 2014-15 and the net book value of the machine as on 31-3-2015 after giving effect of the above change. (5 marks)

Answer:

Book Value of Machine and Depreciation under SLM as on 01-04-2014

Cost of Machine purchased on 01.04.2012	₹ 3,25,000
Less: Residual Value	₹ 25,000
Depreciable amount	₹ 3,00,000
Useful life of Machine	5 Years
Depreciation for 2 Years (3,00,000 x 2/5)	₹ 1,20,000
Book value as on 01.04.2014	₹ 2,05,000

As per AS 6 "Depreciation Accounting", a change from one method of providing depreciation to another should be made only if the adoption of the new method is required by statute or for compliance with an accounting standard or if it is considered that the change would result in a more appropriate preparation or presentation of the financial statements of the enterprise.

When a change in the method of depreciation is made, depreciation should be recalculated in accordance with the new method from the date of the asset coming into use.

The deficiency or surplus arising from retrospective recomputation of depreciation in accordance with the new method should be adjusted in the accounts in the year in which the method of depreciation is changed. In case the change in the method results in deficiency in depreciation in respect of past years, the deficiency should be charged in the statement of profit and loss. In case the change in the method results in surplus, the surplus should be credited to the statement of profit and loss.

Such a change should be treated as change in accounting policy and its effect should be quantified and disclosed.

In the given case, the company cannot change the method of depreciation from year 2014-15 without making re-computations for the previous year's also according to new method.

Depreciation for 2014-15 and net book value of Machine as on 31.3.15 after effect of the change	₹

Purchase value of Machinery as on 01.04.2012	3,25,000
Depreciation for 2 years under WDV @ 20% (₹ 65,000 + ₹ 52,000)	1,17,000
Book value as on 01.04.2014 under WDV (i)	2,08,000
Book value as on 01.04.2014 under SLM (ii)	2,05,000
Excess depreciation credited to Statement of Profit & Loss (i-ii)	3,000
Current year depreciation as per new method (WDV) (2,08,000 X 20%)	41,600
Net Book value as on 31.03.2015 (2,08,000 – 41,600)	1,66,400

Question based on AS - 9

2015 - May [7] Answer the following:

(c) Given the following information of M/s. Paper Products Ltd.

(i) Goods of ₹ 60,000 were sold on 20-3-2015 but at the request of the buyer these were delivered on 10-4-2015.

(ii) On 15-1-2015 goods of ₹ 1,50,000 were sent on consignment basis of which 20% of the goods unsold are lying with the consignee as on 31-3-2015.

(iii) ₹ 1,20,000 worth of goods were sold on approval basis on 1-12-2014. The period of approval was 3 months after which they were considered sold. Buyer sent approval for 75% goods up to 31-1-2015 and no approval or disapproval received for the remaining goods till 31-3-2015.

(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 M/s. Paper Products Ltd., with valid reasons, the amount to be recognized as revenue in above cases in the context of AS-9 and also determine the total revenue to be recognized for the year ending 31-3-2015. (4 marks)

Answer :

(i) 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:

(a) 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

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

In this transaction, the buyer sold goods of ₹ 60,000 on 20-3-2015 but at the request of the buyer these were delivered on 10-4-2015. As per AS-9, goods sold by company the right becomes to revenue recognised whether, the actual physical delivery of goods taken place or not. So here ₹ 60,000 of revenue is to be recognised as Sales in Trading A/c.

(ii) As per AS-9, if the goods are sent on consignment basis and if the agent sells them to third party then only the revenue is recognised by consignor.

→ So here, goods of ₹ 1,50,000 sent on consignment and only 80% goods were sold. Thus, sales recorded will be only ₹ 1,20,000 in Trading A/c as per AS-9.

(iii) As per AS-9, revenue should be recognised on sale on approval basis as follows:

→ Revenue shall be recognised if the buyer formally accepted the goods.

→ Revenue shall also be recognised if the period of rejection has elapsed or where no time has been fixed or a reasonable time has elapsed.

→ Here, total goods worth ₹ 1,20,000 are sold to customers on 1-12-2014, on approval period of 3 months. Buyer sent approval for 75% goods up to 31-1-2015 and no approval or disapproval received for the remaining goods till 31-3-2015. As the approval time is elapsed on 31-3-2015, so all the goods sold on' 1-12-2014 is to be considered as sales.

→ So, ₹ 1,20,000 to be shown in Trading P&L A/c as sales as on

31-3-2015.

(iv) Apart, from above the company has made cash sales of ₹ 7,80,000 (gross). Trade discount of 5% allowed on cash sales, so sale is to be recorded as 7,80,000 – 39,000 = ₹ 7,41,000.

* **Calculation for total revenue to be recognised for the year ending 31-3-2015**

Particulars	**Amount** (₹)
(i) Sale as on 20-3-2015	60,000
(ii) Sale on consignment basis on 15-2-2015	1,20,000
(iii) Sale on approval basis on 1-12-2014	1,20,000
(iv) Sale (Cash) after discount	7,41,000
Total revenue recognized	10,41,000

Question based on AS - 10

2015 - May [7] Answer the following:

(e) M/s. Versatile Limited purchased machinery for ₹ 4,80,000 (inclusive of excise duty of ₹ 40,000). CENVAT credit is available for 50% of the duty paid. The company incurred the following other expenses for installation.

	₹
Cost of preparation of site for installation	21,000
Total labour charges	66,000
(200 out of the total of 600 men hours worked, were spent for installation of the machinery)	
Spare parts and tools consumed in installation	6,000
Total salary of supervisor	24,000
(time spent for installation was 25% of the total time worked)	
Total administrative expenses	32,000
(1/10 relates to the plant installation)	

Test run and experimental production expenses	23,000
Consultancy charges to architect for plant set up	9,000
Depreciation on assets used for the installation	12,000

The machine was ready for use on 15-1-2015 but was used from 1-2-2015. Due to this delay further expenses of ₹ 19,000 were incurred. Calculate the value at which the plant should be capitalized in the books of M/s. Versatile Limited. (4 marks)

Answer:

Calculation of value of Plant & Machinery capitalized in the books of M/s. Versatile Ltd. as on date:

	Particulars	Amount (₹)
	Purchase Price	4,80,000
(–)	Excise duty @ 50% not recoverable	(20,000)
(+)	Cost of preparation of site for installation	21,000
(+)	Labour charges (Only 200 hours work to be considered)	22,000
(+)	Spare parts & tools consumed	6,000
(+)	Salary of Supervisor (25% of total salary)	6,000
(+)	Admin Expenses (1/10)	3,200
(+)	Test run & experimental pro. Exp.	23,000
(+)	Consultancy charges	9,000
	Depreciation of asset (only from put to use)	–
(+)	Delay Expenses	12,000
	Value capitalized in books	5,62,200

Question based on AS - 9

2015 - Nov [1] {C} (a) M/s Umang 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 @ 12% p.a. from the agent. The company has not realized interest from the agent in the past. For the year ended 31st March, 2015 interest due from agent (because of delay in payment) amounts to ₹ 1,72,000. The accountant of M/s Umang Ltd. booked ₹ 1,72,000 as interest income in the year ended 31st March, 2015. Discuss the contention of the accountant with reference to Accounting Standard-9. (5 marks)

Answer:

As per AS-9 "Revenue Recognition", where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of rising any claim, the revenue recognition is postponed to the extent of uncertainty.

In such cases, the revenue is recognised only when it is reasonably certain that the ultimate collection will be made.

So in this case M/s Umang Ltd. never realised interest for the delayed payments made by the agents. Hence, it has to recognize the interest only if the ultimate collection is certain. The interest income of ₹ 1,72,000 is not be recognised in the year ended 31st March, 2015.

So the contention of the accountant is wrong. It should not recognize it as interest income in the books of account for year ended 31st March, 2015.

Question based on AS - 1

2015 - Nov [1] {C} (b) In the books of M/s Prashant Ltd., closing inventory as on 31.03.2015 amounts to ₹ 1,63,000 (on the basis of FIFO method).

The company decides to change from FIFO method to weighted average method for ascertaining the cost of inventory from the year 2014-15. On the basis of weighted average method, closing inventory as on 31.03.2015 amounts to ₹ 1,47,000. Realisable value of the inventory as on 31.03.2015 amounts to ₹ 1,95,000.

Discuss disclosure requirement of change in accounting policy as per AS-1. (5 marks)

Answer:

As per AS-1 Disclosure of Accounting Policies, accounting policies refers to the accounting principles and method of applying those principles in the preparation and presentation of financial statements.

So if there is change in the accounting policies the firm should disclose in it's statements:

1. The fact that there is change in accounting policy.
2. The reason for change in accounting policies.
3. The effect of such change in the financial statements.

So in this case M/s. Prashant Ltd. changes valuation of inventory from FIFO to weighted average. Therefore, the firm should disclose in it's financial statement:

1. **There is a change in valuation of inventory** from FIFO to weighted average.
2. **The reason why such change is to be made:** The company values its inventory at lower of cost and net realisable value. Since net realisable value of all items of inventory in the current year was greater than respective costs, the company valued its inventory at cost. In the present year i.e. 2014-15, the company has changed to weighted average method, which better reflects the consumption pattern of inventory, for ascertaining inventory costs from the earlier practice of using FIFO for the purpose.
3. **The effect of such change in the financial statement:** The change in policy has reduced current profit and value of inventory by ₹ 16,000.

Question based on AS - 6

2015 - Nov [1] {C} (c) A machinery with a useful life of 6 years was purchased on 1st April, 2012 for ₹ 1,50,000. Depreciation was provided on straight line method for first three years considering a residual value of 10% of cost.

In the beginning of fourth year the company reassessed the remaining useful life of the machinery at 4 years and residual value was estimated at 5% of original cost.

The accountant recalculated the revised depreciation historically and charged the difference to profit and loss account. You are required to comment on the treatment by accountant and calculate the depreciation to be charged for the fourth year. (5 marks)

Answer:

As per para 18 of AS 6 “Depreciation Accounting”, if the depreciable assets are revalued, the provision for depreciation should be based on the revalued amount and on the estimate of the remaining useful lives of such assets. In case the revaluation has a material effect on the amount of depreciation, the same should be disclosed separately in the year in which revaluation is carried out.

As per the standard, when there is a revision of the estimated useful life of an asset, the unamortized depreciable amount should be charged over the revised remaining useful life. Accordingly revised depreciation shall be calculated prospectively. Thus, the treatment done by the accountant regarding recalculating the revised depreciation historically i.e. retrospectively is incorrect.

Calculation of Depreciation

Depreciation per year charged for first three years	= ₹ 1,35,000 /6 = ₹ 22,500
WDV of the machine at the beginning of the fourth year	= ₹ 1,50,000 – (₹ 22,500 × 3)
	= ₹ 82,500
Depreciable amount after reassessment of residual vale	= ₹ 82,500 - 7,500
	= ₹ 75,000
Remaining useful life as per revised estimate	= 4 years
Depreciation from the fourth year onwards	= ₹ 75,000/4
	= ₹ 18,750

Question based on AS- 10 & 26

2015 - Nov [1] {C} (d) Briefly explain the treatment of following items as per relevant accounting standards:

– The accountant of Star Limited valued the Goodwill of the company at ₹ 50 lakhs and showed the same as Fixed Asset in Balance Sheet. The corresponding credit was given to Reserves.

– An expense of ₹ 5 crores was incurred on a Machine towards its Repairs and Maintenance. The accountant wants to capitalize the same considering the significance of amount spent.

– A plant was ready for commercial production on 01.04.2014 but could commence actual production only on 01.06.2014. The company incurred ₹ 50 lakhs as administrative expenditure during the period of which 20% was allocable to the plant. The accountant added ₹ 10 lakhs to cost of plant. (5 marks)

Answer:

1. The goodwill is an internally generated asset of the company. So as per AS-26, Valuation of Goodwill, the internally generated goodwill should not be recognised in the books of accounts of the company, but if the goodwill is generated in merger or amalgamation then it shall be recognised at the value determined and credit shall be given to the reserves. So here if there is internally generated goodwill then it shall not be recognised but if it is generated by way of amalgamation then it should be recognised and credit shall be given to the reserves.
2. The repairs and maintenance done on machine is to be treated as revenue expense and charged to P&L A/c if such repair is done to maintain general capacity of the machine. If such repair is to be done to increase the efficiency or capacity of the machine that was previously quoted in the machine then such repair should be capitalised and added to the cost of machine. Here, the accountant wants to capitalize the cost considering the significance of amount spent i.e. 5 crores. So here the perception of accountant is wrong. The repair and maintenance are recognised as per the benefit or capacity of machine not on the basis of the significance of the amount spent.
3. As per AS - 10, any expenses incurred by the organisation till the commercial actual production should be capitalised. So any expenses incurred on plant till it's actual production started should be capitalised and should be added to the cost of plant. So here the allocable administration expenses till the trial run period should be added to the cost of plant. So that ₹ 10 lakh is added to the cost of plant. So it is the correct treatment of accounting.

2016 - May [1] {C} (a) Uday Constructions undertake to construct a bridge for the Government of Uttar Pradesh. The construction commenced during the financial year ending 31.03.2016 and is likely to be completed by the next

financial year. The contract is for a fixed price of ₹ 12 crores with an escalation clause. The costs to complete the whole contract are estimated at ₹ 9.50 crores of rupees. You are given the following information for the year ended 31.03.2016:
Cost incurred upto 31.03.2016 ₹ 4 crores
Cost estimated to complete the contract ₹ 6 crores
Escalation in cost by 5% and accordingly the contract price is increased by 5%.
You are required to ascertain the state of completion and state the revenue and profit to be recognized for the year as per AS-7. (5 marks)

(b) M/s Active Builders Ltd. invested in the shares of another company on 31st October, 2015 at a cost of ₹ 4,50,000. It also earlier purchased Gold of ₹ 5,00,000 and Silver of ₹ 2,25,000 on 31st March, 2013. Market values as on 31st March, 2016 of the above investments are as follows:
Shares ₹ 3,75,000; Gold ₹ 7,50,000 and Silver ₹ 4,35,000
How will the above investments be shown in the books of account of M/s Active Builders Ltd. for the year ending 31st March, 2016 as per the provision of AS-13? (5 marks)

(c) Argon Ltd. purchased a shop on 1st January, 2001 at a cost of ₹ 8,50,000. The useful life of the shop is estimated as 30 years with residual value of ₹ 25,000 and depreciation is provided on a straight line basis. The shop was revalued on 30th June, 2015 for ₹ 19,50,000 and the revaluation was incorporated in the accounts.
Calculate:
(i) The surplus on revaluation;
(ii) Depreciation to be charged in the Profit and Loss account for the year ended on 31st December, 2015. (5 marks)

(d) Z Limited ordered 13,000 kg. of chemicals at ₹ 90 per kg. The purchase price includes excise duty of ₹ 5 per kg. in respect of which full CENVAT credit is admissible. Further, State VAT is leviable at ₹ 2.5 per kg. on purchase price. Freight incurred amounted to ₹ 30,000. Normal transit loss is 4%. The company actually received 12,400 kg. and consumed 10,000 kg. The company has received trade discount in the form of cash

amounting to ₹ 1 per kg. The chemicals were delivered in containers. The containers were not reusable, hence sold for ₹ 500. The administrative expenses incurred to bring the chemicals were ₹ 10,000. Compute the value of inventory and allocate the material cost as per AS-2.
(5 marks)

2016 - May [7] Answer the followings:

(a) Anjana Ltd., is absorbed by Sanjana 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% in 8% debentures issued at a premium of 25% at face value and the payment of ₹ 15 per share in cash and allotment of three 11% preference share of ₹ 10 each at a discount of 10% and four equity share of ₹ 10 each at a premium of 20% fully paid for every five shares in Anjana Ltd. The number of share of the vendor company are 1,50,000 of ₹ 10 each fully paid.
Calculate purchase consideration as per Accounting Standard– 14.
(4 marks)

(d) Classify the following activities as per AS-3 Cash Flow Statement:
(i) Interest paid by financial enterprise
(ii) Dividend paid
(iii) Tax deducted at source on interest received from subsidiary company
(iv) Deposit with Bank for a term of two years
(v) Insurance claim received towards loss of machinery by fire
(vi) Bad debts written off

Which activity does the purchase of business falls under and whether netting off of aggregate cash flows from disposal and acquisition of business units is possible? (4 marks)

KZ - 8 **Knowledge Zone**

Accounting of Revaluation of Assets:– An enterprise may revalue any particular class of fixed assets. Such revaluation is made by making appraisal by competent valuers.

The revalued amounts of fixed assets are presented in financial statements, either by restating both the gross book value and accumulated depreciation so that net book value equal to net revalued amount or by restating the net book value by adding therein the net increase on account of revaluation.

Profit on revaluation of fixed assets is credited to Revaluation Reserve Account and Loss on revaluation is charged to Profit and Loss A/c. If increase in the book value of asset is the reversal of previously recorded decrease, which was charged to P&L A/c, such increase to the extent of previous decrease should be credited to Profit and Loss A/c. If decrease in book value of asset is related to previous increase, such decrease, to the extent of previous increase, will be adjusted against Revaluation Reserve.

- Enhancing the understandability with the following examples:

1. **First time Revaluation of Assets:-**
   - If surplus arises → Surplus should be credited to Revaluation Reserve A/c

     OR

   - If Deficiency arises → Deficiency should be debited to Profit & Loss A/c

   Examples:

   If the Book value of an asset as on 1.4.2014 ₹ 1,00,000 and revalued as on 31.3.2015

   Case I : ₹ 1,20,000 Case II : ₹ 80,000

Case I	Asset A/c Dr. To Revaluation Reserve A/c (Being whole of the surplus transferred to revaluation reserve A/c)	20,000	 20,000
Case II	Profit & Loss A/c Dr. To Asset A/c (Being whole of the deficiency t/f to P&L A/c)	20,000	 20,000

2. **Subsequent Revaluation:**
   i. **Surplus** to the extent of decrease arising on revaluation previously charged to P&L A/c should be credited to P&L A/c and remaining surplus should be credited to Revaluation Reserve A/c.
   ii. **Deficiency** to the extent of increase arising on revaluation previously credited to Revaluation Reserve should be reversed or utilised and remaining deficiency should be charged to P&L A/c.

   Example:

   How should you treat the effect of revaluation which is previously revalued.

	Previously Revalued	Present Revaluation
Case 1	₹ 1,00,000 to ₹ 1,20,000	₹ 1,20,000 to ₹ 1,40,000
Case 2	₹ 1,00,000 to ₹ 1,20,000	₹ 1,20,000 to ₹ 90,000
Case 3	₹ 1,00,000 to ₹ 90,000	₹ 90,000 to ₹ 80,000
Case 4	₹ 1,00,000 to ₹ 90,000	₹ 90,000 to ₹ 1,20,000

Case 1	Asset A/c Dr.	20,000	
	To Revaluation Reserve A/c		20,000
	(Being surplus (₹ 1,40,000 - ₹ 1,20,000) arising on revaluation t/f to Revaluation Reserve A/c).		
Case 2	Revaluation Reserve A/c Dr.	20,000	
	P&L A/c Dr.	10,000	
	To Assets A/c		30,000
	(Being deficiency to the extent of increase arising on revaluation previously credited to Revaluation Reserve utilised and remaining deficiency charged to P&L A/c)		
Case 3	P&L A/c Dr.	10,000	
	To Asset A/c		10,000
	(Being the deficiency i.e. (₹ 90,000 - ₹ 80,000) arising on revaluation t/f to P&L A/c)		

Case 4	**Alternative 1** Asset A/c Dr. To Revaluation Reserve A/c (Being whole of the surplus i.e. (₹ 1,20,000 - ₹ 90,000) t/f to Revaluation Reserve A/c	30,000	 30,000
	Alternative 2 Asset A/c Dr. To P&L A/c To Revaluation Reserve A/c (Being surplus to the extent of decrease arising on revaluation previously charged to P&L A/c credited to P&L A/c and remaining surplus credited to Revaluation Reserve A/c).	 30,000	 10,000 20,000

Table Showing Marks of Compulsory Questions

Year	11 N	12 M	12 N	13 M	13 N	14 M	14 N	15 M	15 N	16 M
Practical	5	15			20	20	20	15	20	20
Total	5	15			20	20	20	15	20	20