FINAL – November 2017

ACCOUNTING STANDARDS

Test Code – 60

Branch (MULTIPLE) (Date : 03.09.2017)

(50 Marks)

Note: All questions are compulsory.

Question 1(8 marks)

Table showing present value of (i) Minium lease payments (MLP) and (ii)

Year	*MLP inclusive of URV*	*Internal rate of return (Discount factor 15%)*	*Present Value*	
	`		`	
1	5,00,000	0.8696	4,34,800	
2	5,00,000	0.7561	3,78,050	
3	5,00,000	0.6575	3,28,750	
4	5,00,000	0.5718	2,85,900	
5	5,00,000	0.4972	2,48,600	
	1,00,000 (guaranteed residual value)	0.4972	49,720	
			17,25,820	(i)
	1,00,000 (unguaranteed residual value)	0.4972	49,720	(ii)
		(i) + (ii)	17,75,540	(b)

Un earned finance income=(a)-(b)

= 27,00,000-17,75,540

=9,24,460/- **(3 marks)**

Journal Entries in the books of Indigo Ltd.

	`	`
*At the inception of lease**(1 mark)***		
Machinery account	Dr. 17,25,820	
To A Ltd.'s account		17,25,820*
(Being lease of machinery recorded at present value of MLP)		
*At the end of the first year of lease **(4 marks)***		
Finance charges account (Refer Working Note)	Dr. 2,58,873	

To A Ltd.'s account (Being the finance charges for first year due)		2,58,873
A Ltd.'s account Dr.	5,00,000	
To Bank account (Being the lease rent paid to the lessor which includes outstanding liability of ` 2,41,127 and finance charge of ` 2,58,873)		5,00,000
Depreciation account Dr.	1,72,582	
To Machinery account (Being the depreciation provided @ 10% p.a. on straight line method)		1,72,582
Profit and loss account Dr.	4,31,455	
To Depreciation account		1,72,582
To Finance charges account (Being the depreciation and finance charges transferred to profit and loss account)		2,58,873

Working Note:

Table showing apportionment of lease payments by B Ltd. between the finance charges and the reduction of outstanding liability.

Year	*Outstanding liability (opening balance)*	*Lease rent*	*Finance charge*	*Reduction in outstanding liability*	*Outstanding liability (closing balance)*
	`	`	`	`	`
1	17,25,820	5,00,000	2,58,873	2,41,127	14,84,693
2	14,84,693	5,00,000	2,22,704	2,77,296	12,07,397
3	12,07,397	5,00,000	1,81,110	3,18,890	8,88,507
4	8,88,507	5,00,000	1,33,276	3,66,724	5,21,783
5	5,21,783	5,00,000	78,267	5,21,783	1,00,050*
			8,74,230	17,25,820	

The difference between this figure and guaranteed residual value (1,00,000) is due to approximation in computing the interest rate implicit in the lease.

Question 2(5 Marks)

As per para 10 of AS 12 '**Accounting for Government Grants', where the government grants are of the nature of promoters' contribution,** i.e. they are given with reference to the total investment in an undertaking or by way of contribution towards its total capital outlay (for example, central investment subsidy scheme) and no repayment is ordinarily expected in respect thereof, the grants are treated as capital reserve which can be neither distributed as dividend nor considered as deferred income. **(2 marks)**

In the given case, the subsidy received is neither in relation to specific fixed asset nor in relation to revenue. Thus, **it is inappropriate to recognise government grants in the profit and loss statement, since they are not earned but represent an incentive provided by government without related costs.** The correct treatment is to credit the subsidy to capital reserve. Therefore, the accounting treatment followed by the company is not proper. **(3 marks)**

Question 3 (5 Marks)

(i) Impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount. **(2 marks)**

Thus, Impairment loss = Carried amount – Recoverable amount*

= ` 500 lakhs – ` 400 lakhs = ` 100 lakhs

*Recoverable amount is higher of asset's net selling price ` 375 lakhs and its value in use 400 lakhs.

ii) Balance sheet of Veenu Ltd as on 31.03.2016 (Rs. In Lakhs)**(1 mark)**

Amt less depreciation	500
Less: Impairment loss	(100)
	$\boxed{400}$

(iii) **Journal Entries (2 marks)**

	Particulars		*Dr. Amount ` in lakhs*	*Cr. Amount ` in lakhs*
(i)	Impairment loss account	Dr.	100	
	To Asset account			100
	(Being the entry for accounting impairment loss)			
(ii)	Profit and loss account	Dr.	100	
	To Impairment loss account			100
	(Being the entry to transfer impairment loss to profit and loss account)			

Question 4(5 Marks)

As per para 19 of **AS 16 'Borrowing Costs', capitalization of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete. (2 ½ marks)**

Therefore, interest on the amount that has been used for the construction of the building upto the date of completion (January, 2005) i.e. **18 lakhs alone can be capitalized. It cannot be extended to ` 25 lakhs.(2 ½ marks)**

Question 5(5 Marks)

As per AS 2 (Revised) on 'Valuation of Inventories', materials and other supplies held for use in the production of inventories are not written down below cost if the finished product in which they will be incorporated are expected to be sold at or above cost. However, 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 realisable value, the materials are written down to net realisable value. In such circumstances, the replacement cost of the materials may be the best available measure of their net realisable value.**(2 marks)**

Cost per kg. of finished goods can be computed as follows: **(3 marks)**

		`
Material cost		125
Direct labour cost		20
Direct variable production overhead		10
Fixed production overhead	` 10, 00, 000 / 1,00,000 kgs	10
Cost of Finished Goods per Unit		165

NRV of finished goods = ` 140/kg

Value of finished goods inventory = Cost of finished goods or NRV whichever is less

Thus, value of 2,000 kgs of finished goods held as inventory at the year -end will be

= ` 2,80,000 (2,000 kgs. x ` 140)

Since cost of finished goods exceed its NRV, raw materials will be valued at Replacement Cost.

Value of raw materials held as inventory = 15,000 kgs × ` 100 = ` 15,00,000

Question 6 (5 Marks)

As per AS 13 'Accounting for Investments', for investment in shares - if the investment is purchased with an intention to hold for short-term period then it will be shown at the realizable value of ` 2,50,000 as on 31st March, 2015. **(1 mark)**

If equity shares are acquired with an intention to hold for long term period then it will continue to be shown at cost 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 the investments.**(1 mark)**

As per 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. Hence, the investment in Gold and Silver (purchased on 1st

April, 2014) shall continue to be shown at cost as on 31st March, 2015 i.e., 3,50,000 and ` 1,50,000 respectively, though their realizable values have been increased.**(2 marks)**

However, if held as short term investment then it should be valued at lower of cost or fair value (market price) and the resultant profit or loss to be charged to the profit and loss account.**(1 mark)**

Question 7 (5 Marks)

Calculation of cost of fixed asset constructed (3 marks)

	`
Materials	7,00,000
Direct expenses	1,80,000
Direct labour	2,00,000
Office and administrative expenses (5% of ` 1,70,000)	8,500
Depreciation (10% of ` 1,90,000)	19,000
Cost of fixed asset	11,07,500

Working Note:

Calculation of direct labour allocated to fixed asset constructed (2 marks)

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Direct labour (excluding allocation to the fixed asset constructed)	18,00,000
Total direct labour	= 18,00,000 x 10/9
	= 20,00,000
Direct labour related to fixed asset constructed	20,00,000 x 1/10
	= 2,00,000

Question 8(5 marks)

(i) Amount of foreseeable loss (1 ½ mark)

	(` in lakhs)
Total cost of construction (350 + 75 + 480)	905
Less: Total contract price	(800)
Total foreseeable loss to be recognized as expense	105

According to para 35 of AS 7 (Revised 2002), when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately.

(ii) Contract work-in-progress i.e. cost incurred to date (1 ½ mark)

	(` in lakhs)
Work certified	350
Work not certified	75
	425
This is 46.96% or 47% (425/905 × 100) of total cost of construction	

Proportion of total contract value recognised as revenue

47% of ` 800 lakhs = ` 376 lakhs

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

= [425 + Nil – 105 – (380 + 120)] ` in lakhs

= [425 – 105 + 500] ` in lakhs

Amount due to customers = ` 180 lakhs. **(2 marks)**

Question 9 (7 marks)

As per AS 21 "Consolidated Financial Statements", the losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. The excess, and any further losses applicable to the minority, are adjusted against the majority interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses. If the subsidiary subsequently reports profits, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered. Accordingly, **(5 marks)**

Year	Details	Minority Interest (MI) (20%)	Minority 's Share of Losses borne by Ram Ltd.
			Balance
Minority Interest at the time of acquisition i.e on 31.3.2012		6,00,000 (W.N)	
2012-13	(15,00,000 x 20%)	(3,00,000)	
On 31.3.2013		3,00,000	
2013-14	(20,00,000 x 20%)	(4,00,000)	
		(1,00,000)	
	Loss amounting 1,00,000 Of minority borne by majority shareholders on application of As 21	1,00,000	1,00,000
On 31.3.2014		Nil	
2014-15	(4,00,000 x 20%)	(80,000)	
	On application of As21, Profit transferred to majority shareholders	(80,000)	(80,000)
On 31.3.2015		Nil	20,000
2015-16	(5,00,000 x 20%) On application of As21, Profit transferred to majority shareholders to the extent earlier loss was borne by majority share holders	1,00,000	
On 31.3.2016		80,000	Nil

Working Note :

Calculation of Minority Interest as on 31.3.2012 (2 marks)

	Total Amount (100%)(‘)	Minority Interest (20%)(‘)
Share Capital (20%) Add: Share in Reserves (20%)	25,00,000 5,00,000	5,00,000 1,00,000 6,00,000

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