INTER CA – NOVEMBER 2018

Sub: ACCOUNTING STANDARDS
Topics – AS 1,4,20,9,11,13,26,10,2,12 (GN in AS 10)
Test Code – N53
Branch: Multiple Date:

(50 Marks)

Question 1 (5 marks)

(a) According to AS 10 on Property, Plant and Equipment, the costs which will be capitalized by ABC Ltd. are as follows:

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Cost of the plant	31,25,000
Initial delivery and handling costs	1,85,000
Cost of site preparation	4,50,000
Consultants' fees	6,50,000
Estimated dismantling costs to be incurred after 5 years	2,50,000
Total cost of Plant	46,60,000

Note: Operating losses before commercial production amounting to ` 3,75,000 will not be capitalized as per AS 10. They should be written off to the Statement of Profit and Loss in the period they are incurred.

Question 2 (5 marks)

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

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

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

Case (i): 25% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ` 3,00,000 (75% of ` 4,00,000) for the year ended on 31.3.17. In case of consignment sale, revenue should not be recognized until the goods are sold to a third party.

Case (ii): The sale is complete but delivery has been postponed at buyer's request. Fashion Ltd. should recognize the entire sale of `1,95,000 for the year ended 31st March, 2017.

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

Thus total revenue amounting ` 7,45,000 (3,00,000+1,95,000+2,50,000) will be recognized for the year ended 31st March, 2017 in the books of Fashion Ltd.

Question 3 (5 marks)

According to AS 4 "Contingencies and Events Occurring after the Balance Sheet Date", assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date.

In the given case, sale of immovable property was carried out before the closure of the books of accounts. This is clearly an event occurring after the balance sheet date but agreement to sell was effected on 1st March, 2013 i.e. before the balance sheet date. Registration of the sale deed on 15th April, 2013, simply provides additional information relating to the conditions existing at the balance sheet date. Therefore, adjustment to assets for sale of land is necessary in the financial statements of Pradeep Ltd. for the year ended 31st March, 2013.

Question 4 (5 marks)

Although legal title has not been transferred, the economic reality and substance is that the rights and beneficial interest in the immovable property have been transferred. Therefore, recording of acquisition/disposal (by the transferee and transferor respectively) would, in substance, represent the purchase/sale. In view of this A Ltd., should record the sales and recognize the profit of `15 lakhs in its profit and loss account. It should eliminate building from its balance sheet. In notes to accounts, it should disclose that building has been sold, full consideration has been received, possession has been handed over to the buyer and documentation and legal formalities are pending.

The buyer should recognize the building as an asset in his balance sheet and charge depreciation on it. The buyer should disclose in his notes to account that possession has been received however documentation and legal formalities are pending.

Question 5 (5 marks)

1. As per AS 13 "Accounting for Investments", current investments should be carried at cost or fair value, whichever is lower. Here, the current Investment should be carried at fair value of ` 48 Lakhs, being the lower of ` 60 Lakhs (cost) or ` 48 Lakhs (fair value). The difference of ` 12 Lakhs should be charged to profit and loss account.
2. Current investment should be carried at cost or fair value, whichever is lower. In the given case, the current investments should be carried at cost of ` 86 Lakhs, being the lower of ` 86 Lakhs (cost) or ` 90 Lakhs (fair value).

Question 6 (5 marks)

As per para 5 of AS 2 "Valuation of Inventories", the inventories are to be valued at lower of cost or net realizable value.

In this case, the cost of inventory is ` 5 lakhs. The net realizable value is ` 4.95 lakhs (` 5.5 lakhs less cost to make the sale @ 10% of ` 5.5 lakhs). So, the closing stock should be valued at ` 4.95 lakhs.

Question 7 (5 marks)

AS 12 'Accounting for Government Grants' regards two methods of presentation, of grants related to specific fixed assets, in financial statements as acceptable alternatives. Under the first method, the grant of ` 5,00,000 can be shown as a deduction from the gross book value of the machinery in arriving at its book value. The grant is thus recognised in the profit and loss statement over the useful life of a depreciable asset by way of a reduced depreciation charge.

Under the second method, it can be treated as deferred income which should be recognised in the profit and loss statement over the useful life of 10 years in the proportions in which depreciation on machinery will be charged. The deferred income pending its apportionment to profit and loss account should be disclosed in the balance sheet with a suitable description e.g., 'Deferred government grants' to be shown after 'Reserves and Surplus' but before 'Secured Loans'.

The following should also be disclosed:

(i) the accounting policy adopted for government grants, including the methods of presentation in the financial statements;

(ii) the nature and extent of government grants recognised in the financial statement of ` 5 lakhs is required to be credited to the profit and loss statement of the current year.

Question 8 (5 marks)

As per para 41 of AS 26 'Intangible Assets', no intangible asset arising from research (or from the research phase of an internal project) should be recognized. Expenditure on research (or on the research phase of an internal project) should be recognized as an expense when it is incurred. Thus the company cannot treat the expenditure as deferred revenue expenditure. The entire amount of `33 lakhs spent on research project should be charged as an expense in the year ended31st March, 2016.

Question 9 (5 marks)

As per para 13 of AS 11 (Revised 2003) 'The Effects of Changes in Foreign Exchange Rates', exchange differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognized as income or expenses in the period in which they arise. Thus exchange differences arising on repayment of liabilities incurred for the purpose of acquiring fixed assets are recognized as income or expense.

Calculation of Exchange Difference:

Foreign currency loan = ` 3,000 lakhs / ` 40 = 75 lakhs US Dollars

Exchange difference = 75 lakhs US Dollars × (42.50 – 40.00) = `187.50 lakhs (including exchange loss on payment of first instalment)

Therefore, entire loss due to exchange differences amounting ` 187.50 lakhs should be charged to profit and loss account for the year.

Note: The above answer has been given on the basis that the company has not exercised the option of capitalization available under para 46 of AS 11. The answer will change if the company exercises the option of capitalization.

Question 10 (5 marks)

Assuming that partly paid shares are entitled to participate in the dividend to the extent of amount paid, number of partly paid equity shares would be taken as 300 for the purpose of calculation of earnings per share.

Computation of weighted average would be as follows:

(1,800 x 12/12) + (300 x 2/12) = 1,850 shares.

In case of a bonus issue or a share split, equity shares are issued to existing shareholders for no additional consideration. Therefore, the number of equity shares outstanding is increased without an increase in resources. The number of equity shares outstanding before the event is adjusted for the proportionate change in the number of equity shares outstanding as if the event had occurred at the beginning of the earliest period reported.

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