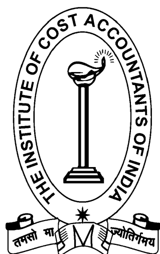
SYLLABUS - 2016

FINAL : PAPER - 17

CORPORATE FINANCIAL REPORTING

FINAL

STUDY NOTES



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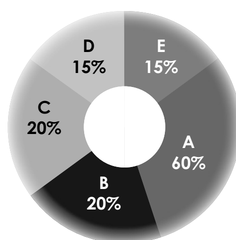
Syllabus- 2016

Syllabus Structure

The syllabus comprises the following topics and study weightage:

A	GAAP and Accounting Standards	30%
B	Accounting of Business Combinations & Restructuring	20%
C	Consolidated Financial Statements	20%
D	Developments in Financial Reporting	15%
E	Government Accounting in India	15%



ASSESSMENT STRATEGY

There will be written examination paper of three hours.

OBJECTIVES

To understand the recognition, measurement, disclosure and analysis of information in an entity's financial statements to cater the needs of the stakeholders

Learning Aims

The syllabus aims to test the student's ability to:

- Demonstrate the financial statements for understanding of stakeholders
- Analyze the impact of GAAP and its application for reporting and compliance
- Evaluate financial statements for strategic decision-making
- Interpret and apply the ongoing developments for financial reporting

Skill set required

Level C: Requiring skill levels of knowledge, comprehension, application, analysis, synthesis and evaluation.

Section A : GAAP and Accounting Standards	**30%**
1. Accounting Standards	
Section B : Accounting of Business Combinations & Restructuring	**20%**
2. Accounting of Business Combinations & Restructuring	
Section C : Consolidated Financial Statements	**20%**
3. Group Financial Statements	
Section D : Developments in Financial Reporting	**15%**
4. Recent Trends in Financial Reporting	
5. Valuation, Accounting and Reporting of Financial Instruments and others	
6. Share based payments	
7. Reporting through XBRL (Extended Business Reporting Language)	
Section E : Government Accounting in India	**15%**
8. Government Accounting Procedure and Standards	

SECTION A: GAAP AND ACCOUNTING STANDARDS [30 MARKS]

1. Accounting Standards

(a) Generally Accepted Accounting Principles in India

(b) Accounting Standards (AS) – Applicability, Interpretation, Scope and Compliance

(c) International Financial Reporting Standards

(d) Over View of Ind AS

(e) Relative view of AS VS Ind AS VS IFRS

SECTION B: ACCOUNTING OF BUSINESS COMBINATIONS & RESTRUCTURING [20 MARKS]

2. Accounting of Business Combinations & Restructuring (as per Ind AS)

(a) Relevant Terms, Types of merger, methods of accounting, treatment of Goodwill arising on merger, Purchase consideration and settlement

(b) Accounting in books of vendor/ transferor and transferee

(c) Accounting for investment in subsidiary

(d) Accounting for Mergers / Acquisitions (including chain holdings, cross holdings, multiple holdings)

(e) Corporate Financial restructuring, Reconstruction Schemes, De-merger, Reverse merger

(g) Notes to Accounts & related disclosures under amalgamation

SECTION C: CONSOLIDATED FINANCIAL STATEMENTS [20 MARKS]

3. Group Financial Statements

(a) Concept of a group, Purposes of consolidated financial statements, Consolidation procedures, Minority interest, Goodwill, Treatment Pre-acquisition profit and Postacquisition profit and concept of Fair value at the time of acquisition.

(b) Consolidation with two or more subsidiaries, consolidation with foreign subsidiary.

(c) Consolidated Income Statement, balance Sheet and Cash Flow Statements for Group of companies.

(d) Impact on group financial statements at the point of acquisition

(e) Treatment of investment in associates in consolidated financial statements. Compare and contrast acquisition and equity methods of accounting

(f) Treatment of investment in joint ventures in consolidated financial statements

SECTION D: DEVELOPMENTS IN FINANCIAL REPORTING AND OTHER ITEM OF REPORTING [15 MARKS]

4. Recent trends in Financial Reporting

Concept of Triple Bottom Line Reporting

5. Valuation, Accounting and Reporting of Financial Instruments and others

(a) Recognition & Valuation Financial Instruments

(b) CENVAT / VAT Accounting

(c) NBFC – Provisioning Norms and Accounting

(d) Valuation of Shares

(e) Valuation of Goodwill

6. Share Based payments

(a) Meaning, Equity settled transactions, Transaction with employees and non-employees

(b) Vesting conditions, Determination of Fair value of Options, Determination of ESOP Provision and Related Disclosure and settlement of ESOP

7. Reporting Through XBRL (Extended Business Reporting Languate)

SECTION E: GOVERNMENT ACCOUNTING IN INDIA [15 MARKS]

8. Government Accounting

(a) General Principles and comparison with commercial accounting

(b) Role of Comptroller and Auditor General of India

(c) Role of Public Accounts Committee, Review of Accounts

(d) Government Accounting Standards issued by Government Accounting Standards Advisory Board (GASAB)

(e) Government Accounting and Reporting

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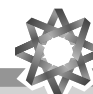
Study Note - 1

ACCOUNTING STANDARDS



This Study Note includes

1.1 Generally Accepted Accounting Principles in India

1.2 Accounting Standards (AS) – Applicability, Interpretation, Scope and Compliance

1.3 International Financial Reporting Standards

1.4 Over View of Ind AS

1.5 Relative view of AS vs. Ind AS vs. IFRS

1.1 GENERALLY ACCEPTED ACCOUNTING PRINCIPLES IN INDIA

INTRODUCTION

Accounting is the language of business. The primary function of the discipline of accounting is to provide financial information to the users of the financial statements. For this purpose, it is required to record the transactions entered into by a concern during an accounting period in different books of accounts. However, different organisations may practice it in different ways. Thus, to ensure uniformity among different entities and to ensure consistency over a period of time, a framework has been developed over the time period. This framework is referred to as 'Generally Accepted Accounting Principles' (GAAP).

Indian GAAP is nothing but a set of accounting standards that every company operating in India has to follow when reporting its financial results. Generally Acceptable Accounting Standards differ for each country as they incorporate policies and procedures that have to be followed for financial disclosures as per the standards set in each country.

Institute of Chartered Accountants of India (ICAI), Ministry of Corporate Affairs (MCA) are the bodies in India that have set the Accounting standards(Indian Accounting Standards) that need to be followed while financial reporting, So Indian Accounting Standards are termed as Indian GAAP.

MEANING OF ACCOUNTING

Accounting may be defined as the process of recording, classifying, summarising, analysing and interpreting financial transactions and communicating the results thereof to the users interested in such communication. In other words, accounting can be defined as an information system that provides information to users about the economic activities and condition of an entity for the purpose of decision-making.

From the above definition, the following attributes of accounting can be observed:

- **Identification** of monetary transactions and events.
- **Measurement** of the identified transactions and events.
- **Recording** of such transactions.
- **Classifying** and **summarising** of the recorded transactions.
- Obtaining the results of operations.
- **Analysing** and **interpreting** the results to help in decision-making.
- **Communicating** such information to the users (both, internal and external).

Primarily the focus of Accounting is limited upto to the preparation of financial statement, later on the communicating function was incorporated in the definition of accounting. It is a service activity to provide qualitative financial information and it is useful in making economic decision.

MEANING OF GAAP

Generally Accepted Accounting Principles (GAAP) refers to accounting policies and procedures that are widely used in practice. It incorporates the body of principles that governs the accounting for financial transactions underlying the preparation of a set of financial statements.

GAAP are the common set of accounting principles, standards and procedures that are used by accountants to prepare the financial statements. They are derived from practice, and on being useful get accepted into the accounting system. These principles are developed by the professional accounting bodies of different countries of the world, with the aim of attaining uniformity in accounting practiced by the entities of the respective countries. As such different GAAP have developed in different countries of the world.

GAAP includes principles on:

- **Recognition:** It deals with the items should be recognized in the financial statements (e.g. assets, liabilities, revenues, and expenses).
- **Measurement:** It determines the amounts should be reported for each of the elements included in financial statements.
- **Presentation:** It states regarding the line items, subtotals and totals should be displayed in the financial statements and how might items be aggregated within the financial statements.
- **Disclosure:** It states about the specific information that is most important to the users of the financial statements.

ACCOUNTING PRINCIPLES

Accounting Principle is the 'grammar' of accounting language. It refers to those **rules of action** which are universally adopted by the accountants for recording accounting transactions. They act as the guidelines for recording and reporting transactions. These have evolved out of assumptions made and conventions followed in accounting. These provide explanations to the current accounting practices.

Accounting Principles can be classified into two categories:

(a) Accounting Concepts; and

(b) Accounting Conventions.

ACCOUNTING CONCEPTS

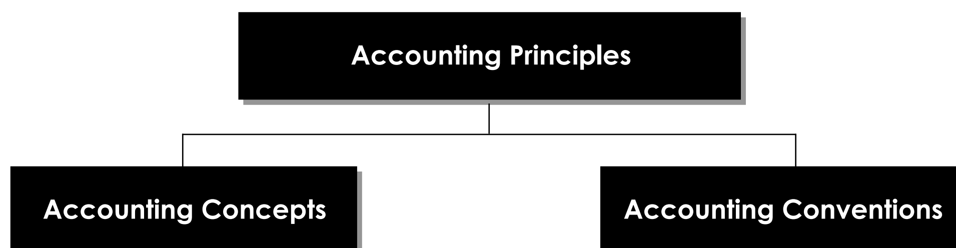
Accounting Concepts refers to the **assumptions** on the basis of which the transactions are recorded in the books of accounts and financial statements are drafted. They are perceived, presumed and accepted in accounting to provide a unifying structure and internal logic to the accounting process. They are also referred to as **Accounting Postulates**. These are the necessary assumptions and ideas which are fundamental to accounting practice. These are the ideas which have been accepted universally.

E.g. Entity concept, Going concern concept, Money measurement concept etc.

ACCOUNTING CONVENTIONS

Accounting conventions are the **traditions or customs** that are observed by the accountants for preparation of financial statements. They have evolved out the different accounting practices followed by different entities over a period of time. They have been developed over a period of time by the accountants by usage and practice.

E.g. convention of conservatism, convention of consistency, convention of materiality etc.



It should be noted that the terms 'Concepts' and 'Conventions' are usually used interchangeably. However, the basic difference between them is that 'Concepts' are primarily concerned with maintenance of books of accounts, while 'Conventions' are applied for preparation of financial statements.

NEED FOR GAAP FOR FINANCIAL REPORTING

The accounting standards developed and established by the standard-setting bodies determine how those financial statements are prepared. The standards are known collectively as Generally Accepted Accounting Principles or GAAP.

GAAP is based on established concepts, objectives, standards and conventions that have evolved over time to guide how financial statements are prepared and presented. GAAP is set with the objective of providing information that is useful to investors, lenders, or others that provide or may potentially provide resources to a profit-seeking concern or not-for-profit organization. Investors, lenders, and other users of financial information rely on financial reporting based on GAAP to make decisions about how to allocate their capital and to help financial markets operate as efficiently as possible.

While establishing GAAP, the standard setting bodies are mainly concerned about the end users of financial statements. End users include people like investors, banks, lenders who use third party financial statements to evaluate business decisions. For instance, an investor will look at a company's financial statements in order to decide whether to invest. The standard setting bodies wants to make consistent standards that help end users understand and use the company's financial data. GAAP's primary intent is not to help businesses. It is intended to help the end users. All of the objectives that MCA and the prior accounting standard setting body(ICAI) wanted to accomplish can be simplified to one main objective: to make financial statements universally understandable and usable for all of their users.

REGULATORY BODIES IN INDIA

- **The Ministry of Corporate Affairs (MCA):** MCA is an Indian Govt. Ministry. The Ministry is primarily concerned with administration of the Companies Act 2013, the Companies Act 1956, the Limited Liability Partnership Act, 2008 & other allied Acts and rules & regulations framed there-under mainly for regulating the functioning of the corporate sector in accordance with law. It is responsible mainly for regulation of Indian enterprises in Industrial and Services sector.

  Presently, they are entrusted with the development of India ASs. The Ind AS are named and numbered in the same way as the corresponding International Financial Reporting Standards (IFRS). National Advisory Committee on Accounting Standards (NACAS) recommend these standards to the Ministry of Corporate Affairs (MCA). MCA has to spell out the accounting standards applicable for companies in India. As on date MCA has notified 39 Ind AS. This shall be applied to the companies of financial year 2015-16 voluntarily and from 2016-17 on a mandatory basis.

- **The Institute of Chartered Accountants of India (ICAI):**ICAI is the national professional accounting body of India. It was enacted by the Parliament (acting as the provisional Parliament of India) to regulate the profession of Chartered Accountancy in India. It recommends the accounting standards to be followed by companies in India to The National Financial Reporting Authority (NFRA) and sets the accounting standards to be followed by other types of organisations. ICAI is solely responsible for setting the auditing and assurance standards to be followed in the audit of financial statements in India. It also issues other technical standards like Standards on Internal Audit (SIA), Corporate Affairs Standards (CAS) etc. to be followed by practicing Chartered Accountants. It works closely with the Government of India, Reserve Bank of India and the Securities and Exchange Board of India in formulating and enforcing such standards.

- **SEBI:** Securities Exchange Board of India (SEBI) was set up in 1988 to regulate the functions of securities market. SEBI promotes orderly and healthy development in the stock market but initially SEBI was not able to exercise complete control over the stock market transactions. It was left as a watch dog to observe the activities but was found ineffective in regulating and controlling them. As a result in May 1992, SEBI was granted legal status. SEBI is a body corporate having a separate legal existence and perpetual succession. The SEBI has been entrusted with both the regulatory and developmental functions. The SEBI plays a pivotal role in the capital

market. They protect the investors so that there is a steady flow of savings into the Capital Market. They ensures the fair practices by the issuers of securities, namely, companies so that they can raise resources at least cost. They help in the promotion of efficient services by brokers, merchant bankers and other intermediaries so that they become competitive and professional. It has initiated the basis for control and regulation of the market, arranged for the licensing of merchant banks, mutual funds etc. and performed the advisory functions to the Govt. The legislation giving powers to SEBI in the form of the Securities & Exchange Board of India Act to protect the interests of investors in securities and to promote the development of and to regulate the securities market and for matters connected therewith or incidental thereto.

COMPONENTS OF FINANCIAL STATEMENTS [SCHEDULE III]

Financial reporting is the language that communicates information about the financial condition and operational results of a company (public or private), not-for-profit organization, or state or local government. A financial statement (or financial report) is a formal record of the financial activities and position of an entity.

Relevant financial information is presented in a structured manner and in a form easy to understand. Specifically, financial reporting includes the following information:

1. **Balance Sheet:** It is also referred to as a statement of financial position, reports on a company's assets, liabilities, and owners' equity at a given point in time.
2. **Income Statement:** It is also known as a statement of comprehensive income, statement of revenue & expense, P&L or profit and loss report, reports on a company's income, expenses, and profits over a period of time. A profit and loss statement provides information on the operation of the enterprise. These include sales and the various expenses incurred during the stated period.
3. **Statement of changes in Equity:** It is also known as equity statement or statement of retained earnings, reports on the changes in equity of the company during the stated period.
4. **Cash Flow Statement:** A cash flow statement reports on a company's cash flow activities, particularly its operating, investing and financing activities.
5. **Notes to accounts:** The notes are an integral part of these financial statements. It warns users that failure to read the notes (or footnotes) to the financial statements will result in an incomplete picture of the company's financial health. Notes provide supplemental information about the financial condition of a company without which the financial statements cannot be fully understood. There are three basic types of notes – (a) notes related to the descriptions of the accounting rules applied in the company's statements; (b) Notes related to additional detail about a line on the financial statements; and (c)Notes related to additional financial disclosures about items not listed on the statements themselves.

FUNDAMENTAL ACCOUNTING ASSUMPTIONS

Transactions are recorded in the books of accounts on the basis of certain assumptions.

There are **three fundamental accounting assumptions** identified by AS-1 issued by ICAI:

(i) **Going Concern:**

The enterprise is normally viewed as a going concern, that is, as continuing in operation for the foreseeable future. It is assumed that the enterprise has either the intention or the necessity of liquidation or of curtailing materially the scale of the operations.

(ii) **Consistency:** It is assumed that accounting policies are consistent from one period to another.

(iii) **Accrual:** Revenues and costs are accrued, that is, recognised as they are earned or incurred (and not as money is received or paid) and recorded in the financial statements of the periods to which they relate. (The considerations affecting the process of matching costs with revenues under the accrual assumption are not dealt within this Statement.)

Every entity is mandatorily required to follow these three fundamental accounting assumptions. In other words, the entity does not have any choice with regard to the fact whether these assumptions should be followed or not.

USER OF ACCOUNTING INFORMATION

Accounting Information refers to the information generated by the accounting system of an entity relating to a particular accounting period. They disclose the operating results, and financial position of the entity. It acts as a mirror of the financial performance of a concern.

The Framework discusses objective of financial statements, qualitative characteristics that determine the usefulness of information contained in the financial statements, definition, recognition and measurement of the elements from which financial statements are constructed and concepts of capital and capital maintenance.

Identification of user of financial statements and their information needs are just the oretical as general purpose financial statements cannot satisfy the specific information need of various user groups. The Frame-work has identified the following user groups and their information needs:

1. Users of Financial Statements and their Information Needs

1. Investors	Information need of the group primarily relates to decision making of buy, hold or sale of the entity's share. Also dividend paying ability of the entity is a matter of interest.
2. Employees	Need to know about the stability and continued profitability of the employer which would ensure payment of remuneration, employee opportunities and retirement benefits.
3. Lenders	Interested in debt servicing ability.
4. Suppliers and other trade creditors	Interested in information about the entity's ability in the short run to pay their dues. Of course, they are interested in long run viability of the entity, if it is the major customer.
5. Customers	Seek information about the continuation of the entity in particular if the entity is the major supplier.
6. Government and their agencies	They have manifold interests like taxation, contribution of the entity in the employment generation and economic activities of the nation and also the infrastructural facilities to be provided to serve the need of the entity commensurate with its contribution to the society.
7. Public	Mostly interested in employment generation and societal contribution.

QUANTITAVE CHARACTERISTICS OF ACCOUNTING INFORMATION

IASC Framework has identified four qualitative characteristics of accounting information:

1. **Reliability:** Reliability is the quality of accounting information that allows the users to depend on it with confidence**.** Reliable accounting information acts as the foundation on which the users can build up their sound and rational decisions.

   To make accounting information reliable, it should have the following secondary qualities:

   (a) Verifiability;

   (b) Representational Faithfulness; and

   (c) Neutrality or Unambiguity.

2. **Relevance:** Relevance refers to that quality which ensures that the information is meaningful and useful to the user of accounting information for the purpose of decision-making. In order to be relevant, accounting information must be capable of making a difference in the decision-making process of the user.

   To make accounting information relevant, it should have the following secondary qualities:

   (a) Timeliness;

   (b) Predictive Value; and

   (c) Feedback Value.

3. **Understandability:** Understandability refers to that quality which makes the information comprehensible to the users of accounting information. For this purpose information should be presented in a lucid and systematic way to the users. But, at the same time the users are expected to have reasonable knowledge of business and accounting.

4. **Comparability:** Comparability is a quality of the relationship between two or more pieces of information. It refers to that quality of the accounting information that enables users to identify similarities in and differences between two sets of financial information.

Comparability with regard to accounting information may be of two types:

- **Horizontal Comparability** i.e. comparison of the financial information of two or more entities pertaining to the same accounting period.
- **Vertical Comparability** i.e. comparison of the financial information of a single entity over different accounting periods.

Presently, with the objectives of financial reporting focused on decision making, comparability is one of the most essential and desirable qualities of accounting information.

1.2 ACCOUNTING STANDARDS (AS) – APPLICABILITY, INTERPRETATION, SCOPE AND COMPLIANCE

Indian Accounting Standards

Accounting standard put together provides a framework of norms as to recognition, measurement and disclosure on the part of all enterprises that follow them to ensure comparability and depiction of true and fair view of the Financial Statements. High quality accounting standards are a prerequisite and important for a sound Capital Market System. The surge in the cross-border capital raising and Investment transactions demands formulation of high quality international accounting standard for financial reporting worldwide.

The various factors that have led to difference in accounting practices comprise widely of the culture, traditions, economic development, economic growth mode, inflation, legal system etc.

The diversity demands unification to the extent possible to develop Generally Accepted Accounting Practices (GAAP).

Indian GAAP comprises of a set of pronouncement issued by various regulatory authorities mostly in consultation with the ICAI. The accounting Standard i.e. Indian GAAP is supplemented by Guidance notes, Interpretation, General Clarification and/or revision from time to time.

The Accounting Standard will apply to "General Purpose Financial statement" e.g. Balance Sheet, Profit & Loss A/c, Statement, Schedules and Notes forming Integral part, issued for use by the Shareholders, Members, Creditors, Employees, and Public at large. AS are intended or items, which are considered material. AS to apply prospectively unless otherwise intended.

AS because of the very nature of these cannot override Local Regulation including the order of the Honourable High Courts as far as these relate and contain preparation and presentation of financial statements.

Companies (Accounting Standards) Rules, 2006.

As per Section 133 of Companies Act, 2013, the Central Government may prescribed the standards of accounting or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under Section 3 of the Chartered Accountants Act, 1949, in notified the rules named "Companies (Accounting Standards) Rules, 2006.

Criteria for classification of companies under the Companies (Accounting Standards) Rules, 2006

Small and Medium-Sized Company (SMC) as defined in Clause 2(f) of the Companies (Accounting Standards) Rules, 2006:

(f) "Small and Medium Sized Company" (SMC) means, a company-

(i) whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India;

(ii) which is not a bank, financial institution or an insurance company;

(iii) whose turnover (excluding other income) does not exceed rupees fifty crore in the immediately preceding accounting year;

(iv) which does not have borrowings (including public deposits) in excess of rupees ten crore at any time during the immediately preceding accounting year; and

(v) which is not a holding or subsidiary company of a company which is not a small and medium-sized company.

Explanation: For the purposes of clause (f), a company shall qualify as a Small and Medium Sized Company, if the conditions mentioned therein are satisfied as at the end of the relevant accounting period.

Non-SMCs

Companies not falling within the definition of SMC are considered as Non- SMCs.

General Instructions for Small and Medium Companies

SMCs shall follow the following instructions while complying with Accounting Standards under these Rules:-

The SMCs that does not disclose the information in line with the exemption provided by the Rules shall disclose the same in the following manner.

"The Company is a Small and Medium Sized Company (SMC) as defined in the General Instructions in respect of Accounting Standards notified under the Companies Act, 2013. Accordingly, the Company has complied with the Accounting Standards as applicable to a Small and Medium Sized Company."

Where a company, being an SMC, has qualified for any exemption or relaxation previously but no longer qualifies for the relevant exemption or relaxation in the current accounting period, the relevant standards or requirements become applicable from the current period and the figures for the corresponding period of the previous accounting period need not be revised merely by reason of its having ceased to be an SMC. The fact that the company was an SMC in the previous period and it had availed of the exemptions or relaxations available to SMCs shall be disclosed in the notes to the financial statements.

If an SMC opts not to avail of the exemptions or relaxations available to an SMC in respect of any but not all of the Accounting Standards, it shall disclose the standard(s) in respect of which it has availed the exemption or relaxation.

If an SMC desires to disclose the information not required to be disclosed pursuant to the exemptions or relaxations available to the SMCs, it shall disclose that information in compliance with the relevant accounting standard. Consultation with and after examination of the recommendations made by the National Financial Reporting Authority.

The SMC may opt for availing certain exemptions or relaxations from compliance with the requirements prescribed in an Accounting Standard, provided that such a partial exemption or relaxation and disclosure shall not be permitted to mislead any person or public.

Applicability of Accounting Standard to Non-Corporate Entities:

Criteria for classification of Non-corporate entities for applicability of Accounting Standards

Level I Entities

Non-corporate entities which fall in any one or more of the following categories, at the end of the relevant accounting period, are classified as Level I entities:

(i) Entities whose equity or debt securities are listed or are in the process of listing on any stock exchange, whether in India or outside India.

(ii) Banks (including co-operative banks), financial institutions or entities carrying on insurance business.

(iii) All commercial, industrial and business reporting entities, whose turnover (excluding other income) exceeds rupees fifty crore in the immediately preceding accounting year.

(iv) All commercial, industrial and business reporting entities having borrowings (including public deposits) in excess of rupees ten crore at any time during the immediately preceding accounting year.

(v) Holding and subsidiary entities of any one of the above.

Level II Entities (SMEs)

Non-corporate entities which are not Level I entities but fall in any one or more of the following categories are classified as Level II entities:

(i) All commercial, industrial and business reporting entities, whose turnover (excluding other income) exceeds rupees forty lakh but does not exceed rupees fifty crore in the immediately preceding accounting year.

(ii) All commercial, industrial and business reporting entities having borrowings (including public deposits) in excess of rupees one crore but not in excess of rupees ten crore at any time during the immediately preceding accounting year.

(iii) Holding and subsidiary entities of any one of the above.

Level III Entities (SMEs)

Non-corporate entities which are not covered under Level I and Level II are considered as Level III entities.

Applicability of Accounting Standards to Non-corporate Entities (As on 1.4.2008)

(I) Accounting Standards applicable to all Non-Corporate Entities in their entirety (Level I, Level II and Level III)

AS 1 Disclosures of Accounting Policies

AS 2 Valuation of Inventories

AS 4 Contingencies and Events Occurring After the Balance Sheet Date

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

AS 7 Construction Contracts (revised 2002)

AS 9 Revenue Recognition

AS 10 Properly Pland and Equipment

AS 11 The Effects of Changes in Foreign Exchange Rates (revised 2003)

AS 12 Accounting for Government Grants

AS 13 Accounting for Investments

AS 14 Accounting for Amalgamations

AS 16 Borrowing Costs

AS 22 Accounting for Taxes on Income

AS 26 Intangible Assets

(II) Exemptions or Relaxations for Non-corporate Entities falling in Level II and Level III (SMEs)

(A) Accounting Standards not applicable to Non-corporate Entities falling in Level II in their entirety:

AS 3 Cash Flow Statements

AS 17 Segment Reporting

(B) Accounting Standards not applicable to Non-corporate Entities falling in Level III in their entirety:

AS 3 Cash Flow Statements

AS 17 Segment Reporting

AS 18 Related Party Disclosures

AS 24 Discontinuing Operations

(C) Accounting Standards not applicable to all Non-corporate Entities since the relevant Regulators require compliance with them only by certain Level I entities

(i) AS 21, Consolidated Financial Statements

(ii) AS 23, Accounting for Investments in Associates with Consolidated Financial Statements

(iii) AS 27, Financial Reporting of Interests in Joint Ventures (to the extent of requirements relating to Consolidated Financial Statements)

(D) Accounting Standards in respect of which relaxations from certain requirements have been given to Non-corporate Entities falling in Level II and Level III (SMEs):

(i) Accounting Standard (AS) 15, Employee Benefits (revised 2005)

As explained in the summary of the Standards.

(ii) AS 19, Leases

Certain paragraphs relating to Disclosure requirements

Level III entities.

(iii) AS 20, Earnings Per Share

Diluted earnings per share (both including and excluding extraordinary items) is not required to be disclosed by non-corporate entities falling in Level II and Level III and information required by paragraph 48(ii) of AS 20 is not required to be disclosed by Level III entities if this standard is applicable to these entities.

(iv) AS 28, Impairment of Assets

Non-corporate entities falling in Level II and Level III are allowed to measure the 'value in use' on the basis of reasonable estimate thereof instead of computing the value in use by present value technique. Consequently, if a non-corporate entity falling in Level II or Level III chooses to measure the 'value in use' by not using the present value technique, the relevant provisions of AS 28, such as discount rate etc., would not be applicable to such an entity. Further, such an entity need not disclose the information required the Standard.

(v) AS 29, Provisions, Contingent Liabilities and Contingent Assets

Disclosure Requirement as laid in the Standards are not applicable to Level II and Level III Enterprises.

(E) AS 25, Interim Financial Reporting, does not require a non-corporate entity to present interim financial report. It is applicable only if a non-corporate entity is required or elects to prepare and present an interim financial report. Only certain Level I non-corporate entities are required by the concerned regulators to present interim financial results, e.g., quarterly financial results required by the SEBI. Therefore, the recognition and measurement requirements contained in this Standard are applicable to those Level I non-corporate entities for preparation of interim financial results.

ADVANTAGES :

1. It provides the accountancy profession with useful working rules.
2. It assists in improving quality of work performed by accountant.
3. It strengthens the accountant's resistance against the pressure from directors to use accounting policy which may be suspect in that situation in which they perform their work.
4. It ensures the various users of financial statements to get complete crystal information on more consistent basis from period to period.
5. It helps the users compare the financial statements of two or more organisaitons engaged in same type of business operation.

DISADVANTAGES :

1. Users are likely to think that said statements prepared using accounting standard are infallible.
2. They have been derived from social pressures which may reduced freedom.
3. The working rules may be rigid or bureaucratic to some user of financial statement.
4. The more standards there are, the more costly the financial statements are to produce.

Accounting Standard No.	Title of Accounting Standard
AS-1	Disclosure of Accounting Policies
AS-2	Valuation of Inventories (Revised)
AS- 3	Cash Flow Statements (Revised)
AS-4	Contingencies and Events (Occurring after the Balance Sheet Date)
AS-5	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies (Revised)
AS-7	Construction Contracts (Revised)
AS- 8	Accounting for Research and Development (stands withdrawn after introduction of AS-26)
AS-9	Revenue Recognition
AS-10	Property, Plant and Equipment
AS-11	The Effect of Changes in Foreign Exchange Rates (Revised)
AS-12	Accounting for Government Grants
AS-13	Accounting for Investments
AS-14	Accounting for Amalgamations
AS-15	Employee Benefits (Revised)
AS-16	Borrowing Cost
AS-17	Segment Reporting
AS-18	Related Party Disclosures
AS-19	Leases
AS-20	Earnings Per Share
AS-21	Consolidated Financial Statements
AS-22	Accounting for Taxes on Income
AS-23	Accounting for Investment in Associates in Consolidated Financial Statements
AS-24	Discontinuing Operations
AS-25	Interim Financial Reporting
AS-26	Intangible Assets
AS-27	Financial Reporting of Interests in Joint Venture
AS-28	Impairment of Assets
AS-29	Provisions, Contingent Liabilities and Contingent Assets
AS-30	Financial Instruments: Recognition and Measurement
AS 31	Financial Instruments: Presentation
AS 32	Financial Instruments: Disclosures

Applicability of Accounting Standards:

A three tier classification has been framed to ensure compliance of accounting standards for reporting enterprises.

Level I Enterprises:

- Enterprises whose equity or debt securities are listed whether in India or outside India.
- Enterprises which are in the process of listing their equity or debt securities as evidenced by the Board resolution in this regard.
- Banks including co-operative banks
- Financial institutions
- Enterprises carrying insurance business
- Enterprises whose turnover exceeds ₹50 crores
- Enterprises having borrowings in excess of ₹10 crores at any time during the accounting period.
- Holding companies and subsidiaries of enterprises falling under any one of the categories mentioned above.

Level II Enterprises:

- Enterprises whose turnover exceeds ₹40 lakhs but does not exceed ₹50 crores.
- Enterprises having borrowings in excess of ₹1 crore but not in excess of ₹10 crores at any time during the accounting period.
- Holding companies and subsidiaries of enterprise falling under any one of the categories mentioned above.

Level III Enterprises:

- Enterprises which are not covered under Level I and Level II.

Accounting Standard	Applicability (Based on the three tier classification)
AS1,2,4-16,22,26,28	All Enterprises
AS 3,17,18,24,	Not applicable to Level II and Level III enterprises in their entirety.
AS 19,20,29	All enterprises but relaxation given to Level I and Level II enterprises for certain disclosure requirements.
AS 21,23,27	Not applicable to Level II and Level III enterprises
AS 25	Not mandatorily applicable to Level II and Level III enterprises
AS 30,31,32	W.e.f. accounting periods commencing on or after 1-4-2009 and will be recommendatory in nature for an initial period of two years.

It will be mandatory for on or after 1-4-2011 for all commercial, industrial and business entities except to a Small and Medium-sized Entity.

AS-1: DISCLOSURE OF ACCOUNTING POLICIES

This standard deals with disclosure of significant accounting policies followed in the preparation and presentation of the financial statements and is mandatory in nature.

The accounting policies refer to the specific accounting principles adopted by the enterprise.

Proper disclosure would ensure meaningful comparison both inter/intra enterprise and also enable the users to properly appreciate the financial statements.

Financial statements are intended to present a fair reflection of the financial position financial performance and cash flows of an enterprise.

Areas involving different accounting policies by different enterprises are

- Methods of depreciation, depletion and amortization
- Treatment of expenditure during construction
- Treatment of foreign currency conversion/translation, Valuation of inventories
- Treatment of intangible assets
- Valuation of investments
- Treatment of retirement benefits
- Recognition of profit on long-term contracts Valuation of fixed assets
- Treatment of contingent liabilities

Factors governing the selection and application of accounting policies are:

- Prudence: Prudence means making of estimates, which is required under conditions of uncertainty. Profits are not anticipated till certain for realization, while provisions are made for all known liabilities ascertainable or based on estimates (e.g. warranty expenses).
- Substance over form: It means that transaction should be accounted for in accordance with actual happening and economic reality of the transactions, i.e. events governed by substance and not merely by the legal form
- Materiality :
  (a) As to the disclosure of all material items, individually or in aggregate in the context of fair presentation of financial statements as a whole if its omission or misstatement could influence the economic or financial decision of the user relying upon the financial statements
  (b) Depends on the size of the items or errors judged in the particular circumstances of its omissions or misstatements.
  (c) Is a cutoff point rather than being a primary qualitative characteristic which information must have.
  (d) This is a matter of judgment, varies from one entity to another and over one period to another.

AS-1 requires that all "significant" (i.e. only accounting policy that is useful for an understanding by the user of the financial statements) accounting policies adopted in the preparation and presentation of financial statements, should be disclosed by way of 'Note in one place as the note No I (this is the basis of the preparation of financial statements.)

Changes in Accounting Policies:

Any change in the accounting policies which has a material effect in the current period or which is reasonably expected to have a material effect in the later period should be disclosed.

In the case of a change in accounting policies, having material effect in the current period, the amount by which any item in the financial statements, is affected by such change should also be disclosed to the extent as ascertainable, otherwise the fact that the effect is not (wholly or partially) ascertainable, should be disclosed.

The following are not considered as changes in accounting policies:

(a) Accounting policies adopted for events or transactions that differ in substance at present (introducing Group Gratuity Scheme for employees in place of adhoc ex-gratia payment earlier followed.)

(b) Accounting policies pertains to events or transactions which did not occur previously or that were immaterial.

Fundamental Accounting Assumptions

Certain basic assumptions, in the preparation of financial statements are accepted and their use are assumed, no separate disclosure is required except for noncompliance in respect of-

(a) *Going Concern:* continuing operation in the foreseeable future and no interim necessity of liquidation or winding' up or reducing scale of operation.

(b) *Consistency:* accounting policies are consistent from one period to another

(c) *Accrual:*

   (i) Revenues and costs are accrued i.e. they are earned or incurred (not actually received or paid) and recorded in the financial statements

   (ii) Extends to matching revenue against relevant costs.

Examples:

1. The gross block of fixed assets are shown at the cost of acquisition, which includes tax, duties (net of MODVAT and set off availed) and other identified direct expenses. Interest on borrowing to finance the fixed assets is considered as revenue.

   — The policy appears to be correct.

2. Compensation payable to employees under voluntary retirement scheme has been deferred to be written off over a period of four years as against the past practice of charging out the same on payment/due basis. Comment.

   — The reason for change must be incorporated with notes to accounts.

3. Sales includes inter-departmental transfers, sales during trial run and are net of discounts. Comment.

   — The policy is not as per AS-9, Revenue Recognition.

AS-2: VALUATION OF INVENTORIES

At the outset AS -2 excludes the following though appears to be inventory in common parlance:

(a) Work-in-progress in construction contract and directly related service contract (ref: AS-2), inventories not forming part of construction work-in-progress will attract AS-2

(b) Work-in-progress arising in the ordinary course of business of service providers Shares, debentures and other financial instruments held as stock-in-trade (ref: AS-13 as Current Investments)

(c) Livestock, agricultural and forest product, mineral oil/gasses as measured at net realizable value as per trade practices at certain stage of production.

AS-2 covers inventories as an item of assets which are

(a) held for sale in the ordinary course of business

(b) in the process of production for such sale

(c) in the form of material or supplies for the process of production or rendering of service

Inventories are valued at lower of cost or net realizable value (NRV)

(a) Cost to include purchase price, conversion and other costs incurred in bringing the inventories to their present location and condition.

   An enterprise should use the same cost formula for all inventories having similar nature and use - specific cost, FIFO, weighted average, standard cost, adjusted selling price

(b) Net realizable value is the estimated selling price in the ordinary course of business reduced by the estimated cost to bring the item in saleable condition, considered on each balance sheet date, usually on item by item basis or under suitable group of similar or related item.

AS 2 — Valuation of Inventories

This Standard should be applied in accounting for inventories other than:

(a) work in progress arising under construction contracts, including directly relatedservice contracts (see Accounting Standard (AS) 7, Construction Contracts);

(b) work in progress arising in the ordinary course of business of service providers;

(c) shares, debentures and other financial instruments held as stock-in-trade; and

(d) producers' inventories of livestock, agricultural and forest products, andmineral oils, ores and gases to the extent that they are measured at netrealisable value in accordance with well-established practices in those industries.

Definition

Inventories are assets:

(a) held for sale in the ordinary course of business;

(b) in the process of production for such sale; or

(c) in the form of materials or supplies to be consumed in the productionprocess or in the rendering of services.

Disclosure

The financial statements should disclose:

(a) the accounting policies adopted in measuring inventories, including the cost formula used; and

(b) the total carrying amount of inventories and its classification appropriate to the enterprise.

AS-3 (REVISED): CASH FLOW STATEMENT

Cash Flow Statement deals with the provision of information about the historical changes in cash and cash equivalents of an enterprise by means of a cash flow statement which classifies cash flows during the period from operating, investing and financing activities.

- **Cash** comprises cash on hand and demand deposits with banks.
- **Cash equivalents** are short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.
- **Cash flows** are inflows and outflows of cash and cash equivalents.
- **Operating activities** are the principal revenue-producing activities of the enterprise and other activities that are not investing or financing activities.
- **Investing activities** are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.
- **Financing activities** are activities that result in changes in the size and composition of the owners' capital (including preference share capital in the case of a company) and borrowings of the enterprise.

Methods of preparing Cash Flow Statement:

1. Direct Method: In this method major classes of gross cash receipts and gross cash payments are disclosed.
2. Indirect Method: Under this method, the following adjustment to reported net profit or loss to be made:
   - Effects of transactions of non-cash nature.
   - Deferrals in accruals of past or future operating receipt or payments.
   - Changes in current assets and liabilities
   - Income & expenses associated with investing and financing cash flows.

Example:

Consider a hypothetical example on the preparation of cash from operating activities under both direct and indirect method of preparing cash flow statement.

Direct Method Cash Flow Statement [Paragraph 18(a)]	(₹ '000)
Cash flows from operating activities	
Cash receipts from customers	33,150
Cash paid to suppliers and employees	(29,600)
Cash generated from operations	3,550
Income taxes paid	(1,860)
Cash flow before extraordinary item	1,690
Proceeds from earthquake disaster settlement	180
Net cash from operating activities	1,870

Indirect Method Cash Flow Statement [Paragraph 18(b)]	(₹ '000)
Cash flows from operating activities	
Net profit before taxation, and extraordinary item	3,350
Adjustments for:	
Depreciation	450
Foreign exchange loss	40
Interest income	(300)
Dividend income	(200)
Interest expense	400
Operating profit before working capital changes	3,740
Increase in sundry debtors	(500)
Decrease in inventories	1,050
Decrease in sundry creditors	(740)
Cash generated from operations	3,550
Income taxes paid	(1,860)
Cash flow before extraordinary item	1,690
Proceeds from earthquake disaster settlement	180
Net cash from operating activities	1,870

Illustration 1.

Oriental Bank of Commerce, received a gross ₹4,500 crores demand deposits from customers and customers withdrawn ₹4,000 crores of demand deposits during the financial year 2014-15. How would you classify such cash flows?

Soltuion:

It will be treated as an Operating activity, on net basis ₹500 crores, inflow.

AS-4 (REVISED): CONTINGENCIES AND EVENTS OCCURRING AFTER THE BALANCE SHEET DATE

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

For the purpose of AS-4 the meaning is restricted to condition or situation at the Balance Sheet date, the financial effect of which is to be determined by future events which may or may not occur.

AS-4 does not deal with the following subjects, though may result in contingencies in respect of:

(a) Liabilities of Life and General Insurance out of policies issued by the enterprise.

(b) Obligations under retirement benefit plan/scheme

(c) Commitment arising from long-term lease contract

Estimates are required to be made for the amounts to be stated in the financial statement for many ongoing and recurring activities of an enterprise. Distinction should be made between an event that is certain and that is uncertain.

Contingent losses depend on the outcome of the contingencies. It should be provided by way of a charge in the statement of profit/loss

(a) if it is probable that future events will confirm after taking into account the probable recovery in this respect, that an asset has been impaired or a liability has been incurred as at the B/S date, and

(b) a reasonable estimate of the resulting loss can be estimated otherwise the existence of the contingent loss should be disclosed in the financial statements.

Provisions for contii1gencies are not made in respect of general or unspecified business risk since they do not relate to conditions or situations existing at the B/S date.

The disclosure requirements apply only for those contingencies or events which affect the financial position of the enterprise to a material extent stating:

(a) The nature of contingency;

(b) The uncertainty which may affect the future outcome;

(c) The estimate of the financial effect;

(d) A statement that such an estimate cannot be made;

Contingent gains are not recognized because of uncertainty of realization; however, there is no restriction to disclose as such in the 'Notes to Accounts' in a manner not likely to mislead the users of the financial statements.

Events occurring after the B/S date or those significant events, both favourable and unfavourable that occur between the B/S date and the date of approval of the financial statements by the appropriate authority (e.g. Board of Directors of a company) can be of:

(a) Those which provide further evidence of condition that existed at the B/S date adjusting events (e.g. insolvency of a customer that occur after B/S date)

(b) Those which are indicative of conditions that arose subsequent to the B/S date non-adjusting events (loss due to earthquake, war)

Events occurring after the B/S date but indicative of the enterprise ceases to be a going concern (destruction of major production plant by fire after B/S date) needs to be considered and evaluated to justify "going concern concept" for preparation of Financial statements.

Illustration 2.

The assets in a factory of a limited company was damaged due to a fire break out on 15th April. The Loss is estimated at ₹ 50 crores out of which ₹35 crores will be recoverable from the insurers. Explain briefly how the loss should be treated in the final account for the previous year.

Solution:

This has to be shown as a disclosure by way of note to account.

Illustration 3.

Board of Directors of a limited company approved the financial account for the year 2014-15 on 31st July, 2015. The following events occurred before the approval of financial statements by Board of Directors. State how would you deal with these situations:

(a) The Board of Directors at their meeting on June 30, 2015 has recommended a dividend of 10% to be paid to the shareholders after it is approved at the annual general meeting.

(b) A debtor, who was declared insolvent on 10th July 2015. The total outstanding amount was ₹2 lacs as on 31st March, 2015.

Solution:

(a) Proposed Dividend must be shown in the Balance Sheet.

(b) A provision for loss should be provided in the books.

AS-5 (REVISED): NET PROFIT OR LOSS FOR THE PERIOD, PRIOR PERIOD ITEMS AND CHANGES IN ACCOUNTING POLICIES.

The statement requires the classification and disclosure of extraordinary and prior period items and the disclosure of certain items within the profit or loss from ordinary activities and also accounting treatment for changes in the accounting estimate, and disclosure regarding changes in Accounting Policies in the financial statement.

To ensure preparation of Profit or Loss statement on a uniform basis, in turn to enhance better comparability of the enterprise over time and with other enterprises.

All items of income and expense, which are recognized in a period, are normally included for the determination of the Net Profit/Loss for the period unless otherwise permitted (AS-22 exception for deferred tax in the income tax).

Each extraordinary items, both income and expense arises from events/transactions, which are clearly distinct from ordinary activities and not ex petted to recur frequently or regularly, should be disclosed as apart of net profit/loss for the period in a distinct manner to understand the impact on current profit/loss.

An event or transaction may be extraordinary for one enterprise but not for the other because of difference between their respective ordinary activities.

Only on rare occasion does an event/transaction give rise to extraordinary items.

Ordinary activities are those undertaken as part of business of ail enterprise and related activities for furtherance of, incidental to or arising from these activities. Frequency of occurrence is not the sole criteria to determine extraordinary or ordinary nature.

However, when items of income or expense within profit/loss from ordinary activities are of such a size, nature or incidence that their disclosure is relevant to explain the performance for the period the nature and amount of such items should be disclosed separately as exceptional items (distinct from extraordinary items) e.g.

(a) write off/ write back of inventories to Net Realizable Value, provision/write back of cost of restructuring

(b) disposal of fixed asset/long term investments

(c) effect of legislative changes with retrospective application

(d) settlement of litigation

(e) other reversal of provisions

Prior period items (income/expense) arise in the current period as a result of errors/ omissions in the preparation of the financial statements, in one or more prior period are generally infrequent in nature and distinct from changes in accounting estimates.

Prior period items are normally included in the determination of net profit/loss for the current period shown after determination of current period profit/loss. The objective is to indicate the "effect of such items in the profit/loss. The separate disclosure is intended to show the impact on the current profit/loss. Disclosure is made:

(a) by showing the prior period items distinctively under the relevant head of income/expenditure

(b) by putting under "Prior Period Adjustment A/c either in the main statement of P/L or in a schedule containing the respective details with the net figure in the P/L A/c of current period in compliance with schedule III part II requirement.

Notes to the Accounts should provide detail description with impact on the current period and tax implication arising thereof (e.g. stock valuation not correctly made in the previous period).

The use of reasonable estimate based on then available information circumstances are an essential part of the preparation of financial statement. There may arise a need to change the estimate on the basis of new information more experience or subsequent development. The revision in estimate does not bring the adjustment within the definition of an extraordinary item or prior period item.

The effect of change in Accounting Estimate should be included in the determination of net profit/loss

(a) in the period of change (if restricted for the period only)

(b) in the period of change and future period (if the change affects both) (e.g. estimate of bad debt for (a) and change in estimated life of a depreciable asset in terms of depreciation.

Classification as to ordinary or extraordinary as previously followed should be maintained to disclose the effect of changes in accounting estimate for better comparability.

The nature and change in an accounting estimates having material effect in the current period or in subsequent period should be disclosed. If quantification is not predictable such fact should also be disclosed.

If it is difficult to distinguish between a change in Accounting Policy and change in Accounting Estimate the change is recognized as change in Accounting Estimate with appropriate disclosure.

Example of various disclosures under AS-5

1. change in depreciation method: change in accounting policy
2. useful life reduced but no change: change in accounting estimate in depreciation method
3. arithmetical error in depreciation computation: prior period item
4. due to oversight depreciation incorrectly computed: prior period item
5. fixed asset destroyed in earth quake: extraordinary item
6. major disposal of fixed items: ordinary activity (exceptional item)
7. maintenance provision no longer required since major part of the assets no longer exist: the write-back. if material should be disclosed as exceptional item and not as extraordinary' or prior period item.

Example:

Mr.Pradip an employee of CCL Ltd.went on leave with a pay for 9 months on 1.1.2015 upto 30.09.2015. His monthly pay was ₹25,000. While preparing the financial statement on 30.6.2015 for the year ended 31.03.15, the expense of salary of Mr.Pradip for 3 months (1.1.15 to 31.03.15) was not provided due to omission. When Mr.Pradip joined on 1.10.15, the whole salary for 9 months was duly paid to him.

In this case, three months salary of ₹75,000 is prior period expense and following entry should be passed:

Salary A/c	Dr. 1,50,000	
Prior period expense (Salary) A/c	Dr. 75,000	
To Bank A/c		2,25,000

If Mr. Pradip was terminated from service on 1.1.15 and was re-instated in service by the Court on 30.09.15 with full pay protection(i.e. total salary was rewarded to him). As the employee was re-instated in service as per the Court's Order as on 1.10.2015, the following entry should be made:

Salary A/c	Dr. 2,25,000	
To Bank A/c		2,25,000

In such a case, there shall arise no error or omission while preparing the financial statements for the earlier years.

DEPRECIATION ACCOUNTING [AS 6] shall stand withdrawn.

AS-7 (REVISED): ACCOUNTING FOR CONSTRUCTION CONTRACTS

The statement applies to accounting for construction contracts, in the financial statements of contractors,

A construction contract may be related to the construction of single asset or a number of assets closely, interrelated or interdependent in terms of the scope of the contract.

For the purpose of this statement construction contract covers:

(a) Contracts for rendering of services directly related to the construction of the asset e.g. service of project-managers, architects etc.

(b) Contracts for destruction/restoration of assets and restoration of environments following demolition.

(c) Consultancy contracts in project management, designing, computers where such contracts are related to the construction of the asset.

(d) Those long-term contracts not relating to construction of an asset.

A construction contract may be

(a) a fixed-price contract with/without escalation

(b) a cost-plus contract (provision for reimbursement of overhead on agreed basis in addition to fixed price/ fees)

(c) a mix of both (a cost-plus contract with a minimum agreed price)

The statement usually apply to each contract separately, however, sometimes it is necessary to apply the statement to the separately identifiable components of a single contract or to a group of contracts together in order to reflect the substance. When a contract covers —

(a) *Number of assets:* each asset treated as separate contract when the proposal, negotiation and cost/revenue can be identified distinctly.

(b) *Negotiated single package of interrelated identifiable with an overall profit margin performed concurrently or continuous sequence:* treated as a single contract whether a single customer or a group of customers.

(c) *Construction of an additional asset as the provision of the contract:* treated as separate contract if there is significant change in design, technology or transaction from original contract in terms of the scope and/or price.

Additional asset should be treated as a separate construction contract if there is significant change in design, technology or function from the assets covered in the original contract price.

Contract revenue comprises of

(a) revenue agreed in the contract

(b) variations in the scope of contract, adverse/favourable

(c) incentive payment (degree of certainty and reliability)

(d) penalties due to delay in execution

Contract costs comprise of

(a) directly related to specific contract

(b) attributable cost relating to contract activity in general and precisely allocable to the contract as reduced by incidental income not included in contract revenue (sale of surplus material, disposal of contract specific plants etc).

Contract cost and revenue are recognized for accounting only when the outcome of the construction contract can be measured reliably with regard to the stage of completion of the contracts activity at its B/S date. All expected losses should recognized as an expense for the contract.

Under the percentage completion method, contract revenue is recognized in the P/L in the accounting period in which the work is performed and the related contract cost is shown as an expense. However, expected excess of total contract is recognized as an expense immediately. Revenue earlier recognized or becoming doubtful/ uncollectable should be treated as an expense.

A long-term contract is subject to fluctuation for various reasons in the original estimation thus likely to affect the determination of contract results. It is necessary that an annual review of the cost already incurred and future cost required to complete the project on schedule. While estimating the future cost care should be taken for foreign exchange rate fluctuation, labour problem, changes in material price etc.

Disclosure under AS -7 (on reporting date by an enterprise)

A) An enterprise should enclose

(a) The amount of contract revenue recognized as revenue in the period

(b) The methods used to determine the contract revenue recognized in the period

(c) Method used to determine the stage of completion of contract in progress

B) An enterprise should disclose the following for contracts in progress at the reporting date

1. The aggregate amount of costs incurred and recognized profit less recognized losses upto reporting date.
2. The amount of advance received and amount retained

C) An enterprise should present

(a) Gross amount due from customer is an asset

(b) Gross amount due to customer is a liability

(c) Contingencies as per AS-4 (warranty cost, penalties, guarantee issued by banks against counter indemnity of contractor)

Illustration 4.

A Company undertook to pay contract for a building for ₹ 40lakhs. As on 31.3.2015, it incurred a cost of ₹ 6 lakhs and expects that there will be ₹ 36 lakhs more for completing the building. It has received ₹ 4 lakhs as progress payment. What is the degree of completion?

$$\text{Percentage of Completion} = \frac{\text{Cost to date}}{\text{Cumulative cost incurred + Estimated cost to complete}} \times 100$$

$$= \frac{6}{6+36} \times 100 = 14.28\%$$

AS-8 ACCOUNTING FOR RESEARCH & DEVELOPMENT

(STANDS WITHDRAWN ON INTRODUCTION OF AS-26 INTANGIBLE ASSETS)

AS-9 REVENUE RECOGNITION

The statement covers the recognition of revenue arising in the course of ordinary activities. of the enterprise *from*

(a) sale of goods

(b) rendering of service

(c) outsourcing of resources yielding interest, royalties and dividend Specific exclusion *from* the standard pertains to:

 (a) construction contracts

 (b) lease/hire purchase agreement

 (c) govt. grants/subsidies

 (d) insurance contract of insurance companies

Essential criterion for recognition for revenue *from* ordinary activities as aforesaid is that the consideration is reasonably determinable even though the payments are made by installments. In the event of uncertainty, the recognition is postponed and considered as revenue of the period in which it is properly recognized.

The standard requires, in addition to the AS- I, that an enterprise should also disclose the circumstances in which revenue recognition has been postponed pending resolution of significant uncertainties.

NOTE:

Revenue include the gross inflow of economic benefits only accrued to an enterprise on its own e.g. sales tax, service tax, VAT etc. do not accrue to the enterprise and thus not considered as revenue under IAS-18 and US GAAP. Practices vary in India and tend to show larger gross turnover for the enterprise (incidentally section 145A of the Income Tax Act '61 require purchase, inventory and turnover inclusive of Tax, duty and cess).

ICAI recommends disclosure in the manner :

Turnover (gross) xxx

Less Excise duty xxx

Net Turnover xxx

Illustration 5.

AB Ltd. Seeks you advise about the treatment of the following in the final statement of accounts for the year ended 31st March 2015:

"As a result of a recent announced price revision, granted by the Government of India with effect from 1st July, 2014, the company stands to receive ₹ 6 lakhs from its customers in respect of sales made in 2014-15"

Solution:

The company is preparing the financial statements for the year ended 31.3.15. Due to price revision granted by the Government of India, the company has to receive an additional sales revenue of ₹ 6 lakhs in respect of sales made during the year 2014-15.

As per AS-9, where uncertainty exists in collection of revenue, its recognition is postponed to the extent of uncertainty involved and it should be recognized as revenue only when it is reasonably certain about its collection.

In view of the above statement, if there is no uncertainty exists as to the collect ability of ₹ 6 lakhs, it should be recognized as revenue in the financial statements for the year ended 31.3.15.

Illustration 6.

Advise D Ltd.about the treatment of the following in the final statement of accounts for the year ended 31st March, 2017.

A claim lodged with the Railways in March, 2015 for loss of goods of ₹ 5 lakhs had been passed for payment in March, 2017 for ₹ 4 lakhs. No entry was passed in the books of the company, when the claim was lodged.

Solution:

The financial statements of the company are prepared for the year ended 31.3.17.

There was a loss of goods of ₹ 5 lakhs in 2014-15 and the claim was lodged in March 2015 with the Railway authorities. No entry was passed in the books of the company when the claim was lodged and the said treatment was correct in view of AS-9, which states that if uncertainty exists as to collectability, the revenue recognition should be postponed.

Since, the claim is passed for payment of ₹ 4 lakhs in March, 2017, it should be recognized as revenue in the financial statements prepared for the year ended 31.3.17.

As per AS-5 Revised, the claim amount received will not be treated as extraordinary item. AS-5 Revised further states that when items of income and expense within profit 0r loss from ordinary activities are of such size, nature, or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately. Accordingly, the nature and amount of this item should be disclosed separately.

Illustration 7.

A private limited company manufacturing fancy terry towels had valued its closing stock of inventories of finished goods at the realisable value, inclusive of profit and the export cash incentives. Firm contracts had been received and goods were packed for export, but the ownership in these goods had not been transferred to the foreign buyer. Comment on the valuation of the stocks by the company.

Solution:

Accounting Standard 2 "Valuation of Inventories" states that inventories should be valued at lower of historical cost and net realisable value. AS 9 on "Revenue Recognition" states, "at certain stages in specific industries, such as when agricultural crops have been harvested or mineral ores have been extracted, performance may be substantially complete prior to the execution of the transaction generating revenue. In such cases, when sale is assured under forward contract or a government guarantee or when market exists and there is a negligible risk of failure to sell, the goods invoiced are often valued at Net-realisable value."

Terry Towels do not fall in the category of agricultural crops or mineral ores. Accordingly, taking into account the facts stated, the closing stock of finished goods (Fancy terry towel) should have been valued at lower of cost and net-realisable value and not at net realisable value. Further, export incentives are recorded only in the year the export sale takes place. Therefore, the policy adopted by the company for valuing its closing stock of inventories of finished goods is not correct.

PROPERTY, PLANT AND EQUIPMENT [AS 10]

Objective:

The objective of this Standard is to prescribe the accounting treatment for property, plant and equipment so that users of the financial statements can discern information about investment made by an enterprise in its property, plant and equipment and the changes in such investment. The principal issues in accounting for property, plant and equipment are the recognition of the assets, the determination of their carrying amounts and the depreciation charges and impairment losses to be recognised in relation to them.

Scope / Applicability:

This Standard should be applied in accounting for property, plant and equipment except when another Accounting Standard requires or permits a different accounting treatment.

This Standard does not apply to:

(a) Biological assets related to agricultural activity other than bearer plants. This Standard applies to bearer plants but it does not apply to the produce on bearer plants; and

(b) Wasting assets including mineral rights, expenditure on the exploration for and extraction of minerals, oil, natural gas and similar non-regenerative resources.

However, this Standard applies to property, plant and equipment used to develop or maintain the assets described in (a) and (b) above.

Other Accounting Standards may require recognition of an item of property, plant and equipment based on an approach different from that in this Standard. For example, AS 19, Leases, requires an enterprise to evaluate its recognition of an item of leased property, plant and equipment on the basis of the transfer of risks and rewards.

However, in such cases other aspects of the accounting treatment for these assets, including depreciation, are prescribed by this Standard.

Investment property, as defined in AS 13, Accounting for Investments, should be accounted for only in accordance with the cost model prescribed in this standard.

Important Terminology:

1. **Agricultural Activity** is the management by an enterprise of the biological transformation and harvest of biological assets for sale or for conversion into agricultural produce or into additional biological assets.
2. **Agricultural Produce** is the harvested product of biological assets of the enterprise.
3. **Bearer plant** is a plant that:
   a) is used in the production or supply of agricultural produce;
   b) is expected to bear produce for more than a period of twelve months; and
   c) has a remote likelihood of being sold as agricultural produce, except for incidental scrap sales.

   The following are not bearer plants:
   a) plants cultivated to be harvested as agricultural produce (for example, trees grown for use as lumber);
   b) plants cultivated to produce agricultural produce when there is more than a remote likelihood that the entity will also harvest and sell the plant as agricultural produce, other than as incidental scrap sales (for example, trees that are cultivated both for their fruit and their lumber); and
   c) annual crops (for example, maize and wheat).

   When bearer plants are no longer used to bear produce they might be cut down and sold as scrap, for example, for use as firewood. Such incidental scrap sales would not prevent the plant from satisfying the definition of a bearer plant.
4. **Biological Asset** is a living animal or plant.
5. **Carrying amount** is the amount at which an asset is recognised after deducting any accumulated depreciation and accumulated impairment losses.
6. **Cost** is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition or construction or, where applicable, the amount attributed to that asset when initially recognised in accordance with the specific requirements of other Accounting Standards.
7. **Depreciable amount** is the cost of an asset, or other amount substituted for cost, less its residual value.
8. **Depreciation** is the systematic allocation of the depreciable amount of an asset over its useful life.
9. **Enterprise -specific value** is the present value of the cash flows an enterprise expects to arise from the continuing use of an asset and from its disposal at the end of its useful life or expects to incur when settling a liability.

10. Fair value is the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.
11. Gross carrying amount of an asset is its cost or other amount substituted for the cost in the books of account, without making any deduction for accumulated depreciation and accumulated impairment losses.
12. An **impairment loss** is the amount by which the carrying amount of an asset exceeds its recoverable amount.
13. Property, plant and equipment are tangible items that: a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and b) are expected to be used during more than a period of twelve months.
14. Recoverable amount is the higher of an asset's net selling price and its value in use.
15. The residual value of an asset is the estimated amount that an enterprise would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.
16. Useful life is: a) the period over which an asset is expected to be available for use by an enterprise ; or b) the number of production or similar units expected to be obtained from the asset by an enterprise.

Recognition:

- The cost of an item of property, plant and equipment should be recognised as an asset if, and only if:
  - (a) it is probable that future economic benefits associated with the item will flow to the enterprise; and
  - (b) the cost of the item can be measured reliably.
- Items such as spare parts, stand-by equipment and servicing equipment are recognised in accordance with this Standard when they meet the definition of property, plant and equipment. Otherwise, such items are classified as inventory.
- This Standard does not prescribe the unit of measure for recognition, i.e., what constitutes an item of property, plant and equipment. Thus, judgment is required in applying the recognition criteria to specific circumstances of an enterprise.
- An enterprise evaluates under this recognition principle all its costs on property, plant and equipment at the time they are incurred. These costs include costs incurred:
  - (a) initially to acquire or construct an item of property, plant and equipment; and
  - (b) subsequently to add to, replace part of, or service it.

Initial Costs:

The definition of 'property, plant and equipment' covers tangible items which are held for use or for administrative purposes. The term 'administrative purposes' has been used in wider sense to include all business purposes other than production or supply ofgoods or services or for rental for others. Thus, property, plant and equipment would include assets used for selling and distribution, finance and accounting, personnel and other functions of an enterprise. Items of property, plant and equipment may also be acquired for safety or environmental reasons. The acquisition of such property, plant and equipment, although not directly increasing the future economic benefits of any particular existing item of property, plant and equipment, may be necessary for an enterprise to obtain the future economic benefits from its other assets. Such items of property, plant and equipment qualify for recognition as assets because they enable an enterprise to derive future economic benefits from related assets in excess of what could be derived had those items not been acquired. For example, a chemical manufacturer may install new chemical handling processes to comply with environmental requirements for the production and storage of dangerous chemicals; related plant enhancements are recognised as an asset because without them the enterprise is unable to manufacture and sell chemicals. The resulting carrying amount of such an asset and related assets is reviewed for impairment in accordance with AS 28, Impairment of Assets.

Subsequent Costs:

- Under the recognition principle (as mentioned above), an enterprise does not recognise in the carrying amount of an item of property, plant and equipment the costs of the day-today servicing of the item. Rather, these costs are recognised in the statement of profit and loss as incurred. Costs of day-to-day servicing are primarily the costs of labour and consumables, and may include the cost of small parts. The purpose of such expenditures is often described as for the 'repairs and maintenance' of the item of property, plant and equipment.
- Parts of some items of property, plant and equipment may require replacement at regular intervals or it may require replacement several times. Items of property, plant and equipment may also be acquired to make a less frequently recurring replacement or to make a non-recurring replacement. Under the recognition principle (as discussed above), an enterprise recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if the recognition criteria are met. The carrying amount of those parts that are replaced is derecognised in accordance with the 'derecognition provisions' of this Standard.
- A condition of continuing to operate an item of property, plant and equipment may be performing regular major inspections for faults regardless of whether parts of the item are replaced. When each major inspection is performed, its cost is recognised in the carrying amount of the item of property, plant and equipment as a replacement if the recognition criteria are satisfied. Any remaining carrying amount of the cost of the previous inspection is derecognised.
- The derecognition of the carrying amount occurs regardless of whether the cost of the previous part / inspection was identified in the transaction in which the item was acquired or constructed. If it is not practicable for an enterprise to determine the carrying amount of the replaced part/ inspection, it may use the cost of the replacement or the estimated cost of a future similar inspection as an indication of what the cost of the replaced part/ existing inspection component was when the item was acquired or constructed.

Measurement at Recognition:

An item of property, plant and equipment that qualifies for recognition as an asset should be measured at its cost.

Elements of Cost:

The cost of an item of property, plant and equipment comprises:

(a) its purchase price, including import duties and non –refundable purchase taxes,, after deducting trade discounts and rebates.

(b) any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

(c) the initial estimate of the costs of dismantling, removing the item and restoring the site on which it is located, referred to as 'decommissioning, restoration and similar liabilities', the obligation for which an enterprise incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.

Measurement of Cost:

- The cost of an item of property, plant and equipment is the cash price equivalent at the recognition date. If payment is deferred beyond normal credit terms, the difference between the cash price equivalent and the total payment is recognised as interest over the period of credit unless such interest is capitalised in accordance with AS 16.
- One or more items of property, plant and equipment may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. The following discussion refers simply to an exchange of one non-monetary asset for another, but it also applies to all exchanges described in the

preceding sentence. The cost of such an item of property, plant and equipment is measured at fair value unless (a) the exchange transaction lacks commercial substance or (b) the fair value of neither the asset(s) received nor the asset(s) given up is reliably measurable.

The acquired item(s) is/are measured in this manner even if an enterprise cannot immediately derecognise the asset given up. If the acquired item(s) is/are not measured at fair value, its/their cost is measured at the carrying amount of the asset(s) given up.

- An enterprise determines whether an exchange transaction has commercial substance by considering the extent to which its future cash flows are expected to change as a result of the transaction. An exchange transaction has commercial substance if:

  (a) the configuration (risk, timing and amount) of the cash flows of the asset received differs from the configuration of the cash flows of the asset transferred; or

  (b) the enterprise-specific value of the portion of the operations of the enterprise affected by the transaction changes as a result of the exchange;

  (c) and the difference in (a) or (b) is significant relative to the fair value of the assets exchanged.

- For the purpose of determining whether an exchange transaction has commercial substance, the enterprise -specific value of the portion of operations of the enterprise affected by the transaction should reflect post-tax cash flows. In certain cases, the result of these analyses may be clear without an enterprise having to perform detailed calculations.

- The fair value of an asset is reliably measurable if (a) the variability in the range of reasonable fair value measurements is not significant for that asset or (b) the probabilities of the various estimates within the range can be reasonably assessed and used when measuring fair value. If an enterprise is able to measure reliably the fair value of either the asset received or the asset given up, then the fair value of the asset given up is used to measure the cost of the asset received unless the fair value of the asset received is more clearly evident.

- Where several items of property, plant and equipment are purchased for a consolidated price, the consideration is apportioned to the various items on the basis of their respective fair values at the date of acquisition. In case the fair values of the items acquired cannot be measured reliably, these values are estimated on a fair basis as determined by competent valuers.

Measurement after Recognition:

An enterprise should choose either the cost model or the revaluation model as its accounting policy and should apply that policy to an entire class of property, plant and equipment. It is discussed hereunder:

(a) **Cost Model:**

After recognition as an asset, an item of property, plant and equipment should be carried at its cost less any accumulated depreciation and any accumulated impairment losses.

(b) **Revaluation Model:**

- After recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably should be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluations should be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date.

- The fair value of items of property, plant and equipment is usually determined from market-based evidence by appraisal that is normally undertaken by professionally qualified valuers.

- If there is no market-based evidence of fair value because of the specialised nature of the item of property, plant and equipment and the item is rarely sold, except as part of a continuing business, an enterprise may need to estimate fair value using an income approach (for example, based on discounted cash flow projections) or a depreciated replacement cost approach which aims at making a realistic

estimate of the current cost of acquiring or constructing an item that has the same service potential as the existing item.

- The frequency of revaluations depends upon the changes in fair values of the items of property, plant and equipment being revalued. When the fair value of a revalued asset differs materially from its carrying amount, a further revaluation is required. Some items of property, plant and equipment experience significant and volatile changes in fair value, thus necessitating annual revaluation. Such frequent revaluations are unnecessary for items of property, plant and equipment with only insignificant changes in fair value. Instead, it may be necessary to revalue the item only every three or five years.
- When an item of property, plant and equipment is revalued, the carrying amount of that asset is adjusted to the revalued amount. At the date of the revaluation, the asset is treated in one of the following ways:

  a. the gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset; or

  b. the accumulated depreciation is eliminated against the gross carrying amount of the asset.
- If an item of property, plant and equipment is revalued, the entire class of property, plant and equipment to which that asset belongs should be revalued.
- The items within a class of property, plant and equipment are revalued simultaneously to avoid selective revaluation of assets and the reporting of amounts in the financial statements that are a mixture of costs and values as at different dates. However, a class of assets may be revalued on a rolling basis provided revaluation of the class of assets is completed within a short period and provided the revaluations are kept up to date.
- An increase in the carrying amount of an asset arising on revaluation should be credited directly to owners' interests under the heading of revaluation surplus. However, the increase should be recognised in the statement of profit and loss to the extent that it reverses a revaluation decrease of the same asset previously recognized in the statement of profit and loss.
- A decrease in the carrying amount of an asset arising on revaluation should be charged to the statement of profit and loss. However, the decrease should be debited directly to owners' interests under the heading of revaluation surplus to the extent of any credit balance existing in the revaluation surplus in respect of that asset.
- The revaluation surplus included in owners' interests in respect of an item of property, plant and equipment may be transferred to the revenue reserves when the asset is derecognised. This may involve transferring the whole of the surplus when the asset is retired or disposed of. However, some of the surplus may be transferred as the asset issued by an enterprise. In such a case, the amount of the surplus transferred would be the difference between depreciation based on the revalued carrying amount of the asset and depreciation based on its original cost. Transfers from revaluation surplus to the revenue reserves are not made through the statement of profit and loss.

Depreciation:

- Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item should be depreciated separately.
- An enterprise allocates the amount initially recognised in respect of an item of property, plant and equipment to its significant parts and depreciates each such part separately. For example, it may be appropriate to depreciate separately the airframe and engines of an aircraft, whether owned or subject to a finance lease.
- A significant part of an item of property, plant and equipment may have a useful life and a depreciation method that are the same as the useful life and the depreciation method of another significant part of that same item. Such parts may be grouped in determining the depreciation charge.
- To the extent that an enterprise depreciates separately some parts of an item of property, plant and equipment, it also depreciates separately the remainder of the item. The remainder consists of the parts of the item that are

individually not significant. If an enterprise has varying expectations for these parts, approximation techniques may be necessary to depreciate the remainder in a manner that faithfully represents the consumption pattern and/or useful life of its parts.

- An enterprise may choose to depreciate separately the parts of an item that do not have a cost that is significant in relation to the total cost of the item.
- The depreciation charge for each period should be recognised in the statement of profit and loss unless it is included in the carrying amount of another asset.
- The depreciation charge for a period is usually recognised in the statement of profit and loss. However, sometimes, the future economic benefits embodied in an asset are absorbed in producing other assets. In this case, the depreciation charge constitutes part of the cost of the other asset and is included in its carrying amount. For example, the depreciation of manufacturing plant and equipment is included in the costs of conversion of inventories (see AS 2). Similarly, the depreciation of property, plant and equipment used for development activities may be included in the cost of an intangible asset recognised in accordance with AS 26, Intangible Assets.

Depreciable Amount and Depreciation Period:

- The depreciable amount of an asset should be allocated on a systematic basis over its useful life.
- The residual value and the useful life of an asset should be reviewed at least at each financial year-end and, if expectations differ from previous estimates, the change(s) should be accounted for as a change in an accounting estimate in accordance with AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies.
- Depreciation is recognised even if the fair value of the asset exceeds its carrying amount, as long as the asset's residual value does not exceed its carrying amount. Repair and maintenance of an asset do not negate the need to depreciate it.
- The depreciable amount of an asset is determined after deducting its residual value.
- The residual value of an asset may increase to an amount equal to or greater than its carrying amount. If it does, depreciation charge of the asset is zero unless and until its residual value subsequently decreases to an amount below its carrying amount.
- Depreciation of an asset begins when it is available for use, i.e., when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Depreciation of an asset ceases at the earlier of the date that the asset is retired from active use and is held for disposal and the date that the asset is derecognised. Therefore, depreciation does not cease when the asset becomes idle or is retired from active use (but not held for disposal) unless the asset is fully depreciated. However, under usage methods of depreciation, the depreciation charge can be zero while there is no production.
- The future economic benefits embodied in an asset are consumed by an enterprise principally through its use. However, other factors, such as technical or commercial obsolescence and wear and tear while an asset remains idle, often result in the diminution of the economic benefits that might have been obtained from the asset. Consequently, all the following factors are considered in determining the useful life of an asset:
  a. expected usage of the asset. Usage is assessed by reference to the expected capacity or physical output of the asset.
  b. expected physical wear and tear, which depends on operational factors such as the number of shifts for which the asset is to be used and the repair and maintenance programme, and the care and maintenance of the asset while idle.
  c. technical or commercial obsolescence arising from changes or improvements in production, or from a change in the market demand for the product or service output of the asset. Expected future reductions

in the selling price of an item that was produced using an asset could indicate the expectation of technical or commercial obsolescence of the asset, which, in turn, might reflect a reduction of the future economic benefits embodied in the asset.

d. legal or similar limits on the use of the asset, such as the expiry dates of related leases.

- The useful life of an asset is defined in terms of its expected utility to the enterprise. The asset management policy of the enterprise may involve the disposal of assets after as pecified time or after consumption of a specified proportion of the future economic benefits embodied in the asset. Therefore, the useful life of an asset may be shorter than its economic life. The estimation of the useful life of the asset is a matter of judgment based on the experience of the enterprise with similar assets.
- Land and buildings are separable assets and are accounted for separately, even when they are acquired together. With some exceptions, such as quarries and sites used for landfill, land has an unlimited useful life and therefore is not depreciated. Buildings have a limited useful life and therefore are depreciable assets. An increase in the value of the land on which a building stands does not affect the determination of the depreciable amount of the building.
- If the cost of land includes the costs of site dismantlement, removal and restoration, that portion of the land asset is depreciated over the period of benefits obtained by incurring those costs. In some cases, the land itself may have a limited useful life, in which case it is depreciated in a manner that reflects the benefits to be derived from it.

Depreciation Method:

- The depreciation method used should reflect the pattern in which the future economic benefits of the asset are expected to be consumed by the enterprise.
- The depreciation method applied to an asset should be reviewed at least at each financial year-end and, if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the method should be changed to reflect the changed pattern. Such a change should be accounted for as a change in an accounting estimate in accordance with AS 5.
- A variety of depreciation methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method and the units of production method. Straight-line depreciation results in a constant charge over the useful life if the residual value of the asset does not change. The diminishing balance method results in a decreasing charge over the useful life. The units of production method results in a charge based on the expected use or output. The enterprise selects the method that most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. That method is applied consistently from period to period unless there is a change in the expected pattern of consumption of those future economic benefits or that the method is changed in accordance with the statute to best reflect the way the asset is consumed.
- A depreciation method that is based on revenue that is generated by an activity that includes the use of an asset is not appropriate. The revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits of the asset. For example, revenue is affected by other inputs and processes, selling activities and changes in sales volumes and prices. The price component of revenue may be affected by inflation, which has no bearing upon the way in which an asset is consumed.

Changes in Existing Decommissioning, Restoration and Other Liabilities:

- The cost of property, plant and equipment may undergo changes subsequent to its acquisition or construction on account of changes in liabilities, price adjustments, changes in duties, changes in initial estimates of amounts provided for dismantling, removing, restoration and similar factors and included in the cost of the asset. Such changes in cost should be accounted for as under:

If the related asset is measured using the cost model:

- ✓ Changes in the liability should be added to, or deducted from, the cost of the related asset in the current period.
- ✓ The amount deducted from the cost of the asset should not exceed its carrying amount. If a decrease in the liability exceeds the carrying amount of the asset, the excess should be recognised immediately in the statement of profit and loss.
- ✓ If the adjustment results in an addition to the cost of an asset, the enterprise should consider whether this is an indication that the new carrying amount of the asset may not be fully recoverable. If it is such an indication, the enterprise should test the asset for impairment by estimating its recoverable amount, and should account for any impairment loss, in accordance with AS 28.

If the related asset is measured using the revaluation model:

- ✓ Changes in the liability alter the revaluation surplus or deficit previously recognised on that asset, so that:
  - a decrease in the liability should be credited directly to revaluation surplus in the owners' interest, except that it should be recognised in the statement of profit and loss to the extent that it reverses a revaluation deficit on the asset that was previously recognised in the statement of profit and loss;

    An increase in the liability should be recognised in the statement of profit and loss, except that it should be debited directly to revaluation surplus in the owners' interest to the extent of any credit balance existing in the revaluation surplus in respect of that asset.
- ✓ In the event that a decrease in the liability exceeds the carrying amount that would have been recognised had the asset been carried under the cost model, the excess should be recognised immediately in the statement of profit and loss.
- ✓ A change in the liability is an indication that the asset may have to be revalued in order to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date. Any such revaluation should be taken into account in determining the amounts to be taken to the statement of profit and loss and the owners' interest. If are valuation is necessary, all assets of that class should be revalued.

The adjusted depreciable amount of the asset is depreciated over its useful life. Therefore, once the related asset has reached the end of its useful life, all subsequent changes in the liability should be recognised in the statement of profit and loss as they occur. This applies under both the cost model and the revaluation model.

Impairment:

To determine whether an item of property, plant and equipment is impaired, an enterprise applies AS 28, Impairment of Assets. AS 28 explains how an enterprise reviews the carrying amount of its assets, how it determines the recoverable amount of an asset, and when it recognises, or reverses the recognition of, an impairment loss.

Compensation for Impairment:

- Compensation from third parties for items of property, plant and equipment that were impaired, lost or given up should be included in the statement of profit and loss when the compensation becomes receivable.
- Impairments or losses of items of property, plant and equipment, related claims for or payments of compensation from third parties and any subsequent purchase or construction of replacement assets are separate economic events and are accounted for separately as follows:
  - ✓ Impairments of items of property, plant and equipment are recognized in accordance with AS 28;
  - ✓ Derecognition of items of property, plant and equipment retired or disposed of is determined in accordance with this Standard;
  - ✓ Compensation from third parties for items of property, plant and equipment that were impaired, lost or given up is included in determining profit or loss when it becomes receivable; and
  - ✓ The cost of items of property, plant and equipment restored, purchased or constructed as replacements is determined in accordance with this Standard.

Retirements:

Items of property, plant and equipment retired from active use and held for disposal should be stated at the lower of their carrying amount and net realizable value. Any write-down in this regard should be recognised immediately in the statement of profit and loss.

Derecognition:

- The carrying amount of an item of property, plant and equipment should be derecognised
  - ✓ on disposal; or
  - ✓ when no future economic benefits are expected from its use or disposal.
- The gain or loss arising from the derecognition of an item of property, plant and equipment should be included in the statement of profit and loss when the item is derecognised (unless AS 19, Leases, requires otherwise on a sale and leaseback).Gains should not be classified as revenue, as defined in AS 9, Revenue Recognition.
- However, an enterprise that in the course of its ordinary activities, routinely sells items of property, plant and equipment that it had held for rental to others should transfer such assets to inventories at their carrying amount when they cease to be rented and become held for sale. The proceeds from the sale of such assets should be recognised in revenue in accordance with AS 9, Revenue Recognition.
- The disposal of an item of property, plant and equipment may occur in a variety of ways (e.g. by sale, by entering into a finance lease or by donation). In determining the date of disposal of an item, an enterprise applies the criteria in AS 19 for recognizing revenue from the sale of goods. AS 19, Leases, applies to disposal by a sale and lease back.
- If, under the recognition principle, an enterprise recognises in the carrying amount of an item of property, plant and equipment the cost of a replacement for part of the item, then it derecognises the carrying amount of the replaced part regardless of whether the replaced part had been depreciated separately. If it is not practicable for an enterprise to determine the carrying amount of the replaced part, it may use the cost of the replacement as an indication of what the cost of the replaced part was at the time it was acquired or constructed.
- The gain or loss arising from the derecognition of an item of property, plant and equipment should be determined as the difference between the net disposal proceeds, if any, and the carrying amount of the item.
- The consideration receivable on disposal of an item of property, plant and equipment is recognised in accordance with the principles enunciated in AS 9.

Disclosure:

- The financial statements should disclose, for each class of property, plant and equipment:
  - (a) the measurement bases (i.e., cost model or revaluation model) used for determining the gross carrying amount;
  - (b) the depreciation methods used;
  - (c) the useful lives or the depreciation rates used. In case the useful lives or the depreciation rates used are different from those specified in the statute governing the enterprise, it should make a specific mention of that fact;
  - (d) the gross carrying amount and the accumulated depreciation(aggregated with accumulated impairment losses) at the beginning and end of the period; and
  - (e) a reconciliation of the carrying amount at the beginning and end of the period showing: additions; assets retired from active use and held for disposal; acquisitions through business combinations; increases or decreases resulting from revaluations and from impairment losses; recognised or reversed directly in revaluation surplus in accordance with AS 28;impairment losses recognised in the statement of profit and loss in accordance with AS 28;impairment losses reversed in the statement of profit and loss in accordance with AS 28;depreciation;the net exchange differences arising on the translation of the financial statements of a non-integral foreign operation in accordance with AS 11, The Effects of Changes in Foreign Exchange Rates; and other changes.

- The financial statements should also disclose: the existence and amounts of restrictions on title, and property, plant and equipment pledged as security for liabilities; the amount of expenditure recognised in the carrying amount of an item of property, plant and equipment in the course of its construction; the amount of contractual commitments for the acquisition of property, plant and equipment; if it is not disclosed separately on the face of the statement of profit and loss, the amount of compensation from third parties for items of property, plant and equipment that were impaired, lost or given up that is included in the statement of profit and loss; and the amount of assets retired from active use and held for disposal.
- Selection of the depreciation method and estimation of the useful life of assets are matters of judgement. Therefore, disclosure of the methods adopted and the estimated useful lives or depreciation rates provides users of financial statements with information that allows them to review the policies selected by management and enables comparisons to be made with other enterprises. For similar reasons, it is necessary to disclose: depreciation, whether recognised in the statement of profit and loss or as a part of the cost of other assets, during a period; and accumulated depreciation at the end of the period.
- In accordance with AS 5, an enterprise discloses the nature and effect of a change in an accounting estimate that has an effect in the current period or is expected to have an effect in subsequent periods. For property, plant and equipment, such disclosure may arise from changes in estimates with respect to: residual values; the estimated costs of dismantling, removing or restoring items of property, plant and equipment; useful lives; and depreciation methods.
- If items of property, plant and equipment are stated at revalued amounts, the following should be disclosed: the effective date of the revaluation; whether an independent valuer was involved; the methods and significant assumptions applied in estimating fair values of the items; the extent to which fair values of the items were determined directly by reference to observable prices in an active market or recent market transactions on arm's length terms or were estimated using other valuation techniques; and the revaluation surplus, indicating the change for the period and any restrictions on the distribution of the balance to shareholders.
- An enterprise is encouraged to disclose the following: the carrying amount of temporarily idle property, plant and equipment; the gross carrying amount of any fully depreciated property, plant and equipment that is still in use; for each revalued class of property, plant and equipment, the carrying amount that would have been recognised had the assets been carried under the cost model; the carrying amount of property, plant and equipment retired from active use and not held for disposal.

Translation Provisions:

- Where an entity has in past recognized an expenditure in the statement of profit and loss which is eligible to be included as a part of the cost of a project for construction of property, plant and equipment in accordance with the requirements, it may do so retrospectively for such a project. The effect of such retrospective application of this requirement, should be recognised net-of-tax in revenue reserves.
- The requirements regarding the initial measurement of an item of property, plant and equipment acquired in an exchange of assets transaction should be applied prospectively only to transactions entered into after this Standard becomes mandatory.
- On the date of this Standard becoming mandatory, the spare parts, which hitherto were being treated as inventory under AS 2, Valuation of Inventories, and are now required to be capitalised in accordance with the requirements of this Standard, should be capitalised at their respective carrying amounts. The spare parts so capitalised should be depreciated over their remaining useful lives prospectively as per the requirements of this Standard.
- The requirements regarding the revaluation model should be applied prospectively. In case, on the date of this Standard becoming mandatory, an enterprise does not adopt the revaluation model as its accounting policy but the carrying amount of item(s) of property, plant and equipment reflects any previous revaluation it should adjust the amount outstanding in the revaluation reserve against the carrying amount of that item. However, the carrying amount of that item should never be less than residual value. Any excess of the amount outstanding as revaluation reserve over the carrying amount of that item should be adjusted in revenue reserves.

AS-11: THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES

The statement applies mandatorily in respect of:

(a) Accounting for transaction in foreign currencies

(b) Translating the financial statements of foreign branches for inclusion in the financial statements of the reporting enterprise.

A transaction in a foreign currency is recorded in the financial records of an enterprise normally at the rate

(a) On the date of transaction i.e. spot rate,

(b) Approximate actual rate i.e. averaging the rates during the week/month in which transactions occur if there is no significant fluctuations.

(c) Weighted average in the above line.

However, for interrelated transaction (by virtue of being set off against receivables and payables) it is translated with reference to the net amount on the date of transaction.

After initial recognition, the exchange difference on the reporting date of financial statement should be treated as under:

(a) Monetary items like foreign currency balance, receivables, payables, loans at closing rate (in case of restriction or remittance other than temporary or when the closing rate is unrealistic, it is reported at the rate likely to be realized).

(b) Non-monetary items like fixed assets, which are recorded at historical cost, should be made at the rate on the date of transaction.

(c) Non-monetary items other than fixed assets are carried at fair value or net realizable value on the date which they are determined i.e. B/S date (inventories, investments in equity-shares).

Exchange difference on repayment of liabilities incurred for acquiring fixed assets should be adjusted in the carrying amount of fixed assets on reporting date. The same concept applies to revaluation as well but in case such adjustment on revaluation should result into showing the actual book value of the fixed assets/or class of, exceeding the recoverable amount, the remaining amount of the increase in liability should be debited to Revaluation Reserve or P/L Statement in case of inadequacy/ absence of Revaluation Reserve.

Except as stated above (fixed assets) other exchange difference should be recognized as income or expense in the period in which they arise or spread over to pertaining accounting period.

Depreciation as per AS-6 should be provided on the unamortised carrying amount of depreciable assets (after taking into account the effect of exchange difference).

Disclosure under AS -11: An enterprise should disclose:

(a) The amount of exchange difference included in the net profit or loss for the period.

(b) The amount of exchange difference adjusted in the carrying amount of fixed assets during the accounting period.

(c) The amount of exchange difference in respect of forward contracts to be recognized in the profit/loss for one or more subsequent accounting period.

(d) Foreign currency risk management policy.

Illustration 8.

	Exchange Rate
Goods purchased on 24.3.15 of US $1,00,000	₹ 46.60
Exchange rate on 31.3.2015	₹ 47.00
Date of actual payment 5.6.2016	₹ 47.50

Calculate the loss/gain for the financial years 2014-15 and 2015-16.

Solution:

As per AS-11, all foreign currency transactions should be recorded by applying the exchange rate at the date of transaction. Therefore, goods purchased on 24.03.2015 and corr sponding creditor would be recorded at ₹ 46.60

= 1,00,000 x 46.60 = 46,60,000

As per AS-11, at the balance sheet date all monetary items should be reported using the closing rate. Therefore, the creditors of US $1,00,000 outstanding on 31.3.2015 will be reported as:

1,00,000 x 47.00= 47,00,000.

Exchange loss ₹ 40,000 (= 47,00,000 – 46,60,000) should be debited in Profit and Loss Account for 2014-15.

As per AS-11, exchange difference on settlement on monetary items should be transferred to Profit and Loss Account as gain or loss thereof:

1,00,000 x 47.50 = 47,50,000 -47,00,000 = ₹50,000 should be debited to profit or loss for the year 2014-15.

Illustration 9.

Z Ltd. acquired a machine on 1.4.2014 costing US $ 1,00,000. The suppliers agreed to the following terms of payment:

1.4.2014	:	down payment 50%
1.4.2015	:	25%
1.4.2016	:	25%

The company depreciates machinery @ 10% on the Straight Line Method. The rate of exchange is steady at US $ 1= ₹40 upto 30.9.2015. On 1.10.2015, due to an official revaluation of rates, the exchange rate is adjusted to US $ 1= ₹48.

Show the extracts of the relevant entries in the Profit and Loss Account for the year ending 31st March, 2016 and the Balance Sheet as on that date, showing such workings as necessary.

Working Notes:

2014-15:

1. Original Cost of the machine = $1,00,000 x ₹40 = ₹40,00,000
2. Depreciation (SLM) @ 10% = ₹4,00,000

2015-16:

1. Original Cost of the machine upto 30.9.2015 = ₹40,00,000

2. Revised cost of the machine as on 1.10.2015

Due to official revaluation of exchange rates, the US $ 1 = ₹48. There is a foreign exchange loss of ₹ 8 for each dollar liability. The total loss on foreign currency fluctuation was $25,000 x ₹8 = ₹2,00,000. This has to be added to the original cost of the machine. Therefore, revised cost of the machine as on 1.10.2015 is ₹42,00,000 (i.e. ₹40,00,000 + ₹2,00,000)

The revised cost of the machine as on 1.10.2015 :		₹
Original Cost on 1.4.2014		40,00,000
Less: Depreciation:		
1.4.2010 to 31.3.2015	4,00,000	
1.4.2011 to 30.9.2015	2,00,000	6,00,000
		34,00,000
Add: Loss on foreign exchange fluctuation as on 1.10.2015		2,00,000
		36,00,000
Depreciation:		
1.4.2015 to 30.9.2015	(40,00,000 x 10/100 x 6/12)	2,00,000
1.10.2015 to 31.3.2016	$\left(\frac{36,00,000 \times 6}{8.5 \times 12}\right)$	2,11,765
Total Depreciation for the year 2015-16		4,11,765

Note: As per AS-6 Revised, 'Depreciation Accounting', in case of change in historical cost due to foreign exchange fluctuation, depreciation on the revised unamortized depreciable amount should be provided prospectively over the residual life of the asset. In this case, the residual life is 8.5 years.

Profit and Loss Account (extract)

for the year ended 31st March, 2016

Particulars	₹	Particulars	₹
To Depreciation on Machinery	4,11,765		

Balance Sheet (extract) as at 31st March, 2016

Liabilities	₹	***Assets***		₹
Current Liabilities	12,00,000	Fixed Assets		
Creditors for Supply of Machinery		Machinery (at cost)	40,00,000	
		Add: Adj.for foreign		
		Exchange fluctuation	2,00,000	
			42,00,000	
		Less: Accumulated		
		Depreciation	8,11,765	
				33,88,235

AS -12: ACCOUNTING FOR GOVERNMENT GRANTS

Government refers to Union/State, Govt. Agencies and similar bodies - Local, National or International.

Grants also include subsidies, cash incentive, and duty drawback either in cash or kind/benefits to an enterprise on recognition of compliance in the past or future compliance with condition attached to it.

The accounting for the grant should be appropriate to reveal the extent of benefit accrued to the enterprise during the reporting period.

For the purpose of the statement, following are not dealt with.

(a) Effects of changing prices or in supplementary information

(b) Government assistance other than grants.

(c) Ownership participation by government.

In order to recognize the income there should be conclusive evidence that conditions attached to the grant have been or will be fulfilled to account for such earned benefits estimated on a prudent basis, even though the actual amount may be finally settled/received after the accounting period. Mere receipt would not suffice for income recognition.

AS-4 (contingencies etc) and AS-5 (Prior period etc) would be applicable as the case may be.

The accounting for Govt. grants should be based on the nature of the relevant grant:

(a) In the nature of promoter's contribution as shareholder's fund (capital approach)

(b) Otherwise as Income Approach to match with related cost recognizing AS-1 accrual concept disclosure.

Government grants in the form of non-monetary assets e.g. land or other resources is accounted for at the acquisition cost or recorded at nominal value if it is given free of cost.

Grants received specifically for fixed asset is disclosed in the financial statement either

(a) by way of deduction from the gross block of the asset concerned, thus grant is recognized in P/L Account through reduced depreciation (in case of funding of specific asset Cost entirely, the asset should be stated at a nominal value in B/S); or

(b) the grant treated as deferred revenue income and charged off on a systematic and rational basis over the useful life of the asset, until appropriated disclosed as "Deferred Govt. grant under Reserve and Surplus in the B/S (grants relating to depreciable assets should be credited to Capital Reserve and suitably credited to P/L Account to offset the cost charged to income).

Disclosure under AS-12

(a) the accounting policy, method of presentation in the financial statements.

(b) the nature and extent of Govt. grants recognized in the financial statements, including grants of non-monetary assets given at a concessional rate or free of cost.

Illustration 10.

Z Ltd. has set up its business in designated backward area which entitles it to receive as per a public scheme announced by the Government of India, a subsidy of 25% of the cost of investment. Having fulfilled the conditions laid down under the scheme, the company on its investment of ₹100 lakhs in capital assets during its accounting year ending on 31st March, 2015, received a subsidy of ₹25 lakhs in January, 2015 from the Government of India. The Accountant of the company would like to record the receipt as an item of revenue and to reduce the losses on the Profit and Loss Account for the year ended 31st March, 2015. Is his action justified?

Solution:

As per AS-12, the Government grants related to depreciable fixed assets to be treated as deferred income which should be recognized in the Profit and Loss Account on a systematic and rational basis over the useful life of the asset. Such grants should be allocated to income over the periods and in proportions in which depreciation on those assets is charged.

The company has received ₹25 lakhs subsidy for investment in capital assets which are depreciable in nature. In view of the provisions under AS-12, the subsidy amount ₹25 lakhs received should not be credited to the Profit and Loss Account for the year ended 31st March, 2015. the subsidy should be recognized and credited to the Profit and Loss Account in the proportion of depreciation charge over the life of the subsidized assets.

Illustration 11.

Hero Ltd. belongs to the engineering industry. The Chief Accountant has prepared the draft accounts, taking note of the mandatory accounting standards.

"The company purchased on 1.4.2014 a special purpose machinery for ₹50 lakhs. It received a Central Government grant for 20% of the price. The machine has an effective life of 5 years".

Solution:

AS-12 prescribes two methods in accounting treatment of Government grants for specific fixed assets.

Method I: Government grants related to depreciable fixed assets to be treated as deferred income which is to be recognized in the Profit and Loss Account in proportion in which depreciation on those assets is charged over the useful life of the asset. The deferred income pending its apportionment to Profit and Loss Account to be disclosed in the balance sheet separately with a suitable description,e.g. Deferred Government Grants, to be shown after "Reserves & Surplus" but before " Secured Loans".

AS-13: ACCOUNTING FOR INVESTMENTS

The Standard deals with accounting for investments in the financial statements of an enterprise and relevant disclosure requirement. Investments are assets held for earning income, capital appreciation or for other benefits to the investing enterprise, obviously investments held as 'stock-in-trade' are not 'Investments'.

The following are outside the purview of AS-13:

(a) Recognition of income on investment as dealt with under AS-9 (Revenue Recognition)

(b) Operating or Finance Lease.

(c) Investment of retirement benefit plans and Life Insurance Enterprise.

(d) Mutual fund, Asset Management Companies, Banks, Public Financial Institution, enacted under specific Act/ Companies Act, 2013.

Reasons, type, purposes etc varies widely and for this the standard is set to harmonize the accounting.

Cost of investment, means and includes,

(a) Acquisition charges e.g. brokerage, fees, duties etc.

(b) If acquired by issue of shares/securities, the acquisition cost is the fair market value, may be with reference to issue price determined by statutory authorities.

Fair market value may be determined with reference to market value or net realizable value (net of expenses to be incurred) or net of recovery of cost (dividend or interest accrued and included in the price of investments).

Current investment/Short term investment:

(a) Readily realizable and not intended to be held for more than a year from date of investment.

(b) The carrying amount on the reporting date is taken at lower of cost or fair value to prudently account for the unrealized losses but not the unrealized gains, considering individual or category of investments (not on overall basis).

(c) Any reduction to the fair value and any reversal to such reduction is included in the P/L Account.

Long-term investment:

(a) Investments held otherwise even if readily marketable are long term investments

(b) Intended to protect, facilitate and furtherance to existing operation, also known as Trade investments (not meant to provide additional cash resources)

(c) Long-term investments are normally carried at cost unless there is a permanent diminution in the value when the same is recognized in the carrying amount by charging or reversing through P/L Account.

(d) The carrying amount is determined on individual investment basis.

On disposal, the difference between the carrying amount and the net proceed of disposal is recognized in the P/L Account.

Investment in Property is in Land or Building, not intended for occupation substantially for use by or in the operation of the Investing Enterprise, should be treated as long-term investment.

Reclassification of Investments:

1) Long term to current : Take lower of cost and "carrying amount"

2) Current to Long term: Take lower of cost and " fair value"

Disclosure under AS-13:

(a) Accounting policy for determination of carrying amount

(b) Income separately for long-term and current investments, at gross i.e. inclusive of TDS.

(c) Profit or loss on disposal and changes in carrying amount separately for long term and current investments.

(d) Significant restrictions on the right of ownership, realisability of investments or the remittance of income and proceeds of disposal.

(e) The aggregate amount of quoted and unquoted investments and aggregate market value of quoted investments.

(f) other specific disclosure as required by Statute governing the enterprise, (e.g. Schedule III requires classifications to be disclosed in terms of Govt. or Trust securities, shares, debentures or bonds, investment properties others)

Illustration 12.

In preparing the financial statements of X Ltd.for the year ended 31st March, 2015, you come across the following information. State with reasons, how would you deal with them in the financial statements:

"An unquoted long term investment is carried in the books at a cost of ₹ 5 lakhs. The published accounts of the unlisted company received in June 2016 showed that the company was incurring cash losses with declining market share and the long term investment may not fetch more than ₹ 1 lakh".

Solution:

As per AS-13, the long term investments should be carried in the financial statements at cost. If there is a diminution in the value of long term investments, which is not temporary in nature, provision should be made for each investment individually. Any reduction in the carrying amount should be charged to the Profit and Loss Account.

The long term investments are carried at a cost of ₹ 5 lakhs in the books of accounts. The value of investments fall down to ₹ 1 lakh due to cash losses and the declining market share of the company in which the investments were made.

In view of the provision contained in AS-13, the carrying amount of long-term investments should be brought down to ₹ 1 lakh and ₹ 4 lakhs should be charged to Profit and Loss Account for the year ended 31st March, 2016.

Illustration 13.

A company has invested a substantial amount in the shares of another company under the same management. The market price of the shares of the aforesaid company is about half of that at which these shares were acquired by the company. The management is not prepared to provide for the fall in the value of shares on the ground that the loss is only notional till the time the shares are actually sold?

Solution:

As per AS-13, for the purpose of determining carrying amount of shares the investment has to be classified into long-term and current; in the instant case, it appears that the investment is long-term, hence it should be carried at

cost, unless there is a permanent diminution in value of investment. At the market price, investment is half of its cost. The reduction appears to be heavy and permanent, hence the provision for permanent diminution(decrease) in value of investment should be made. The contention of management is not as per AS-13.

Illustration 14.

MAGIC Bank has classified its total investment on 31.3.2015 into three categories: (a) held to maturity (b) available for sale (c) held for trading.

Held to maturity investment is carried at acquisition cost less amortised amount. Available for sale are carried at marked to market. Held for trading investments are valued at weekly intervals at market rates or as per the prices declared by FIMMDA. Net depreciation, if any, is charged to revenue and net appreciation, if any, is ignored. Comment on the policy of the bank in accordance with AS-13.

Solution:

As per para 2(d) of AS-13, the accounting standard is not applicable to bank, insurance company, mutual funds. In this case, MAGIC Bank is a bank, therefore AS-13 does not apply here. For the banks, the RBI has issued guidelines for classification and valuation of the investment. Therefore, the MAGIC Bank should comply with RBI guidelines.

AS -14: ACCOUNTING FOR AMALGAMATIONS

Amalgamation refers to an amalgamation as per the provision of the Companies Act, 2013 or any other law applicable to Companies. Sections 230 to 232 if Companies Act, 2013 governs the provisions of amalgamation.

Amalgamation may be categorized broadly as:

I) **Merger :** - genuine pooling of assets and liabilities and shareholder's interest of the amalgamation companies.

II) **Purchase:** - the shareholder of the acquired company do not continue to have proportionate share in the combined company or where the business of the former is not intended to be continued.

Amalgamation in the nature of merger:

(a) All the assets and liabilities of the transferor company are taken over by the transferee company.

(b) Such assets and liabilities are incorporated without any adjustment (except to ensure uniformity of accounting policies) in the financial statements of the transferee.

(c) At least 90 percent equity holders of transferor become equity shareholders of transferee by virtue of the amalgamation.

(d) The consideration for the amalgamation is discharged by equity shareholders in the transferee, except for fractional shares by cash.

(e) The business of the transferor is intended to be carried on by the transferee.

Amalgamation in the nature of Purchase:

Absence/non-fulfillment of one or more conditions as above will make the amalgamation in the nature of purchase.

Accounting methods:

1) **Merger - Pooling of interest method: -**

    (a) In preparing the balance sheet of the transferee company after amalgamation, line by line addition of the respective assets and liabilities of the transferor and transferee company should be made except for share capital;

    (b) If Purchase Consideration is **more** than Share capital(equity + preference) of the transferor company, the difference will be adjusted with Reserves. No goodwill can be created or recognized since there is no acquisition. If Purchase consideration is less than share capital, such shall be recognized as Capital Reserve, as per the Expert Advisory Committee (EAC) of the ICAI, April 2004.

2) **Purchase method:**

(a) The transferee record the assets and liabilities at their existing carrying amount or by allocating the consideration to individual identifiable assets and liabilities (even may be unrecorded in transferors' financial statements) at fair value on the date of amalgamation;

(b) If Purchase consideration is **more** than the value of net asset acquired by transferee be recognized as "Goodwill" in the financial statement. (if feasible and practicable, the goodwill is amortised over the useful life, otherwise over a period of not exceeding 5 years). In a **reverse** situation it is Capital Reserve which cannot be transferred to General Reserve.

(c) In case of amalgamation in the nature of purchase the identity of reserves other than Statutory Reserve (Development Allowance/ Investment Allowance Reserve under I.T Act), is not preserved.

Disclosure under AS-14 (in the first financial statement after the amalgamation)

(a) Names and general nature of business of the amalgamating companies

(b) Effective date of amalgamation for accounting purpose

(c) The method of accounting used

(d) Particulars of the scheme sanctioned under statute

(e) Additional disclosure for merger

1. Description and number of shares issued

2. Percentage of each company's equity shares exchanged under amalgamation

3. The amount of difference between the consideration and the value of net identifiable assets acquired and treatment thereof

(f) Additional disclosure under 'Purchase' method

1. Consideration for the amalgamation and a description of the consideration paid or contingently payable

2. Amount of difference as above and the treatment/amortization period for goodwill

(g) Where the scheme sanctioned under a statute prescribes a different treatment other than AS-14, for better understanding:

1. A description of the accounting treatment and reasons for variation with AS-14

2. Deviation in the accounting treatment as prescribed in he scheme under statute as compared to AS-14, if followed had there been no treatment prescribed by the scheme.

Illustration 15.

X Ltd. having a share capital of ₹ 20 lakhs and Y Ltd.having a share capital of ₹30 lakhs. Z Ltd. was formed to take over the business of X Ltd and Y Ltd. at a purchase consideration of ₹ 25 lakhs and ₹ 28 lakhs, payable in shares of Z Ltd. The assets and liabilities were taken at their carrying amounts.

Solution:

Since the purchase consideration is payable in shares of the transferee company and all the assets and liabilities are taken over at their carrying amounts, the amalgamation is in the nature of merger, i.e. pooling of interests method.

For X Ltd. Purchase consideration	= ₹ 25 lakhs
Less: Share capital of X Ltd	= ₹ 20 lakhs
Excess of purchase consideration	= ₹5 lakhs. This shall have to be adjusted against the Reserves of Z Ltd.
For Y Ltd. Purchase Consideration	= ₹28 lakhs
Less: Share Capital of Y Ltd	= ₹30 lakhs

since purchase consideration is less than share capital of the transferor company, ₹2 lakhs shall be treated as Capital Reserve.

Note: In case of amalgamation in the nature of purchase, goodwill shall have to be shown in the Balance Sheet of the Transferee company. Such goodwill shall have to be written off over a maximum period of 5 years.

Illustration 16.

Net Assets of the Transferor Campany : ₹ 20 lakhs. If Purchase Consideration is (i) ₹ 18 lakhs (ii) ₹23 lakhs & amalgamation is in the nature of purchase.

Solution:

(i) Net Assets ₹20 lakhs > Purchase Consideration ₹18 lakhs. So, ₹2 lakhs will be treated as Capital Reserve.

(ii) Net Assets ₹20 lakhs < Purchase Consideration ₹23 lakhs. So, ₹3 lakhs will be treated as Goodwill.

AS-15: EMPLOYEE BENEFITS

The statement applies to benefit usually comprising of Provident Fund, Superannuation/Pension Fund, Gratuity, Leave encashment or retirement, Post retirement health and welfare schemes and other benefits provided by an employer to employees either in pursuance of legal requirement or otherwise, but does not extend to employers' obligation which cannot be reasonably estimated (e.g. ex-gratia ad-hoc on retirement).

There may be obligation on the part of the employer either against defined contribution plan or defined benefit schemes as elaborated below:

a) Defined Contribution Plans (DCP):

  1) Retirement benefit is determined by contribution at agreed/specified rate to the Fund together with earnings thereof.

  2) Contribution (e.g. PF) whether paid or payable for the reporting period is charged to P/L statement

  3) Excess if any is treated as prepayment

b) Defined Benefit Plans (DBP):

  1) Amount paid is usually determined with reference to employee's earnings and/or years of service (if the basis of contribution are determined, it will be treated as defined contribution scheme)

  2) However, if the employer's responsibility is subject to specified benefits or a specified level of benefits, it is defined benefit scheme.

  3) The extent of employer's obligation is largely uncertain and subject to estimation of future condition and events beyond control.

Accounting treatment for Gratuity benefit and other defined benefit schemes depends on the arrangement made by the employer:

(a) No separate fund i.e. out of nonspecific own fund:

  1) Provision for accruing liability in the P/L Account for the accounting period is made.

  2) The provision is based on an actuarial method or some other rational method (assumption that all employers are eligible at the end of the accounting period)

(b) *Own separate/specific fund established through Trust:*

The amount required to be contributed on actuarial basis is certified by the Actuary, and the actual contribution plus and shortfall to meet the actuarial amount is charged to P/L Account for the accounting period, any excess payment treated as prepayment.

(c) *Fund established through Insurer:* in the same manner as in (b) above

Actual valuation may be carried out annually (cost can be easily determined for the purpose of contribution as a charge to P/L) or periodically (say, once in 3 years) where Actuary's certificate specifies contribution on annual basis during inter-valuation period.

Leave encashment is an accrued estimated liability based on employers' past experience as to such benefit actually availed off and probability of encashment in future and therefore should relate to the period in which relevant service is rendered in compliance with section 128 - accrual basis and AS-15.

Disclosure under AS-15:

(a) In view of the varying practices, adequate disclosure of method of accounting for an understanding of the significance of such costs to an employer.

(b) Disclosure separately made for statutory compliance or otherwise the retirement benefit costs are treated as an element of employee remuneration without specific disclosure.

(c) Financial statements should disclose whether actuarial valuation is made at the end of the accounting period or earlier (in which case the date of actuarial valuation and the method used for accrual period if not based on actuary report).

Treatment of Voluntary Retirement scheme payments:

1) Termination benefits to be paid irrespective of the voluntary retirement scheme i.e. balance in P.F, leave encashment; gratuity etc.

2) Termination benefits which are payable on account of VRS i.e. monetary payment on the basis of years of completed service or for the balance period of service whichever is less and notice pay.

Expert Advisory Committee (EAC) opines in favour of treating the costs (except gratuity which should have been provided for in the respective accounting period) as deferred revenue expenditure since it is construed upon as saving in subsequent periods, on some rational basis over a period, preferably over 3 - 5 year. However, the terminal benefit is, to the extent these are not deferred should be treated as expense in the P/L Account with disclosure.

Illustration 17.

ZERO Bank has followed the policies for retirement benefits as under:

(a) contribution to pension fund is made based on actuarial valuation at the year end. In respect of employees who have opted for pension scheme.

(b) Contribution to the gratuity fund is made based on actuarial valuation at the year end.

(c) Leave encashment is accounted for on "PAY-AS-YOU-GO" method.

Comment whether the policy is in accordance with AS-15.

Solution:

(a) As the contribution to Pension Fund is made on actuarial basis every year, there fore the policy is as per AS-15, which is based on actuarial basis of a counting.

(b) As the contribution is being made on annual basis to gratuity fund on actuarial basis, the policy is in accordance with AS-15.

(c) As regard leave encashment, which is accounted for on PAY-AS-YOU-GO basis, it is not in accordance with AS-15. It should be accounted for on accrual basis.

Illustration 18.

In the context of relevant Accounting Standards, give your comment on the following matter for the financial year ending 31st March, 2015:

"Increase in pension liability on account of wage revision in 2014-15 is being provided for in 5 instalments commencing from that year. The remaining liability of ₹300 lakhs as redetermined in actuarial valuation will be provided for in the next 2 years"

Solution:

As per AS-15, the costs arising from an alteration in the retirement benefits to employees should be treated as follows:

(i) The cost may relate to the current year of service or to the past years of service.

(ii) In case of costs relating to the current year, the same may be charged to Profit and Loss Account

(iii) Where the cost relates to the past years of service these should be charged to Profit and Loss Account as 'prior period' items in accordance with AS-5.

(iv) Where retirement benefit scheme is amended in a manner which results in additional benefits being provided to retired employees, the cost of the additional benefits should be taken as " Prior Period and Extraordinary Items" as per AS-5.

In view of the above, the method adopted for accounting the increase in pension liability is not in consonance to the provisions mentioned in AS-15.

AS-16: BORROWING COST

Borrowing costs are interests and other costs incurred by an enterprise in connection with the borrowing of funds.

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

Examples of qualifying assets:

- Any tangible fixed assets, which are in construction process or acquired tangible fixed assets, which are not ready for use or resale. Such as plants and machinery.
- Any intangible assets, which are in development phase or acquired but not ready for use or resale, such as patent.
- Investment property.
- Inventories that require a substantial period(i.e. generally more than one accounting period) to bring them to a saleable condition.

The Statement is applied in accounting for borrowing costs which include:

1. Interest and commitment charges on bank borrowing and other short term borrowings
2. Amortization of discounts/premium relating to borrowings
3. Amortization of ancillary cost incurred in connection with arrangement of borrowings
4. Finance charges for assets acquired under finance lease or other similar arrangement
5. Exchange difference in foreign currency borrowing to the extent it relates to interest element

Borrowing cost incurred on assets, which takes substantial period, is treated as cost of that asset in respect of (1) above.

As per the Guidance Note on Audit of Miscellaneous Expenditure issued by ICAI, deferment for amortization cost upto the time the asset is put to use, in respect of (2) and (3), should be capitalized (see below for AS-16 provision).

Finance charges as in (4) can be capitalized upto the time the asset is put to use (AS-19 deals with elaborate provision)

Conditions for capitalization of borrowing costs:

- Directly attributable costs for acquisition, construction or production of qualifying asset, are eligible for capitalization.
- Qualifying assets will render future economic benefit to the enterprise and the cost can be measured reliably.

Amount of borrowing costs eligible for capitalization (specific borrowing):

- Amount of borrowing eligible for capitalization = Actual borrowing cost incurred during the period less income generated on the temporary investment of amount borrowed.

All other borrowing costs are charged to P/L Account:

AS-16 establishes a key test for capitalization which states that "borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are those costs that would have been avoided if the expenditure on the qualifying asset had not been made".

Accounting treatment of borrowing cost as per AS-16:

(a) Borrowing costs should either be capitalized or charged to P/L Account depending on the situation but deferment is not permitted.

(b) Borrowing costs are capitalized as part of cost of qualifying asset when it is probable that they will result in future economic benefits and cost can be measured reliably - other borrowing costs are charged to P/L Account in the accounting period in which they are incurred.

(c) Capitalization, on one hand reflects closely the total investment in the asset and on the other hand to charge the cost to future period against accrual of revenue.

(d) Notional interest cost are not allowed to be capitalized.

(e) A qualifying asset is an asset that necessarily takes a substantial period of time (usually a period of 12 months unless otherwise justified on the basis of facts and circumstances) to get ready for its intended use or sale.

(f) Capitalization should be suspended during extended period in which active development is interrupted.

(g) Capitalization should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

(h) Capitalization also ceases 'when part is completed, which is capable of being used independent of the whole.

Disclosure under AS- 16

(a) Accounting Policy adopted

(b) Amount of borrowing cost capitalized during the accounting period

Illustration 19.

A company capitalizes interest cost of holding investments and adds to cost of investment every year, thereby understating interest cost in profit and loss account. Whether it leads to unusual accounting?

Solution:

The Accounting Standard Board (ASB) has opined that investments other than investment properties are not qualifying assets as per AS-16, Borrowing Costs. Therefore, interest cost of holding such investments cannot be capitalized. Further, even interest in respect of investment properties can only be capitalized if such properties meet the definition of qualifying assets, namely, that it necessarily takes a substantial period of time to get ready for its intended use or sale, even where the investment properties meet the definition of "qualifying asset", for the capitalization of borrowing costs the other requirements of the standard such as that borrowing costs should be directly attributable to the acquisition or construction of the investment property and suspension of capitalization as per paragraphs 17 and 18 of AS-16 have to be complied with.

Illustration 20.

X Ltd. has obtained an institutional loan of ₹ 800 lakhs for modernization and renovation of its machinery. Machinery acquired under the modernization scheme and installation completed on 31.3.15 amounts to ₹ 600 lakhs. ₹ 80 lakhs has been advanced to suppliers for additional assets and balance loan of ₹120 lakhs has been utilized for working capital purpose. The total interest paid for the above loan amounted to ₹80 lakhs during 2014-15.

You are required to state how the interest on the institutional loan is to be accounted in the year 2014-15.

Solution:

The total interest of ₹80 lakhs is related to two periods. Upto the date of installation of the machinery, amount disbursed is ₹680 lakhs(₹600 + 80). Interest on such amounting to ₹68 lakhs should be capitalized and the balance of the interest ₹12 lakhs (i.e. ₹80-68) should be treated as an expense.

Illustration 21.

Happy Ltd.has taken a loan of US $10 lakhs on 1st April, 2014, for a specific project at an interest rate of 10% p.a., payable annually. On 1st April, 2014, the exchange rate between the currencies was ₹45 per US $. The exchange rate, as at 31st March, 2015, is ₹ 48 per US $. The corresponding amount could have been borrowed by Happy Ltd. in local currency at an interest rate of 15% p.a. as on 1st April, 2014.

The following computation would be made to determine the amount of borrowing costs for the purposes of paragraph 4(e) of AS-16.

(a) Interest for the period = US $10,00,000 x 10% x ₹48 per US $ = ₹ 48,00,000

(b) Increase in the liability towards the principal amount = US $ 10,00,000 x (48-45)= ₹30,00,000.

(c) Interest that would have resulted if the loan was taken in Indian currency = US $ 10,00,000 x 45 x 15% = ₹67,50,000

(d) Difference between interest on local currency borrowing and foreign currency borrowing = ₹67,50,000 – ₹ 48,00,000 = ₹ 19,50,000

Therefore, out of ₹30,00,000 increase in the liability towards principal amount, only ₹ 19,50,000 will be considered as the borrowing cost. Thus, total borrowing cost would be ₹67,50,000 being the aggregate of interest of ₹48,00,000 on foreign currency borrowings (as per Para 4(a) of AS-16) plus the exchange difference to the extent of difference between interest on local currency borrowing and interest on foreign currency borrowing of ₹19,50,000. Thus, ₹67,50,000 would be considered as the borrowing cost to be accounted for as per AS-16 and the remaining ₹10,50,000 would be considered as the exchange difference to be accounted for as per AS-11 "The Effects of Changes in Foreign Exchange Rates".

Illustration 22.

On 30.4.2015 MNC Ltd.obtained a loan from the bank for ₹50 lakhs to be utilized as under:

(i)	Construction of a factory shed	₹2 crores.
(ii)	Purchase of Machinery	₹ 1.5 crores.
(iii)	Working Capital	₹ 1 crore.
(iv)	Advance for Purchase of truck	₹ 50 lakhs.

In March 2011, construction of shed was completed and machinery installed. Delivery of truck was not received. Total interest charged by the bank for the year ended 31.3.15 was ₹90 lakhs. Show the treatment of interest as per AS-16.

Solution:

As per AS-16, borrowing cost(interest) should be capitalized if borrowing cost is directly attributable to the acquisition, construction or production of qualifying asset. ₹5 crores borrowed from Bank was utilized for four different purposes, only construction of factory shed is a qualifying asset as per AS-16, while the other three payments are not for the qualifying asset. Therefore, borrowing cost attributable to the construction of a factory shed should only be capitalized which will be equal to ₹ 90 lakhs x 2/5= ₹36 lakhs.

The balance of ₹ 54 lakhs (₹90 lakhs – ₹36 lakhs) should be treated as an expense and debited to Profit and Loss Account.

AS 17: SEGMENT REPORTING

In view of the complexities of types of businesses, the aggregated financial information is not adequate to evaluate a company's and management's operating and financial strategies with regard to specific or distinct line of activities i.e. segment. As an enterprise deals in multi-product/ multiple services and operates in different geographical areas, the degree of risk and return also varies considerably.

Segment information will enable the users to understand better and also to assess the underlying risks and returns of an enterprise.

Initially the segment needs to be broadly classified into either 'Business Segments' or 'Geographical Segments' before being slotted as 'Primary' or 'Secondary' for reporting in the financial statements as per AS- 7.

A 'Business Segment' is a distinguishable component of an enterprise that is engaged in providing an individual product or service or a group of products or services, and that is subject to risk and return as distinctly different from those of other business segments. For grouping related products or services, following factors are considered:

(a) The nature of product/service;

(b) The nature of production processes (e.g. labour or capital intensive);

(c) The type or Class of customer (e.g. gender, income).

(d) The method used to describe the products or provide services (e.g. wholesaler, franchisee, dealer) similarity of economic and political condition relationship between operations in different geographical areas proximity of operation special risks associated with operation in a particular area exchange control regulation underlying currency risk (geographical location means the location of production or service facilities and other assets of an enterprise and the location of markets and customers).

(e) Nature of regulatory environment e.g. insurance, banking, public utilities etc the majority of the factors will be considered to form a single segment even though, there may be dissimilarities and a single business segment does not include products and services with significant differing risks and returns (risk in investment and potential earnings as reward).

A 'Geographical segment' is a distinguishable component of an enterprise that is engaged in providing products or services within a particular economic environment and that is subject to risk and returns that are different from those of components operating in other economic environments. Factors for identification of geographical segments are:

(a) Significant difference in risk and rewards;

(b) Internal MIS and organization structure;

(c) Essential factors that defines a business segment.

Segment accounting policies: AS-17 does not require that the enterprise apply accounting policies to reportable segments on stand-alone reporting entities, hence, additional segment information may be disclosed provided that:

(i) Information is reported internally to the Board or CEO for the purpose of making decisions about allocating resources to the segment and assessing its performance.

(ii) The basis of measurement for additional information is closely described.

Segment Revenue is the aggregate of the portion of enterprise's total revenue that is attributable to a segment on a reasonable basis as distinct from other segments including inter-segment transfer with the exception of

(a) extra ordinary item as AS-5

(b) income by way of interest/dividend etc unless the operation of the segments are primarily of a financial nature

(c) gains or sale of investment or on extinguishments of debts unless the operation of the segment, are primarily of a financial nature

Inter-segment transfer should be made on the basis that is actually used to price those transfers i.e. at cost, below cost or market price and the same should be disclosed and followed consistently.

Segment result is segment revenue less segment expense

Segment Assets comprise of directly attributable or reasonably allocable operating asset to the segment as reduced by related allowances or provisions pertaining to those assets including allocable common assets, however exclude:

(a) income tax asset

(b) general enterprise asset/H.O asset

Segment liabilities are worked out or above basis but excluding:

(a) income tax liabilities

(b) general enterprise liabilities/H.O lease liabilities.

For primary segment disclosure required for:

(a) segment revenue with a break-up of sales to external customers and inter segment result deduction made to arrive at segment result in respect of total amount of non cash expenses (provisions, unrealized foreign exchange gain/loss as included in segment expenses);

(b) total amount of depreciation and amortization in respect of segment assets (not required if cash flow of the enterprise reports operating, investing and financing activities;

(c) total carrying amount of segment assets;

(d) total amount of segment liabilities;

(e) total cost incurred during the period to acquire segment assets that are expected to be used for more than one period (both fixed assets and intangible assets).

For secondary segment, disclosure required for:

(a) If primary format for reporting segment is business segment, it should also report;

1. segment revenue from external customers by geographical location of customers for each geographical segment consisting 10 percent or more of enterprise revenue.

2. total carrying amount of segment assets, by geographical location of assets for each of such geographical segment accounting for 10 percent or more of the total assets of all geographical segments.

3. total cost incurred during the accounting period to acquire segment assets, which are expected to be used for more than one accounting period with 10 percent more criteria as in the aforesaid line.

(b) where primary format is geographical, disclosure also required for each business segment accounting for 10 percent or more of revenue from sales to external customers of enterprises' total revenue or whose segment assets are 10 percent or more of the total assets of all business segments:

1. segment revenue from external customers
2. total carrying amount of segment assets
3. total cost incurred during the accounting period to acquire segment assets with expected use extending beyond one accounting period (both tangible and intangible) of all geographical location where geographical segment used for primary format is based on a location, of assets which is different from location of customers.

Additional disclosure required for

1) revenue from sales to external customers for each customer based geographical segment whose revenue from sales to external customers constitutes 10 percent or more of enterprise's revenue.

2) in a reverse situation, disclosure for

   (i) total carrying amount of segment assets by geographical location of assets

   (ii) total cost incurred during the accounting period to acquire segment assets expected to be used for more than one accounting period both tangible and intangible by location of assets.

Illustration 23.

M/S ABC Ltd. Has three segments namely A, B, C. The total assets of the company are ₹ 10.00 crs. Segment A has ₹ 2.00 crs. Segment B has ₹ 3.00 crs and Segment C has ₹ 5.00 crs. Deferred tax assets included in the assets of each segments are A – ₹ 0.50 crs. B- ₹ 0.40 crs. C- ₹ 0.30 crs. The accountant contends that al the three segments are reportable segments. Comment.

Solution:

According to AS-17 "Segment Reporting, segment assets do not include income tax assets. So, assets of

Segment A = 2.00 – 0.50 =	₹ 1.50 crs.
Segment B = 3.00 – 0.40 =	₹ 2.60 crs.
Segment C = 5.00 – 0.30 =	₹ 4.70 crs.
Total Segment Assets	₹ 8.80 crs.

Since each segment's assets is more than 10% of total segment assets (i.e. ₹ 0.88 crs.) all segments are reportable segments.

Illustration 24.

M Ltd. Group has three divisions A, B and C. Details of their turnover, results and net assets are given below:

	₹ ('000)
Division A	
Sales to B	9,150
Other Sales (Home)	180
Export Sales	12,270
	21,600
Division B	
Sales to C	90
Exports Sales to Europe	600
	690
Division C	
Export Sales to America	540

	Head Office ₹ ('000)	A ₹ ('000)	B ₹ ('000)	C ₹ ('000)
Operating Profit or Loss before tax		480	60	(24)
Re-allocated cost from Head Office		144	72	72
Interest cost		12	15	3
Fixed assets	150	600	120	360
Net current assets	144	360	120	270
Long-term liabilities	114	60	30	360

Prepare a Segmental Report for publication in M Ltd. Group.

Solution:

M Ltd.

Segmental Report

(₹ in '000)

	Division				
Segment Revenue	A	B	C	Inter segment Eliminations	Consolidated Total
Sales:					
Domestic	180				180
Export	12,270	600	540		13,410
External Sales	12,450	600	540		13,590
Inter-segment Sales	9,150	90		9,240	
Total Revenue	21,600	690	540	9,240	13,590
Segment result (given)	480	60	(24)		516
Head office expenses					(288)
Operating profit					228
Interest expenses					(30)
Profit before tax					198
Other information:					
Fixed assets	600	120	360		1,080
Net current assets	360	120	270		750
Segment assets	960	240	630		1,830
Unallocated corporate assets					294
Segment liabilities	60	30	360		450
Unallocated corporate liabilities					114

Sales Revenue by Geographical Market

(₹ in '000)

	Home Sales	Export Sales (by division A)	Export to Europe	Export to America	Consolidated Total
External Sales	180	12,270	600	540	13,590

Illustration 25.

Identify the reportable segment by profitability test is demonstrated as follows for XYZ Ltd.

Segment	Prof it (Loss)
A	450
B	50
C	(350)
D	(40)
E	(210)

Solution :

First, the operating segments are grouped accordi ng to whether they incurred a profit or loss, as follows :

Segments Incurring Profits		Segments Incurring Losses	
Segment	Profit (₹)	Segment	Loss (₹)
A	450	C	(350)
B	50	D	(40)
	-	E	(210)
	500		600

From this point on the profitability test, only absolute amounts are used. The combined total of those segments incurring a loss is larger than the combined total of those segments incu rring a profit. Therefore, any segment for which the absolute amount of its operating profit or loss equals or exceeds ₹ 60 (i.e., 10% of ₹ 600) meets the profitability test and is therefore a reportable segment. Segments A, C and E meet the profitability test, summarized as follows :

Operating Segment	Absolute amount of Profit or loss	₹ 60	
A	450	Yes	(reportable segment)
B	50	No	
c	350	Yes	(reportable segment)
D	40	No	
E	210	Yes	(reportable segment)

If the total external reven ue (*i.e.,* sales to unaffiliated customers) of the reportable segments is less than 75% of total consolidated revenue, additional operating segments must be identified as reportable segments (even if they do not otherwise qualify as a reportable segment) until at least 75% of total consolidated revenue is included in reportable segments.

Information about all operating segments that did not qualify as reportable segments must be combined and disclosed in an "all other" category.

If an operating segment was identified in the immediately preceding prior period as a reportable segment and management deems that segment to be of continuing significance, information about that segment should continue to be reported separately in the current period even if that segment does not otherwise qualify as a reportable segment in the current period.

If an operating segment qualifies in the current period as a reportable segment but did not qualify as a reportable segment in the prior period(s), prior-period segment data presented for comparative purposes should be restated as if the segment qualified as a reportable segment in the prior period(s).

Illustration 26.

The Chief Accountant of Sports Ltd. gives the following data regarding its six segments:

Particulars	M	N	0	p	Q	R	Total
Segment Assets	40	80	30	20	20	10	200
Segment Result	50	-190	10	10	-10	30	-100
Segment Revenue	300	620	80	60	80	60	1200

The Chief Accountant is of the opinion that segments "M" and "N" alone should be reported. Is he justified in his view? Discuss.

Solution:

No, he is not justified in his view, because as per Para 27 of AS-17 "Segment Reporting", Business Segment or geographical segment which has been identified as reportable segment shall be further divided to include sub-segments based on the following conditions:

+ Segment revenue from sales to external customers and internal transfer is

10% or more than total external and internal revenue of all segments.

Or

+ 10% or more of segment result

+ (Segment result means: if some segments are in loss then total loss of all loss making segments or if some segments are profit, total profit of all profit making segments. Whichever is higher *i.e.,* total profit or total loss figure in absolute term.)

Or

+ Segment asset is 10% or more than total assets of all segments.

+ Ensure whether at least 75% of total external revenue should be in the reportable segments.

In the question, the segments "M" and "N" are reportable segments on the basis of 10% of more segment revenue other two criteria should also be applied to make reportable segment as per AS-17. I0% of segment result which is 20 or more (loss) (190+10) × 10%. By these criteria "R" is also reportable segment. As per the 1096 or more asset criteria "0", "P" and "Q" also becomes the reportable segments; therefore all the 6 segments should be reportable segments.

AS -18: RELATED PARTY DISCLOSURE

The scope and objective of the standard is to establish requirements for disclosure of (a) related party relationship (b) transaction between a reporting enterprise and its related parties.

This disclosure would make the financial statements of the reporting enterprise more transparent and allow the users to compare both intra-enterprise with corresponding earlier accounting period and inter-enterprise as well.

However disclosure is not required

(i) if there is statutory bar on the reporting enterprise on confidentiality (banks) in respect of constituents

(ii) in case of consolidated financial statements in respect members of the group (holding & subsidiary) with exception for transaction with Associated Enterprise accounted for under equity method

(iii) in the financial statement of State (Central or State) controlled enterprises with other state controlled enterprise even related party relationship exists. When parties are considered related?

If at any time during the reporting period one party has the ability

(a) to control the other party

(b) to exercise significant influence over the other party in making financial and/or operating decisions, then by virtue of AS -18 both parties would be considered as related.

Definition

(a) Control:

  (i) ownership directly or indirectly, of more than 50 percent of the voting power of an enterprise

  (ii) the composition of the board of directors (company) or the Governing Body (other enterprise)

  (iii) a substantial interest in voting power and the power to direct by Statute or by agreement, the financial/ operating policies of the enterprise (20 percent or more interest in voting power)

(b) Significant Influence:

  (i) refers to participation in the financial and/or operating policy decisions of an enterprise but not control of those policies.

  (ii) may be gained by ownership in share (including investment through intermediaries restricted to mean subsidiaries as defined in AS-21 Consolidated Financial Statement)

Related party disclosures are applicable only to the following related party relationships:

1. enterprises that directly or indirectly through one or more intermediaries control or are controlled by or under common control with the reporting enterprise

2. associates and joint venturers of the reporting enterprise and the investing party or venturer in respect of which the reporting enterprise is an associate or joint venturer,.

3. individuals owning directly or indirectly an interest in the voting power of the reporting enterprise that gives them control or significant influence over the enterprise and relatives of any such individual.

4. key management personnel and relatives of such individuals.

5. enterprise over which any person in (3) and (4) is able to exercise significant influence (including enterprise owned by directors or major shareholders of the reporting enterprise and enterprise that have a member of key management in common with the reporting enterprise).

Related party transactions involve transfer of resources or obligations between related parties, regardless of whether or not .a price is charged, e.g. use of logo/brand name provision of management services, providing financial guarantee use of common infrastructure etc.

Type of disclosure under AS-18

(a) in case of related party relationship by virtue of significant influence (not control) e.g. those of associates, key management personnel, relatives, there is no need. to disclose the related party relationship unless there have been actual transaction during the reporting period with such related parties.

(b) in the event of transaction between related parties during the existence of a related party relationship (control or significant influence) the reporting enterprise should disclose:

  (i) the name of transacting related party

  (ii) description of the relationship between parties

  (iii) description of nature of transaction

  (iv) volume of transaction, either in amount or approximate proportions

  (v) any other element of the related party transactions necessary for understanding of financial statements (e.g. transfer of major asset taken at price different from normal commercial terms i.e. not at fair value)

(vi) either in amount or proportion of outstanding items and provisions for doubtful debts pertaining to related parties on B/S date.

(vii) amounts written off/back in the accounting period in respect of debts due from or to related parties.

AS -19: LEASES

Lease is an arrangement by which the "Lessor" gives the right to use an asset for given period of time to the "Lessee" on rent.

It involves two parties, a Lessor and a Lessee and an asset which is to be leased. The Lessor, who owns the asset, agrees to allow to the Lessee to use it for a specified period of time in return for periodic rent payments.

Types of lease

(a) ***Finance Lease*** – It is a lease, which transfers substantially all the risks and rewards incidental to ownership of an asset to the Lessee by the Lessor but not the legal ownership. In following situations, the lease transactions are called Finance Lease.

- The lessee will get the ownership of leased asset at the end of the lease term.
- The lessee has an option to buy the leased asset at the end of term at price, which is lower than its expected fair value at the date on which option will be exercised.
- The lease term covers the major part of the life of asset.
- At the beginning of lease term, present value of minimum lease rental covers substantially the initial fair value of the leased asset.
- The asset given on lease to lessee is of specialized nature and can only be used by the lessee without major modification.

(b) ***Operating Lease*** – It is a lease which does not transfer substantially all the risk and reward incidental to ownership.

Classification of lease is made at the inception of the lease; if at any time the Lessee and Lessor agree to change the provision of lease and it results in different category of lease, it will be treated as separate agreement.

Applicability

The Accounting Standard is not applicable to following types of lease:

- Lease agreement to explore natural resources such as oil, gas, timber, metal and other mineral rights.
- Licensing agreements for motion picture film, video recording, plays, manuscripts, patents and other rights.
- Lease agreement to use land.

Definitions

1. Guaranteed Residual value – (G.R.V.)

- **In respect of Lessee:** Such part of the residual value (R.V.), which is guarantee by or on behalf of the lessee.
- **In respect of Lessor:** Such part of the residual value, which is guaranteed by or on behalf of the lessee or by an independent third party.

For the Lessor the residual value guaranteed by the third party can arise when the asset is leased to the third party after the first lease has expired and therefore it can be called the residual value guaranteed by the third party to the Lessor.

2. ***Unguaranteed Residual Value (U.R.V)*** – The difference between residual value of asset and its guaranteed residual value is unguaranteed residual value. [R.V- G.R.V.]

3. ***Gross Investment (MLP+URV)*** – Gross investment in lease is the sum of the following:
   - Minimum lease payment (from the standpoint of Lessor) and
   - Any unguaranteed residual value accruing to the Lessor.
4. ***Interest rate implicit in the lease*** – When the Lessor gives an asset on lease (particularly on finance lease), the total amount, which he receives over lease period by giving the asset on lease, includes the element of interest plus payment of principal amount of asset. The rate at which the interest amount is calculated can be simply called implicit rate of interest. It can be expressed as under:-

It is the discount rate at which

Fair Value of leased Asset = Present value of [Minimum lease payment (in respect of Lessor)]

(At the inception of lease) + Any unguaranteed residual value accruing to the Lessor.

5. ***Contingent Rent*** – Lease Rent fixed on the basis of percentage of sales, amount of usage, price indices, market rate of interest is called contingent rent. In other words, lease rent is not fixed, but it is based on a factor other than time.
6. ***Minimum lease payments [MLP]***
   - For Lessor = Total lease rent to be paid by lessee over the lease terms + any guaranteed residual value (by or on behalf of lessee) – contingent Rent – cost for service and tax to be paid by the reimbursed to Lessor + residual value guaranteed by third party.
   - For Lessee = Total lease rent to be paid by lessee over the lease terms + any guaranteed residual value (for lessee) – contingent rent – cost for service and tax to be paid by and reimbursed to Lessor.
7. ***Lease includes Hire Purchase*** – The definition of a 'lease' includes agreements for the hire of an asset, which contain a provision giving the hirer an option to acquire title to the asset upon the fulfillment of agreed conditions. These agreements are commonly known as hire purchase agreements.

Accounting for Finance Lease – In the books of Lessee

- Leased asset as well as liability for lease should be recognized at the lower of –
  - ✓ Fair value of the leased asset at he inception of lease or
  - ✓ Present value of minimum lease payment from the lessee point of view.
- Apportionment of lease payment-Each lease payment is apportioned between finance charge and principal amount.
- The lessee in its books should charge depreciation on finance lease asset as per AS-6(in this case, straight line method will be followed)
- Initial direct cost for financial lease is included is asset under lease.

Accounting for Finance Lease – In the books of Lessor

- The Lessor should recognize asset given under finance lease as receivable at an amount equal to net investment in the lease and corresponding credit to sale of asset.

  Net Investment = Gross Investment – Unearned Finance Income.

  Gross Investment = Minimum lease payment from Lessor point of view + Unguaranteed residual value.

  Unearned Finance Income=Gross Investment – Present Value of Gross Investment.

- Recognition of Finance Income

  The Lessor should recognize the finance income based on a pattern reflecting, constant periodic return on the net investment outstanding in respect of the finance lease. In simple words interest / finance income will be recognized in proportion to outstanding balance receivable from lease over lease period.

Accounting for Operating Lease- In the books of Lessor:

- Record leased out asset as the fixed asset in the balance sheet.
- Charge depreciation as per AS-6
- Recognize lease income in profit & loss account using straight line method. If any other method reflects more systematic allocation of earning derived from the diminishing value of leased out asset, that approach can be adopted.
- Other costs of operating lease should be recognized as expenses in the year in which they are incurred.
- Initial direct cost of the lease may be expensed immediately or deferred.

Accounting for operating lease – In the Books of Lessee

Lease payments should be recognized as an expense in the profit and loss account on a straight line basis over the lease term. If any other method is more representative of the time pattern of the user's benefit, such method can be used.

"Sale and Lease back"

A sale and lease back transaction involves the sale of an asset by vendor and leasing of the same asset back to the vendor.

Accounting treatment of Sale and Lease back

1. ***If lease back is Finance Lease***

   - Any profit or loss of sale proceeds over the carrying amount should **not** be immediately recognized as profit or loss in the financial statements of a seller-lessee.
   - It should be deferred and amortized over lease term in proportion to the depreciation of leased asset.

Example 1 – H Ltd. Sells machinery, WDV of which was ₹ 400 lakhs for ₹ 500 lakhs to B Ltd. The same machinery was leased back to H Ltd. by BLtd. for 10 years resulting in finance lease. What should be the treatment of profit in the books of seller lessee (H Ltd.)?

The profit of ₹10 lakhs on sale of machinery by H Ltd. (seller lessee) should not be immediately recognized in books rather it should be deferred and amortized over 10 years in proportion of the depreciation amount to be charged by the H Ltd. on the machinery.

2. ***If lease back is Operating Lease***

   Any profit or loss arising out of sale transaction is recognized immediately when sale price is equal to fair value.

   (A) *If Sale price" below" fair value*

   - Profit – i.e. carrying amount (=book value or value as per balance sheet) is **less** than the sale value, recognize profit immediately.
   - Loss – i.e. carrying amount is **more** than the sale value, recognize loss immediately, provided loss is **not** compensated by future lease payment.
   - Loss – i.e. carrying amount is **more** than sale price defer and amortize loss if loss is compensated by future lease payment.

   (B) If Sale price "above" fair value

   - If carrying amount is **equal** to fair value which will result in profit, amortize the profit over lease period.
   - Carrying amount **less** than fair value will result in profit – amortize and defer the profit equal to "sale price less fair value" and recognize balance profit immediately.

- Carrying amount is **more** than the fair value – which will result in loss equal to – (carrying amount less than fair value), should be recognized immediately. Profit equal to – selling price less fair value – should be amortized.

Example : H Ltd. sold machinery having WDV of ₹ 400 Lakhs to B Ltd. for ₹ 500 Lakhs and the same machinery was leased back by B Ltd. to H Ltd. The Lease back is operating lease.

Comment if –

(a) Sale price of ₹ 500 lakhs is equal to fair value

(b) Fair value is ₹ 600 lakhs

(c) Fair value is ₹ 450 lakhs and sale price is ₹ 380 lakhs

(d) Fair value is ₹ 400 lakhs and sale price is ₹ 500 lakhs

(e) Fair value is ₹ 460 lakhs and sale price is ₹ 500 lakhs

(f) Fair value is ₹ 350 lakhs and sale price is ₹ 390 lakhs

Answer:

(a) H ltd. should immediately recognize the profit of ₹ 100 lakhs in its books.

(b) Profit ₹ 100 lakhs should be immediately recognized by H Ltd.

(c) Loss of ₹ 20 lakhs to be immediately recognized by H Ltd. in its books provided loss is not compensated by future lease payment.

(d) Profit of ₹ 100 lakhs is to be amortized over the lease period.

(e) Profit of ₹ 60 lakhs (460-400) to be immediately recognized in its books and balance profit of ₹ 40 lakhs (500-460) is to be amortized / deferred over lease period.

(f) Loss of ₹ 50 lakhs (400-350) to be immediately recognized by H Ltd. in its books and profit of ₹ 40 lakhs (390-350) should be amortized / deferred over lease period.

Illustration 27.

Viraj Limited wishes to obtain a machine costing ₹45 lakhs by way of lease. The effective life of the machine is 14 years, but the company requires it only for the first 5 years. It enters into an agreement with Jhalak Ltd., for a lease rental for ₹4.5 lakhs p.a. payable in arrears and the implicit rate of interest is 15%. The chief accountant of Viraj Limited is not sure about the treatment of these lease rentals and seeks your advise.

Solution:

As per AS 19 'Leases', a lease will be classified as finance lease if at the inception of the lease, the present value of minimum lease payment amounts to at least substantially all of the fair value of leased asset. In the given case, the implicit rate of interest is given at 15%. The present value of minimum lease payments at 15% using PV- Annuity Factor can be computed as follows:

Annuity Factor (Year 1 to Year 5) 3.36 (approx.)

Present value of minimum lease payments (for ₹4.5 lakhs each year) ₹15.12lakhs (approx.)

Thus, present value of minimum lease payments is ₹15.12 lakhs and the fair value of the machine is ₹45 lakhs. In a finance lease, lease term should be for the major part of the economic life of the asset even if title is not transferred. However, in the given case, the effective useful life of the machine is 14 years while the lease is only for five years. Therefore, lease agreement is an operating lease. Lease payments under an operating lease should be recognized as an expense in the statement of profit and loss on a straight line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

Illustration 28.

Milind Softex Ltd. has taken the assets on lease from ABC Impex Ltd. The following information is given below:

Lease Term = 4 years

Fair value at inception of lease = ₹ 16,00,000

Lease Rent = ₹ 5,00,000 p.a. at the end of year

Guaranteed Residual Value = ₹ 1,00,000

Expected Residual Value = ₹ 2,00,000

Implicit Interest Rate = 14.97%

Do the accounting in the book of lease?

Solution :

Present value of minimum lease payment

Year	MLP ₹	Discount rate 14.97%	PV ₹
1	5,00,000	0.8698	4,34,900
2	5,00,000	0.7565	3,78,250
3	5,00,000	0.6580	3,29,000
4	6,00,000 (including 1,00,000)	0.5724	3,43,440
	21,00,000		14,85,590

Present value of minimum lease payment (₹ 14,85,590) is less than Fair value at the inception of lease (₹ 16,00,000) so the leased asset and liability should be recognized at ₹ 14,85,590.

Apportionment of finance lease : Rate of Interest 14.97%

Year	Liability ₹	MLP ₹	Finance Charge ₹	Principal Amount of reduction ₹
0	14,85,590	-	-	-
1	12,07,983	5,00,000	2,22,393	2,77,607
2	8,88,818	5,00,000	1,80,835	3,19,165
3	5,21,874	5,00,000	1,33,056	3,66,944
4	-	6,00,000	78,1245	5,21,875

Books of Milind Softex

Lease Rent Account

Year	Particulars	Amount ₹	Particulars	Amount ₹
1st year	To, Bank A/c	5,00,000	By, Finance Charges A/c By, Lease liability A/c	2,22,393 2,77,607
		5,00,000		5,00,000
2nd year	To, Bank A/c	5,00,000	By, Finance Charges A/c By, Lease liability A/c	1,80,835 3,19,165
		5,00,000		5,00,000
3rd year	To, Bank A/c	5,00,000	By, Finance Charges A/c By, Lease liability A/c	1,33,056 3,66,944
		5,00,000		5,00,000
4th year	To, Bank A/c	5,00,000	By, Finance Charges A/c By, Lease liability A/c	78,126 5,21,874
		5,00,000		5,00,000

Lease Liability Account (Lessor)

Year	Particulars	Amount ₹	Particulars	Amount ₹
1st year	To, Lease Rent A/c To, Balance c/d	2,77,607 12,07,983	By, Balance b/d	14,85,590
		14,85,590		14,85,590
2nd year	To, Lease Rent A/c To, Balance c/d	3,19,165 8,88,818	By, Balance b/d	12,07,903
		12,07,903		12,07,903
3rd year	To, Lease Rent A/c To, Balance c/d	3,66,944 5,21,874	By, Balance b/d	8,88,818
		8,88,818		8,88,818
4th year	To, Lease Rent A/c	5,21,874	By, Balance b/d	5,21,874
		5,21,874		5,21,874

Extract of Profit and Loss Account

Year	Particulars	Amount ₹
1st year	To, Finance Charge To Depreciation on leased Asset under SLM	2,22,393 3,71,397
2nd year	To, Finance Charge To Depreciation on leased Asset under SLM	1,80,835 3,71,397
3rd year	To, Finance Charge To Depreciation on leased Asset under SLM	1,33,056 3,71,397
4th year	To, Finance Charge To Depreciation on leased Asset under SLM	78,125 3,71,397

Extract balance Sheet

Year	Liability	Amount ₹	Asset	Amount ₹
1st year	Lease Liability A/c	12,07,983	Fixed Asset under Finance Lease Less: Depreciation	14,85,590 3,71,397 11,41,193
2nd year	Lease Liability A/c	8,88,818	Fixed Asset under Finance Lease Less: Depreciation	14,85,590 7,42,794 7,42,796
3rd year	Lease Liability A/c	5,21,874	Fixed Asset under Finance Lease Less: Depreciation	14,85,590 11,14,191 3,71,399
4th year	Lease Liability A/c	NIL	Fixed Asset under Finance Lease Less: Depreciation	14,85,590 14,85,590 NIL

Illustration 29.

Milind Softex Ltd. has taken the assets on lease from ABC Impex Ltd. The following information is given below:

Lease Term	=	4 years
Fair value at inception of lease	=	₹ 16,00,000
Lease Rent	=	₹ 5,00,000 p.a. at the end of year
Guaranteed Residual Value	=	₹ 1,00,000
Expected Residual Value	=	₹ 2,00,000
Implicit Interest Rate	=	14.97%

How the accounting is done in the book of lessor ?

Solution :

Lessor should recognize asset given under lease at net investment in lease.

Net investment in lease = Gross investment – unearned finance income

Gross Investment = MLP + Guarenteed residual value + Unguaranteed residual value

= ₹20,00,000 + ₹1,00,000 + ₹1,00,000

= ₹22,00,000

Unearned Finance Income = Gross Investment – present value of gross investment

Year	Value of MLP ₹	Gross investment discount factor	Present Value ₹
1	5,00,000	0.8698	4,34,900
2	5,00,000	0.7565	3,78,250
3	5,00,000	0.6580	3,29,000
4	7,00,000	0.5724	4,00,680
	22,00,000		15,42,830

Unearned Finance Income = ₹22,00,000 - ₹15,42,830 = ₹6,57,170

Apportionment of MLP into Capital recovery & Finance income

Year	Balance of lease receivable	Cash receipts	Finance	Capital recovery reduced from receivable
0	15,42,830	-	-	-
1	12,73,792	5,00,000	2,30,962	2,69,038
2	9,64,479	5,00,000	1,90,687	3,09,313
3	6,08,862	5,00,000	1,44,383	3,55,617
4		7,00,000	91,147	6,08,853
			6,57,179	15,42,821

The lease receivable account shown in the books of lessor will not tally with the lease liability account as shown by the leasee in his book. Difference will remain because of guaranteed residual value from the third party or/ and unguaranteed residual value from the leasee point of view.

Illustration 30.

Amit purchased a computer for ₹44,000 and leased out it to Sumit for four years on leases basis, after the lease period, value of the computer was estimated to be ₹3,000; whichhe realized after selling it in the second hand market. Lease amount payable at the beginning of each year is ₹22,000; ₹13,640; ₹6,820 & ₹3,410. Depreciation was charged @ 40% p.a. You are required to pass the necessary journal entries in the books of both Amit and Sumit.

Solution:

Journals

In the books of Amit

	Particulars		Dr. ₹	Cr. ₹
1st	**Purchase of Computers:**			
	Computer A/c	Dr.	44,000	
	To, Bank A/c			44,000
	Payment of first Year's Lease:			
	Bank A/c	Dr.	22,000	
	To, Lease Rent A/c			22,000
	Depreciation for First Year:			
	Depreciation A/c	Dr.	17,600	
	To, Computer A/c			17,600
	Transfer to Profit & Loss Account:			
	Profit & Loss A/c	Dr.	17,600	
	To, Depreciation A/c			17,600
	Lease Rent A/c	Dr.	22,000	
	To, Profit & Loss A/c			22,000
2nd	**Payment of Second Year's Lease:**			
	Bank A/c	Dr.	13,640	
	To, Lease Rent A/c			13,640
	Depreciation for Second Year:			
	Depreciation A/c	Dr.	10,560	
	To, Computer A/c			10,560
	Transfer to Profit & Loss Account:			
	Profit & Loss A/c	Dr.	10,560	
	To, Depreciation A/c			10,560
	Lease Rent A/c	Dr.	13,640	
	To, Profit & Loss A/c			13,640
3rd	**Payment of Third Year's Lease:**			
	Bank A/c	Dr.	6,820	
	To, Lease Rent A/c			6,820
	Depreciation for Third Year:			
	Depreciation A/c	Dr.	6,336	
	To, Computer A/c			6,336
	Transfer to Profit & Loss Account:			
	Profit & Loss A/c	Dr.	6,336	
	To, Depreciation A/c			6,336
	Lease Rent A/c	Dr.	6,820	
	To, Profit & Loss A/c			6,820
4th	**Payment of Fourth Year's Lease:**			
	Bank A/c	Dr.	3,410	
	To, Lease Rent A/c			3,410
	Depreciation for Fourth Year:			
	Depreciation A/c	Dr.	3,802	
	To, Computer A/c			3,802

	Particulars		Dr.	Cr.
	Transfer to Profit & Loss Account: Profit & Loss A/c To, Depreciation A/c Lease Rent A/c To, Profit & Loss A/c	 Dr. Dr.	 3,802 3,410	 3,802 3,410
	Sale of Lease assets: Bank A/c Loss on Sale A/c To, Computer A/c	 Dr. Dr.	 3,000 2,702	 5,702

In the books of Sumit

	Particulars		Dr. ₹	Cr. ₹
	Purchase of Computer:		No Entry	
	Payment of First Year's Lease: Lease Rent A/c To, Bank A/c	 Dr.	 22,000	 22,000
	Depreciation for First Year:		No Entry	
	Transfer to Profit & Loss Account: Profit and Loss A/c To, Lease Rent A/c	 Dr.	 22,000	 22,000
	Payment of Second Year's Lease: Lease Rent A/c To, Bank A/c	 Dr.	 13,640	 13,640
	Depreciation for Second Year:		No Entry	
	Transfer to Profit & Loss Account: Profit and Loss A/c To, Lease Rent A/c	 Dr.	 13,640	 13,640
	Payment of Third Year's Lease: Lease Rent A/c To, Bank A/c	 Dr.	 6,820	 6,820
	Depreciation for Third Year:		No Entry	
	Transfer to Profit & Loss Account: Profit and Loss A/c To, Lease Rent A/c	 Dr.	 6,820	 6,820
	Payment of Fourth Year's Lease: Lease Rent A/c To, Bank A/c	 Dr.	 3,410	 3,410
	Depreciation for Fourth Year:		No Entry	
	Transfer to Profit & Loss Account: Profit and Loss A/c To, Lease Rent A/c	 Dr.	 3,410	 3,410
	Sale of Lease Assets:		No Entry	

AS -20: EARNING PER SHARE (EPS)

Disclosure under AS-20:

(a) The applicability of the standard is mandatory with effect from accounting year commencing on or after 01-04-2001 in respect of enterprises whose equity shares or potential equity shares are listed on a recognized stock exchange in India.

(b) However under Schedule III of the Companies' Act, 2013 every company is required to disclose EPS in accordance with AS-20, whether listed on a recognized stock exchange or not.

(c) Presentation of EPS is required to be made both on the basis of consolidated financial statement, as well as individual financial statements of the parent company.

(d) Presentation should be made in terms of Basic and Diluted EPS on the face of 'the Profit & Loss Account for each class of equity share that has a different right to share in the net profit for the accounting period. For equity shares having different nominal value but carrying same voting rights should be covered into equivalent number of shares of the same nominal value.

(e) Both Basic and Diluted EPS should be presented with equal prominence for all periods even if the amounts are negative (a loss per share).

(f) In addition to above, following are also disclosed:

1. the amount used as the numerator and a reconciliation of those amounts to the net profit/loss for the accounting period.
2. the weighted average number of equity shares used as the denominator and a reconciliation of those denominator to each other.
3. the nominal value of shares along with EPS figure.

(g) Disclosure may also be made of terms and conditions of contracts generating potential equity which affect the basic and diluted EPS both on the weighted average number of shares outstanding and any consequent adjustments to net profit attributable to equity shareholders, following the computation of the denominator in accordance with AS-20.

Basic EPS:

(a) Basic EPS is worked out by dividing the net profit /loss for the accounting period by the equity share using weighted average number of equity shares outstanding during the same period.

(b) Net profit or loss should be arrived at after considering all income and expense recognized during the period including tax expense extraordinary as reduced by preference dividend in respect of non cumulative and cumulative for the period

(c) Disclosure as an alternative may be presented for basic and diluted on the basis of earning excluding extraordinary items (net of tax expenses).

Impact of bonus element in rights issue on EPS denominator:

In a right issue the exercise price in often less than fair value of shares thus it includes a bonus element and moreover, an adjustment is needed to recompute the fair value in relation to theoretical ex-right value per share.

Diluted EPS indicates the potential variability or risk attached to the basic EPS as a consequence of the issue of potential equity shares and potential dilutive securities having significant impact on lowering EPS. However, no potential equity shares be included in the computation of any diluted per share amount in case of continuing loss from operation, even though the entity reports an overall net profit.

(i) Adjustments should be made both in numerator and denominator consequent upon the conversion of potential dilution to arrive at diluted EPS in keeping with the nature of conversion including tax implication thereon in the respective year.

(ii) Potential equity shares are:

   (a) debt instruments/preference share convertible into equity shares

   (b) share warrants

   (c) employees and other stock option plans which entitles them to receive equity shares as part of their remuneration and other similar plans

   (d) contingently issuable shares under contractual arrangements e.g. acquisition of a business/assets, loan converted to equity on default

   (e) share application pending allotment if not statutorily required to be kept separately and is being utilized for business is treated as potential (dilutive) equity share.

Illustration 31.

Weighted avg. number of equity shares has been illustrated in AS-20 in the following line:

Accounting year: 2014-15				
Date	Description	Shares Issued (Nos)	Buyback (Nos)	O/S
01/04/2014	Op. Balance	1800	-	1800
30/09/2014	Issued for Cash	600	-	2400
29/02/2015	Buyback	-	300	2100
31/03/2015	Cl. Balance	2400	300	2100

Solution:

Weighted average number

(a) (1800 x 5/12) + (2400 x 5/12) + (2100 x 2/12) i.e. 2100 shares

   or

(b) (1800 x 12/12) + (600 x 7/12) - (300 x 2/12) i.e. 2100 shares

Illustration 32.

Net profit for 2014-15: ₹ 18,00,000; Net profit for 2015-16: ₹ 60,00,000; No. of equity shares as on 31.12.15: ₹ 20,00,000.

Bonus issued on 1-1-16 : 2 equity shares for each Equity Share outstanding at 31-12-16 i.e. ₹ 40,00,000.

Solution:

EPS for 2015-16: (₹ 60,00,000)/(20,00,000+40,00,000) = ₹1.00

Adjusted EPS for 2014-15: (earliest period reported) [₹18,00,000/60,00,000] = ₹ 0.30

Illustration 33.

Compute EPS:

(a) Net profit for 2014-15 ₹ 11,00,000

   Net profit for 2015-16 ₹ 15,00,000

(b) Nos. of shares outstanding prior to Right Issue: 5,00,000 shares

(c) Right Issue: one new share for 5 outstanding i.e. 1,00,000 new shares

(d) Right price: ₹ 15

(e) Last date of right option: 1st March 2016

(f) Fair value prior to the right option on 1st march 2016: ₹ 21 per equity share

Computation:

1) Theoretical ex-right fair value per share:

[(₹ 21 x 5,00,000) + (₹ 15 x 1,00,000)] / (5,00,000+ 1,00,000)

i.e. 1,20,00,000/6,00,000 = ₹ 20

2) Adjustment factor:- fair value prior to exercise of rights/theoretical ex-right value. i.e. 21/20=1.05

3) Computation of EPS:

Year 2014-15 EPS as originally reported	
₹ 11,00,000/5,00,000 shares	₹ 2.20
EPS restated for right issue	
₹ 11,00,000/(5,00,000 x ₹ 1.05)	₹ 2.10
Year 2015-16 EPS-for 2016 including rights	
₹ 15,00,000/(5,00,000 x 1.05 x 2/12) + (6,00,000 x 10/12)	₹ 2.25

AS -21: CONSOLIDATED FINANCIAL STATEMENTS

Consolidated financial statements are presented by the parent or holding enterprise to provide financial information about the economic activities of its group - information about the parent and subsidiaries as a single economic entity revealing economic resources controlled by the group, the obligation of the group and the result that the group achieved with its resources.

AS-21 lays down the principles and procedures for preparation and presentation of consolidated financial statements in the backdrop of the facts that the Companies Act 2013 doesn't provide for consolidation vis-à-vis the compliance to be made by listed companies in terms of AS-21.

Thus in parent enterprise's separate financial statements, investment in subsidiaries should be accounted for as per AS-13, i.e. Accounting for Investments.

The consolidated financial statements even if made voluntarily should comply with AS -21.

The key note is the control by the parent which means and includes:

(i) the ownership, directly or indirectly through subsidiary/subsidiaries of more than 50% of the voting power of an enterprise or,

(ii) control of the composition of the Board of Directors or Governing Body (e.g. in the form of restriction, holding a position and right in nomination exercisable by the parent with reference to the subsidiary) as the case may be so as to obtain economic benefits from its activities.

Further "Control" is also further screened to exclude a subsidiary if;

(a) it is intended to be temporary i.e. the subsidiary is acquired and held exclusively with a view to subsequent disposal in near further, in other words not intended for long term purpose.

(b) there is long term restriction on the subsidiary which significantly impair its ability to transfer funds to the parent enterprise. (e.g. embargo on fund transfer by foreign subsidiary-severe devaluating currency)

In above cases investment would be valued as per AS -13 and not AS-21. AS- does not deal with the specific AS as under:

(i) AS-14 - Accounting for Amalgamation

(ii) AS-23 - Accounting for Investment in Association

(iii) AS-27 - Accounting for investment in Joint Venture

Since schedule III is not tailored to the presentation of consolidated financial statement. ICAI has provided general guideline vide GC-5/2002 which broadly states that the following principles should be served:

(a) notes which are necessary for presenting a true and fair view of the consolidated finance statements should be included as an integral part thereof.

(b) Only the notes involving items, which are material, need to be disclosed and the materiality is judged in the context of consolidated financial statement. Applicability of other Accounting Standard, in the preparation and presentation of consolidated statements are stated below:

    (i) irrespective of the format followed, the minimum disclosure under various mandatory standards should be made.

AS-1: disclosure of accounting policies (e.g. going concern)

AS-22: accounting for taxes and income as applicable to the individual entity only cannot be given setoff treatment in CFS.

Specific items to AS in respect of balances of individual enterprise and not as a group e.g. “Current Investment valued at lower of cost or market price” Segmental information on consolidated numbers of individual enterprise in the group only.

Disclosure relating -to operating lease (AS-19) would not be required since the same is setoff and eliminated at consolidated level.

Related party transaction, within the group would not require discloser since eliminated at consolidated level.

Accounting related treatment for in consolidated financial statements:

(a) Consolidation should be made on line by line basis by adding together like items- assets, liabilities, income and expense

(b) All group balances and group transactions and unrealized profits arising thereon should eliminated

(c) Dividend - minority share when paid is deduced from opening “Minority Interest” A/c and the portion attributable to parent is eliminated from Consolidated Reserves.

(d) Excess of cost to the parent of its investment in a subsidiary over the parent’s portion of equity of the subsidiary on date of investment is recognized as ‘goodwill’ or in reverse situation as ‘capital reserve’ and the ‘minority interest’ as a liability separately in the consolidated financial statement as a distinct item.

(e) When carrying amount of the investment in the subsidiary is different from its cost, the carrying amount is considered

(f) Usually consolidated financial statements are drawn upto the same date for reporting. In case, the reporting dates are different, the subsidiary normally prepares statements as at the same date of the parent. However, impracticable, different dates may be reported but the difference should not be more than six months with adjustments made for the effects, of significant transactions during the intervening period in respect all the items in the financial statements pertaining to that transaction e.g. cost of sales, inventory, unrelated gains, inter group balances. If not material otherwise, may be adjusted in income statement.

(g) AS-21 permits the use of different accounting policies and estimates between group members, as long as the proportion of these in the in the context of the CFS are properly disclosed and explained.

(h) AS-21 allows the use of financial statements of the subsidiary for the immediately preceding period if the financial statements as on the date of investments are not available or impracticable to draw the financial statements as on that date. As stated earlier, effects of significant transactions or events occur between the two dates are made.

(i) I several investments are Trade over time to make it 51% control, goodwill may be determined when the last investment is made to bring the slake to 51% or alternatively on each step-up investment basis.

(j) Goodwill is determined on the basis of carrying value of assets/liabilities of the subsidiary at the balance sheet date, thus fair value accounting for acquisition is not permitted under AS-21.

(k) Where a group has acquired several subsidiaries, some resulting in goodwill and others a capital reserve, set off is not made for consolidation purpose.

Disclosure in terms of AS-21

(a) Disclosure should be made in accordance with the format of the parent company's financial statements. Further disclosure under all the mandatory accounting standards when material and also compliance with General Classification no. 5/2002 should be made in order to ensure comparability for one period to the next, supplementary information about the effect of acquisition and disposal of subsidiaries on the financial position at the reporting date and results for the reporting period with comparative preceding period amount, should be disclosed.

(b) Reasons for exclusion from consolidation of subsidiaries should be disclosed. List of all subsidiaries- name, country of incorporation/residence, proportion of ownership interest and if different proportion of voting power.

(c) Nature of relationship if the parent does not own directly or indirectly more than 50% of voting power of the subsidiary.

(d) Names of subsidiary/subsidiaries of which reporting dates are different from that of the parent and the difference in reporting dates.

AS-22: ACCOUNTING FOR TAXES ON INCOME

The need for establishing a standard arises due to difference between profit computed for accounting and that for tax purpose. As per this standard, the income tax-expense should be treated just like any other expenses on accrual basis irrespective of the timing of payment of tax.

Tax expense = current tax + deferred tax

Current tax is the amount of income-tax determined to be payable (recoverable) in respect of the taxable income (tax loss) for a period.

Deferred tax is the tax effect of timing difference.

The difference accounts for:

(a) treatment of revenue and expenses as appearing in the profit and loss Ale and as considered for the tax purpose.

(b) the amount of revenue or expenses as recognized in the P/L A/c and as allowed for tax purpose.

The difference as arising in the above context gives rise to 'deferred tax' and it needs to be ensured that the tax charges in future accounting period is not vitiated.

The difference in accounting profit and taxable profit can be broadly categorized into two:

(a) *Permanent difference:* which originates in one period and do not reverse in subsequent periods, e.g. personal expenses disallowed, interest/penalty disallowed as expense or tax-free agricultural income, various deduction under section 10, benefit/reliefs under section 80 in computing taxable income.

Permanent differences do not result in deferred taxes.

(b) *Timing difference:* which originates in one period and is capable of reversal in subsequent period(s):

- difference in net block of fixed assets as per accounts and as per tax due to difference in the rate and method of depreciation;

- provision for doubtful debts and advances, provision for warranties, provision for VRS, provision for asset write-off, disallowed payments under 43B of Income Tax Act, provision for excise liabilities, provision for diminution in value of investments, scientific research expenditure (not weighted deduction which is a permanent difference), amortization of deferred revenue expenditure, lease income.

Situations which leads to Deferred Tax:

Deferred tax is the tax effect due to timing difference. They arise due to the following reasons:

- Accounting Income less than Tax Income
- Accounting Income more than Tax Income
- Income as per Accounts but loss as per IT Act
- Loss as per Accounts but income as per IT Act

Impact of such timing differences may lead to:

- Deferred Tax Liability (DTL): postponement of tax liability, which states Save Now, Pay Later.

  Profit and Loss A/c………..Dr.

  To Deferred Tax Liability A/c

- Deferred Tax Asset (DTA): pay you tax liability in advance, which states Pay Now, Save Later.

  Deferred Tax Asset A/c……….Dr.

  To Profit and Loss A/c

In the year of reversing time difference, either DTL is written back to profit and loss or the DTA is reversed by debiting profit and loss account.

For the recognition of DTA, prudence should be applied. Such recognition is based on " reasonable certainty" that sufficient taxable income would be available in the future to realize the DTA.

In case of unabsorbed depreciation and carry forward losses, DTA should only be recognized to the extent that there is "virtual certainty" that in future sufficient taxable income would be available to realize the DTA.

Reasonable certainty shall be deemed to be in existence if the probability of future taxable income is greater than 50%.

Virtual certainty shall be deemed to be in existence only when the evidence suggests that there will be sufficient taxable income in the future.

Disclosure under AS-22 Mandatory :

(a) Break up of the deferred tax asset/liability.

(b) DTL should be shown after the head "Unsecured Loans" and DTA after the head "Investments" with a separate heading.

Illustration 34.

From the following information for R Ltd. for the year ended 31st March, 2015, calculate the deferred tax asset/ liability as per AS-22

Accounting Profit	₹10,00,000
Book Profit as per MAT(Minimum Alternate Tax)	₹9,00,000
Profit as per Income Tax Act	₹1,00,000
Tax Rate	30%
MAT Rate	10%

Solution:

Tax as per accounting profit : 10,00,000 x 30% = 3,00,000

Tax as per Income Tax profit : 1,00,000 x 30% = 30,000

Tax as per MAT : 9,00,000 x 10% = 90,000

Tax expense = Current tax + Deferred tax

3,00,000 = 30,000 + Deferred tax

Therefore, Deferred Tax Liability as on 31.3.2015 = ₹ 3,00,000 – ₹ 30,000 = ₹ 2,70,000.

Amount of tax to be debited in Profit and Loss Account for the year 31.03.2015:

= Current tax + Deferred tax liability + Excess of MAT over current tax

= 30,000 + 2,70,000 + (90,000 – 30,000)

= 3,60,000

Illustration 35.

Z Ltd,has provided depreciation as per accounting records ₹ 40 lakhs but as per tax records ₹60 lakhs. Unamortized preliminary expenses, as per tax records is ₹20,000. there is adequate evidence of future profit sufficiency. How much deferred tax asset/liability should be recognized as transition adjustment? Tax rate 30%.

Solution:

As per Para 13 of AS-22, deferred tax should be recognized for all the timing differences. In this situation, the timing difference i.e. the difference between taxable income and accounting income is :

Excess depreciation as per tax ₹ (60 – 40) lakhs	=	₹ 20.00 lakhs
Less: Expenses provided in taxable income	=	₹ 0.20 lakhs
Timing difference		₹ 19.80 lakhs

As tax expense is more than the current tax due to timing difference of ₹19.80 lakhs, therefore deferred tax liability = 30% of ₹19.80 lakhs = ₹5.94 lakhs.

Profit and Loss A/c…………Dr.	5.94	
To Deferred Tax Liability A/c		5.94

Illustration 36.

Om Limited is working on different projects which are likely to be completed within 3 years period. It recognizes revenue from these contracts on percentage of completion method for financial statements during 2015, 2016 and 2017 for ₹11,00,000, ₹16,00,000 and ₹21,00,000 respectively. However, for income-tax purpose, it has adopted the completed contract method under which it has recognized revenue of ₹7,00,000, ₹18,00,000 and ₹23,00,000 for the years 2015, 2016 and 2017 respectively. Income-tax rate is 40%. Compute the amount of deferred tax asset/ liability for the years 2015, 2016 and 2017.

Solution:

Om Limited

Calculation of Deferred Tax Asset/Liability

Year	Accounting Income	Taxable Income	Timing Difference (balance)	Deferred Tax Liability (balance)
2015	11,00,000	7,00,000	4,00,000	1,40,000
2016	16,00,000	18,00,000	2,00,000	70,000
2017	21,00,000	23,00,000	NIL	NIL
	48,00,000	48,00,000		

AS-23: ACCOUNTING FOR INVESTMENTS IN ASSOCIATES IN CONSOLIDATED FINANCIAL STATEMENTS (CFS)

An enterprise that presents CFS should account for investments in Associates as per this standard.

This standard is not applicable for preparing and presenting stand-alone Investors' financial statement (in such cases AS 3 is followed).

An Associate is an enterprise in which the investor has significant influence (power to participate in the financial/ operating policy decisions of the investee but not control over those policies) and which is neither a subsidiary nor a joint venture of the Investor. The 'control' for the purpose of AS-23 is similar to that of AS-21.

Significant influence may be evidenced in one or more ways in the following line:

a) Representation on the Board of Directors or Governing Body of the Investee.

b) Participation in policy making process

c) Material transaction between investor and investee.

d) Interchange of managerial personnel

e) Provision of essential technical information

But it does not extend to power to govern the financial and/or operating policies of an enterprise.

Significant influence may be gained through share ownership, statute or agreement:

a) For share ownership, 20% or more in voting power in investee (held directly or indirectly through subsidiary) indicates significant influence but that is not the ultimate, the significant influence must be clearly demonstrated.

b) A substantial or majority ownership by another investor in the investee does not necessarily preclude an investor to have significant influence.

c) Voting power is determined on the basis of current outstanding securities and not potential equity.

Non applicability of AS-23:

1) Investment in associates are accounted for using the 'equity method' in the CFS except when,

    a) the investment is made and held exclusively with a view to subsequent disposal in the near future, or

    b) the associate operates under severe long-term restrictions that significantly impairs its ability to transfer funds to investor. Investments in such a situation is accounted for in accordance with AS-3 in CFS.

2) Equity method of accounting is also not applicable if

    a) it has no investment in Association

    b) it has investment in Association but has no subsidiaries, CFS is not required

    c) it has subsidiaries and associates but these are not material, hence CFS is not prepared.

    d) It is not listed enterprise hence not mandatory to present CFS or has not chosen voluntarily to present CFS.

Equity method of accounting recognizes the investment initially recorded at cost identifying goodwill/capital reserve at the time of acquisition. The carrying amount of investment is thereafter adjusted for the post-acquisition charge in the investor's share of net assets of the investee and consolidated P/L A/c reflect the investor's shares in the result of operation of the investee. Further any permanent decline in the value of investment is reduced to arrive at the carrying amount for each such investment.

Except inconsistent with AS-23, other accounting treatment would follow AS-21 Disclosure under AS-23

a) Reasons for not applying Equity Method in accounting for investments in associates in CFS .

b) Goodwill/capital reserve as included in the carrying amount of investment in Associates disclosed separately.

c) Description of associates, proportion of ownership interest and if different proportion of voting power held disclosed in CFS.

d) Investment using equity method should be classified as long-term investment in consolidated balance sheet, similarly investor's share in profit/loss in consolidated P/L Account and also investor's share of extraordinary or prior period items should be disclosed separately.

e) The names of associates of which reporting date is different from that of the financial statements of the investor and difference in reporting date should be disclosed in CFS.

f) Difference in the accounting policies if not practicable for appropriate adjustment in Associate's financial statement for being adjusted in CFS, the fact as such with description of difference in accounting policies should be disclosed.

g) In compliance with AS-4, Contingencies and events occurring after the balance sheet date, the investor discloses in the CFS:

   (i) its share of contingencies and capital commitments of an Associate for which the investor is contingently liable, and

   (ii) those contingencies that arise because the investor is severely liable for the liabilities of the associate.

Illustration 37.

X holds, 25% share in Y Ltd at a cost of ₹5 lakhs as on 31-03-2015. Out of Y's shares capital and reserve ₹20 Lakh each.

For the year ended 31-03-2015 Y made a profit of ₹80,000 and 50% distributed as dividend. Compute the value (carrying amount) as at 31.03.2015 to be shown in the CFS.

Solution:

	₹ in Lakhs
Cost of shares in Y Ltd.	5.00
Share of Reserve	5.00
Share of profit	0.20
	10.20
Less: dividend received	0.10
Value of investment as at 31.03.15	10.10

Illustration 38.

Style Ltd. acquired 30% of Ugly Ltd.'s shares on April 10,2015, the price paid was ₹ 20,00,000.

	₹
Equity shares(Paid up)	5,00,000
Securities Premium	5,00,000
Reserve	5,00,000
	25,00,000

Further, Ugly Ltd reported a net income of ₹3,00,000 and paid dividends of ₹1,00,000. Style Ltd. has subsidiary on 31.3.15. Calculate the amount at which the investment in Ugly Ltd should be shown in the consolidated Balance Sheet of Style Ltd. as on 31.3.15.

Solution:

As per AS-23, when the investor company prepares the consolidated Balance Sheet, the investment in associate i.e. Ugly Ltd. shall be carried by equity method and goodwill and capital reserve to be identified and disclosed separately.

Value of the investment as per equity method

= 20,00,000 + 30% (3,00,000 – 1,00,000) = ₹20,40,000.

Goodwill identified = (20,00,000 – 30% of 25,00,000) = ₹ 12,50,000

AS-24: DISCONTINUING OPERATION

AS-24 requires disclosure to be made when the discontinuation is in process and not merely once it has been fully completed for reporting information, to enhance the ability of the user of the financial statements to study projection of cash flow, earnings generating capacity and financial information differentiating between 'continuing' and 'discontinuing' operation.

Prerequisites to determine 'discontinuing operation' –

1. The enterprise in term a single plan:

   a) disposing substantially in its entirety e.g. by selling the component in a single transaction or by demerger or spin-off of ownership of the component to the enterprise's shareholder, or

   b) disposing in piecemeal manner e.g. selling off the assets-and settling its liabilities individually or

   c) terminating through abandonment

2. That represent, a separate major line of business or geographical area of operation, and

3. That can be distinguished operationally for financial reporting purpose.

A restructuring event or transaction that does not meet with the definition of a 'discontinuing operation' within the ambit of AS-24, should not be called or treated as discontinuing operation. Typical example of instances which by itself does not mean 'discontinuing operation' but may lead to such in combination with other circumstances:

a) gradual or evolutionary phasing out of a product line or class of service

b) abrupt discontinuing of several products within an ongoing line of business

c) shifting of some production or marketing activities for a particular line of business from one location to another

d) closing of a factory to achieve productivity improvements or other cost savings. 'discontinuing operation' are expected to occur infrequently, but resulting income or expenses arising thereof needs to be disclosed in terms of AS-5 to explain the performance of the enterprise for the period.

Above all any transaction or event or in combination in order to be treated as 'discontinuing operation.' must be in terms of an overall plan falling within the prerequisites of 'discontinuing operation.

AS- 17 for segment reporting would normally satisfy the definition of 'discontinuing operation', but the significance for reporting under AS-24 will depend on individual judgment e.g. an enterprise operates in a single business/ geographical segment though not reportable under AS- 17 may fall within the ambit of AS-24.

The criteria of discontinuation which can be distinguished operationally and for financial repotting purpose must fulfill the following:

a) the operating assets/liabilities of the component can be directly attributed to it.

b) revenue can be directly attributed to it

c) at least a majority of operating expenses can be directly attributed to it.

Going concern concept is not disturbed if an enterprise merely disposes off few of its segments but continues to operate its other business profitably, on the other hand if a substantial part of its operation is discontinued and there is no operation to carry as a result, it will cease to be going concern.

Discontinuing process need not necessarily arise out of binding sale agreement but relates back to the announcement of a detailed, formal plan approved by the Board of Directors /Governing Body, if precedes sales agreement and therefore require initial disclosure event/transaction. However the announcement must demonstrate the commitment to discontinue resulting into a constructive obligation for the enterprise. Requirement of initial disclosure in the financial statement for the period in which the event of discontinuing operation occur, are:

1. A description of discontinuing operation

2 The date and nature of initial disclosure event

3. Probable date or period by which the discontinuance is expected to be completed

4. Carrying amount of the total of assets to be disposed off and the total of liabilities to be settled as of the Balance sheet date

5. The amount of revenue and expenses in respect of ordinary activities attributable to the discontinuing operation during the current financial reporting period.

   the pre-tax profit/loss and tax expense (AS-22) in the above line. the amount of net cash flow attributable to the operating/investing/financing activities of the discontinuing operation during the current financial reporting period. If the initial disclosure event occurs in between the balance sheet date and the date of approval of financial statements by the board of directors/corresponding approving authority, disclosure compliance should be made as per AS-4 not under AS-24. Disclosure should continue till the discontinuance is substantially completed or abandoned, irrespective of receipt of payments from its buyer.

   In case the discontinuance plan is abandoned or withdrawn as previously reported, the fact, reasons and effects thereof including reversal of any prior impairment of loss or provision that was recognized in the plan, should be disclosed.

Disclosure under AS-24

1. By way of a note in the financial statement in respect of each discontinuing operation, in addition to disclosure on the face of the statements of profit/loss in respect of:

   (a) the amount of pre-tax profit/loss from ordinary activities, income tax expense as attributable to discontinuing operation, during the current financial reporting period; and

   (b) the amount of pre-tax gain or loss recognized on the disposal of assets or settlement of liabilities attributable to the discontinuing operation.

2. Comparative information for prior period that is presented in financial statements prepared after the initial disclosure should be restated to segregate assets, liabilities revenue expense and cash flows of continuing and discontinuing operations.

3. AS-24 does not provide for the principles to recognize and measure profit/loss in respect of discontinuing operation and therefore, other accounting standards would be applicable e.g. AS-4, AS-10 and other AS as and when applicable.

Illustration 39.

A Company belonging to the process industry carries out three consecutive processes. The output of the first process is taken as input of the second process, and the output of the second process is taken as input of the third process. The final product emerges out of the third process. It is also possible to outsource the intermediate products. It has been found that over a period time cost of production of the first process is 10% higher than the market price of the intermediate product available freely in the market. The company has decided to close down the first process as a measure of cost saving (vertical spin off) and outsource. Should this event be treated as discontinuing operation?

Solution:

The change made by the company is focused on outsourcing of services, in respect of one single process – in a sequence of process. The net effect of this change is closure of facility relating to process.

This has been done by the company with a view to achieving productivity improvement and savings in costs.

Such a change does not meet definition criteria in paragraph 3(a) of AS-24 namely, disposing of substantially in its entirety, such as by selling a component of the enterprise in a single transaction. The change is merely a cost-saving endeavor. Hence, this change over is not a discontinuing operation.

Illustration 40.

A FMCG company is manufacturing two brands of soap. Cinthol and Breeze. Company has gradually planned to shift all the manufacturing operation engaged in two soaps to manufacture only 'Breeze Soap' without closing the factory/plant producing the 'Cinthol Soap', rather utilizing the production facilities of 'Cinthol Soap' for producing the 'Breeze Soap'. Can we consider the operation to have been discontinued ?

Solution:

Discontinuing operation is relatively large component of an enterprise which is major line of business or geographical segment, that is distinguishable operationally or for financial reporting such component of business is being disposed on the basis of an overall plan in its entirety or in piecemeal. Discontinuance will be carried either through demerger or spin-off, piecemeal disposal of assets and settling of liabilities or by abandonment.

In the given case, it is not a discontinuing operation.

Illustration 41.

B Ltd. is a software company, has subsidiary C Ltd. B Ltd.hold 70% shares in C Ltd. During 2014-15, B Ltd. sold its entire investment in C Ltd. Is it a discontinuing operation?

Solution:

As per the definition and scope of 'discontinuing operation', the sell of investments in subsidiary company does not attract the provisions of AS-24.

Hence, it is not a discontinuing operation.

Illustration 42.

C Ltd.has three major lines of business: steel, tea and power generation. It has decided to sell the tea division during the financial year 2014-15. A sale agreement has been entered into on 30th September 2014 with P Ltd. under which the tea division shall be transferred to P Ltd. on 31st March, 2015. Is it a discontinuing operation?

Solution:

This is a case of disposing of the tea division substantially and in its entirety. It will be considered as a discontinuing operation.

However, if a special resolution is passed for sale of various assets and to repay the various liabilities individually of the tea division, it is a case of "disposing by piecemeal" and not a "discontinuing operation".

Note: Any planned change in the product line may not be treated as a discontinuing operation.

AS-25: INTERIM FINANCIAL REPORTING

Interim financial reporting is the reporting for periods of less than a year, generally for a period of 3 months. As per Clause 41 of listing agreement the companies are required to publish the financial results on a quarterly basis.

AS-25 prescribe minimum content of an interim financial report and principles for recognition and measurement in a complete or condensed financial statement for an interim period or specific dates in respect of asset, liability, income and expense.

There are certain typical problems not faced while preparing annual account as the reporting period is shortened, the effect of errors in estimation and allocation are magnified e.g.

(i) accrual of tax credits in different interim period, makes determination of tax expense often difficult, one period may reveal tax profit while the other interim period have tax losses;

(ii) benefit of expenses spread beyond interim period e.g. advertising expenses, major repair and maintenance expenses;

(iii) determination of approximate amount of provisions, e.g. warranties, pension, gratuity, maybe complex 'and time consuming;

(iv) revenue may be seasonal or cyclical, hence concentration falls in certain interim periods;

(v) inter-company reconciliation, full stock-taking and valuation may be cumbersome and time consuming;

(vi) transaction based on Annual Targets e.g.: bonus or incentives would be difficult to estimate.

The standard itself does not categorize the enterprise or frequency of interim financial report and the time limit for presentation from the end of an interim period, but if it is required to prepare and present, it should comply with AS-25.

Instances for interim financial report:

(i) quarterly report to the board of directors or bank

(ii) incase of merger and amalgamation

(iii) for IPO purpose

(iv) for consolidation of parent and subsidiary when year ends are different

(v) for declaring interim dividend' Accounting for interim transaction:

 (a) interim period is considered as integral part of annual accounting period e.g. annual operating expc!1ses are estimated and then allocated to the interim period based on estimated sales or other parameters and results of subsequent interim periods are adjusted for estimation errors (integral approach)

 (b) each interim period is considered as discrete and separate accounting period like a full accounting period e.g. no estimation or allocation and operating expenses are recognized in the concerned interim period irrespective of benefit accruing to other interim period (discrete approach).

Form and contents of interim financial statement:

(a) AS 25 doesn't prohibit an enterprise from presenting a complete set of financial statements (e.g. balance sheet, profit & loss statement, cash flow statement notes to account and accounting policies, other statements and other explanatory' materials as forming integral part of the financial statement).

(b) The recognition and measurement principles as stated in AS-25 also apply to complete set of financial statements for an interim period, full disclosure under this statement and other accounting standard will be required.

(c) Alternatively, the statement allows preparation and presentation 'of interim financial report in a condensed form, containing as a minimum, a set of condensed financial statements, providing update on the latest annual financial statements (does not duplicate the information already reported)

Contents of a condensed Interim Financial Statements as a minimum:

1. A statement that the same accounting policies are followed as in the most recent annual financial statements - for change, description of the nature and effect of the change.

 Explanatory comment, about the seasonality of the interim operations the nature and amount of items affecting assets, liability, equity, net income or cash flows that are unusual because of their nature, size or incidence.

2. The nature and amount of changes in estimates of amounts reported in prior interim periods of the current financial year or changes in estimates of amount reported in prior financial year - if the those changes have a material effect in the current interim period.

3. Issues, buy-back, repayment and restructuring of debt, equity and potential equity shares.

4. Dividends, aggregate per share (in absolute or percentage) separately for equity and other shares

5. If compliance required under AS-17, segment revenue, segment capital employed and segment result for Business or Geographical segments (whichever is primary for reporting).

6. Effect of changes in the composition of the enterprise during the interim period (e.g. amalgamation, acquisition. or disposal of subsidiaries and long term investments, restructuring and discontinuing operation.

7. Material change in contingent liabilities since last annual *B/S* date.

The above selected explanatory notes should normally be reported on a financial year to date basis.

Period of Interim Financial Statement: interim reports should include interim financial statements (condensed or complete) for periods as follows:

(a) Balance Sheet:

(1) As at the end of current interim period

(2) As at the end of the immediately preceding financial year

(b) Statement of Profit and Loss:

(1) For the current period

(2) Cumulative for the current financial year to date

(3) Comparative for the comparable interim period (current arid year to date

(c) Cash flow Statement:

(1) Current financial year to date

(2) Comparative for the comparable year to date for immediately preceding financial year.

Illustration 43.

S Ltd. presents interim financial report quarterly on 1.4.2014. S Ltd.has carried forward loss of ₹800 lakhs for income tax purpose for which deferred tax asset has not been recognized. S Ltd.earns ₹ 600 lakhs; ₹700 lakhs; ₹750 lakhs and ₹800 lakhs respectively in the subsequent quarters, excluding the carried forward losses. Income tax rate is 30%. Calculate the amount of tax expense to be reported in each quarter.

Solution:

The estimated payment of the annual tax on ₹2,850 lakhs earnings for the current year = ₹(2,850 – 800) lakhs = ₹2,050 lakhs.

Therefore, tax = 30% of ₹2,050 lakhs = ₹615 lakhs.

Average annual effective tax rate = (615/2,850) x 100 = 21.58%

Tax expense to be shown:	₹ lakhs
1st quarter = 600 x 21.58%	= 129.48
2nd quarter = 700 x 21.58%	= 151.06
3rd quarter = 750 x 21.58%	= 161.85
4th quarter = 800 x 21.58%	= 172.64

Illustration 44.

M Ltd. presents interim financial report(IFR) quarterly, earns ₹800 lakhs pre-tax profit in the first quarter ending 30.6.14 but expect to incur losses of ₹250 lakhs in each of the remaining three quarters. Effective income tax rate is 35%. Calculate the income-tax expense to be reported for each quarter as per AS-25.

Solution:

Tax expense to be reported in each of the quarters are:

1st quarter = 800 x 35% = ₹280.00 lakhs

2nd quarter = (250) x 35% = ₹ (87.5)lakhs

3rd quarter = (250) x 35% = ₹ (87.5)lakhs

4th quarter = (250) x 35% = ₹ (87.5) lakhs

Annual Tax Expense = ₹17.5 lakhs

AS – 26: INTANGIBLE ASSETS

An intangible asset is an identifiable non-monetary asset, without physical substance held for production or supply of goods and services for rental to others or for administrative purposes.

(i) prescribes the accounting treatment for intangible assets that are not specifically covered in other accounting standard;

(ii) recognizes an intangible asset on fulfillment of certain criteria;

(iii) deals with deferment of expenses except in a few specific instances.

However AS -26 does not apply to:

(a) Intangible assets covered by other accounting standards e.g. AS-2 (valuation of inventories), AS-7 (accounting for construction contracts), AS-22 (accounting for taxes on income), leases falling within scope of AS-19, goodwill on amalgamation (AS-14) and on consolidation (AS-21).

(b) Mineral rights and expenditure on the exploration .for or development and extraction of minerals, oils, natural gas and similar non-generative resources and intangible assets arising in insurance enterprises from contracts with policy holders however, computer software expenses, start up cost pertaining to above activities are covered by AS-26).

(c) Discount Premium on borrowings.

AS-26 applies, among other things, to expenditure on advertisement, training, startup, R&D activities, Rights under Licensing Agreement for motion picture video recording, plays, manuscript, patents and copyrights, the criteria is that expenditure should provide future economic benefits to an enterprise.

Sometimes, an asset may incorporate both tangible and intangible component and it is practically inseparable. "Judgment is required to determine the applicability of AS-10 (fixed asset) and AS-26 (intangible asset).

Example:

(1) computer software which is integral part and without that the computer-controlled machine cannot operate - treated as fixed asset.

(2) computer software, not an integral part of related' hardware - treated as. an intangible asset,

Essential criteria for recognition of an intangible asset:

(a) *identifiable:*- It must be separate from goodwill and the enterprise could rem. sell: exchange or distribute the future economic benefits attributable to the asset without disposing of future economic benefits that flow from other assets in the same revenue earning activity - but goodwill cannot be meaningfully transferred to a new owner without also selling the other assets or the operation of the business. e.g. patents, copyrights, license, brand name, import quota, computer software, lease hold right, marketing rights, technical know-how etc.

(b) *control:*- The enterprise has the power to obtain the future economic benefits, flowing from the underlying resources and also can restrict the access of others I to those benefits (not necessarily legal right and may be in some other way – I market and technical knowledge may give rise to future economic benefit).

(c) *future economic benefits:*- An enterprise should asses the probability of future economic benefits using reasonable and supportable assumptions that represent best estimate of the set of economic conditions that will exist over the useful life of the asset on the basis of weight age to external evidence available at the time of initial recognition.

(d) Cost can be measured reliably :

   (i) Initially recognized at cost - purchase price, taxes duty and other directly attributable expenses to make the asset ready for its intended use, if acquired separately - purchase consideration in the form of cash or other monetary asset.

(ii) In exchange for shares or securities at fair value of those shares or securities.

(iii) In exchange or part exchange for another asset - as per AS-10.

The cost of an internally generated intangible asset comprises all expenditure that can be directly attributed or allocated on a reasonable and consistent basis for creating, producing and making the asset ready for its intended use, but in no case once treated as an expense, cannot be reversed for capitalization even if the essential criteria for recognition are complied with a later date.

Normally the following cost are not recognized for internally generated intangible asset:

1) selling, administrative and other general overhead unless directly attributable.

2) clearly identified inefficiencies and initial operating loses incurred before an asset achieves planned performance.

3) expenditure on training the staff to operate the asset.

Subsequent expenditure on an internally generated intangible asset after its purchase or completion is normally treated as expense unless it is assessed to generate future economic benefits over and above the originally assessed standard of performance or it can be measured and reliably attributed to the concerned intangible asset.

Amortization is the systematic allocation of the depreciable amount (cost less residual value usually "NIL" unless determined in terms of committed value by a third party or determined by active market price) of an intangible asset over its useful life (period of time for use, number of production or other similar units expected to obtain or legal restriction).

Under AS-26, useful life shall not exceed 10 years from the date the asset is available for use unless there is persuasive evidence to establish useful life longer than 10 years provided the enterprise

(a) amortizes over the best estimated useful life

(b) estimates the recoverable amount at least annually to identify the impairment loss

(c) disclose the reasons and factors in determining a longer life.

The amortization period and the amortization method should be reviewed at least at each, financial year and if the expected life is revised, the amortization period is revised accordingly but in no case it would tantamount to inappropriate deferment to later years.

AS-5 will be relevant in this regard as to what constitutes a change in accounting policy and what constitutes a change in estimate e.g. a change from straight-line to diminishing method or vice-versa would be change in accounting policy whereas reduction in the amortization period is change in accounting estimate.

Disclosure under AS-26

A) General

1. for each class of intangible asset distinguishing between internally generated and others

    (a) useful lives and amortization rates used

    (b) amortization method used

    (c) gross carrying amount and the accumulated amortization including impairment loss at the beginning and end of the reporting period

    (d) a reconciliation of the carrying amount (opening balance/addition/ disposal/impairment/loss charged/reversed/amortization for the period and other changes)

2. class of intangible asset by grouping of a similar nature and use by the enterprise informa tion on impaired intangible asset under AS-28 change in accounting policy or accounting estimate as per AS-5 reasons for amortization beyond 10 years with list of factors considered in determining the useful life.

3. Description, the carrying amount and remaining amortization period of any individual asset what is material to the financial statement as a whole.

4. Existence and carrying amount of intangible assets whose title is restricted and the carrying amount of intangible asset pledged as security for liabilities.

5. Amount of commitments for acquisition of intangible assets.

B) R&D expenditure: R&D expense (that is directly attributable or reasonably allocated on a consistent basis) recognized as an expense during the period.

C) Other information: encouraged to disclose a description of only fully amortized intangible asset but still in use.

Specific guideline for internally generated computer software - criteria for capitalization: apart from the broad recognition principles, AS-26 provides for specific guidance on internally generated computer software.

(a) At preliminary project stage, it is not recognized as an asset since the enterprise cannot demonstrate then exists as an asset from which future economic benefit will follow (making strategic decision, determination of performance requirements alternative means to achieve specified performance requirements. determination of technology to achieve performance requirements and selection of consultant to assist in development and/or installation of the software)

(b) At development stage involving detailed program design, coding working model in operative version for all major planned function and testing to bring it to a completed version together with related documentation and training material.

At this stage the internally generated computer software can be recognized as an asset on satisfying

1. The technical feasibility to make it available for internal use

2. Intention to complete to perform individual functions e.g. commitment for funding the project.

3. Ability to use the software

4. Usefulness of the software to generate future economic benefit

5. Availability of technical, financial and other resources to complete the development and use

6. Reliably measure the expenditure to the software development (b) cost has some connotation as described earlier in the standard.

(c) Accounting for software acquired or purchased should meet with the basic principle of AS-26 as discussed elsewhere in this standard.

For computer software considering the fact technological change and obsolescence.It is 3-5 years of useful life, which needs to be reasoned in the disclosure.

Expenditure for Website:

The expenditure for purchasing, developing, maintaining and enhancing hardware (servers, internet connection) related to web site are accounted for under AS-10 (fixed asset).

The expenditure may be incurred internally when developing enhancing and maintaining its own website in the context of planning, application and infrastructure development, graphical design and content development and operating stage which are directly attributable or allocable on a reasonable basis to creating, producing and preparing the asset for intended use. The nature of each activity should be evaluated to decide web site stage of development.

Accounting treatment and recognition:

(a) planning stage expenditure are akin to research cost and recognized as expense when incurred.

(b) expenditure arising onward development stage complying with the development criteria (refer to computer software) should be recognized as an Intangible asset.

Illustration 45.

On February 2015, J Ltd.bought a trademark from I Ltd. for ₹50 lakhs. J Ltd. retained an independent consultant, who estimated the trademark's remaining life to be 14 years. Its unamortized cost on I ltd. records was ₹35 lakhs. J Ltd.decided to amortize the trademark over the maximum period allowed. In J Ltd.'s Balance Sheet as on 31st December 2015, what amount should be reported as accumulated amortization?

Solution:

As per para 23 of AS-26, intangible assets should be measured initially at cost therefore. J Ltd. should amortize the trademark at its cost of ₹50 lakhs. The unamortized cost on the seller's books ₹35 lakhs is irrelevant to the buyer. Although the trademark has a remaining useful life of 14 years, intangible assets are generally amortized over a maximum period of 10 years as per AS-26. Therefore, the maximum amortization expense and accumulated amortization is ₹5 lakhs (₹50 lakhs/10).

Illustration 46.

During 2014-15, A Ltd.incurred organization costs/preliminary expenses of ₹40,000. What portion of the organization costs will A Ltd. defer to years subsequent to the 2014-15?

Solution:

As per para 56(a) of AS-26, organization costs /preliminary expenses are those incurred in the formation of a corporation. Since uncertainty exists concerning the future benefit of these costs in future years, they are properly recorded as an expense in 2014-15.

Illustration 47.

D Ltd. is developing a new distribution system of its material, following the costs incurred at different stages on research and development of the system:

Year ended 31.3	Phase/Expenses	Amount (₹ In lakhs)
2012	Research	8
2013	Research	10
2014	Development	30
2015	Development	36
2016	Development	50

On 31.3.12, D Ltd. identified the level of cost savings at ₹ 16 lakhs expected to be achieved by the new system over a period of 5 years, in addition this system developed can be marketed by way of consultancy which will earn cash flow of ₹10 lakhs per annum. D Ltd.demonstrated that new system meet the criteria of asset recognition as on 1.4.2014.

Determine the amount/cash which will be expensed and to be capitalized as intangible assets, presuming that no active market exist to determine the selling price of product i.e. system developed. System shall be available for use from 1.4.2012.

Solution:

As per AS-26, research cost of ₹18 lakhs to be treated as an expense in respective year ended 31st March 2012 and 2013 respectively.

The development expenses can be capitalized from the date the internally generated assets (new distribution system in this given case) meet the recognition criteria on and from 1.4.2012. Therefore, cost of ₹ (30 + 36 + 50) = ₹116 lakhs is to be capitalized as an intangible asset.

However, as per para 62 of AS-26, the intangible asset should be carried at cost less accumulated amortization and accumulated impairment losses.

At the end of 31st March, 2016, D Ltd. should recognize impairment loss of ₹22.322 lakhs = (116 - 93.678) and carry the new distribution system at ₹ 93.678 lakhs in the Balance Sheet as per the calculation given below:

Impairment loss is excess of carrying amount of asset over recoverable amount. Recoverable amount is higher of two i.e. value in use (discounted future cash inflow) and market realizable value of asset.

The calculation of discounted future cash flow is as under assuming 12% discount rate.

(₹ Lakhs)

Year	Cost Savings	Inflow by introducing the system	Total cash inflow	Discounted at 12%	Discounted cash flow
2017	16	10	26	0.893	23.218
2018	16	10	26	0.797	20.722
2019	16	10	26	0.711	18.486
2020	16	10	26	0.635	16.51
2021	16	10	26	0.567	14.742
					93.678

No amortization of asset shall be done in 2012 as amortization starts after use of asset which is during the year 2016-17.

Illustration 48.

M.S. International Ltd. is developing a new production process. During the financial year ending 31st March, 2015, the total expenditure incurred was ₹50 lakhs. This process met the criteria for recognition as an intangible asset on 1st December, 2014. Expenditure incurred till this date was ₹22 lakhs. Further expenditure incurred on the process for the financial year ending 31st March, 2016 was ₹80 lakhs. As at 31st March, 2016, the recoverable amount of know-how embodied in the process is estimated to be ₹72 lakhs. This includes estimates of future cash outflows as well as inflows.

You are required to calculate:

(i) Amount to be charged to Profit and Loss A/c for the year ending 31st March, 2015 and carrying value of intangible as on that date.

(ii) Amount to be charged to Profit and Loss A/c and carrying value of intangible as on 31st March, 2016. Ignore depreciation.

Solution:

As per AS 26 'Intangible Assets'

(i) For the year ending 31.03.2015

(a) Carrying value of intangiblet as on 31.03.2015:

At the end of financial year 31st March 2015, the production process will be recognized (i.e. carrying amount) as an intangible asset at a cost of ₹28 lakhs (expenditure incurred since the date the recognition criteria were met, i.e., on 1st December 2014).

(b) Expenditure to be charged to Profit and Loss account: The ₹ 22 lakhs is recognized as an expense because the recognition criteria were not met until 1st December 2015. This expenditure will not form part of the cost of the production process recognized in the balance sheet.

(ii) For the year ending 31.03.2016

(a) Expenditure to be charged to Profit and Loss account:

(₹ in lakhs)

Carrying Amount as on 31.03.2015	28
Expenditure during 2015 – 2016	80
Total book cost	108
Recoverable Amount	72
Impairment loss	36

₹ 36 lakhs to be charged to Profit and loss account for the year ending 31.03.2016.

(b) Carrying value of intangible as on 31.03.2016:

(₹ in lakhs)

Total Book Cost	108
Less: Impairment loss	36
Carrying amount as on 31.03.2016	72

AS-27: FINANCIAL REPORTING OF INTEREST IN JOINT VENTURE

AS-27 is applicable for accounting in joint venture interest and reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturer and investors, regardless of the structure or forms under which the joint venture activities take place,

The statement provides for display and disclosure requirement for accounting for the investment in the stand-alone and consolidated financial statements of the venturer.

A joint venture is a contractual arrangement between two or more parties undertaking an economic activity, subject to joint control (control is the power to govern the financial and operating policies of an economic activity to obtain benefit from it).

The arrangement may be:

(a) Jointly controlled operations

(b) Jointly controlled asset

(c) Jointly controlled entities

In the event an enterprise by a contractual arrangement establishes joint control over an entity which is a subsidiary of that enterprise within the meaning of AS-21(CFS), it will be treated as joint venture as per AS-27. Joint control requires all the venturers to jointly agree on key decisions, else decision cannot be taken, as such even a minority holder (owner) may enjoy joint control.

Contractual arrangement is normally made in writing touching upon:

(a) The activity, duration and reporting obligation

(b) The appointment of the board of director/governing body and the respective voting rights/capital contribution/sharing by ventures of the output, income, expenses or results of the joint venture.

Contractual arrangement and joint control together makes an activity a joint venture, (investment in Associates in which the investor has significant influence is covered by AS-23)

Some joint ventures involve use of own fixed assets and other resources on its own and obligation of its own.

For its interest in jointly controlled operations, a venturer should recognize in its separate financial statements and consequently in its CFS,

(a) the assets that it controls and the liabilities it incurs

(b) the expense it incurs and the share of income earned from the joint venture.

As the above are already recognized in stand-alone financial statements of the venturer and consequently in the CFS, there us no requirement for adjustment or other consolidation procedure, when the venturer present the CFS. Separate accounting records may not be required for the joint venture itself and financial statements may not be prepared for the joint venture.

Some joint ventures involve joint control; by means of joint ownership by the venturers of one or more assets contributed/acquired for the purpose of joint venture - the asset are used to obtain economic benefit for the venturers, agreeing to share the output from the assets and sharing of expenses incurred.

In respect of jointly controlled assets, each venturer recognize in its separate financial statement and consequently in its CFS:

(a) Share of the jointly controlled assets under distinct head of each asset and not as an investment

(b) Any liability incurred (e.g. financing its share of the assets)

(c) Share of joint liability in respect of the venturer

(d) Any income from sale or use of its share of the output in the joint venture and share of expenses.

(e) Expense is incurred in respect of its in the joint ventures e.g. financing the venturer's interests in the asset and selling its share of output The treatment of jointly controlled assets, recognizes the substance and economic reality (legal from of the joint venture) separate financial statements may not be prepared for the joint venture itself.

A jointly controlled entity involves the establishment of a corporation, partnership or lither entity in which each venturer has an interest as per contractual arrangement.

(a) in a separate/stand alone financial statement of each venturer, the interest in a jointly controlled entity should be accounted for as an investment as per AS-13 only the resources contributed, forms a part of the investment and the share' of joint venture result is treated in the income statement of the venturers.

(b) proportionate consolidation for joint venture is applied in case where the preparation and presenting a CFS is required, reflecting the substance and economic reality of the arrangement in the CFS. Many of the procedure in this regard are similar to AS-21 and require to be followed for treatment and disclosure.

Joint venture interest in the financial statements, of an investor is treated appropriately in terms of AS-13, AS-21 or AS-23 in CFS but for separate financial statements is should be accounted for as per *AS-13.*

Disclosure under AS-27:

In separate and CFS in respect of:

(a) Aggregate amount of contingent liabilities unless the probability of loss is remote separately from other contingent liabilities in relation to:

    1. Its interest in joint venture and its share in each of the contingent liabilities incurred jointly

    2. Its share of the contingent liability of the joint ventures themselves for which it is contingently liable.

    3. Those liabilities which arise because of the venturer is contingently liable for the liability of other venturers.

(b) Aggregate of commitments in respect of joint venture separately from other commitments in respect of:

    1. Capital commitment of its own and shares in the capital commitment incurred jointly with other ventures in relation to the joint venture.

    2. Share of capital commitment of the joint ventures themselves

(c) A list of all joint ventures and description of interest in significant joint venture and for jointly controlled entities the properties of ownership interest name of the country of incorporation/residence.

Illustration 49.

N Ltd has 80% shares in a joint venture with Suzuki Ltd. N Ltd. sold a plant WDV ₹20 lakhs for ₹30 lakhs. Calculate how much profit N Ltd. should recognize in its book in case joint venture is:

(a) jointly controlled operation;

(b) jointly controlled asset;

(c) jointly controlled entity.

Solution:

As per AS-27, in case of jointly controlled operation and jointly controlled assets joint venture, the venture should recognize the profit to the extent of other venturer's interest.

In the given case, N Ltd. should recognize profit of:

= ₹(30 – 20)lakhs = ₹10 x 20%= ₹2 lakhs only.

However, in case of jointly controlled entities N Ltd. should recognize full profit of ₹10 lakhs in its separate financial statement. However, while preparing consolidated financial statement it should recognize the profit only to the extent of 20% i.e. ₹ 2 lakhs only.

AS-28: IMPAIRMENT OF ASSETS

An asset is impaired if its carrying amount exceeds the amount to be recovered through use or sale of the asset and given the situation the standard requires the enterprise to recognize an impairment loss i.e. the amount by which the carrying amount of an asset exceeds its recoverable amount.

Impairment loss is a normal expense and thus will have impact on distributable profit and other provisions of the company's act and applicable enactment (Acceptance of Deposit Rules, BIFR etc)

Impairment loss may be discussed in the following areas:

1) Impairment loss on a specific asset;

2) Impairment loss for a cash generating unit;

3) Impairment loss for discontinuing operation.

Impairment Loss = Carrying amount of the Asset – Recoverable amount.

Carrying amount is the amount at which asset is shown in the Balance Sheet.

Recoverable amount of an asset is higher of:

- Net selling price
- Value in use

Net Selling Price= Expected realizable value of an asset – cost of disposal

Net Selling price can be obtained from:

- Active market for the asset
- Binding sale agreement
- Best estimate based on information

Value in Use= Present value of estimated future cash flow arising from the use of asset + residual value at the end of its useful life.

Present value is calculated by applying discount rate to future cash flows.

Estimated cash flows includes :

- Cash inflows from continuing use of the asset
- Projected cash outflows to generate cash inflows from continuing use of the asset.
- Net cash flows if any to be received(or paid) for the disposal of the asset at the end of its useful life.

Estimated cash flows excludes:

- Cash flows from financing activities
- Payment /refund of income tax

Discount rate: It is the cost of capital to be applied to calculate the present value of estimated cash flows and is based on the following factors:

- Pre-tax rate
- Current market assessment of time value of money after considering specific risk of the asset.
- Enterprises weighted average cost of capital or incremental financial cost.
- The current rate of inflation is also considered.

AS-28 does not apply to:

- inventories (as per AS 2);
- construction contract assets (as per AS 7);
- deferred tax assets (as per AS 22);
- investments covered by AS-13 and financial instruments, because other AS provide for recognizing and measuring these assets.

1) Assessment for impairment of assets needs to be made at the B/S date: as to any indication in this context based on external or internal source of information.

External sources:

- Market value changes with passage of time or normal use (typewriter on invention of computer)
- Adverse effect in the light of technological, market, economic, or legal environment in which the enterprise operates.
- Change in market rate of interest or returns on investment affect the discount rates used to assess an assets value in use (if the effect is not a short-term phenomenon).
- Carrying amount of the net asset, exceeds its market capitalization (determined by future growth, profitability, threat of new products/entrants etc).

Internal sources:

- Obsolescence /physical damage is evident.
- Indication obtained internally that economic performance of an asset has worsened or likely to worse than expected.
- Continuous cash loss may indicate that one or more of the business division is impaired.

Assessment for impairment should be made on individual asset basis, except when;

(i) The asset value in use cannot be estimated to be close to the net se1ling price i.e. future cash flow from continuing use of the asset cannot be estimated to be negligible or there is no plan to dispose of the assets in near future.

(ii) The asset does not generate cash inflows from continuing use that are largely independent of those from other assets.

In the exceptional case as above, the value in use/recoverable amount can be determined with regard assets cash generating units (generate cash inflows from outside the reporting enterprise and independent of cash inflows from other assets / group of assets.

2) Impairment Loss to a cash generating unit :

Cash generating unit (CGU): The smallest group of an asset for which cash flows can be determined independently.

Even if the cash flows can determined independently, aggregation of cash generating units becomes necessary in some situations.

To determine impairment loss of a CGU, we have to follow 'bottom up' or 'top down' test.

3) Impairment Loss for discontinuing operation :

In this type of situation, the impairment loss shall depend on the way the discontinuing operation is disposed off:

(a) substantially in its entirety;

(b) as piecemeal sales;

(c) by abandonment.

Illustration 50.

X Ltd.purchased a machinery on 1.1.2009 for ₹20 lakhs. WDV of the machine as on 31.3.15 ₹12 lakhs. The Recoverable amount of the machine is ₹11 lakhs. What is the impairment loss?

Solution:

Impairment Loss = Carrying amount – Recoverable Amount

= ₹12 lakhs – ₹11 lakhs = ₹ 1 lakh.

Ilustration 51.

Carrying amount ₹200 lakhs. Net Selling Price ₹210 lakhs. Value in use ₹ 220 lakhs. What is the impairment loss?

Solution:

Carrying amount ₹200 lakhs

Recoverable amount ₹ 220 lakhs (being the higher of net selling price and value in use)

Since, recoverable amount is more than carrying amount of the asset, there will arise no impairment loss.

Ilustration 52.

C Ltd.acquired a machine for ₹3.2 crores on 1.1.2012. It has a life of 5 years with a salvage value of ₹40 lakhs. Apply the test of impairment on 31.3.2015:

(a) Present value of future cash flow ₹ 1.3 crores

(b) Net selling price ₹ 1.2 crores

Solution:

Carrying amount of the asset: [3.2 – (3.2 – 0.4) x 39/60] = 1.38 crores.

Time period for use of the asset: 1.1.2012 to 31.3.2015 = 39 months

Total life period of the asset = 5 years = 60 months.

Recoverable amount: being the higher of present value and net selling price = ₹1.3 crores.

Impairment Loss = ₹(1.38 – 1.3) crores = ₹0.08 crores.

AS 29: PROVISIONS, CONTINGENT LIABILITIES AND CONTINGENT ASSETS

The objective of this Standard is to ensure that appropriate recognition criteria and measurement bases are applied to provisions and contingent liabilities and that sufficient information is disclosed in the notes to the financial statements to enable users to understand their nature, timing and amount.

The objective of this Standard is also to lay down appropriate accounting for contingent assets.

This standard is not applicable to:

- Financial instruments carried at fair value
- Insurance enterprises
- Contract under which neither party has performed any of its obligations or both parties have partially performed their obligation to an equal extent
- AS 7,AS 15,AS 19 and AS 22.

A provision is a liability which can be measured only by using a substantial degree of estimation.

A liability is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.

An obligating event is an event that creates an obligation that results in an enterprise having no realistic alternative to settling that obligation.

A contingent liability is:

(a) a possible obligation that arises from past events and the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise; or

(b) a present obligation that arises from past events but is not recognized because:

  (i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation;

  or

  (ii) a reliable estimate of the amount of the obligation cannot be made.

A contingent asset is a possible asset that arises from past events the existence of which will be confirmed only by the occurrence or nonoccurrence of one or more uncertain future events not wholly within the control of the enterprise.

Present obligation - an obligation is a present obligation if, based on the evidence available, its existence at the balance sheet date is considered probable, i.e., more likely than not.

Possible obligation - an obligation is a possible obligation if, based on the evidence available, its existence at the balance sheet date is considered not probable.

A restructuring is a programme that is planned and controlled by management, and materially changes either:

(a) the scope of a business undertaken by an enterprise; or

(b) the manner in which that business is conducted.

Past Event- A past event that leads to a present obligation is called an obligating event. For an event to be an obligating event, it is necessary that the enterprise has no realistic alternative to settling the obligation created by the event.

Best Estimate: The amount recognized as a provision should be the best estimate of the expenditure required to settle the present obligation at the balance sheet date. The amount of a provision should not be discounted to its present value.

Risks and Uncertainties: The risks and uncertainties that inevitably surround many events and circumstances should be taken into account in reaching the best estimate of a provision.

Future Events : Future events that may affect the amount required to settle an obligation should be reflected in the amount of a provision where there is sufficient objective evidence that they will occur.

Disclosure:

For each class of provision, an enterprise should disclose:

(a) the carrying amount at the beginning and end of the period;

(b) additional provisions made in the period, including increases to existing provisions;

(c) amounts used (i.e. incurred and charged against the provision) during the period; and

(d) unused amounts reversed during the period.

An enterprise should disclose the following for each class of provision:

(a) a brief description of the nature of the obligation and the expected timing of any resulting outflows of economic benefits;

(b) an indication of the uncertainties about those outflows. Where necessary to provide adequate information, an enterprise should disclose the major assumptions made concerning future events, as addressed in paragraph 41; and

(c) the amount of any expected reimbursement, stating the amount of any asset that has been recognised for that expected reimbursement.

Ilustration 53.

There is a income tax demand of ₹2.5 lakhs against the company relating to prior years against which the company has gone on appeal to the appellate authority in the department. The ground of appeal deals with the points covering ₹1.8 lakhs of the demand. State how the matter will have to be dealt with in the financial account for the year.

Solution:

A provision of ₹0.7 lakhs and a contingent liability of ₹ 1.8 lakhs should be provided in the financial accounts for the year.

Ilustration 54.

A company follows a policy of refunding money to the dissatisfied customers if they claim within 15 days from the date of purchase and return the goods. It appears from the past experience that in a month only 0.10% of the customers claim refunds. The company sold goods amounting to ₹20 lakhs during the last month of the financial year. Is there any contingency?

Solution:

There is a probable present obligation as a result of past obligating event. The obligating event is the sale of the product. Provision should be recognized as per AS-29. The best estimate for provision is ₹2,000 (₹20 lakhs x 0.1%).

Illustration 55.

Mega Ltd. took a factory premises on lease on 1.4.2014 for ₹2,00,000 per month. The lease is operating lease. During March, 2015, Mega Ltd. relocates its operation to a new factory building. The lease on the old factory premises continues to be live upto 31.12.2017. The lease cannot be cancelled and cannot be sub-let to another user. The auditor insists that lease rent of balance 33 months upto 31.12.2017 should be provided in the accounts for the year ending 31.3.2015. Mega Ltd. seeks your advice.

Solution:

In accordance with AS 29 'Provisions, Contingent Liabilities and Contingent Assets' and ASI 30 'Applicability of AS 29 to Onerous Contracts', if an enterprise has a contract that is onerous, the present obligation under the contract should be recognized and measured as a provision. In the given case, the operating lease contract has become onerous as the economic benefit of lease contract for next 33 months up to 31.12.2017 will be nil. However, the lessee, Mega Ltd., has to pay lease rent of ₹ 66,00,000 (i.e.2,00,000 p.m. for next 33 months).

Therefore, provision on account of ₹66,00,000 is to be provided in the accounts for the year ending 31.03.15. Hence auditor is right.

AS-30: FINANCIAL INSTRUMENTS: RECOGNITION AND MEASUREMENT

The objective of this Standard is to establish principles for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items.

Requirements for presenting information about financial instruments are in Accounting Standard (AS) 31, *Financial Instruments: Presentation.* Requirements for disclosing information about financial instruments are in Accounting Standard (AS) 32, *Financial Instruments:*

Definitions:

The terms defined in AS 31, *Financial Instruments: Presentation* are used in this Standard with the meanings specified in paragraph 7 of AS 31. AS 31 defines the following terms:

- financial instrument
- financial asset
- financial liability
- equity instrument

and provides guidance on applying those definitions.

Definition of a Derivative:

A derivative is a financial instrument or other contract within the scope of this Standard with all three of the following characteristics:

(a) its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract (sometimes called the 'underlying');

(b) it requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and

(c) it is settled at a future date.

Definitions of Four Categories of Financial Instruments :

A financial asset or financial liability at fair value through profit or loss is a financial asset or financial liability that meets either of the following conditions.

(a) It is classified as held for trading. A financial asset or financial liability is classified as held for trading if it is:

  (i) acquired or incurred principally for the purpose of selling or repurchasing it in the near term; or

  (ii) part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking; or

  (iii) a derivative (except for a derivative that is a financial guarantee contract or a designated and effective hedging instrument).

(b) Upon initial recognition it is designated by the entity as at fair value through profit or loss.

Accounting Standard (AS) 32, Financial Instruments: Disclosures , requires the entity to provide disclosures about financial assets and financial liabilities it has designated as at fair value through profit or loss, including how it has satisfied these conditions.

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that an entity has the positive intention and ability to hold to maturity other than:

(a) those that the entity upon initial recognition designates as at fair value through profit or loss;

(b) those that meet the definition of loans and receivables; and

(c) those that the entity designates as available for sale.

An entity should not classify any financial assets as held to maturity if the entity has, during the current financial year or during the two preceding financial years, sold or reclassified more than an insignificant amount of held-to-maturity investments before maturity (more than insignificant in relation to the total amount of held-to-maturity investments) other than sales or reclassifications.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

(a) those that the entity intends to sell immediately or in the near term, which should be classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss;

(b) those that the entity upon initial recognition designates as available for sale; or

(c) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which should be classified as available for sale.

Available-for-sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified as (a) loans and receivables, (b) held-to-maturity investments, or (c) financial assets at fair value through profit or loss.

Definition of a financial guarantee contract

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

Definitions Relating to Recognition and Measurement

The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, and minus any reduction (directly or through the use of an allowance account) for impairment or uncollectibility.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.

Derecognition is the removal of a previously recognised financial asset or financial liability from an entity's balance sheet.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

A regular way purchase or sale is a purchase or sale of a financial asset under a contract whose terms require delivery of the asset within the time frame established generally by regulation or convention in the marketplace concerned.

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability. An incremental cost is one that would not have been incurred if the entity had not acquired, issued or disposed of the financial instrument.

Definitions Relating to Hedge Accounting

A firm commitment is a binding agreement for the exchange of a specified quantity of resources at a specified price on a specified future date or dates.

A forecast transaction is an uncommitted but anticipated future transaction.

Functional currency is the currency of the primary economic environment in which the entity operates.

A hedging instrument is (a) a designated derivative or (b) for a hedge of the risk of changes in foreign currency exchange rates only, a designated non-derivative financial asset or non-derivative financial liability whose fair value or cash flows are expected to offset changes in the fair value or cash flows of a designated hedged item.

A hedged item is an asset, liability, firm commitment, highly probable forecast transaction or net investment in a foreign operation that (a) exposes the entity to risk of changes in fair value or future cash flows and (b) is designated as being hedged.

Hedge effectiveness is the degree to which changes in the fair value or cash flows of the hedged item that are attributable to a hedged risk are offset by changes in the fair value or cash flows of the hedging instrument.

Embedded Derivative:

An embedded derivative is a component of a hybrid (combined) instrument that also includes a non-derivative host contract—with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative.

AS 31: FINANCIAL INSTRUMENTS: PRESENTATION

The objective of this Standard is to establish principles for presenting financial instruments as liabilities or equity and for offsetting financial assets and financial liabilities. It applies to the classification of financial instruments, from the perspective of the issuer, into financial assets, financial liabilities and equity instruments; the classification of related interest, dividends, losses and gains; and the circumstances in which financial assets and financial liabilities should be offset.

The principles in this Standard complement the principles for recognising and measuring financial assets and financial liabilities in Accounting Standard (AS) 30.

Definitions

The following terms are used in this Standard with the meanings specified:

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

A financial asset is any asset that is:

(a) cash;

(b) an equity instrument of another entity;

(c) a contractual right:

  (i) to receive cash or another financial asset from another entity; or

  (ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the entity; or

(d) a contract that will or may be settled in the entity's own equity instruments and is:

(i) a non-derivative for which the entity is or may be obliged to receive a variable number of the entity's own equity instruments; or

(ii) a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.

A financial liability is any liability that is:

(a) a contractual obligation:

(i) to deliver cash or another financial asset to another entity; or

(ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity; or

(b) a contract that will or may be settled in the entity's own equity instruments and is:

(i) a non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or

(ii) a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity 's own equity instruments. For this purpose the entity's own equity instruments do not include instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Financial Instruments: Recognition and Measurement and are used in this Standard with the meaning specified in AS 30.

- amortised cost of a financial asset or financial liability
- available-for-sale financial assets
- derecognition
- derivative
- effective interest method
- financial asset or financial liability at fair value through profit or loss
- financial guarantee contract
- firm commitment
- forecast transaction
- hedge effectiveness
- hedged item
- hedging instrument
- held-to-maturity investments

- loans and receivables
- regular way purchase or sale
- transaction costs.

In this Standard, 'contract' and 'contractual' refer to an agreement between two or more parties that has clear economic consequences that the parties have little, if any, discretion to avoid, usually because the agreement is enforceable by law. Contracts, and thus financial instruments, may take a variety of forms and need not be in writing.

In this Standard, 'entity' includes individuals, partnerships, incorporated bodies, trusts and government agencies.

AS 32: FINANCIAL INSTRUMENTS: DISCLOSURES

The objective of this Standard is to require entities to provide disclosures in their financial statements that enable users to evaluate:

(a) the significance of financial instruments for the entity's financial position and performance; and

(b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the reporting date, and how the entity manages those risks.

The principles in this Accounting Standard complement the principles for recognising, measuring and presenting financial assets and financial liabilities in Accounting Standard

(AS) 30, Financial Instruments: Recognition and Measurement and Accounting Standard (AS) 31, Financial Instruments: Presentation.

Significance of financial instruments for financial position and performance

An entity should disclose information that enables users of its financial statements to evaluate the significance of financial instruments for its financial position and performance.

Balance sheet

Categories of financial assets and financial liabilities

The carrying amounts of each of the following categories, as defined in AS 30, should be disclosed either on the face of the balance sheet or in the notes:

(a) financial assets at fair value through profit or loss, showing separately

  (i) those designated as such upon initial recognition and

  (ii) those classified as held for trading in accordance with AS 30;

(b) held-to-maturity investments;

(c) loans and receivables;

(d) available-for-sale financial assets;

(e) financial liabilities at fair value through profit or loss, showing separately

  (i) those designated as such upon initial recognition and

  (ii) those classified asheld for trading in accordance with AS 30; and

(f) financial liabilities measured at amortised cost.

Financial assets or financial liabilities at fair value through profit or loss

If the entity has designated a loan or receivable (or group of loans or receivables) as at fair value through profit or loss, it should disclose:

(a) the maximum exposure to credit risk of the loan or receivable (or group of loans or receivables) at the reporting date.

(b) the amount by which any related credit derivatives or similar instruments mitigate that maximum exposure to credit risk.

(c) the amount of change, during the period and cumulatively, in the fair value of the loan or receivable (or group of loans or receivables) that is attributable to changes in the credit risk of the financial asset determined either:

 (i) as the amount of change in its fair value that is not attributable to changes in market conditions that give rise to **market risk**; or

 (ii) using an alternative method the entity believes more faithfully represents the amount of change in its fair value that is attributable to changes in the credit risk of the asset. Changes in market conditions that give rise to market risk include changes in an observed (benchmark) interest rate, commodity price, foreign exchange rate or index of prices or rates.

(d) the amount of the change in the fair value of any related credit derivatives or similar instruments that has occurred during the period and cumulatively since the loan or receivable was designated.

If the entity has designated a financial liability as at fair value through profit or loss in accordance with AS 30, it should disclose:

(a) the amount of change, during the period and cumulatively, in the fair value of the financial liability that is attributable to changes in the credit risk of that liability determined either:

 (i) as the amount of change in its fair value that is not attributable to changes in market conditions that give rise to market risk ,or

 (ii) using an alternative method the entity believes more faithfully represents the amount of change in its fair value that is attributable to changes in the credit risk of the liability.

Changes in market conditions that give rise to market risk include changes in a benchmark interest rate, the price of another entity's financial instrument, a commodity price, a foreign exchange rate or an index of prices or rates. For contracts that include a unit-linking feature, changes in market conditions include changes in the performance of the related internal or external investment fund.

(b) the difference between the financial liability's carrying amount and the amount the entity would be contractually required to pay at maturity to the holder of the obligation.

Reclassification

If the entity has reclassified a financial asset as one measured:

(a) at cost or amortised cost, rather than at fair value; or

(b) at fair value, rather than at cost or amortised cost,

it should disclose the amount reclassified into and out of each category and the reason for that reclassification.

1.3 INTERNATIONAL FINANCIAL REPORTING STANDARDS

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

IFRS — The Global Standard

- ✓ International Financial Reporting Standards (IFRS) are accounting standards issued by the International Accounting Standards Board (IASB). These are global accounting standards that are issued with the intention of ensuring uniformity in accounting across the globe.
- ✓ These areintended to provide investors and other stake-holders the ability to compare the financial performance of publicly listed companies.
- ✓ 'IFRSs' is the trademark of the International Accounting Standards Committee Foundation. The Foundation owns the copyright to IFRS in all languages.
- ✓ IFRSs are now mandated for use by more than 140 countries, including the European Union and by more than two-thirds of the G20 nations. The G20 and other international organisations including the World Bank, IMF, Basel Committee etc. have consistently supported the work of the IASB and its mission of global accounting standards.

Features of IFRS

The characteristics of IFRS are:

- These are global accounting standards.
- These standards are 'principle based', and not 'rule-based'.
- IFRS are developed and maintained by the IASB.
- These are issued with the intention of applying these standards across the globe on a consistent basis.
- It ensures high quality transparent reporting that would ensure comparability among the entities across the globe.
- Every standard has a specific structure to ensure uniformity and facilitate reading, interpretation and application. They are: Introduction, Standards, Basis of Conclusion (BC), Implementation Guidelines (IG), Illustrative Examples (IE), and Dissenting Opinions of board members.

Journey from IASC to IASB

- The story of International Accounting Standards started in the mid-1960s when the need was felt to form an international institution dealing with and addressing the uniformity of accounting practices. This led to the formation of Accounts International Study Group (AISG) in 1967. This group put ahead the idea for a single international body for evolving accounting standards.
- It was the year 1973, when an agreement was reached to establish an international body with the sole purpose of drafting and issuing accounting standards which are to be used internationally. Thus, the **International Accounting Standards Committee (IASC)** was formed in June 1973 in London through an agreement made by professional accountancy bodies from Australia, Canada, France, Germany, Japan, Mexico, the Netherlands, the United Kingdom and Ireland, and the United States of America.
- The International Accounting Standards Committee was essentially the structure, rather than a committee in the traditional sense of a group of people. There was no actual "committee" of that name.The IASC Board promulgated a substantial body of Standards, Interpretations, a Conceptual Framework, and other guidance that was adopted directly by many companies and that was looked to by many national accounting standard-setters in developing national accounting standards.
- er nearly 25 years of achievement, IASC concluded in 1997 that to continue to perform its role effectively, it must find a way to bring about convergence between national accounting standards and practices and

high-quality global accounting standards. To do that, IASC saw a need to change its structure. In late 1997 IASC formed a Strategy Working Party to re-examine its structure and strategy.

- After nearly 25 years of achievement, IASC concluded in 1997 that to continue to perform its role effectively, it must find a way to bring about convergence between national accounting standards and practices and high-quality global accounting standards. To do that, IASC saw a need to change its structure. In late 1997 IASC formed a **Strategy Working Party** to re-examine its structure and strategy.
- The Strategy Working Party published its Report, in the form of a Discussion Paper, in December 1998. After soliciting comments, the Working Party published its Final Recommendations in November 1999.The IASC Board approved the proposals unanimously in December 1999, and the IASC member bodies did the same in May 2000. A new IASB Constitution took effect from 1 July 2000. The standards-setting body was renamed the **International Accounting Standards Board (IASB).** It would operate under a new International Accounting Standards Committee Foundation (IASCF, presently called the IFRS Foundation).
- Accordingly, from 1 April 2001, the standards-setting work of the IFRS Foundation was then conducted by the International Accounting Standards Board (IASB). The IFRS Interpretations Committee develops and solicits comment on interpretive guidance for applying Standards promulgated by the IASB, but the IASB must approve the Interpretations developed by IFRIC.

IFRS Organisation Structure:

The IFRS Organisation structure includes the following:

✓ **IFRS Foundation Monitoring Board**: The Monitoring Board is a body of publically accountable markets authorities which was created in January 2009 with the aim of "providing a formal link between the Trustees and public authorities" for enhancing the public accountability of the IFRS Foundation. The Monitoring Board's main responsibilities are to ensure that the Trustees continue to discharge their duties as defined by the IFRS Foundation Constitution, as well as approving the appointment or reappointment of Trustees. The Monitoring Board meets the Trustees at least once a year, or more often if appropriate.

✓ **IFRS Foundation Trustees**: The IFRS Foundation Trustees are responsible for the governance and oversight of the International Accounting Standards Board (IASB).It is to be noted that the Trustees are not involved in any technical matters relating to the Standards, the responsibility of which rests solely with the IASB. However, the Trustees are accountable to the IFRS Foundation Monitoring Board.

✓ **IFRS Foundation**: The two main functions of the IFRS Foundation are – 'Governance & Oversight' and 'Operations'. The two primary wings operating under the IFRS Foundation are the International Accounting Standards Board (IASB) and the IFRS Interpretations Committee. They share a common view on the role that the Interpretations Committee should play; both bodies see the Interpretations Committee as working in partnership with the IASB to give guidance that responds to the implementation needs of those applying IFRS. Both bodies also focus on the importance of achieving a balance between the principle-based approach of IFRS and providing guidance with sufficient detail to ensure that it is useful and practical. The structures and responsibilities of these two bodies are discussed hereunder:

(a) **International Accounting Standards Board (IASB):** It is an independent group of 14 experts in setting accounting standards, in preparing, auditing, or using financial reports, and in accounting education. These IASB members are responsible for the development and publication of IFRS, including the IFRS for SMEs. The IASB is also responsible for approving Interpretations of IFRS as developed by the IFRS Interpretations Committee (formerly IFRIC). The IASB members are appointed by the Trustees.

(b) **IFRS Interpretations Committee:** The IFRS Interpretations Committee is the interpretative body of the IASB. The objectives of the Interpretations Committee are to interpret the application of IFRS, provide timely guidance on financial reporting issues that are not specifically covered in IFRS and undertake other responsibilities at the request of the IASB. The IFRS Interpretations Committee comprises 14 voting members drawn from a variety of countries and professional backgrounds. They are appointed by the Trustees of the IFRS Foundation. This Committee is responsible for reviewing on a timely basis

implementation issues that have arisen within the context of current IFRS and to provide authoritative guidance (IFRIC Interpretations) on those issues. For the development of such interpretations, the Interpretations Committee works closely with similar national committees and follows a transparent, thorough and open due process.

✓ **IFRS Advisory Council:** The IFRS Advisory Council is the formal advisory body to the IFRS Foundation Trustees and the IASB. Members of the Advisory Council are appointed by the Trustees. It consists of a wide range of representatives from different interested and affected groups, and include investors, financial analysts and other users of financial statements, as well as preparers, academics, auditors, regulators, professional accounting bodies and standard-setters. The Advisory Council generally meets in London three times a year for a period of two days.

✓ **Accounting Standards Advisory Forum (ASAF):**The ASAF is an advisory forum where members can constructively contribute towards the achievement of the IASB's goal of developing globally accepted high-quality accounting standards. The ASAF generally meets in London four times a year for two days.

The primary objectives for establishment of the ASAF are:

(i) to support the IFRS Foundation in its objectives, and contribute towards the development, in the public interest, of a single set of high quality understandable, enforceable and globally accepted financial reporting standards to serve investors and other market participants in making informed resource allocations and other economic decisions;

(ii) to formalise and streamline the IASB's collective engagement with the global community of national standard-setters and regional bodies in its standard setting process to ensure that a broad range of national and regional input on major technical issues related to the IASB's standard setting activities are discussed and considered; and

(iii) to facilitate effective technical discussions on standard-setting issues, primarily on the IASB's work plan, but which may include other issues that have major implications for the IASB's work, in sufficient depth, with representatives at a high level of professional capability and with a good knowledge of their jurisdictions/ regions.

Constituents of IFRS

The term IFRS constitutes in its fold:

- International Accounting Standards (IAS);
- International Financial Reporting Standards (IFRS);
- SIC Interpretations; and
- IFRIC Interpretations.

International Accounting Standards (IAS): The international accounting standards (IAS) were an older set of standards stating how particular types of transactions and other events should be reflected in financial statements. In the past, International Accounting Standards were issued by the Board of the International Accounting Standards Committee (IASC);

International Financial Reporting Standards (IFRS): Since 2001, the new set of standards has been known as the International Financial Reporting Standards (IFRS) and has been issued by the International Accounting Standards Board (IASB).

SIC Interpretations: These were interpretations that were issued by the erstwhile Standard Interpretations Committee (SIC). In total 33 SICs were issued during the period 1997 to 2001.

IFRIC Interpretations: These are publications issued by IFRS Interpretations Committee on specific issues that arisen within the context of current International Financial Reporting Standards (IFRSs). These provide appropriate accounting treatment and authoritative guidance on those issues. In total 21 IFRICs have been issued during the period 2004 to 2013.

Process of Developing IFRS

The International Accounting Standards Board (IASB) is the independent standard-setting body of the IFRS Foundation. For the purpose of developing the standards, the IASB engages closely with various stakeholders from across the globe, which includes investors, analysts, regulators, business leaders, accounting standard-setters and the accountancy profession.

The national and regional standard setting bodies happen to be important participants of the IASB standard setting process. Some of the significant parties include: Asian-Oceanian Standard Setters Group (AOSSG), European Financial Reporting Group (EFRAG) and Group of Latin American Standard Setters (GLASS).

International Financial Reporting Standards (IFRS) are developed through an international consultation process, called the '**Due Process'.** This process involves interested individuals and organisations from around the world. The 'Due Process' comprises six stages, providing the Trustees of the IFRS Foundation with the opportunity to ensure compliance at various points.

These six stages are:

1. Setting the agenda:

The IASB evaluates the merits of adding a potential item to its agenda, also know as the work plan, mainly by reference to the needs of investors. In this regard, the IASB takes into consideration the following points:

- the relevance to users of the information and the reliability of information that could be provided;
- whether existing guidance is available;
- the possibility of increasing convergence;
- the quality of the standard to be developed; and
- resource constraints.

To help the IASB in considering its future agenda, their staffs are asked to identify, review and raise issues that might warrant the IASB's attention.

New issues may also arise from a change in the IASB's Conceptual Framework. In addition, the IASB raises and discusses potential agenda items in the light of comments from other standard-setters and other interested parties, the IFRS Advisory Council and the IFRS Interpretations Committee, and staff research and other recommendations.

The IASB receives requests from constituents to interpret, review or amend existing publications. The staff consider all such requests, summarise major or common issues raised, and present them to the IASB from time to time as candidates for when the IASB is next considering its agenda.

2. Planning the project:

At this stage, the IASB takes decision regarding whether to conduct the project alone, or jointly with another standard-setter. After considering the nature of the issues and the level of interest among constituents, the IASB may establish a **Consultative Group** at this stage.

A team is selected for the project by the two most senior members of the technical staff – The Director of Technical Activities and the Director of Research. The project manager draws up a project plan under the supervision of those Directors. The team may also include members of staff from other accounting standard-setters, as deemed appropriate by the IASB.

3. Developing and publishing the Discussion Paper, including public consultation:

The IASB usually publishes a Discussion Paper as its first publication on any major new topic. It is done for explaining the issue and solicits early comment from constituents. It is to be, however, noted that a Discussion Paper is not mandatory**.** If the IASB decides to omit this step, it should state the reason for not doing so.

Typically, a Discussion Paper includes:

- ✓ a comprehensive overview of the issue;

- ✓ possible approaches in addressing the issue;
- ✓ the preliminary views of its authors or the IASB; and
- ✓ an invitation to comment.

This approach may differ if another accounting standard-setter develops the research paper.

All discussions of technical issues related to the draft paper take place in public sessions.

4. Developing and publishing the Exposure Draft, including public consultation:

An Exposure Draft happens to be IASB's main vehicle for consulting the public. Irrespective of whether the IASB has published a Discussion Paper, the publication of an Exposure Draft is a mandatory step in Due Process. Unlike a Discussion Paper, an Exposure Draft sets out a specific proposal in the form of a proposed Standard (or amendment to an existing Standard).

The development of an Exposure Draft begins with the IASB considering:

- ✓ issues on the basis of staff research and recommendations;
- ✓ comments received on any Discussion Paper; and
- ✓ suggestions made by the IFRS Advisory Council, Consultative groups and accounting standard-setters, and arising from public education sessions.

After resolving issues at its meetings, the IASB instructs the staff to draft the Exposure Draft.

When the draft has been completed, and the IASB has balloted on it, the IASB publishes it for public comment.

5. Developing and publishing the Standard:

After taking into consideration the comments on the Exposure Draft, development of an IFRS Standard is carried out during IASB meetings. The IASB, after resolving the issues that arose from the Exposure Draft, considers whether it should expose its revised proposals for public comment, for example by publishing a second Exposure Draft.

In considering the need for re-exposure, the IASB:

- ✓ identifies substantial issues that emerged during the comment period on the Exposure Draft that it had not previously considered;
- ✓ assesses the evidence that it has considered;
- ✓ evaluates whether it has sufficiently understood the issues and actively sought the views of constituents; and
- ✓ considers whether the various viewpoints were aired in the Exposure Draft and adequately discussed and reviewed in the basis for conclusions.

Drafting the Standard

The IASB's decision on whether to publish its revised proposals for another round of comments is made in an IASB meeting. If the IASB decides that re-exposure is necessary, the Due Process to be followed is the same as for the first Exposure Draft. When the IASB is satisfied that it has reached a conclusion on the issues arising from the Exposure Draft, it instructs the staff to draft the Standard.

A *pre-ballot draft* is usually subject to external review, normally by the IFRS IC. Shortly before the IASB ballots the Standard, a near-final draft is posted on *e-IFRS*.

Finally, after the due process is satisfactorily completed, all outstanding issues are resolved, and the IASB members have balloted in favour of publication, the Standard is issued.

6. Procedures after a Standard is issued:

After a Standard is issued, the staff and the IASB members hold regular meetings with interested parties, including other standard-setting bodies, to help understand unanticipated issues related to the practical implementation and potential impact of its proposals.

The IFRS Foundation also fosters educational activities to ensure consistency in the application of IFRS Standards.

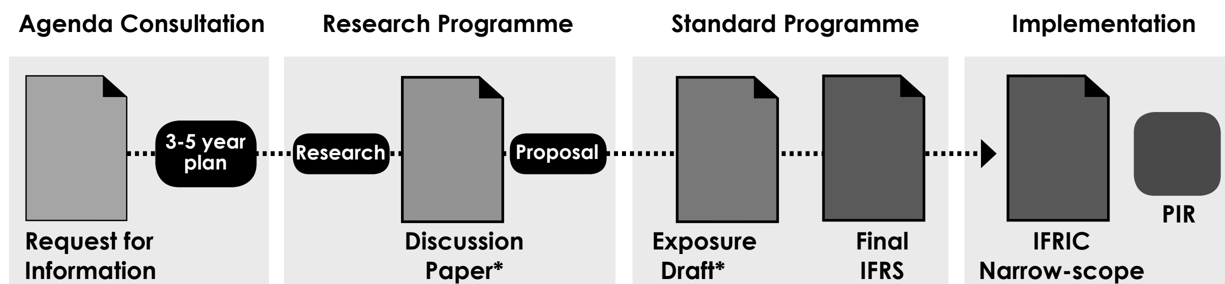
After a suitable time, the IASB may consider initiating studies in the light of:

✓ its review of the Standard's application;

✓ changes in the financial reporting environment and regulatory requirements; and

✓ comments by the IFRS Advisory Council, the IFRS Interpretations Committee, standard-setters and constituents about the quality of the Standard.

Those studies may result in items being added to the IASB's work plan.



The Standard Setting Process [Source: www.ifrs.org]

Process of developing IFRS Interpretations

IFRS Interpretations are constituents of IFRS that are designed for general application and are not issued to resolve matters that are specific to a particular entity. The IASB and the IFRS Interpretations Committee (simply, referred to as the 'Interpretations Committee') are responsible for the maintenance of IFRS. The types of issues that the Interpretations Committee is called on to deal with include the identification of divergent practices that have emerged for accounting for particular transactions, cases of doubt about the appropriate accounting treatment for a particular circumstance or concerns expressed by investors about poorly specified disclosure requirements.

The IFRS Interpretations Committee's 'due process' comprises the following stages:

a. Identification of Matters:

Any relevant issue may be put forward by any party(an individual or organisation) with an interest in financial reporting to the Interpretations Committee when it feels that it is important that the matter be addressed by the IASB or the Interpretations Committee. When any issue is referred to the Interpretations Committee, it usually consults the national accounting standard-setting bodies, regional bodies and securities regulators. The IASB staff assesses the issue and prepares an analysis concerning the scope of the issue and whether it meets the agenda criteria.

b. Setting up of the Agenda:

The IFRS Interpretations Committee decides after debate in a public meeting whether to add an issue to its agenda. A simple majority of Interpretations Committee members present can decide, after the debate in the public meeting, whether to add any issue to its work programme. An *Agenda Paper* is developed for the Interpretations Committee's consideration after a thorough review of the authoritative accounting literature and possible alternatives, including consultation when appropriate with national standard-setters and securities regulators.

However, if the Interpretations Committee does not plan to add an item to its work programme, it publishes this as a tentative rejection notice in the IFRIC Update and on the IFRS IC Activities page, and requests comments on the matter. The comment period for rejection notices is normally at least 60 days. After considering the comments received, the Interpretations Committee will either confirm its decision and issue a rejection notice add the issue to its work programme, or refer the matter to the IASB.

c. Meetings and Voting of the IFRS Interpretations Committee:

The Interpretations Committee meets in public and follows procedures similar to the IASB's general policy for its IASB meetings. To constitute a quorum for the Interpretations Committee there must be 10 voting members present in person or by telecommunications. At such meetings, the Interpretations Committee debates both matters that are already on its agenda and items proposed to be added to its agenda. Interpretations Committee members and appointed observers are expected to attend meetings in person. However, meetings may be held using teleconference, videoconference or any other communication facilities that permit simultaneous communication among all members and appointed observers, and allow public observers to hear all participants.

Each Interpretations Committee voting member has one vote. Members vote in accordance with their own independent views, not as representatives of any firm, organisation or constituency with which they may be associated. It is to be noted that proxy voting by members of the Interpretations Committee is not permitted.

d. Development of Minor or Narrow-scope Amendments to Standards:

Minor or Narrow-scope Amendments to Standards (including Annual Improvements) do not need to follow the IASB's formal consultation process. In these cases, involving minor or narrow-scope amendments to Standards, the IASB considers developing an Exposure Draft. In other cases, the IASB may seek the assistance of the Interpretations Committee in developing an amendment to a Standard.

Some proposed amendments to Standards or Interpretations that are sufficiently minor or narrow in scope are usually packaged together and exposed in one document even though the amendments are unrelated. Such amendments are called *Annual Improvements.* Annual Improvements follow the same 'due process' as other amendments to Standards.

e. Development of Interpretations:

Interpretations are developed by the Interpretations Committee. However, since they are part of IFRS, they must be ratified by the IASB. Three members of the IASB usually attend meetings of the Interpretations Committee. In addition, a report of each meeting of the Interpretations Committee is presented to the IASB at one of its public meetings.

A draft interpretation is developed on which the Interpretations Committee votes. Voting takes place at a public meeting. General agreement on the draft Interpretation is achieved when no more than four members have voted against the proposal. The publication of the draft Interpretation happens to the next step. It is a mandatory step in the due process before a new Interpretation can be issued. It is the main vehicle for consulting the public, and therefore includes an invitation to comment, setting out the issues that have been identified as being of particular significance. The IASB and the Interpretations Committee usually allow a minimum period of 90 days for comments on a draft Interpretation. However, if the matter is narrow in scope and urgent the IASB may consider a lesser comment period, but not less than 30 days. Comment letters are made publicly available unless confidentiality is requested by the commentator. A staff summary and analysis of the comment letters is provided to the Interpretations Committee. The Interpretations Committee reconsiders the summary conclusions in the draft Interpretation based on the comments received and detailed staff analysis. However, if the draft Interpretation is changed significantly, the Interpretations Committee will consider whether it should be re-exposed.

When the Interpretations Committee has reached a consensus on an Interpretation, the Interpretation is put to the IASB for ratification before being issued. Ratification of an Interpretation takes place in a public meeting of the IASB and requires a supermajority i.e. the same level of support by IASB members as is required for a new or amended Standard. These ratified Interpretations are issued by the IASB. If an Interpretation is not approved by the IASB, the IASB provides the Interpretations Committee with reasons for the objection.

If the Interpretations Committee believes that a Standard or the Conceptual Framework should be modified, or an additional Standard should be developed, it refers such conclusions to the IASB. The IASB can also decide to address minor matters that have a narrow scope without involving the Interpretations Committee. The Interpretations Committee applies a principle-based approach founded on the *Conceptual Framework*.

It considers the principles established in the relevant Standards to develop its interpretative guidance and to determine that the proposed guidance does not conflict with IFRS. It follows that, in providing interpretative guidance, the Interpretations Committee is not seeking to create an extensive rule-oriented environment, nor does it act as an urgent issues group.

IFRS — The Present Global Scenario

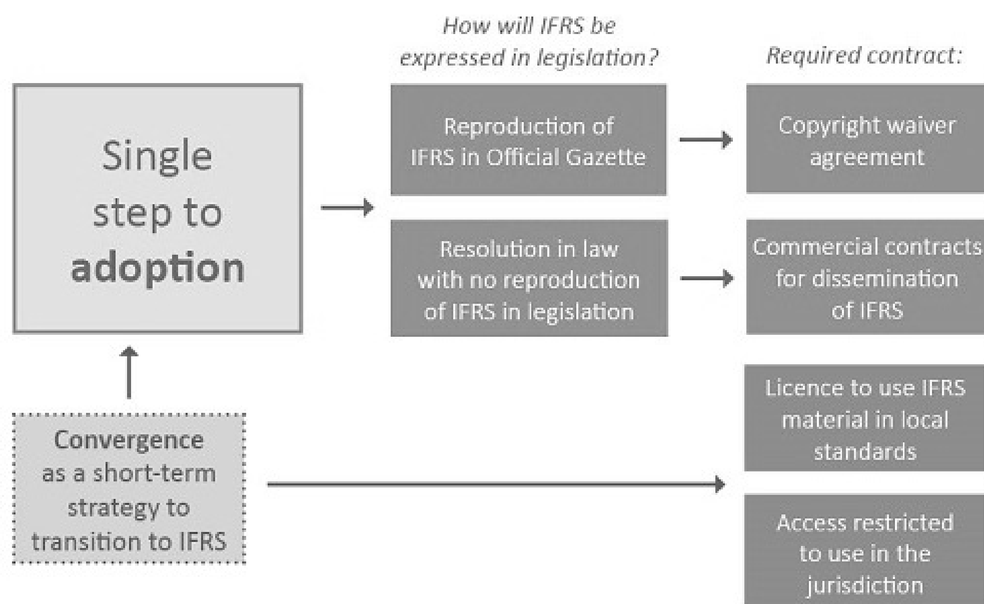
- ✓ Most of the world has been reporting under the International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). However, many jurisdictions that maintain their own local GAAP claim that their local GAAP is "based on" or "similar to" or "converged with" IFRSs. In some cases the wording changes seem minor, and in other cases the wording is quite different. Sometimes, the jurisdiction's local GAAP is not in English. Often, not all IASs/IFRSs have been adopted locally. Often there is a time lag in adopting an IFRS as local GAAP.
- ✓ In July 2002, a regulation was passed in the European Parliament requiring the adoption of IFRS by all EU listed companies from 2005. The initial ideas around the adoption of the EU IAS regulations were very positive.
- ✓ Since then, most countries across the globe have adopted/ converged with IFRS. The last of the developed countries to adopt IFRS was Japan. Earlier, one of the present day global super-power – China too converged with IFRS, but retained only one difference between Chinese GAAP and IFRS.
- ✓ After this, only two significant countries, viz., India and USA, were not using IFRS. However, USA allows IFRS for foreign private issuers with securities traded on US exchanges. There is renewed optimism that the US may allow even US companies to voluntarily adopt IFRS in the future. Besides since long, the US standard-setters and the IASB have been converging and working together on numerous accounting standards. This has resulted in the US GAAP slowly inching forward closer to IFRS.
- ✓ India has fulfilled its promise of compliance with international financial reporting standards (IFRSs) by adopting an amended version of IFRS, known as the Indian Accounting Standards (Ind ASs).

Process of introduction and implementation of IFRS

- ✓ On the basis of the approach adopted for transition from national standards to the common global accounting standards, there are two avenuesany one of which may be followed by a particular economy. These two processes are –'Adoption' or 'Convergence'.
- ✓ Accordingly, the countries/ economies across the globe are either 'Adopting IFRS' or getting 'Converged with IFRS'.
- ✓ **Adoption of IFRS** refers to the process under which the standard setting body of the economy/ country willing to make transition to the globally common accounting standards wouldaccept the IFRS (as issued by the IASB)in its original form,and would fully comply with the necessary guidelines issued by IASB in this regard.
- ✓ **Convergence with IFRS** refers to the process under which the standard setting body of the economy/ country that is willing to make transition to the common global accounting standards would develop its own set of accounting standards after taking into consideration the IFRS as issued by the IASB and making necessary modifications thereto. Such convergence ensures that the specific accounting practices of the concerned economy/ country gets maintained. However, such modification of standards conflicts with the aim of a single set of high quality accounting standards that are globally accepted. Accordingly, convergence should be considered a means of making the transition to full adoption of IFRS, and not an end in itself. Permission from the Foundation for the use of IFRS in local standards is required.

Methods of Adoptions of IFRS

- ✓ When a country adopts IFRS, it is often necessary to publish the IFRSs in the official gazette, and allow free access and distribution. The IFRS Foundation recognises this approach, and work with the entity that has the legal authority to set financial reporting standards in the particular jurisdiction. This is done to ensure that copyright restrictions on the material adopted do not prevent the adoption of IFRS.
- ✓ Each jurisdiction that opts for transition is assigned a Translation, Adoption and Copyright ('TAC') Project Manager whose responsibility is to act as the key support and contact in this respect.



Methods of Adoption of IFRS [Source: www.ifrs.org]

✓ The IFRS Foundation recommends transition to IFRS in a single step, which can be done in two ways:

Option 1: IFRS will be published as law in the Official Gazette in print and online to allow free access and distribution within your jurisdiction; or

Option 2: Resolution in law without reproducing IFRS in the legislation (this is known as **adoption by reference**). A jurisdiction using this model of adoption should consider how its constituents will access IFRS in order to apply it appropriately.

OVERVIEW OF INTERNATIONAL STANDARDS (IFRS & IAS)

List of International Standards

✓ As on Jan. 1, 2016, there are 16 International Financial Reporting Standards (IFRS), 23 International Accounting Standards (IAS), 11 IFRIC interpretations, and 5 SIC interpretations.

✓ The list of IFRS as on 01.01.2016 is given in the Table below:

IFRS Code	IFRS Title
IFRS 1	First-time Adoption of International Financial Reporting Standards
IFRS 2	Share-based Payment
IFRS 3	Business Combinations
IFRS 4	Insurance Contracts
IFRS 5	Non-current Assets Held for Sale and Discontinued Operations
IFRS 6	Exploration for and Evaluation of Mineral Resources
IFRS 7	Financial Instruments: Disclosures
IFRS 8	Operating Segments
IFRS 9	Financial Instruments

IFRS 10	Consolidated Financial Statements
IFRS 11	Joint Arrangements
IFRS 12	Disclosure of Interest in Other Entities
IFRS 13	Fair Value Measurement
IFRS 14	Regulatory Deferral Accounts
IFRS 15	Revenue from Contracts with Customers
IFRS 16	Leases

✓ The list of IAS as on 01.01.2016 is given in the following Table:

IAS Code	IAS Title
IAS 1	Presentation of Financial Statements
IAS 2	Inventories
IAS 3	Consolidated Financial Statements [superseded by IAS 27 and IAS 28]
IAS 4	Depreciation Accounting [superseded by IAS 36]
IAS 5	Information to Be Disclosed in Financial Statements [superseded by IAS 1]
IAS 6	Accounting Responses to Changing Prices [superseded by IAS 15]
IAS 7	Statement of Cash Flows
IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors
IAS 9	Accounting for Research and Development Activities [superseded by IAS 38]
IAS 10	Events after the Reporting Period
IAS 11	Construction Contracts
IAS 12	Income Taxes
IAS 13	Presentation of Current Assets and Current Liabilities [superseded by IAS 1]
IAS 14	Segment reporting [superseded by IFRS 8]
IAS 15	Information Reflecting the Effects of Changing Prices [Not Applicable]
IAS 16	Property, Plant and Equipment
IAS 17	Leases [will be superseded by IFRS 16]
IAS 18	Revenue [will be superseded by IFRS 15]
IAS 19	Employee Benefits
IAS 20	Accounting for Government Grants and Disclosure of Government Assistance
IAS 21	The Effects of Changes in Foreign Exchange Rates
IAS 22	Business Combinations [superseded by IFRS 3]
IAS 23	Borrowing Costs [superseded by IAS 39 and IAS 40]
IAS 24	Related Party Disclosures
IAS 25	Accounting for Investments
IAS 26	Accounting and Reporting by Retirement Benefit Plans
IAS 27	Separate Financial Statements
IAS 28	Investments in Associates and Joint Ventures
IAS 29	Financial Reporting in Hyperinflationary Economies
IAS 30	Disclosures in the Financial Statements of Banks and Similar Financial Institutions [superseded by IFRS 3]
IAS 31	Interests in Joint Ventures [superseded by IFRS 11 and IFRS 12]

IAS 32	Financial Instruments: Presentation
IAS 33	**Earnings per Share**
IAS 34	Interim Financial Reporting
IAS 35	Discontinuing Operations [superseded by **IFRS 5**]
IAS 36	Impairment of Assets
IAS 37	**Provisions, Contingent Liabilities** and Contingent Assets Intangible Asset
IAS 38	Intangible Asset
IAS 39	Financial Instruments: Recognition and Measurement[superseded by **IFRS 9**]
IAS 40	Investment Property Financial Instruments: Recognition and Measurement
IAS 41	Agriculture

The IFRSs and IASs that stood issued as on 01.01.2016 are briefly discussed hereunder:

IFRS 1: First Time Adoption of International Financial Reporting Standards

- IFRS 1 was issued by the International Accounting Standards Board in 2003. The Standard has been effective since January 1, 2004.
- This IFRS is applied when an entity adopts IFRSs for the first time by an explicit and unreserved statement of compliance with IFRSs. It provides the framework for switching over from existing set of accounting principles to IFRSs based accounting principles.
- IFRS1requiresanentitytocomplywitheachIFRSeffectiveatthereportingdateforitsfirstIFRSfinancialstatements.
- IFRS 1 requires an entity to do the following in the opening IFRS balance sheet that it prepares as a starting point for its accounting under IFRSs:
  - ✓ Recognise all assets and liabilities whose recognition is required by IFRSs;
  - ✓ Donot recognise items as assets or liabilities if IFRSs do not permit such recognition;
  - ✓ Reclassify items that it recognised under previous GAAP as one type of asset, liability, or component of equity, which are different type of asset, liability or component of equity under IFRSs; and
  - ✓ Apply IFRSs in measuring all recognised assets and liabilities.
- The standard sets out certain concession that is granted to the first time adopter for applying accounting policies as per IFRS and restatement of accounts.

IFRS 2: Share-based Payment

- IFRS 2 was issued by the International Accounting Standards Board in 2004. The Standard has been effective since January 1, 2005.
- This standard deals with the recognition of share-based payment transactions of an entity.
- IFRS 2 requires an entity to recognise share-based payment transactions in its financial statements, including transactions with employees or other parties to be settled in cash, other assets, or equity instruments of the entity.
- IFRS 2 recognises three types of share based payments. They are:
  1. Equity-settled transactions for goods or services acquired by an entity;
  2. Cash-settled but price or value of the goods or services based on the equity instrument of the entity; and
  3. Transactions for goods or services acquired by the entity in which either the entity can settle or supplier can claim settlement by equity instruments of the entity.

IFRS 3: Business Combinations

- IFRS 3 was issued by the International Accounting Standards Board in 2004. The Standard has been effective from April 1, 2004.
- A business combination is a transaction or event in which acquirer obtains control over a business (e.g. acquisition of shares or net assets, legal mergers, reverse acquisitions).
- IFRS 3 establishes principles for how an acquirer:
  - ✓ Recognises and measures the identifiable assets acquired, liabilities assumed and non-controlling interests.
  - ✓ Recognises and measures goodwill acquired in a business combination or a gain from a bargain purchase.
  - ✓ Determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination.
- All business combinations in the scope of IFRS 3 should be accounted for using the Acquisition Method of accounting.

IFRS 4: Insurance Contracts

- IFRS 4 was issued by the International Accounting Standards Board in 2004. The Standard has been effective from April 1, 2004.
- IFRS 4 sets out the reporting requirements for entities that issue insurance and reinsurance contracts.
- Issuance of IFRS 4 was a first step towards standardizing the diverse accounting practices that existin the insurance sector.
- It allows insurers to continue to use their existing accounting policies for liabilities arising from insurance contracts as long as the existing policies meet certain minimum requirements set out in IFRS 4.

IFRS 5: Non-current Assets Held for Sale and Discontinued Operations

- IFRS 5 was issued by the International Accounting Standards Board in 2004. The Standard has been effective from January 1, 2005.
- This standard provides the principles for measurement and presentation of 'held for sale' asset and liabilities, and related profit or loss.
- The assets which meet the criteria to be classified as held for sale are to be measured at the lower of carrying amount and Fair Value *less* Costs to Sell*,* and depreciation charge on such assets to ceases.
- Held for sale assets and liabilities are required to be presented separately in the statement of financial position as current assets or current liabilities.
- Moreover, the results of discontinued operations to be presented separately in the statement of comprehensive income.

IFRS 6: Exploration for and Evaluation of Mineral Resources

- IFRS 6 was issued by the International Accounting Standards Board in 2004. The Standard has been effective from January 1, 2006.
- The entities engaged in extractive activities incur significant amount of exploration and evaluation expenditures.
- Exploration and evaluation assets are measured at initial recognition at cost. IFRS 6 specifies various cost elements. This standard also explains measurement after initial recognition and impairment.
- The IASB wanted to make limited change to the existing accounting practices. As per this standard, an entity adopting IFRS 6 may continue to use the accounting policies applied immediately before adopting the IFRS. This includes continuing to use recognition and measurement practices that are part of those accounting policies.

IFRS 7: Financial Instruments: Disclosures

- IFRS 7 was issued by the International Accounting Standards Board in 2005. The Standard has been effective from January 1, 2007.
- This standard focuses on disclosure of financial assets and financial liabilities covered in IAS 32 and IAS 39.
- IFRS 7 requires entities to provide disclosures in their financial statements that enable users to evaluate:
  - ✓ the significance of financial instruments for the entity's financial position and performance; and
  - ✓ the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the end of the reporting period, and how the entity manages those risks.

IFRS 8: Operating Segments

- IFRS 8 was issued by the International Accounting Standards Board in 2006. The Standard has been effective from January 1, 2009.
- IFRS 8 requires identification of operating segments on the basis of internal reports.
- This standard specifies how an entity should report information about its operating segments in annual financial statements and how it would present selected information about its operating segments in interim financial reports prepared in pursuant to IAS 34.*Interim Financial Reporting.*
- It also sets out requirements for related disclosures about products and services, geographical areas and major customers.

IFRS 9: Financial Instruments

- IFRS 9 was first issued by the International Accounting Standards Board in 2009. On 24 July 2014, the IASB issued the fourth and final version of IFRS 9 has been issued in July 2014. The Standard will be effective from January 1, 2018.
- The new standard includes revised guidance on the classification and measurement of financial assets, including impairment, and supplements the new hedge accounting principles.
- IFRS 9 introduces a single classification and measurement model for financial asset.

IFRS 10: Consolidated Financial Statements

- IFRS 10 was issued by the International Accounting Standards Board in 2011. The Standard has been effective from January 1, 2013. It replaced IAS 27.
- IFRS 10 outlines the requirements for the preparation and presentation of consolidated financial statements when an entity controls one or more other entities, requiring such entities to consolidate the entities it controls.
- The aim of IFRS 10 is to establish a single control model that is applied to all entities including special purpose entities.

IFRS 11: Joint Arrangements

- IFRS 11 was issued by the International Accounting Standards Board in 2011. The Standard has been effective from January 1, 2013.
- This standard classifies joint arrangements into two types—joint operations and joint ventures.
- This standard requires a joint operator to recognise and measure the assets and liabilities (and recognise the related revenues and expenses) in relation to its interest in the arrangement in accordance with relevant IFRSs applicable to the particular assets, liabilities, revenues and expenses.
- It replaces a portion of IAS 31 that relates to joint operations. Accounting for joint ventures has also been amended and a revised standard IAS 28 *Investments in Associates and Joint Ventures* has been issued.

IFRS 12: Disclosure of Interests in Other Entities

- IFRS 12 was issued by the International Accounting Standards Board in 2011. The Standard has been effective from January 1, 2013.
- This standard is a consolidated disclosure standard requiring a wide range of disclosures about an entity's interests in subsidiaries, joint arrangements, associates and unconsolidated 'structured entities'.
- IFRS 12 emphasises that it is necessary for financial statement preparers to strike a balance between burdening financial statements with excessive detail that may not assist users of financial statements and obscuring information as a result of too much aggregation.

IFRS 13: Fair Value Measurement

- IFRS 13 was issued by the International Accounting Standards Board in 2011. The Standard has been effective from January 1, 2013.
- This standard applies to IFRSs that require or permit fair value measurements (both initial and subsequent) or disclosures and provides a single IFRS framework for measuring fair value and requires disclosures about fair value measurement. The Standard defines fair value on the basis of an 'exit price' notion and uses a 'fair value hierarchy', which results in a market-based, rather than entity-specific, measurement.

IFRS 14: Regulatory Deferral Accounts

- IFRS 14 was issued by the International Accounting Standards Board in 2014. The Standard has been effective from January 1, 2016.
- This standard permits an entity which is a first-time adopter of International Financial Reporting Standards to continue to account, with some limited changes, for 'regulatory deferral account balances' in accordance with its previous GAAP, both on initial adoption of IFRS and in subsequent financial statements.
- This standard permits recognition of assets and liabilities out of deferral of expenses and income in respect of a rate regulated entity which has been allowed by a regulator. It describes regulatory deferral account balances as amounts of expense or income that would not be recognised as assets or liabilities in accordance with other Standards, but that qualify to be deferred in accordance with this IFRS 14.
- Regulatory deferral account balances, and movements in them, are presented separately in the statement of financial position and statement of profit or loss and other comprehensive income, and specific disclosures are required.

IFRS 15: Revenue from Contracts with Customers

- IFRS 14 was issued by the International Accounting Standards Board in 2014. The Standard will be effective from January 1, 2018.
- It specifies how and when an IFRS reporter will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures.
- This standard establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers.
- The standard provides a single, principles based five-step model to be applied to all contracts with customers.
- This IFRS 15 supersedes:

  (a) IAS 11 Construction Contracts; (b) IAS 18 Revenue; (c) IFRIC 13 Customer Loyalty Programmes; (d) IFRIC 15 Agreements for the Construction of Real Estate; (e) IFRIC 18 Transfers of Assets from Customers; and (f) SIC-31 Revenue—Barter Transactions Involving Advertising Services.

IFRS 16: Leases

- IFRS 16 was issued by the International Accounting Standards Board in 2016. The Standard will be effective from January 1, 2019.
- IFRS 16 specifies how an IFRS reporter will recognise, measure, present and disclose leases.
- The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases (excepting for leases whose lease term is 12 months or less or the underlying asset has a low value).
- Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17.

IAS 1: Presentation of Financial Statements

- IAS 1 was, for the first time issued by the International Accounting Standards Committee in 1975 with the title 'Disclosure of Accounting Policies. Thereafter, it was thoroughly revised and issued with the title 'Presentation of Financial Statements' in 1997. The existing version of IAS 1 was reissued in September 2007, although it has been subject to amendments thereafter. It applies to annual periods beginning on or after January 1, 2009.
- IAS 1 outlines the overall requirements for financial statements, including how they should be structured, the minimum requirements for their content and overriding concepts such as going concern, the accrual basis of accounting and the current/non-current distinction.
- The standard requires a complete set of financial statements to comprise a Statement of Financial Position, a Statement of Profit or Loss and Other Comprehensive Income, a Statement of Changes in Equity and a Statement of Cash Flows.
- This IFRS is applied when an entity adopts IFRSs for the first time by an explicit and unreserved statement of compliance with IFRSs. It provides the framework for switching over from existing set of accounting principles to IFRSs based accounting principles.

IAS 2: Inventories:

- IAS 2 was, for the first time issued by the International Accounting Standards Committee in 1975 with the title 'Valuation and Presentation of Inventories in the Context of the Historical Cost System'. Thereafter, it was subject to thorough revision and the existing version of IAS 2 was issued in December 2003. This standard applies to annual periods beginning on or after January 1, 2005.
- The objective of IAS 2 is to prescribe the accounting treatment for inventories.
- Inventories include assets held for sale in the ordinary course of business (finished goods), assets in the production process for sale in the ordinary course of business (work in process), and materials and supplies that are consumed in production (raw materials).
- It provides guidance for determining the cost of inventories and for subsequently recognising an expense, including any write-down to net realisable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.
- It contains the requirements on how to account for most types of inventory. The standard requires inventories to be measured at the lower of cost and net realisable value (NRV) and outlines acceptable methods of determining cost, including specific identification (in some cases), first-in first-out (FIFO) and weighted average cost.

IAS 7: Statement of Cash Flows

- IAS 7 was, for the first time issued by the International Accounting Standards Committee in 1977 with the title 'Statement of Changes in Financial Position'. Thereafter, it was thoroughly revised and issued with the title 'Cash Flow Statements' in 1992, retitled in September 2007. It is operative for financial statements covering periods beginning on or after January 1, 1994.

- The objective of IAS 7 is to require the presentation of information about the historical changes in cash and cash equivalents of an entity by means of a statement of cash flows, which classifies cash flows during the period according to operating, investing, and financing activities.
- All entities that prepare financial statements in conformity with IFRSs are required to present a statement of cash flows. The statement of cash flows analyses changes in cash and cash equivalents during a period.
- This standard requires an entity to present a statement of cash flows as an integral part of its primary financial statements. Cash flows are classified and presented into operating activities (either using the 'direct' or 'indirect' method), investing activities or financing activities, with the latter two categories generally presented on a gross basis.

IAS 8: Accounting Policies, Changes in Accounting Estimates and Errors

- IAS 8 was, for the first time issued by the International Accounting Standards Committee in 1978 with the title 'Unusual and Prior Period Items and Changes in Accounting Policies'. Thereafter, it was thoroughly revised and issued with the title 'Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies' in 1992. It was reissued in December 2005 and applies to annual periods beginning on or after January 1, 2005.
- IAS 8 is applied in selecting and applying accounting policies, accounting for changes in estimates and reflecting corrections of prior period errors.
- The standard requires compliance with any specific IFRS applying to a transaction, event or condition, and provides guidance on developing accounting policies for other items that result in relevant and reliable information.
- Changes in accounting policies and corrections of errors are generally retrospectively accounted for, whereas changes in accounting estimates are generally accounted for on a prospective basis.

IAS 10: Events after Reporting Period

- IAS 10 was, for the first time issued by the International Accounting Standards Committee in 1978 with the title 'Contingencies and Events Occurring After the Balance Sheet Date'. Its existing version was reissued in December 2005 and applies to annual periods beginning on or after January 1, 2005.
- The objective of this Standard is to prescribe when an entity should adjust its financial statements for events after the reporting period; and the disclosures that an entity should give about the date when the financial statements were authorised for issue and about events after the reporting period.
- The Standard also requires that an entity should not prepare its financial statements on a going concern basis if events after the reporting period indicate that the going concern assumption is not appropriate.
- It contains requirements for when events after the end of the reporting period should be adjusted in the financial statements.

IAS 11: Construction Contracts

- IAS 11 was, for the first time issued by the International Accounting Standards Committee in 1979 with the title 'Accounting for Construction Contracts'. Its existing version was reissued in December 1993 and is applicable for periods beginning on or after January 1, 1995.
- The objective of IAS 11 is to prescribe the accounting treatment of revenue and costs associated with construction contracts.
- This standard provides the requirements on the allocation of contract revenue and contract costs to accounting periods in which construction work is performed.
- Contract revenues and expenses are recognised by reference to the stage of completion of contract activity where the outcome of the construction contract can be estimated reliably, otherwise revenue is recognised only to the extent of recoverable contract costs incurred.

IAS 12: Income Taxes

- IAS 12 was, for the first time issued by the International Accounting Standards Committee in 1979 with the title 'Accounting for Taxes on Income'. Its existing version was reissued in October 1996 and is applicable to annual periods beginning on or after January 1, 1998.
- The objective of IAS 12 is to prescribe the accounting treatment for income taxes.
- This standard implements a so-called 'comprehensive balance sheet method' of accounting for income taxes which recognises both the current tax consequences of transactions and events and the future tax consequences of the future recovery or settlement of the carrying amount of an entity's assets and liabilities.
- Differences between the carrying amount and tax base of assets and liabilities, and carried forward tax losses and credits, are recognised, with limited exceptions, as deferred tax liabilities or deferred tax assets, with the latter also being subject to a 'probable profits' test.

IAS 16: Property, Plant and Equipment

- IAS 16 was, for the first time issued by the International Accounting Standards Committee in 1982 with the title 'Accounting for Property, Plant and Equipment'. Thereafter, it was thoroughly revised and issued with the title 'Property, Plant and Equipment' in 1993. The existing version of IAS 16 was reissued in December 2003. It applies to annual periods beginning on or after January 1, 2005.
- This standard sets out the accounting treatment for most types of property, plant and equipment.
- IAS 16 applies to the accounting for property, plant and equipment, except where another standard requires or permits differing accounting treatments
- Property, plant and equipment is initially measured at its cost, subsequently measured either using a cost or revaluation model, and depreciated so that its depreciable amount is allocated on a systematic basis over its useful life.

IAS 17: Leases

- IAS 17 was, for the first time issued by the International Accounting Standards Committee in 1982 with the title 'Accounting for Leases'. Its existing version was reissued in December 2003 and applies to annual periods beginning on or after January 1, 2005. IAS 17 will be superseded by IFRS 16 Leases as of 1 January 2019.
- The objective of IAS 17 is to prescribe, for lessees and lessors, the appropriate accounting policies and disclosures to apply in relation to finance and operating leases.
- It applies to all leases other than lease agreements for minerals, oil, natural gas, and similar regenerative resources and licensing agreements for films, videos, plays, manuscripts, patents, copyrights, and similar items.
- It prescribes the accounting policies and disclosures applicable to leases, both for lessees and lessors.
- Leases are required to be classified as either finance leases (which transfer substantially all the risks and rewards of ownership, and give rise to asset and liability recognition by the lessee and a receivable by the lessor) and operating leases (which result in expense recognition by the lessee, with the asset remaining recognised by the lessor).

IAS 18: Revenue:

- IAS 18 was, for the first time issued by the International Accounting Standards Committee in 1982 with the title 'Revenue Recognition'. Thereafter, it was thoroughly revised and issued with the title 'Revenue'. Its existing version was reissued in December 1993 and applies to annual periods beginning on or after January 1, 1995. However, this standard will be superseded by IFRS 15 on and from January 1, 2018.
- The objective of IAS 18 is to prescribe the accounting treatment for revenue arising from certain types of transactions and events.
- This standard sets out the accounting requirements for when to recognise revenue from the sale of goods, rendering of services, and for interest, royalties and dividends. Revenue is measured at the fair value of the consideration received or receivable and recognised when prescribed conditions are met, which depend on the nature of the revenue.

IAS 19: Employee Benefits

- The present version of IAS 19 was issued in 2011, which supersedes IAS 19 Employee Benefits (1998). It is applicable to annual periods beginning on or after January 1, 2013.
- The objective of IAS 19 is to prescribe the accounting and disclosure for employee benefits, requiring an entity to recognise a liability where an employee has provided service and an expense when the entity consumes the economic benefits of employee service.
- It outlines the accounting requirements for employee benefits, including short-term benefits (e.g. wages and salaries, annual leave), post-employment benefits such as retirement benefits, other long-term benefits (Eg: long service leave) and termination benefits.
- The standard establishes the principle that the cost of providing employee benefits should be recognised in the period in which the benefit is earned by the employee, rather than when it is paid or payable, and outlines how each category of employee benefits are measured, providing detailed guidance in particular about post-employment benefits.

IAS 20: Accounting for Government Grants and Disclosure of Government Assistance

- IAS 20 was issued in April 1983 and is applicable to annual periods beginning on or after 1 January 1984.
- The objective of IAS 20 is to prescribe the accounting for, and disclosure of, government grants and other forms of government assistance.
- IAS 20 applies to all government grants and other forms of government assistance. However, it does not cover government assistance that is provided in the form of benefits in determining taxable income. Moreover, it does not cover government grants covered by IAS 41 Agriculture.
- This standard outlines how to account for government grants and other assistance. Government grants are recognised in profit or loss on a systematic basis over the periods in which the entity recognises expenses for the related costs for which the grants are intended to compensate, which in the case of grants related to assets requires setting up the grant as deferred income or deducting it from the carrying amount of the asset.

IAS 21: The Effects of Changes in Foreign Exchange Rates

- The present version of IAS 21 was reissued in December 2003 and applies to annual periods beginning on or after January 1, 2005.
- The objective of IAS 21 is to prescribe how to include foreign currency transactions and foreign operations in the financial statements of an entity and how to translate financial statements into a presentation currency.
- The principal issues are which exchange rate(s) to use and how to report the effects of changes in exchange rates in the financial statements.
- It outlines how to account for foreign currency transactions and operations in financial statements, and also how to translate financial statements into a presentation currency. An entity is required to determine a functional currency (for each of its operations if necessary) based on the primary economic environment in which it operates and generally records foreign currency transactions using the spot conversion rate to that functional currency on the date of the transaction.

IAS 23: Borrowing Costs

- IAS 23 was, for the first time issued by the International Accounting Standards Committee in 1984 with the title 'Capitalisation of Borrowing Costs'. Its existing version was reissued in March 2007 and applies to annual periods beginning on or after January 1, 2009. However, it is to be noted that the annual improvement of this standard is due. The IASB formally added this project to its agenda in October 2015. An exposure draft is expected in 2016.
- The objective of IAS 23 is to prescribe the accounting treatment for borrowing costs. Borrowing costs include interest on bank overdrafts and borrowings, finance charges on finance leases and exchange differences on foreign currency borrowings where they are regarded as an adjustment to interest costs.

- This standard requires that borrowing costs directly attributable to the acquisition, construction or production of a 'qualifying asset' (one that necessarily takes a substantial period of time to get ready for its intended use or sale) are included in the cost of the asset. Other borrowing costs are recognised as an expense.

IAS 24: Related Party Disclosures

- IAS 24 was, for the first time issued by the International Accounting Standards Committee in 1984 with the title. Its existing version was reissued in November 2009 and applies to annual periods beginning on or after 1 January 2011.
- The objective of IAS 24 is to ensure that an entity's financial statements contain the disclosures necessary to draw attention to the possibility that its financial position and profit or loss may have been affected by the existence of related parties and by transactions and outstanding balances with such parties.
- This standard requires disclosures about transactions and outstanding balances with an entity's related parties. The standard defines various classes of entities and people as related parties and sets out the disclosures required in respect of those parties, including the compensation of key management personnel.

IAS 26: Accounting and Reporting by Retirements Benefit Plans

- IAS 26 was issued in January 1987 and applies to annual periods beginning on or after 1 January 1988.
- The objective of IAS 26 is to specify measurement and disclosure principles for the reports of retirement benefit plans. All plans should include in their reports a statement of changes in net assets available for benefits, a summary of significant accounting policies and a description of the plan and the effect of any changes in the plan during the period.
- This standard sets out the requirements for the preparation of financial statements of retirement benefit plans. It outlines the financial statements required and discusses the measurement of various line items, particularly the actuarial present value of promised retirement benefits for defined benefit plans.

IAS 27: Separate Financial Statements

- The present version of IAS 27 was reissued in May 2011 superseding the erstwhile IAS 27 Consolidated and Separate Financial Statements. It applies to annual periods beginning on or after January 1, 2013.
- IAS 27 does not mandate which entities produce separate financial statements available for public use. It applies when an entity prepares separate financial statements that comply with International Financial Reporting Standards.
- IAS 27 has the objective of setting standards to be applied in accounting for investments in subsidiaries, jointly ventures, and associates when an entity elects, or is required by local regulations, to present separate (non-consolidated) financial statements.
- IAS 27 Separate Financial Statements (as amended in 2011) outlines the accounting and disclosure requirements for 'separate financial statements', which are financial statements prepared by a parent, or an investor in a joint venture or associate, where those investments are accounted for either at cost or in accordance with IAS 39 Financial Instruments: Recognition and Measurement or IFRS 9 Financial Instruments.
- The standard also outlines the accounting requirements for dividends and contains numerous disclosure requirements.

IAS 28: Investment in Associates and Joint Ventures

- IAS 28 was, for the first time issued by the International Accounting Standards Committee in 1989 with the title 'Accounting for Investments in Associates. Its existing version was reissued in May 2011 and applies to annual periods beginning on or after January 1, 2013.
- The objective of this standard is to prescribe the accounting for investments in associates, and, this standard sets out how to apply the equity method to investments in associates and joint ventures (with certain limited exceptions). Moreover, it also sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures.

- The standard also defines an associate by reference to the concept of "significant influence", which requires power to participate in financial and operating policy decisions of an investee (but not joint control or control of those polices).

IAS 29: Financial Reporting in Hyperinflationary Economics

- IAS 29 was issued by the International Accounting Standards Committee in July 1989. The standard had been operative for periods beginning on or after January 1, 1990.
- IAS 29 applies where an entity's functional currency is that of a hyperinflationary economy. The standard does not prescribe when hyperinflation arises but requires the financial statements (and corresponding figures for previous periods) of an entity with a functional currency that is hyperinflationary to be restated for the changes in the general pricing power of the functional currency.
- The objective of IAS 29 is to establish specific standards for entities reporting in the currency of a hyperinflationary economy, so that the financial information provided is meaningful.
- The basic principle in IAS 29 is that the financial statements of an entity that reports in the currency of a hyperinflationary economy should be stated in terms of the measuring unit current at the balance sheet date. Comparative figures for prior period(s) should be restated into the same current measuring unit.

IAS 32: Financial Instruments: Presentation

- The present version of IAS 32 was reissued in December 2003 and applies to annual periods beginning on or after 1 January 2005.
- The stated objective of IAS 32 is to establish principles for presenting financial instruments as liabilities or equity and for offsetting financial assets and liabilities.
- This standard outlines the accounting requirements for the presentation of financial instruments, particularly as to the classification of such instruments into financial assets, financial liabilities and equity instruments. The standard also provides guidance on the classification of related interest, dividends and gains/losses, and when financial assets and financial liabilities can be offset.

IAS 33: Earning per Shares

- The present version of IAS 33 was reissued in December 2003 superseding the erstwhile IAS 33. It applies to annual periods beginning on or after January 1, 2005.
- The objective of IAS 33 is to prescribe principles for determining and presenting earnings per share (EPS) amounts to improve performance comparisons between different entities in the same reporting period and between different reporting periods for the same entity.
- It applies to all entities whose securities are publicly traded or that are in the process of issuing securities to the public. Other entities that choose to present EPS information must also comply with IAS 33.
- It sets out how to calculate both Basic EPS and Diluted EPS. The calculation of Basic EPS is based on the weighted average number of ordinary shares outstanding during the period, whereas Diluted EPS also includes dilutive potential ordinary shares (such as options and convertible instruments) if they meet certain criteria.

IAS 34: Interim Financial Reporting

- IAS 34 was issued by the International Accounting Standards Committee in 1998. The Standard is operative for periods beginning on or after January 1, 1999.
- The objective of IAS 34 is to prescribe the minimum content of an interim financial report and to prescribe the principles for recognition and measurement in financial statements presented for an interim period.
- This standard applies when an entity prepares an interim financial report, without mandating when an entity should prepare such a report. Permitting less information to be reported than in annual financial statements (on the basis of providing an update to those financial statements), the standard outlines the recognition, measurement and disclosure requirements for interim reports.

IAS 36: Impairment of Assets

- The present version of IAS 36 was reissued in March 2004 and applies to goodwill and intangible assets acquired in business combinations for which the agreement date is on or after 31 March 2004, and for all other assets prospectively from the beginning of the first annual period beginning on or after 31 March 2004.
- The objective of this standard is to ensure that assets are carried at no more than their recoverable amount (i.e. the higher of fair value less costs of disposal and value in use).
- The standard goes on to define how recoverable amount is determined. With the exception of goodwill and certain intangible assets for which an annual impairment test is required, entities are required to conduct impairment tests where there is an indication of impairment of an asset, and the test may be conducted for a 'cash-generating unit' where an asset does not generate cash inflows that are largely independent of those from other assets.

IAS 37: Provisions, Contingent Liabilities and Contingent Assets

- IAS 37 was issued by the International Accounting Standards Committee in September 1998. The standard is operative for periods beginning on or after July 1, 1999.
- The objective of IAS 37 is to ensure that appropriate recognition criteria and measurement bases are applied to provisions, contingent liabilities and contingent assets and that sufficient information is disclosed in the notes to the financial statements to enable users to understand their nature, timing and amount.
- It outlines the accounting for provisions (liabilities of uncertain timing or amount), together with contingent assets (possible assets) and contingent liabilities (possible obligations and present obligations that are not probable or not reliably measurable).
- Provisions are measured at the best estimate (including risks and uncertainties) of the expenditure required to settle the present obligation, and reflects the present value of expenditures required to settle the obligation where the time value of money is material. The key principle established by the Standard is that a provision should be recognised only when there is a liability i.e. a present obligation resulting from past events. The Standard thus aims to ensure that only genuine obligations are dealt with in the financial statements – planned future expenditure, even where authorised by the board of directors or equivalent governing body, is excluded from recognition.

IAS 38: Intangible Assets

- The present version of IAS 38 was revised in March 2004. It applies to intangible assets acquired in business combinations occurring on or after March 31, 2004 or otherwise to other intangible assets for annual periods beginning on or after March 31, 2004.
- The objective of IAS 38 is to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another IFRS.
- It sets out the accounting requirements for intangible assets, which are non-monetary assets which are without physical substance and identifiable (either being separable or arising from contractual or other legal rights).
- The Standard requires an entity to recognise an intangible asset if, and only if, certain criteria are met.
- The Standard also specifies how to measure the carrying amount of intangible assets and requires certain disclosures regarding intangible assets. Intangible assets meeting the relevant recognition criteria are initially measured at cost, subsequently measured at cost or using the revaluation model, and amortised on a systematic basis over their useful lives (unless the asset has an indefinite useful life, in which case it is not amortised).

IAS 40: Investment Property

- IAS 40 was, for the first time issued by the International Accounting Standards Committee in 1986 with the title 'Accounting for Investments'. Its existing version was reissued in December 2003 and applies to annual periods beginning on or after January 1, 2005.

- The objective of this Standard is to prescribe the accounting treatment for investment property and related disclosure requirements.
- This standard applies to the accounting for property (land and/or buildings) held to earn rentals or for capital appreciation (or both). Investment properties are initially measured at cost and, with some exceptions. may be subsequently measured using a cost model or fair value model, with changes in the fair value under the fair value model being recognised in profit or loss.

IAS 41: Agriculture

- IAS 41 was issued by the International Accounting Standards Committee in 2000. The Standard will be effective from January 1, 2003.
- The objective of IAS 41 is to establish standards of accounting for agricultural activity – the management of the biological transformation of biological assets (living plants and animals) into agricultural produce (harvested product of the entity's biological assets).
- IAS 41 applies to biological assets with the exception of bearer plants, agricultural produce at the point of harvest, and government grants related to these biological assets. It does not apply to land related to agricultural activity, intangible assets related to agricultural activity, government grants related to bearer plants, and bearer plants. However, it does apply to produce growing on bearer plants.

  NB: Bearer plants were excluded from the scope of IAS 41 by Agriculture: Bearer Plants (Amendments to IAS 16 and IAS 41), which applies to annual periods beginning on or after January 1, 2016.
- The standard generally requires biological assets to be measured at Fair Value *less* Costs to Sell.

1.4 OVERVIEW OF INDIAN ACCOUNTING STANDARDS (Ind AS)

- Accounting Standards in India had been issued by the Institute of Chartered Accountants of India (ICAI). India has finally embarked on the path of accounting reforms by converging with the International Standards on Financial Reporting. Presently, these standards are aligned with International Financial Reporting Standards (IFRS). Accordingly, New Indian Accounting Standards (Ind AS) are introduced by Central Government.
- The government has also notified the Indian Accounting Standards (Ind AS) for application by these companies.
- The adoption of Ind-AS will substantially bridge the gap and bring India at par with the world at large that has adopted/ converged with IFRS. India has gone for conversion approach as against adoption of IASB IFRS and Ind-AS contain certain changes vis-a-vis IASB IFRS. Consequently, financial statements prepared in accordance with Ind-AS may not be fully compliant with IASB IFRS.
- IND AS are numbered in line with IFRS numbering. All the IND AS which are based on IAS have same numbers. Further, all the IND AS which are based on IFRS starts from 100 series. For example, IND AS 32 is based on IAS 32. Similarly IND AS 109 is based on IFRS 9.
- IND AS notified have been in line with corresponding IFRS, except some minor departures which are being made considering the economic environment of the country. For example, instead of using the terms used in IFRS like "Statement of Financial Position" & "Statement of Comprehensive income", the terms "Balance Sheet" and "Statement of Profit and Loss" respectively are being used.

ROADMAP FOR APPLICABILITY OF IND AS

- In India, the Ind ASs are to be introduced in a phased manner, and not to be implemented in a 'Big Bang' approach.
- These Ind ASs were notified through the Companies (Indian Accounting Standards) Rules, 2015 by the Ministry of Corporate Affairs on Feb. 16, 2015. These rules are in force from 1st April 2015.

- On February 16, 2015, the Ministry of Corporate Affairs (MCA) notified the ***Companies (Indian Accounting Standards) Rules, 2015*** laying down the roadmap for application of IFRS converged standards (Ind-AS) to companies other than Banking Companies, Insurance Companies and Non- Banking Finance Companies (NBFCs).
- On September 29, 2015, RBI recommended a road map to MCA for implementation of Ind AS from 2018-19 onwards for banks and NBFCs. The RBI then issued a circular on February 11, 2016 confirming the Ind AS implementation date for scheduled commercial banks.
- On 18 January 2016, the MCA issued a press release laying down Ind AS roadmap for banks, insurance companies and NBFCs.
- The Rules notified in February 2015, contained the roadmap for applicability of Ind AS for companies other than insurance companies, banking companies, and non-banking finance companies.
- In March 2016, the MCA notified a road-map for Non-Banking Financial Companies (NBFCs) through the Companies (Indian Accounting Standards) (Amendment) Rules, 2016. The roadmap for Banking companies and insurance companies will be provided by the Reserve Bank of India (RBI) and the Insurance Regulatory Development Authority (IRDA), respectively.
- The Ministry of Corporate Affairs (MCA) has notified Companies (Indian Accounting Standards) Amendment Rules, 2016, in consultation with the National Advisory Committee on Accounting Standards (NACAS), vide Notification dt 30th March 2016, effective from the date of publication in the Official Gazette. These Amendment Rules have mainly extended the scope of applicability of Ind AS to certain NBFCs and have inserted a) Ind AS 11 (Construction Contracts); & b) Ind AS 18 (Revenues). Besides various amendments have been carried out in other Ind AS by these Rules.
- On 30 March 2016, the Ministry of Corporate Affairs (MCA) notified the ***Companies (Indian Accounting Standards) (Amendment) Rules, 2016***, which include a road map for implementation of Indian Accounting Standards (Ind AS) by Non-Banking Financial Companies (NBFCs)
- **NBFC road map**: NBFCs will be required to comply with Ind AS in a phased manner, from accounting periods beginning on or after 1 April 2018 for the first phase and 1 April 2019 for the second phase. This circular confirms the timeline for Ind AS implementation by NBFCs that was specified by MCA in its press release dated 18 January 2016.

DATES FOR APPLICABILITY OF IND AS

- The Ind ASs are applicable in a phased manner to companies, depending on their listing status and the net worth.

Voluntary compliance

- Any company may comply with Ind AS for Financial statements beginning with period on or after 1st April 2015, with the comparatives of period ending on March 31, 2015, or thereafter.

Mandatory Compliance

- It is mandatory for the certain specified companies to comply with Indian AS for financial statements beginning with period on or after April 1, 2016, with the comparatives of period ending on March 31, 2016, or thereafter. These companies are:
  - ✓ Companies whose securities are listed or are in process of listing in any stock exchange in India or outside India and having net worth of ` 500 crore or more;
  - ✓ Companies other than above and having net worth of ` 500 Crore or more;
  - ✓ Holding, subsidiaries, joint venture or associates of above companies.
- It is also mandatory for the following companies to comply with Indian AS for financial statements beginning with period on or after April 1, 2017, with the comparatives of period ending on 31st March, 2016, or thereafter:

- ✓ Companies whose securities are listed or are in process of listing in any stock exchange in India or outside India and having net worth of less than `500 crore or more;
- ✓ Companies other than above and having net worth of `250 Crore but less than `500 Crore or more;
- ✓ Holding, subsidiaries, joint venture or associates of above companies.

Note: The following points are to be noted regarding the above mentioned provisions:

- Securities listed or in process of listed in SME Exchange are not included in above companies.
- The net worth is calculated based on standalone financial statements of company as on 31st March 2014 or first audited financial statements after this date.
- The companies which were not in existence or exiting companies falling under above rules of applicability of AS, the net worth is calculated based on the first audited financial statements ending after that date. If these companies are meeting the net worth limit for first time at the end of financial year, then they shall follow the Indian AS from next accounting year. For example if the companies meet the net worth limit as on 31st march 2017 then the Ind AS will be applicable from financial year 2017-18.
- Ind AS will be applied to both stand alone financial statements and consolidated financial statements.
- Overseas subsidiaries, associates, joint ventures and other similar entities of an Indian company may prepare its standalone financial statements in accordance to requirement of specific jurisdiction.
- Once any Indian company applies Ind AS voluntarily or mandatory, then it must follow them consistently for future years.

General Instructions for application of Ind As

- Indian AS are intended to be in conformity with the provisions of laws. However, if due to amendments in the law, a particular Indian AS is found to be not in conformity with such law, the provisions of the said law shall prevail and the financial statements shall be prepared in conformity with such law.
- Indian AS are intended to apply only to items which are material.
- The Indian AS having paragraphs in bold italic type and plain type, have equal authority. Paragraphs in bold italic type just indicate the main principles of the particular AS.

PRESENT STATUS OF IND AS APPLICABILITY

- Among these 39 standards, were 2 standards that the world decided to postpone – IFRS 9 (Ind AS 109) *Financial Instruments*, and IFRS 15 (Ind AS 115) *Revenue from Contracts with Customers*. India became the first country to adopt these standards.However, keeping an eye on the global developments, the regulators finally decided to postpone the application of Ind AS 115 and instead brought in Ind AS 18 *Revenue* and Ind AS 11 *Construction Contracts*. This takes the total number of Ind AS on June 1, 2016 to 40. The new standards along with some amendments in other standards were notified through the Companies (Indian Accounting Standards) (Amendment) Rules, 2016 on March 30, 2016.
- The 39 Ind ASs issued till May 31, 2016 and their titles are as under:

Standard Number	Standard Title
Indian Accounting Standard (Ind AS) 101	First-time Adoption of Indian Accounting Standards
Indian Accounting Standard (Ind AS) 102	Share-based Payment
Indian Accounting Standard (Ind AS) 103	Business Combinations
Indian Accounting Standard (Ind AS) 104	Insurance Contracts
Indian Accounting Standard (Ind AS) 105	Non-current Assets Held for Sale and Discontinued Operations
Indian Accounting Standard (Ind AS) 106	Exploration for and Evaluation of Mineral Resources

Indian Accounting Standard (Ind AS) 107	Financial Instruments: Disclosures
Indian Accounting Standard (Ind AS) 108	Operating Segments
Indian Accounting Standard (Ind AS) 109	Financial Instruments
Indian Accounting Standard (Ind AS) 110	Consolidated Financial Statements
Indian Accounting Standard (Ind AS) 111	Joint Arrangements
Indian Accounting Standard (Ind AS) 112	Disclosure of Interests in Other Entities
Indian Accounting Standard (Ind AS) 113	Fair Value Measurement
Indian Accounting Standard (Ind AS) 114	Regulatory Deferral Accounts
Indian Accounting Standard (Ind AS) 115	Revenue from Contracts with Customers
Indian Accounting Standard (Ind AS) 1	Presentation of Financial Statements
Indian Accounting Standard (Ind AS) 2	Inventories
Indian Accounting Standard (Ind AS) 7	Statement of Cash Flows
Indian Accounting Standard (Ind AS) 8	Accounting Policies, Changes in Accounting Estimates and Errors
Indian Accounting Standard (Ind AS) 10	Events after the Reporting Period
Indian Accounting Standard (Ind AS) 12	Income Taxes
Indian Accounting Standard (Ind AS) 16	Property, Plant and Equipment
Indian Accounting Standard (Ind AS) 17	Leases
Indian Accounting Standard (Ind AS) 19	Employee Benefits
Indian Accounting Standard (Ind AS) 20	Accounting for Government Grants and Disclosure of Government Assistance
Indian Accounting Standard (Ind AS) 21	The Effects of Changes in Foreign Exchange Rates
Indian Accounting Standard (Ind AS) 23	Borrowing Costs
Indian Accounting Standard (Ind AS) 24	Related Party Disclosures
Indian Accounting Standard (Ind AS) 27	Separate Financial Statements
Indian Accounting Standard (Ind AS) 28	Investments in Associates and Joint Ventures
Indian Accounting Standard (Ind AS) 29	Financial Reporting in Hyperinflationary Economies
Indian Accounting Standard (Ind AS) 32	Financial Instruments: Presentation
Indian Accounting Standard (Ind AS) 33	Earnings per Share
Indian Accounting Standard (Ind AS) 34	Interim Financial Reporting
Indian Accounting Standard (Ind AS) 36	Impairment of Assets
Indian Accounting Standard (Ind AS) 37	Provisions, Contingent Liabilities and Contingent Assets
Indian Accounting Standard (Ind AS) 38	Intangible Assets
Indian Accounting Standard (Ind AS) 40	Investment Property
Indian Accounting Standard (Ind AS) 41	Agriculture

OBJECTIVES AND SCOPE OF INDIAN ACCOUNTING STANDARDS

Ind AS – 101: First-time Adoption of Indian Accounting Standards

Objective

The objective of this Ind AS is to ensure that an entity's first Ind AS *financial statements*, and its interim financial reports for part of the period covered by those financial statements, contain high quality information that:

(a) is transparent for users and comparable over all periods presented;

(b) provides a suitable starting point for accounting in accordance with *Indian Accounting Standards* (Ind ASs); and

(c) can be generated at a cost that does not exceed the benefits.

Scope

An entity shall apply this Ind AS in:

(a) its first Ind AS financial statements; and

(b) each interim financial report, if any, that it presents in accordance with Ind AS 34, *Interim Financial Reporting,* for part of the period covered by its first Ind AS financial statements.

An entity's first Ind AS financial statements are the first annual financial statements in which the entity adopts Ind ASs, in accordance with Ind ASs notified under the Companies Act, 2013 and makes an explicit and unreserved statement in those financial statements of compliance with Ind AS.

This Ind AS does not apply to changes in accounting policies made by an entity that already applies Ind ASs. Such changes are the subject of:

(a) requirements on changes in accounting policies in Ind AS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; and

(b) specific transitional requirements in other Ind ASs.

Ind AS – 102: Share-based Payment

Objective

The objective of this Standard is to specify the financial reporting by an entity when it undertakes a *share-based payment transaction*. In particular, it requires an entity to reflect in its profit or loss and financial position the effects of share-based payment transactions, including expenses associated with transactions in which *share options* are granted to employees.

Scope

An entity shall apply this Standard in accounting for all share-based payment transactions, whether or not the entity can identify specifically some or all of the goods or services received, including:

(a) equity-settled share-based payment transactions,

(b) cash-settled share-based payment transactions, and

(c) transactions in which the entity receives or acquires goods or services and the terms of the arrangement provide either the entity or the supplier of those goods or services with a choice of whether the entity settles the transaction in cash (or other assets) or by issuing equity instruments.

(d) A share-based payment transaction may be settled by another group entity (or a shareholder of any group entity) on behalf of the entity receiving or acquiring the goods or services. Paragraph 2 also applies to an entity that:

  (i) receives goods or services when another entity in the same group (or a shareholder of any group entity) has the obligation to settle the share-based payment transaction, or

  (ii) has an obligation to settle a share-based payment transaction when another entity in the same group receives the goods or services unless the transaction is clearly for a purpose other than payment for goods or services supplied to the entity receiving them.

Ind AS – 103: Business Combination

Objective

The objective of this Indian Accounting Standard (Ind AS) is to improve the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements about a *business combination* and its effects. To accomplish that, this Ind AS establishes principles and requirements for how the *acquirer*:

(a) recognises and measures in its financial statements the *identifiable* assets acquired, the liabilities assumed and any *non-controlling interest* in the *acquiree*;

(b) recognises and measures the *goodwill* acquired in the business combination or a gain from a bargain purchase; and

(c) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination.

Scope

This Ind AS applies to a transaction or other event that meets the definition of a business

combination. This Ind AS does not apply to:

(a) the accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself.

(b) the acquisition of an asset or a group of assets that does not constitute a business.

In such cases the acquirer shall identify and recognise the individual identifiable assets acquired (including those assets that meet the definition of, and recognition criteria for, *intangible assets* in Ind AS 38, Intangible Assets) and liabilities assumed. The cost of the group shall be allocated to the individual identifiable assets and liabilities on the basis of their relative *fair values* at the date of purchase. Such a transaction or event does not give rise to goodwill.

Ind AS – 104: Insurance Contracts

Objective

The objective of this Indian Accounting Standard (Ind AS) is to specify the financial reporting for *insurance contracts* by any entity that issues such contracts (described in this Ind AS as an *insurer*). In particular, this Ind AS requires:

(a) limited improvements to accounting by insurers for insurance contracts;

(b) disclosure that identifies and explains the amounts in an insurer's financial statements arising from insurance contracts and helps users of those financial statements understand the amount, timing and uncertainty of future cash flows from insurance contracts.

Scope

An entity shall apply this Ind AS to:

(a) insurance contracts (including *reinsurance contracts*) that it issues and reinsurance contracts that it holds.

(b) financial instruments that it issues with a *discretionary participation feature* (see paragraph 35). Ind AS 107, Financial Instruments*:* Disclosures, requires disclosure about financial instruments, including financial instruments that contain such features.

This Ind AS does not address other aspects of accounting by insurers, such as accounting for financial assets held by insurers and financial liabilities issued by insurers (Ind AS 32, *Financial Instruments:* Presentation, Ind AS 107 and Ind AS 109, Financial Instruments*)*.

An entity shall not apply this Ind AS to:

(a) product warranties issued directly by a manufacturer, dealer or retailer (Ind AS 115, Revenue from Contracts with Customers, and Ind AS 37, Provisions, Contingent Liabilities and Contingent Assets).

(b) employers' assets and liabilities under employee benefit plans (India AS 19, Employee Benefits, and Ind AS 102, Share-based Payment) and retirement benefit obligations reported by defined benefit retirement plans.

(c) contractual rights or contractual obligations that are contingent on the future use of, or right to use, a non-financial item (for example, some licence fees, royalties, contingent lease payments and similar items), as well as a lessee's residual value guarantee embedded in a finance lease (Ind AS 17, Leases, Ind AS 115, Revenue from Contracts with Customers, and Ind AS 38, Intangible Assets).

(d) financial guarantee contracts unless the issuer has previously asserted explicitly that it regards such contracts as insurance contracts and has used accounting applicable to insurance contracts, in which case the issuer may elect to apply either Ind AS 32, Ind AS 107 and Ind AS 109 or this Ind AS to such financial guarantee contracts. The issuer may make that election contract by contract, but the election for each contract is irrevocable.

(e) contingent consideration payable or receivable in a business combination (see Ind AS 103, Business Combinations).

(f) direct insurance contracts that the entity holds (ie direct insurance contracts in which the entity is the policyholder). However, a cedant shall apply this Standard to reinsurance contracts that it holds.

For ease of reference, this Ind AS describes any entity that issues an insurance contract as an insurer, whether or not the issuer is regarded as an insurer for legal or supervisory purposes.

A reinsurance contract is a type of insurance contract. Accordingly, all references in this Ind AS to insurance contracts also apply to reinsurance contracts.

Ind AS — 105: Non-current Assets Held for Sale and Discontinued Operations

Objective

The objective of this Indian Accounting Standard (Ind AS) is to specify the accounting for assets held for sale, and the presentation and disclosure of discontinued operations. In particular, this Ind AS requires:

(a) assets that meet the criteria to be classified as held for sale to be measured at the lower of carrying amount and fair value less costs to sell, and depreciation on such assets to cease; and

(b) assets that meet the criteria to be classified as held for sale to be presented separately in the balance sheet and the results of discontinued operations to be presented separately in the statement of profit and loss.

Scope

The classification and presentation requirements of this Ind AS apply to all recognised non-current assets and to all disposal groups of an entity. The measurement requirements of this Ind AS apply to all recognised non-current assets and disposal groups (as set out in paragraph 4), except for those assets listed in paragraph 5 which shall continue to be measured in accordance with the Standard noted.

Assets classified as non-current in accordance with Ind AS 1, Presentation of Financial Statements, shall not be reclassified as current assets until they meet the criteria to be classified as held for sale in accordance with this Ind AS.

Assets of a class that an entity would normally regard as non-current that are acquired exclusively with a view to resale shall not be classified as current unless they meet the criteria to be classified as held for sale in accordance with this Ind AS.

Ind AS – 106 : Exploration for and Evaluation of Mineral Resources

Objective

The objective of this Indian Accounting Standard (Ind AS) is to specify the financial

reporting for the exploration for and evaluation of mineral resources.

In particular, the Ind AS requires:

(a) limited improvements to existing accounting practices for exploration and evaluation expenditures.

(b) entities that recognise exploration and evaluation assets to assess such assets for impairment in accordance with this Ind AS and measure any impairment in accordance with Ind AS 36, Impairment of Assets.

(c) disclosures that identify and explain the amounts in the entity's financial statements arising from the exploration for and evaluation of mineral resources and help users of those financial statements understand the amount, timing and certainty of future cash flows from any exploration and evaluation assets recognised.

Scope

An entity shall apply this Ind AS to exploration and evaluation expenditures that it incurs.

This Ind AS does not address other aspects of accounting by entities engaged in the exploration for and evaluation of mineral resources.

An entity shall not apply this Ind AS to expenditures incurred:

(a) before the exploration for and evaluation of mineral resources, such as expenditures incurred before the entity has obtained the legal rights to explore a specific area.

(b) after the technical feasibility and commercial viability of extracting a mineral resource are demonstrable.

Ind AS – 107: Financial Instruments: Disclosures

Objective

The objective of this Indian Accounting Standard (Ind AS) is to require entities to provide disclosures in their financial statements that enable users to evaluate:

(a) the significance of financial instruments for the entity's financial position and performance; and

(b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the end of the reporting period, and how the entity manages those risks.

The principles in this Ind AS complement the principles for recognising, measuring and presenting financial assets and financial liabilities in Ind AS 32, Financial Instruments: Presentation, and Ind AS 109, Financial Instruments.

Scope

This Ind AS shall be applied by all entities to all types of financial instruments, except:

(a) those interests in subsidiaries, associates or joint ventures that are accounted for in accordance with Ind AS 110, Consolidated Financial Statements, Ind AS 27, Separate Financial Statements or Ind AS 28, Investments in Associates and Joint Ventures. However, in some cases, Ind AS 110, Ind AS 27 or Ind AS 28 require or permit an entity to account for an interest in a subsidiary, associate or joint venture using Ind AS 109; in those cases, entities shall apply the requirements of this Ind AS and, for those measured at fair value, the requirements of Ind AS 113 Fair Value Measurement. Entities shall also apply this Ind AS to all derivatives linked to interests in subsidiaries, associates or joint ventures unless the derivative meets the definition of an equity instrument in Ind AS 32.

(b) employers' rights and obligations arising from employee benefit plans, to which Ind AS 19, Employee Benefits, applies.

(c) insurance contracts as defined in Ind AS 104, Insurance Contracts. However, this Ind AS applies to derivatives that are embedded in insurance contracts if Ind AS 109 requires the entity to account for them separately. Moreover, an issuer shall apply this Ind AS to financial guarantee contracts if the issuer applies Ind AS 109 in recognising and measuring the contracts, but shall apply Ind AS 104 if the issuer elects, in accordance with paragraph 4(d) of Ind AS 104, to apply Ind AS 104 in recognising and measuring them.

(d) financial instruments, contracts and obligations under share-based payment transactions to which Ind AS 102, Share-based Payment, applies, except that this Ind AS applies to contracts within the scope of Ind AS 109.

(e) instruments that are required to be classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D of Ind AS 32.

Ind AS – 108: Operating Segments

Core principle

An entity shall disclose information to enable users of its financial statements to evaluate the nature and financial effects of the business activities in which it engages and the economic environments in which it operates.

Scope

This Accounting Standard shall apply to companies to which Indian Accounting Standards (Ind ASs) notified under the Companies Act apply.

If an entity that is not required to apply this Ind AS chooses to disclose information about segments that does not comply with this Ind AS, it shall not describe the information as segment information.

If a financial report contains both the consolidated financial statements of a parent that is within the scope of this Ind AS as well as the parent's separate financial statements, segment information is required only in the consolidated financial statements.

Ind AS – 109: Financial Instruments

Objective

The objective of this Standard is to establish principles for the financial reporting of financial assets and financial liabilities that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of an entity's future cash flows.

Scope

This Standard shall be applied by all entities to all types of financial instruments except:

(a) those interests in subsidiaries, associates and joint ventures that are accounted for in accordance with Ind AS 110 ConsolidatedFinancial Statements, Ind AS 27 Separate Financial Statements orInd AS 28 Investments in Associates and Joint Ventures. However, in some cases, Ind AS 110, Ind AS 27 or Ind AS 28 require or permit an entity to account for an interest in a subsidiary, associate or joint venture in accordance with some or all of the requirements of this Standard. Entities shall also apply this Standard to derivatives on an interest in a subsidiary, associate or joint venture unless the derivative meets the definition of an equity instrument of the entity in Ind AS 32 Financial Instruments: Presentation.

(b) rights and obligations under leases to which Ind AS 17 Leases applies. However:

    (i) lease receivables recognised by a lessor are subject to the derecognition and impairment requirements of this Standard;

    (ii) finance lease payables recognised by a lessee are subject to the derecognition requirements of this Standard; and

    (iii) derivatives that are embedded in leases are subject to the embedded derivatives requirements of this Standard.

(c) employers' rights and obligations under employee benefit plans, to which Ind AS 19 Employee Benefits applies.

(d) financial instruments issued by the entity that meet the definition of an equity instrument in Ind AS 32 (including options and warrants) or that are required to be classified as an equity instrument in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D of Ind AS 32. However, the holder of such equity instruments shall apply this Standard to those instruments, unless they meet the exception in (a).

(e) rights and obligations arising under (i) an insurance contract as defined in Ind AS 104 Insurance Contracts, other than an issuer's rights and obligations arising under an insurance contract that meets the definition of

a financial guarantee contract, or (ii) a contract that is within the scope of Ind AS 104 because it contains a discretionary participation feature. However, this Standard applies to a derivative that is embedded in a contract within the scope of Ind AS 104 if the derivative is not itself a contract within the scope of Ind AS 104. Moreover, if an issuer of financial guarantee contracts has previously asserted explicitly that it regards such contracts as insurance contracts and has used accounting that is applicable to insurance contracts, the issuer may elect to apply either this Standard or India AS 104 to such financial guarantee contracts. The issuer may make that election contract by contract, but the election for each contract is irrevocable.

(f) any forward contract between an acquirer and a selling shareholder to buy or sell an acquiree that will result in a business combination within the scope of Ind AS 103 Business Combinations at a future acquisition date. The term of the forward contract should not exceed a reasonable period normally necessary to obtain any required approvals and to complete the transaction.

(g) loan commitments other than those loan commitments described in paragraph 2.3. However, an issuer of loan commitments shall apply the impairment requirements of this Standard to loan commitments that are not otherwise within the scope of this Standard. Also, all loan commitments are subject to the derecognition requirements of this Standard.

(h) financial instruments, contracts and obligations under share-based payment transactions to which Ind AS 102 Share-based Payment applies, except for contracts within the scope of paragraphs 2.4–2.7 of this Standard to which this Standard applies.

(i) rights to payments to reimburse the entity for expenditure that it is required to make to settle liability that it recognises as a provision in accordance with Ind AS 37 Provisions, ontingentLiabilities and Contingent Assets, or for which, in an earlier period, it recognised a rovision in accordance with Ind AS 37.

(j) rights and obligations within the scope of Ind AS 115 Revenue from Contracts with Customers that are financial instruments, except for those that Ind AS 115 specifies are accounted for in accordance with this Standard.

The impairment requirements of this Standard shall be applied to those rights that Ind AS 115 specifies are accounted for in accordance with this Standard for the purposes of recognising impairment gains or losses.

The following loan commitments are within the scope of this Standard:

(a) loan commitments that the entity designates as financial liabilities at fair value through profit or loss. An entity that has a past practice of selling the assets resulting from its loan commitments shortly after origination shall apply this Standard to all its loan commitments in the same class.

(b) loan commitments that can be settled net in cash or by delivering or issuing another financial instrument. These loan commitments are derivatives. A loan commitment is not regarded as settled net merely because the loan is paid out in instalments.

(c) commitments to provide a loan at a below-market interest rate.

This Standard shall be applied to those contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contracts were financial instruments, with the exception of contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the entity's expected purchase, sale or usage requirements. However, this Standard shall be applied to those contracts that an entity designates as measured at fair value through profit or loss in accordance with paragraph 2.5.

A contract to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contract was a financial instrument, may be irrevocably designated as measured at fair value through profit or loss even if it was entered into for the purpose of the receipt or delivery of a non-financial item in accordance with the entity's expected purchase, sale or usage requirements. This designation is available only at inception of the contract and only if it eliminates or significantly reduces a recognition inconsistency (sometimes referred to as an 'accounting mismatch') that would otherwise arise from not recognising that contract because it is excluded from the scope of this Standard.

Ind AS – 110: Consolidated Financial Statements

Objective

The objective of this Indian Accounting Standard (Ind AS) is to establish principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities.

For the purpose of meeting the above stated objective, this Ind AS:

(a) requires an entity (the parent) that controls one or more other entities (subsidiaries) to present consolidated financial statements;

(b) defines the principle of control, and establishes control as the basis for consolidation;

(c) sets out how to apply the principle of control to identify whether an investor controls an investee and therefore must consolidate the investee;

(d) sets out the accounting requirements for the preparation of consolidated financial statements; and

(e) defines an investment entity and sets out an exception to consolidating particular subsidiaries of an investment entity.

Scope

An entity that is a parent shall present consolidated financial statements. This Ind AS applies

to all entities, except as follows:

(a) A parent need not present consolidated financial statements if it meets all the following conditions:

(i) it is a wholly-owned subsidiary or is a partially-owned subsidiary of another entity and all its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting consolidated financial statements;

(ii) its debt or equity instruments are not traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets);

(iii) it did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; and

(iv) its ultimate or any intermediate parent produces consolidated financial statements that are available for public use and comply with Ind ASs.

(b) post-employment benefit plans or other long-term employee benefit plans to which India AS 19, Employee Benefits, applies.

(c) an investment entity need not present consolidated financial statements if it is required, in accordance with paragraph 31 of this Ind AS, to measure all of its subsidiaries at fair value through profit or loss.

Ind AS – 111: Joint Arrangements

Objective

The objective of this Indian Accounting Standard (Ind AS) is to establish principles for financial reporting by entities that have an interest in arrangements that are controlled jointly (i.e. *joint arrangements*).

For the purpose of meeting the above stated objective, this Ind AS defines *joint control* and requires an entity that is a *party to a joint arrangement* to determine the type of joint arrangement in which it is involved by assessing its rights and obligations and to account for those rights and obligations in accordance with that type of joint arrangement.

Scope

This Ind AS shall be applied by all entities that are a party to a joint arrangement.

Ind AS – 112: Disclosure of Interests in Other Entities

Objective

The objective of this Indian Accounting Standard (Ind AS) is to require an entity to disclose information that enables users of its financial statements to evaluate:

(a) the nature of, and risks associated with, its interests in other entities; and

(b) the effects of those interests on its financial position, financial performance and cash flows.

For the purpose of meeting the above stated objective, an entity shall disclose:

(a) the significant judgements and assumptions it has made in determining:

  (i) the nature of its interest in another entity or arrangement;

  (ii) the type of joint arrangement in which it has an interest;

  (iii) that it meets the definition of an investment entity, if applicable; and

(b) information about its interests in:

  (i) subsidiaries;

  (ii) arrangements and associates; and

  (iii) structured entities that are not controlled by the entity (unconsolidated structured entities).

Scope

This Ind AS shall be applied by an entity that has an interest in any of the following:

(a) subsidiaries

(b) joint arrangements (i.e. joint operations or joint ventures)

(c) associates

(d) unconsolidated structured entities.

This Ind AS does not apply to:

(a) post-employment benefit plans or other long-term employee benefit plans to which Ind AS 19, Employee Benefits, applies.

(b) an entity's separate financial statements to which Ind AS 27, Separate Financial Statements, applies. However, if an entity has interests in unconsolidated structured entities and prepares separate financial statements as its only financial statements, it shall apply the requirements in paragraphs 24–31 when preparing those separate financial statements.

(c) an interest held by an entity that participates in, but does not have joint control of, a joint arrangement unless that interest results in significant influence over the arrangement or is an interest in a structured entity.

(d) an interest in another entity that is accounted for in accordance with Ind AS 109, Financial Instruments. However, an entity shall apply this Ind AS:

  (i) when that interest is an interest in an associate or a joint venture that, in accordance with Ind AS 28, Investments in Associates and Joint Ventures, is measured at fair value through profit or loss; or

  (ii) when that interest is an interest in an unconsolidated structured entity.

Ind AS – 113: Fair Value Measurement

Objective

This Ind AS: (a) defines fair value; (b) sets out in a single Ind AS a framework for measuring fair value; and (c) requires disclosures about fair value measurements.

Scope

This Ind AS applies when another Ind AS requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements), except as specified in paragraphs 6 and 7 of the standard.

Ind AS-114: Regulatory Deferral Accounts

Objective

The objective of this Standard is to specify the financial reporting requirements for regulatory deferral account balances that arise when an entity provides goods or services to customers at a price or rate that is subject to rate regulation.

In meeting this objective, the Standard requires:

(a) limited changes to the accounting policies that were applied in accordance with previous generally accepted accounting principles (previous GAAP) for regulatory deferral account balances, which are primarily related to the presentation of these accounts; and

(b) disclosures that:

   (i) identify and explain the amounts recognised in the entity's financial statements that arise from rate regulation; and

   (ii) help users of the financial statements to understand the amount, timing and uncertainty of future cash flows from any regulatory deferral account balances that are recognised.

Scope

An entity is permitted to apply the requirements of this Standard in its first Ind AS financial statements if and only if it: (a) conducts rate-regulated activities; and (b) recognised amounts that qualify as regulatory deferral account balances in its financial statements in accordance with its previous GAAP. An entity shall apply the requirements of this Standard in its financial statements for subsequent periods if and only if, in its first Ind AS financial statements 1, it recognised regulatory deferral account balances by electing to apply the requirements of this Standard.

Ind AS – 115: Revenue from Contracts with Customs

Objective

The objective of this Standard is to establish the principles that an entity shall apply to report useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer.

For the purpose of meeting the above stated objective, the core principle of this Standard is that an entity shall recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. An entity shall consider the terms of the contract and all relevant facts and circumstances when applying this Standard. An entity shall apply this Standard, including the use of any practical expedients, consistently to contracts with similar characteristics and in similar circumstances. 4 This Standard specifies the accounting for an individual contract with a customer. However, as a practical expedient, an entity may apply this Standard to a portfolio of contracts (or performance obligations) with similar characteristics if the entity reasonably expects that the effects on the financial statements of applying this Standard to the portfolio would not differ materially from applying this Standard to the individual contracts (or performance obligations) within that portfolio. When accounting for a portfolio, an entity shall use estimates and assumptions that reflect the size and composition of the portfolio.

Scope

An entity shall apply this Standard to all contracts with customers, except the following:

(a) lease contracts within the scope of Ind AS 17, Leases;

(b) insurance contracts within the scope of Ind AS 104, Insurance Contracts;

(c) financial instruments and other contractual rights or obligations within the scope of Ind AS 109, Financial Instruments, Ind AS 110, Consolidated Financial Statements, Ind AS 111, Joint Arrangements, Ind AS 27, Separate Financial Statements and Ind AS 28, Investments in Associates and Joint Ventures; and

(d) non-monetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers. For example, this Standard would not apply to a contract between two oil companies that agree to an exchange of oil to fulfill demand from their customers in different specified locations on a timely basis.

Ind AS – 1: Presentation of Financial Statements

Objective

This Standard prescribes the basis for presentation of general purpose financial statements to ensure comparability both with the entity's financial statements of previous periods and with the financial statements of other entities. It sets out overall requirements for the presentation of financial statements, guidelines for their structure and minimum requirements for their content.

Scope

An entity shall apply this Standard in preparing and presenting general purpose financial statements in accordance with Indian Accounting Standards (Ind ASs)

Purpose of financial statements: Financial statements are a structured representation of the financial position and financial performance of an entity. The objective of financial statements is to provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users in making economic decisions. Financial statements also show the results of the management's stewardship of the resources entrusted to it. To meet this objective, financial statements provide information about an entity's assets, liabilities, equity, income and expenses (including gains and losses), contributions by and distributions to owners in their capacity as owners, and cash flows. This information, along with other information in the notes, assists users of financial statements in predicting the entity's future cash flows and, in particular, their timing and certainty.

Complete set of financial statements: A complete set of financial statements comprises:

(a) A balance sheet as at the end of the period (including statement of changes in equity which is presented as a part of the balance sheet);

(b) A statement of profit and loss for the period;

(c) Statement of changes in equity;

(d) A statement of cash flows for the period;

(e) Notes, comprising a summary of significant accounting policies and other explanatory information; and

(f) Comparative information in respect of the preceding period;

(g) A balance sheet as at the beginning of the earliest comparative period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.

Ind AS – 2: Inventories

Objective

The objective of this Standard is to prescribe the accounting treatment for inventories. A primary issue in accounting for inventories is the amount of cost to be recognised as an asset and carried forward until the related revenues are recognised. This Standard deals with the determination of cost and its subsequent recognition as an expense, including any write-down to net realisable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.

Scope

This Standard applies to all inventories, except:

(a) financial instruments; and

(b) biological assets (i.e. living animals or plants) related to agricultural activity and agricultural produce at the point of harvest (Ind AS 41, Agriculture)

Ind AS – 7: Statement of Cash Flows

Objective:

- Information about the cash flows of an entity is useful in providing users of financial statements with a basis to assess the ability of the entity to generate cash and cash equivalents and the needs of the entity to utilise those cash flows. The economic decisions that are taken by users require an evaluation of the ability of an entity to generate cash and cash equivalents and the timing and certainty of their generation.
- The objective of this Standard is to require the provision of information about the historical changes in cash and cash equivalents of an entity by means of a statement of cash flows which classifies cash flows during the period from operating, investing and financing activities.

Scope:

An entity shall prepare a statement of cash flows in accordance with the requirements of this Standard and shall present it as an integral part of its financial statements for each period for which financial statements are presented.

Ind AS – 8: Accounting Policies, Changes in Accounting Estimates and Errors

Objective:

The objective of this Standard is to prescribe:

- the criteria for selecting and changing accounting policies, together with the accounting treatment and disclosure of changes in accounting policies, changes in accounting estimates and corrections of errors. The Standard is intended to enhance the relevance and reliability of an entity's financial statements, and the comparability of those financial statements over time and with the financial statements of other entities.
- The disclosure requirements for accounting policies (except those for changes in accounting policies that are set out in India AS 1, Presentation of Financial Statements).

Scope:

This Standard shall be applied in selecting and applying accounting policies, and accounting for changes in accounting policies, changes in accounting estimates and corrections of prior period errors.

Ind AS – 10: Events after the Reporting Period

Objective

The objective of this Standard is to prescribe:

(a) When an entity should adjust its financial statements for events after the reporting period; and

(b) the disclosures that an entity should give about the date when the financial statements were approved for issue and about events after the reporting period.

The Standard also requires that an entity should not prepare its financial statements on a going concern basis if events after the reporting period indicate that the going concern assumption is not appropriate.

Scope

This Standard shall be applied in the accounting for, and disclosure of, events after the reporting period.

Ind AS – 12: Income Taxes

Objective

The objective of this Standard is to prescribe the accounting treatment for income taxes. The principal issue in accounting for income taxes is how to account for the current and future tax consequences of:

(a) the future recovery (settlement) of the carrying amount of assets (liabilities) that are recognised in an entity's balance sheet; and

(b) transactions and other events of the current period that are recognised in an entity's financial statements.

Scope

1. This Standard shall be applied in accounting for income taxes.

2. For the purposes of this Standard, income taxes include all domestic and foreign taxes which are based on taxable profits. Income taxes also include taxes, such as withholding taxes, which are payable by a subsidiary, associate or joint arrangement on distributions to the reporting entity.

3. This Standard does not deal with the methods of accounting for government grants (Ind AS 20, Accounting for Government Grants and Disclosure of Government Assistance) or investment tax credits. However, this Standard does deal with the accounting for temporary differences that may arise from such grants or investment tax credits.

Ind AS – 16: Property, Plant and Equipment

Objective

The objective of this Standard is to prescribe the accounting treatment for property, plant and equipment so that users of the financial statements can discern information about an entity's investment in its property, plant and equipment and the changes in such investment. The principal issues in accounting for property, plant and equipment are the recognition of the assets, the determination of their carrying amounts and the depreciation charges and impairment losses to be recognised in relation to them

Scope

This Standard shall be applied in accounting for property, plant and equipment except when another Standard requires or permits a different accounting treatment.

Ind AS – 17: Lease

Objective

The objective of this Standard is to prescribe, for lessees and lessors, the appropriate accounting policies and disclosure to apply in relation to leases.

Scope

This Standard shall be applied in accounting for all leases other than:

(a) leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources; and

(b) licensing agreements for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights.

However, this Standard shall not be applied as the basis of measurement for:

(a) property held by lessees that is accounted for as investment property;

(b) investment property provided by lessors under operating leases;

(c) biological assets by lessees under finance leases; or

(d) biological assets within the scope of Ind AS 41 provided by lessors under operating leases.

Ind AS – 19: Employee Benefits

Objective

The objective of this Standard is to prescribe the accounting and disclosure for employee benefits. The Standard requires an entity to recognise:

(a) a liability when an employee has provided service in exchange for employee benefits to be paid in the future; and

(b) an expense when the entity consumes the economic benefit arising from service provided by an employee in exchange for employee benefits.

Scope

This Standard shall be applied by an employer in accounting for all employee benefits, except those to which Ind AS 10 Share-based Payment applies.

However, this Standard does not deal with reporting by employee benefit plans.

Ind AS – 20: Accounting for Government Grants and Disclosure of Government Assistance

Scope

This Standard shall be applied in accounting for, and in the disclosure of, government grants and in the disclosure of other forms of government assistance.

Government grants are recognised when there is reasonable assurance that the entity will comply with the conditions related to them and that the grants will be received.

Ind AS – 21: The Effects of Changes in Foreign Exchange Rates

Objective

An entity may carry on foreign activities in two ways. It may have transactions in foreign currencies or it may have foreign operations. In addition, an entity may present its financial statements in a foreign currency. The objective of this Standard is to prescribe how to include foreign currency transactions and foreign operations in the financial statements of an entity and how to translate financial statements into a presentation currency. The principal issues are which exchange rate(s)to use and how to report the effects of changes in exchange rates in the financial statements.

Scope

This Standard shall be applied:

(a) in accounting for transactions and balances in foreign currencies, except for those derivative transactions and balances that are within the scope of India AS 109 Financial Instruments;

(b) in translating the results and financial position of foreign operations that are included in the financial statements of the entity by consolidation or the equity method; and

(c) in translating an entity's results and financial position into a presentation currency.

Ind AS – 23: Borrowing Costs

Core principle

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset form part of the cost of that asset. Other borrowing costs are recognised as an expense.

Scope

An entity shall apply this Standard in accounting for borrowing costs. The Standard does not deal with the actual or imputed cost of equity, including preferred capital not classified as a liability.

An entity is not required to apply the Standard to borrowing costs directly attributable to the acquisition, construction or production of:

(a) a qualifying asset measured at fair value, for example, a biological asset within the scope of Ind AS 41 Agriculture; or

(b) inventories that are manufactured, or otherwise produced, in large quantities on a repetitive basis.

Ind AS – 24: Related Party Disclosures

Objective

The objective of this Standard is to ensure that an entity's financial statements contain the disclosures necessary to draw attention to the possibility that its financial position and profit or loss may have been affected by the existence of related parties and by transactions and outstanding balances, including commitments, with such parties.

Scope

This Standard shall be applied for the following purposes:

(a) Identifying related party relationships and transactions;

(b) Identifying outstanding balances, including commitments, between an entity and its related parties;

(c) Identifying the circumstances in which disclosure of the items in (a) and (b) is required; and

(d) Determining the disclosures to be made about those items.

Ind AS – 27: Separate Financial Statements

Objective

The objective of this Standard is to prescribe the accounting and disclosure requirements for investments in subsidiaries, joint ventures and associates when an entity prepares separate financial statements.

Scope

This Standard shall be applied in accounting for investments in subsidiaries, joint ventures and associates when an entity elects, or is required by law, to present separate financial statements.

Ind AS – 28: Investments in Associates and Joint Ventures

Objective

The objective of this Standard is to prescribe the accounting for investments in associates and to set out the requirements for the application of the equity method when accounting for investments in associates and joint ventures.

Scope

This Standard shall be applied by all entities that are investors with joint control of, or significant influence over, an investee.

Ind AS – 29: Financial Reporting in Hyperinflationary Economies

Scope

This Standard shall be applied to the financial statements, including the consolidated financial statements, of any entity whose functional currency is the currency of a hyperinflationary economy.

Ind AS – 32: Financial Instruments: Presentation

Objective

The objective of this Standard is to establish principles for presenting financial instruments as liabilities or equity and for offsetting financial assets and financial liabilities. It applies to the classification of financial instruments, from the perspective of the issuer, into financial assets, financial liabilities and equity instruments; the classification of related interest, dividends, losses and gains; and the circumstances in which financial assets and financial liabilities should be offset.

The principles in this Standard complement the principles for recognizing and measuring financial assets and financial liabilities in Ind AS 109 Financial Instruments, and for disclosing information about them in Ind AS 107 Financial Instruments: Disclosures.

Scope

This Standard shall be applied by all entities to all types of financial instruments except:

(a) those interests in subsidiaries, associates or joint ventures that are accounted for in accordance with Ind AS 110, Consolidated Financial Statements, Ind AS 27, Separate Financial Statements, or Ind AS 28, Investments in Associates and joint ventures. However, in some cases, Ind AS 110, Ind AS 27 or Ind AS 28 require or permit an entity to account for an interest in a subsidiary, associate or joint venture using Ind AS 109; in those cases, entities shall apply the requirements of this Standard. Entities shall also apply this Standard to all derivatives linked to interests in subsidiaries, associates or joint ventures.

(b) employers' rights and obligations under employee benefit plans, to which Ind AS 19, Employee Benefits;

(c) insurance contracts as defined in Ind AS 104, Insurance Contracts. However, this Standard applies to derivatives that are embedded in insurance contracts if Ind AS 109 requires the entity to account for them separately. Moreover, an issuer shall apply this Standard to financial guarantee contracts if the issuer applies Ind AS 109 in recognising and measuring the contracts, but shall apply Ind AS 104 if the issuer elects, in accordance with paragraph 4(d) of Ind AS 104, to apply Ind AS 104 in recognising and measuring them.

(d) financial instruments that are within the scope of Ind AS 104 because they contain a discretionary participation feature. The issuer of these instruments is exempt from applying to these features paragraphs 15–32 and AG25–AG35 of this Standard regarding the distinction between financial liabilities and equity instruments. However, these instruments are subject to all other requirements of this Standard. Furthermore, this Standard applies to derivatives that are embedded in these instruments.

(e) financial instruments, contracts and obligations under share-based payment transactions to which Ind AS 102, Share-based Payment, applies, except for:

  (i) contracts within the scope of paragraphs 8–10 of this Standard, to which this Standard applies,

  (ii) paragraphs 33 and 34 of this Standard, which shall be applied to treasury shares purchased, sold, issued or cancelled in connection with employee share option plans, employee share purchase plans, and all other share-based payment arrangements.

This Standard shall be applied to those contracts to buy or sell a nonfinancial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contracts were financial instruments, with the exception of contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the entity's expected purchase, sale or usage requirements. However, this Standard shall be applied to those contracts that an entity designates as measured at fair value through profit or loss in accordance with Ind AS 109 Financial Instruments.

Ind AS – 33: Earning per Share

Objective

The objective of this Standard is to prescribe principles for the determination and presentation of earnings per share, so as to improve performance comparisons between different entities in the same reporting period and between different reporting periods for the same entity. Even though earnings per share data have limitations because of the different accounting policies that may be used for determining 'earnings', a consistently determined denominator enhances financial reporting. The focus of this Standard is on the denominator of the earnings per share calculation.

Scope

- An entity that discloses earnings per share shall calculate and disclose earnings per share in accordance with this Standard.

- When an entity presents both consolidated financial statements and separate financial statements prepared in accordance with Ind AS 110, *Consolidated Financial Statements*, and Ind AS 27, *Separate Financial Statements,* respectively, the disclosures required by this Standard shall be presented both in the consolidated financial statements and separate financial statements. In consolidated financial statements such disclosures shall be based on consolidated information and in separate financial statements such disclosures shall be based on information given in separate financial statements. An entity shall not present in consolidated financial statements, earnings per share based on the information given in separate financial statements and shall not present in separate financial statements, earnings per share based on the information given in consolidated financial statements.

Ind AS – 34: Interim Financial Reporting

Objective

The objective of this Standard is to prescribe the minimum content of an interim financial report and to prescribe the principles for recognition and measurement in complete or condensed financial statements for an interim period. Timely and reliable interim financial reporting improves the ability of investors, creditors, and others to understand an entity's capacity to generate earnings and cash flows and its financial condition and liquidity.

Scope

This Standard does not mandate which entities should be required to publish interim financial reports, how frequently, or how soon after the end of an interim period. However, governments, securities regulators, stock exchanges, and accountancy bodies often require entities whose debt or equity securities are publicly traded to publish interim financial reports. This Standard applies if an entity is required or elects to publish an interim financial report in accordance with Indian Accounting Standards.

Ind AS – 36: Impairment of Assets

Objective

The objective of this Standard is to prescribe the procedures that an entity applies to ensure that its assets are carried at no more than their recoverable amount. An asset is carried at more than its recoverable amount if its carrying amount exceeds the amount to be recovered through use or sale of the asset. If this is the case, the asset is described as impaired and the Standard requires the entity to recognise an impairment loss. The Standard also specifies when an entity should reverse an impairment loss and prescribes disclosures.

Scope

This Standard shall be applied in accounting for the impairment of all assets, other than:

(a) Inventories (Ind AS 2, Inventories);

(b) contract assets and assets arising from costs to obtain or fulfill a contract that are recognised in accordance with Ind AS 115, Revenue from Contracts with Customers;

(c) deferred tax assets (Ind AS 12, Income Taxes);

(d) assets arising from employee benefits (see Ind AS 19, Employee Benefits);

(e) financial assets that are within the scope of Ind AS 109, Financial Instruments;

(f) biological assets related to agricultural activity within the scope of Ind AS 41 Agriculture that are measured at fair value less costs to sell ;

(g) deferred acquisition costs, and intangible assets, arising from an insurer's contractual rights under insurance contracts within the scope of Ind AS 104, Insurance Contracts; and

(h) non-current assets (or disposal groups) classified as held for sale in accordance with Ind AS 105, Non-current Assets Held for Sale and Discontinued Operations.

Ind AS – 37: Provisions, Contingent Liabitities and Contingent Assets

Objective

The objective of this Standard is to ensure that appropriate recognition criteria and measurement bases are applied to provisions, contingent liabilities and contingent assets and that sufficient information is disclosed in the notes to enable users to understand their nature, timing and amount.

Scope

This Standard shall be applied by all entities in accounting for provisions, contingent liabilities and contingent assets, except:

(a) those resulting from executory contracts, except where the contract is onerous; and

(b) those covered by another Standard.

Ind AS – 38: Intangible Assets

Objective

The objective of this Standard is to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another Standard. This Standard requires an entity to recognise an intangible asset if, and only if, specified criteria are met. The Standard also specifies how to measure the carrying amount of intangible assets and requires specified disclosures about intangible assets.

Scope

This Standard shall be applied in accounting for intangible assets, except:

(a) intangible assets that are within the scope of another Standard;

(b) financial assets, as defined in Ind AS 32, Financial Instruments: Presentation;

(c) the recognition and measurement of exploration and evaluation assets (Ind AS 106, Exploration for and Evaluation of Mineral Resources); and

(d) expenditure on the development and extraction of minerals, oil, natural gas and similar non-regenerative resources.

Ind AS – 40: Investment Property

Objective

The objective of this Standard is to prescribe the accounting treatment for investment property and related disclosure requirements.

Scope

This Standard shall be applied in the recognition, measurement and disclosure of investment property.

Ind AS – 41: Agriculture

Objective

The objective of this Standard is to prescribe the accounting treatment and disclosures related to agricultural activity.

Scope

This Standard shall be applied to account for the following when they relate to agricultural activity:

(a) biological assets;

(b) agricultural produce at the point of harvest; and

(c) government grants covered by paragraphs 34 and 35 of this standard.

1.5 RELATIVE VIEW OF AS vs IND AS vs IFRS

TOPIC	AS	IFRS	IND AS
Presentation of Financial Statements: Source Standards	AS 1 — Disclosure of Accounting Policies/ Schedule III to the Companies Act, 2013 AS 5 — Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies	IAS 1: Presentation of Financial Statements	Ind AS 1: Presentation of Financial Statements
Components of financial statements	The requirements for the presentation of financial statements are set out in Schedule III to the Companies Act, 2013, Schedule III to the Banking Regulation Act, 1949 (for banks), the regulations issued by the Insurance Regulatory and Development Authority (for insurance companies) and the SEBI Guidelines for Mutual Funds (for mutual funds) together with the Accounting Standards notified under the Companies (Accounting Standards) Rules, 2006. As per the Companies Act, 2013 'financial statement' in relation to a company, includes (a) a balance sheet as at the end of the financial year; (b) a profit and loss account, or in the case of a company carrying on any activity not for profit, an income and expenditure account for the financial year; (c) cash flow statement for the financial year; (d) a statement of changes in equity, if applicable; and (e) any explanatory note annexed to, or forming part of, any document referred to above.	A complete set of financial statements under IFRS comprises of: a) a statement of financial position; b) a statement of profit or loss and other comprehensive income; c) a statement of changes in equity; d) a statement of cash flows; and e) notes comprising significant accounting policies and other explanatory information. Comparative figures are presented for one year. When a change in accounting policy has been applied retrospectively or items of financial statements have been restated/ reclassified, a statement of financial position is required as at the beginning of the earliest comparative period. Additional comparative information may be presented, if it is in accordance with IFRS, but it need not comprise a complete set of financial statements.	A complete set of financial statements under Ind AS comprises a) a balance sheet as at the end of the period; b) statement of profit and loss; c) statement of changes in equity; d) a statement of cash flows; e) notes including summary of accounting policies and other explanatory information. Comparative figures are presented for one year. When a change in accounting policy has been applied retrospectively or items of financial statements have been restated, or reclassified, a Balance Sheet is required as at the beginning of the earliest period presented. Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Proforma of financial statements	Schedule III prescribes the minimum requirements for disclosure on the face of the Balance Sheet and Statement of Profit And Loss and Notes. AS 3 provides guidance on line items to be presented in the statement of cash flows.	Specifies the line items to be presented in the statement of financial position, statement of profit or loss and other comprehensive income and statement of changes in equity. IAS 7 provides the proforma of the statement of cash flows.	Ind AS 1 does not include any specific format for the financial statements. The ICAI has issued an exposure draft of the Ind AS-compliant Schedule III. Ind AS 7 provides the proforma of the statement of cash flows.
Regarding Material information	Financial statements should disclose all "material" items, i.e. items, the knowledge of which might influence the decisions of the user of the financial statements.	Omissions or misstatements are considered material if individually or collectively they could influence the economic decisions that users take on the basis of financial statements. An entity should not reduce the understandability of its financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures or functions. Where some IFRSs specify minimum information that is required to be included in the financial statements including the notes, such a specific disclosure is not required to be provided if the information resulting from that disclosure is not material.	Similar to IFRS. Under Ind AS 1, a specific disclosure required by an Ind AS is not provided if the information is not material except when required by law.
Classification of financial liabilities under refinancing arrangements	There is no guidance in the existing standards.	Classified as Current liability.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Classification of financial liabilities upon breach of covenants	There is no guidance in the existing standards.	When an entity breaches a provision of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand. It classifies the liability as current, even if the lender agreed, after the reporting period and before the authorisation of the financial statements for issue, not to demand payment as a consequence of the breach. However the liability can be classified as non-current if the lender has agreed before the end of the reporting period to provide a grace period of minimum 12 months after the reporting period.	Where there is a breach of a material provision of a long-term arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand on the reporting date, if the lender has agreed, after the reporting period and before the approval of the financial statements for issue, not to demand payment as a consequence of the breach, the loan will not be classified as current.
Reflection of items of incomes and expenses in income statement	There is no guidance in the existing standards.	An analysis of expenses is presented using a classification based on either the nature of expenses or their function whichever provides information that is reliable and more relevant. If presented by function, specific disclosures by nature are provided in the notes. When items of income or expense are material, their nature and amount are separately disclosed.	Entities should present an analysis of expenses recognised in profit or loss using a classification based only on the nature of expense.
Presentation of profit or loss attributable to non-controlling interests (minority interests)	Profit or loss attributable to minority interests is disclosed as deduction from the profit or loss for the period as an item of income or expense (as per AS 21).	Profit or loss attributable to non-controlling interests and equity holders of the parent are disclosed in the statement of profit or loss and other comprehensive income as allocations of profit or loss and total comprehensive income for the period.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Statement of profit or loss and statement of comprehensive income (other comprehensive income)	Statement of profit and loss is the Indian GAAP equivalent separate statement of profit or loss under IFRS. Some items (such as revaluation surplus) which are treated as 'other comprehensive income' under IFRS/ Ind AS are recognised directly in equity under Indian GAAP.	The statement of profit or loss and other comprehensive income includes all items of income and expense — (i.e. all 'non-owner' changes in equity). It includes (a) components of profit or loss and (b) other comprehensive income (i.e. items of income and expense that are not recognised in profit or loss as required or permitted by other IFRS5). These items may be presented either: • in a single statement which consists of profit or loss and other comprehensive income (in which there is a sub-total for profit or loss); or • in a separate statement of profit or loss (displaying components of profit or loss) and a statement of profit or loss and other comprehensive income (beginning with profit or loss and displaying components of other comprehensive income).	An entity is required to present all items of income and expense including components of other comprehensive income in a period in a single statement of profit and loss.
Statement of changes in equity	Not specifically provided. A statement of changes in equity is not drafted.	The statement of changes in equity includes the following information: • total comprehensive income for the period; • the effects on each component of equity of retrospective application or retrospective restatement in accordance with AS 8; and • for each component of equity, a reconciliation between the opening and closing balances, separately disclosing each change.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Extraordinary items	Extraordinary items are disclosed separately in the statement of profit and loss and are considered for the determination of net profit or loss for the period.	Presentation of any items of income or expense as extraordinary is prohibited.	Similar to IFRS.
Reclassification	A disclosure is made in financial statements that comparative amounts have been reclassified to conform to the presentation in the current period. However, additional disclosures for the nature, amount and reason for reclassification.	When comparative amounts are reclassified, nature, amount and reason for reclassification are disclosed.	Similar to IFRS.
Critical judgements	Does not specifically require disclosure of judgements made by management in the summary of significant accounting policies or other notes.	Requires disclosure of critical judgements made by management in applying accounting policies.	Similar to IFRS.
Estimation uncertainty	AS 1 does not specifically require an entity to disclose information about the assumptions that it makes about the future and other major sources of estimation uncertainty at the end of the reporting period. However, other standards may require certain disclosures of the same.	Requires disclosure of key sources for estimating uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. The nature of the uncertainty and the carrying amounts of such assets and liabilities at the end of the reporting period are required to be disclosed.	Similar to IFRS.
Disclosure regarding capital	Not required to disclose information that enables the users of financial statements to evaluate the entity's objectives, policies and processes of managing capital.	Requires disclosure of information about management of capital and compliance with externally imposed capital requirements, if any.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Inventories – Source Standards	**AS 2 — Valuation of Inventories**	**IAS 2 Inventories**	**Ind AS - 2 Inventories**
Scope	There is no scope exemption for any inventories held by commodity traders. Further, AS 2 totally excludes from its scope producers' inventories of livestock, agricultural and forest products, and mineral oils, ores and gases to the extent that they are measured at net realisable value in accordance with well-established practices in those industries, Work-in-progress arising under construction contracts, including directly related service contracts and work in progress arising in the ordinary course of business of service providers are also outside the scope of AS 2.	Measurement requirements do not apply to inventories held by commodity broker-traders who measure their inventories at fair value less costs to sell and producers of agricultural and forest products, agricultural produce after harvest and minerals and mineral products to the extent that they are measured at net realisable value in accordance with well-established practices in those industries. The standard also scopes out the biological assets related to agricultural activity and agricultural produce at the point of harvest Changes in fair value less costs to sell/changes in net realisable value are recognised in profit or loss in the period of the change.	Similar to IFRS.
Deferred settlement terms	Inventories purchased on deferred settlement terms are not explicitly dealt with in the accounting standard on inventories. The cost of inventories generally will be the purchase price for deferred credit terms unless the contract states the interest payable for deferred terms.	Difference between the purchase price of inventories for normal credit terms and the amount paid for deferred settlement terms is recognised as interest expense.	Similar to IFRS.
Cost formula	Not compulsorily required to use the same cost formula consistently for all inventories that have a similar nature and use to the entity. The formula used should reflect the fairest possible approximation to the cost incurred in bringing the items of inventory to their present location and condition.	Requires an entity to use the same cost formula for all inventories having a similar nature and use to the entity. For inventories with a different nature or use, different cost formulas may be justified.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Reversal of write-down of inventory	No specific guidance provided for reversal of write-down of inventories in AS 2. However, reversals may be permitted as AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies requires this to be disclosed as a separate line item in the statement of profit and loss.	Write-down of inventory is reversed if circumstances that previously caused inventories to be written down below cost no longer exist or when there is clear evidence of an increase in the net realisable value because of changes in economic circumstances. The amount of reversal is limited to the amount of the original write-down.	Similar to IFRS.
Statement of Cash Follows — Source Standards	**AS 3 — Cash Flow Statements**	**IAS 7 Statement of Cash Flows**	**Ind AS 7 — Statement of Cash Flows**
Regarding bank overdrafts	Bank overdrafts are considered as financing activities.	Included as cash and cash equivalents if they form an integral part of an entity's cash management.	Similar to IFRS.
Regarding cash flows from extraordinary items	Classified as arising from operating, investing or financing activities as appropriate, and separately disclosed.	Presentation of items as extraordinary is not permitted, so the cash flow statement does not reflect any items of cash flow as extraordinary.	Similar to IFRS.
Regarding interest and dividend	<u>For Financial enterprises</u>: Interest paid and interest and dividend received are reflected as operating activities; Dividend paid is reflected as financing activity. <u>For other enterprises</u>: Interest and dividends received are reflected as investing activities; Interest and dividends paid are reflected as financing activities.	May be classified as operating, investing or financing activities in a manner consistent from period to period.	Similar to Indian GAAP.
Regarding acquisition and disposal of properties held for rental to others	Not specifically provided.	Entities might routinely sell items of property, plant and equipment that they have previously held for rental to others. Cash payments/ receipts in respect of acquisition/ disposal of such assets are reflected as operating activities.	Similar to IFRS.
Changes in ownership interest	Not specifically provided.	Changes in ownership interest in a subsidiary without loss of control are reflected as financing activities.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Accounting Policies, Changes in Accounting Estimates and Errors – SourceStandards	**AS 5 — Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies**	**IAS 8 — Accounting Policies, Changes in Accounting Estimates and Errors**	**Ind AS 8 — Accounting Policies, Changes in Accounting Estimates and Errors**
Changes in accounting policies	Changes in accounting policies should be made only if it is required by statute, for compliance with an Accounting Standard or for a more appropriate presentation of the financial statements on a prospective basis (unless transitional provisions, if any, of an accounting standard require otherwise) together with a disclosure of the impact of the same, if material. If a change in the accounting policy has no material effect on the financial statements for the current period, but is expected to have a material effect in the later periods, the same should be appropriately disclosed.	Requires retrospective application of changes in accounting policies by adjusting the opening balance of each affected component of equity for the earliest prior period presented and the other comparative amounts for each period presented as if the new accounting policy had always been applied (unless transitional provisions of an accounting standard require otherwise).	Similar to IFRS.
Prior period items (Errors)	Prior period items are included in determination of net profit or loss of the period in which the error pertaining to a prior period is discovered and are separately disclosed in the statement of profit and loss in a manner that the impact on current profit or loss can be perceived.	Material prior period errors are corrected retrospectively by restating the comparative amounts for prior periods presented in which the error occurred or if the error occurred before the earliest period presented, by restating the opening statement of financial position.	Similar to IFRS.
New accounting pronouncements	Not required to be disclosed.	New accounting pronouncements that have been issued but are not yet effective as at the end of the reporting period are disclosed, if thay are not applied. In such a case, known or reasonably estimable information relevant to assessing the possible impact that application of the new accounting pronouncements will have on the financial statements on initial application is also disclosed.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Absence of standard or interpretation that specifically applies to a transaction	Not specifically provided.	In the absence of an IFRS that specifically applies to a transaction, it is permitted to consider the recent pronouncements by other standard setting bodies that use a similar conceptual framework to IFRS to the extent these pronouncements do not conflict with IFRS.	In the absence of an Ind AS that specifically applies to a transaction, other event or condition, the management, while using judgment in developing and applying an accounting policy, should first consider the most recent pronouncements of the IASB, and in absence thereof those of the other standard setting bodies that use a similar conceptual framework to develop accounting standards.
Events after the Reporting Period — Source Standard	**AS 4 Contingencies and Events Occurring after the Balance Sheet Date**	**IAS 10— Events After the Reporting Period**	**Ind AS 10— Events After the Reporting Period**
Dividends	Dividends stated to be in respect of the period covered by the financial statements, which are proposed or declared after the balance sheet date but before approval of the financial statements are recorded as a provision.	Liability for dividends declared to holders of equity instruments are recognised in the period when declared. It is a non-adjusting event.	Similar to IERS.
Breach of a long-term loan Adjusting event	Not specifically provided.	When an entity breaches a provision of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand, an agreement by the lender after the reporting period and before the authorisation of the financial statements for issue not to demand payment is not considered as an adjusting event.	Where there is a breach of a long-term loan arrangement before the end of the reporting period whereby the liability becomes payable on demand on the reporting date, the agreement by lender before the approval of the financial statements for issue not to demand payment as a consequence of the breach, will be considered as an adjusting event.
Income Taxes - Source Standards	**AS 22 Accounting for Taxes on Income**	**IAS 12 — Income Taxes**	**Ind AS 12 — Income Taxes**
Deferred income taxes	Deferred taxes are computed for timing differences in respect of recognition of items of profit or loss for the purposes of financial reporting and for income taxes.	Deferred taxes are computed for temporary differences between the carrying amount of an asset or liability in the statement of financial position and its tax base.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Recognition of deferred tax assets and liabilities	Deferred taxes are generally recognised for all timing differences.	Deferred income taxes are recognised for all temporary differences between accounting and tax base of assets and liabilities except to the extent which arise from a) initial recognition of goodwill or b) asset or liability in a transaction which i) is not a business combination; and ii) at the time of the transaction, affects neither the accounting nor the tax profit.	Similar to IFRS.
Recognition of taxes on items recognised in other comprehensive income or directly in equity	Not specifically provided.	Current tax and deferred tax are recognised outside profit or loss if the tax relates to items that are recognised in the same or a different period, outside profit or loss. Therefore, the tax on items recognised in other comprehensive income or directly in equity, is also recorded in other comprehensive income or in equity, as appropriate.	Similar to IFRS.
Recognition of deferred tax assets for unused tax losses etc.	Deferred tax asset for unused tax losses and unabsorbed depreciation is recognised only to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available against which such deferred tax assets can be realised. Deferred tax asset for all other unused credits/timing differences is recognised only to the extent that there is a reasonable certainty that sufficient future taxable income will be available against which such deferred tax assets can be realised.	Deferred tax asset is recognised for carry forward unused tax losses and unused tax credits to the extent that it is probable that future taxable profit will be available against which the deferred tax asset can be utilised. Where an entity has a history of tax losses, the entity recognises a deferred tax asset only to the extent that the entity has sufficient taxable temporary differences or there is convincing other evidence that sufficient taxable profit will be available.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Investments in subsidiaries, branches, and associates and interests in joint arrangements	No deferred tax liability is recognised. Deferred tax expense is an aggregation from separate financial statements of each group entity and no adjustment is made on consolidation,	Deferred tax liability for all taxable temporary differences are recognised except to the extent: • the parent, the investor, the venturer or joint operator is able to control timing of the reversal of the temporary difference, and • it is probable that the temporary difference will not reverse in the foreseeable future.	Similar to IFRS.
Deferred tax in respect of business combinations	Not specifically provided.	If the potential benefit of the acquiree's income tax loss carry forwards or other deferred tax assets did not satisfy the criteria in IFRS 3 for separate recognition when the business combination was initially accounted but if such benefit is subsequently recognised, goodwill is reduced to record pre-acquisition deferred tax assets which are recognised within 12 months of the acquisition date as a result of new information on facts and circumstances that existed on the acquisition date. If the carrying amount of goodwill is zero, any remaining deferred tax benefit is recognised in profit or loss. All other deferred tax benefits are recognised in profit or loss (or if IAS 12 so requires, outside profit or loss).	Similar to IFRS, except that if the carrying amount of goodwill is zero, any remaining deferred tax benefits are recognised in other comprehensive income and accumulated in equity as capital reserve or recognised directly in capital reserve depending on whether there exists clear evidence of the underlying reasons for classifying the business combination as a bargain purchase as specified in Ind AS 103—Business Combinations.
Deferred tax on unrealised intra-group profits	Deferred tax is not recognised.	Deferred tax on unrealised intra- group profits is recognised at the buyer's rate.	Similar to IFRS.
Classification of deferred tax assets and liabilities	Not specifically provided.	Always classified as non-current, if current and non-current classification is presented.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Disclosure	Certain additional disclosures like rate reconciliation, tax holidays and their expiry and unrecognised deferred tax liability on undistributed earnings of subsidiaries, branches, associates and joint ventures are not required.	Additional disclosures required under IFRS include: • A reconciliation between the income tax expense (income) reported and the product of accounting profit multiplied by the applicable tax rate. Either a numerical reconciliation or tax rate reconciliation is required to be presented. • Details of tax holidays and expiry. • Unrecognised deferred tax liability on undistributed earnings of subsidiaries, branches, associates and joint ventures.	Similar to IFRS.
Tax benefits related to share-based payments	Not specifically provided.	Deferred tax benefit is calculated based on tax deduction for the share based payment under the applicable tax law (for example intrinsic value).	Similar to IFRS.
Recovery of revalued non-depreciable assets	Revaluation is treated as a permanent difference and, hence, the question of recognising deferred tax effects of the same does not arise at all,	Measurement of deferred tax liability or asset arising from revaluation is based on the tax consequences from the sale of asset rather than through use.	Similar to IFRS.
Recovery of investment property measured under fair value model	N.A.	In the case of investment property measured using fair value model, for measuring deferred taxes, there is a rebuttable presumption that the carrying amount will be recovered through sale.	Similar to Indian GAAP.
Recognition on foreign currency denominated non-monetary assets/ liabilities when the tax reporting currency is not the functional currency	N.A..	Non-monetary assets and liabilities of an entity are measured in its functional currency. If the entity's taxable profit or tax loss is determined in a different currency, changes in the exchange rate give rise to temporary differences that result in a recognised deferred tax liability or asset.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Changes in Tax Status of an Entity or its Shareholders	Not specifically provided.	Current and deferred tax consequences are included in the profit or loss of the period of change unless the consequences relate to transactions or events recognised outside profit or loss either in other comprehensive income or directly in equity in the same or a different period.	Similar to IFRS.
Property, Plant and Equipment primary literature - Source Standards	**AS 6 — Depreciation Accounting** **AS 10 –Accounting for Fixed Assets**	**IAS 16 — Property, Plant and Equipment**	**Ind AS 16 Property, Plant and Equipment**
Scope	There is no exemption in AS 10 for property under development for future use as investment property.	Property under construction or development for future use as investment property is excluded from the scope of IAS 16 and is within the scope of IAS 40, Investment Property. Biological assets that meet the definition of a bearer plant is expected to bear produce for more than one period and which will not be sold as agricultural produce are included in property, plant and equipment.	Similar to IFRS.
Regarding major spare parts	Machinery spares are usually charged to the profit and loss statement as and when consumed, However, if such spares can be used only in connection with an item of fixed asset and their use is expected to be irregular, it may be appropriate to allocate the total cost on a systematic basis over a period not exceeding the useful life of the principal item.	Spare parts are recognised in accordance with IAS 16 when they meet the definition of property, plant and equipment. Otherwise, such items are classified as inventory.	Similar to IFRS.
Estimated costs of dismantling, removing or restoring items of property, plant and equipment	No such specific requirement.	The initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located is required to be included in the cost of the respective item of property plant and equipment.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Replacement costs	Replacement cost of an item of PPE is generally expensed when incurred. Only expenditure that increases the future benefits from the existing asset beyond its previously assessed standard of performance is capitalised. From financial years commencing on or after 1 April 2015, Schedule II mandated that fixed assets to be reported component-wise and therefore, the position will be similar to that under IFRS.	Replacement cost of an item of PPE is capitalised if replacement meets the recognition criteria. Carrying amount of items replaced is derecognised.	Similar to IFRS.
Cost of major inspections	Costs of major inspections are generally expensed when incurred.	Cost of major inspections is recognised in the carrying amount of PPE as a replacement, if recognition criteria are satisfied and any remaining carrying amount of the cost of previous inspection is derecognised.	Similar to IFRS.
Revaluation	No specific requirement on frequency of revaluation.	If an entity adopts the revaluation model, revaluations are required to be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period.	Similar to IFRS.
Depreciation	Assets not required to be reported component-wise and depreciated separately, although it states that such an approach may improve the accounting for an item of fixed asset.	Property, plant and equipment are reported component-wise and are depreciated separately. There is no concept of minimum statutory depreciation under IFRS.	Similar to IFRS.
Compensation for impairment	No specific requirement. In practice, compensation is offset against replaced items of property, plant and equipment.	Compensation from third parties for impairment or loss of items of property, plant and equipment are included in profit or loss when the compensation becomes receivable.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Transfers from revaluation reserve	Not specifically provided.	Transfers from revaluation reserve to retained earnings are made directly and not through profit or loss.	Similar to IFRS.
Updating the Residual value	Estimates of residual value are not required to be updated.	Estimates of residual value need to be reviewed at least at each year end.	Similar to IFRS.
Reassessment of useful life and depreciation method	Not specifically stated.	Requires annual reassessment of useful life and depreciation method.	Similar to IFRS.
Acceptable methods of depreciation	Depreciation methods include the straight-line method, the diminishing balance method and the units of production method.	A variety of depreciation methods can be used to allocate based on asystematic basis over its useful life, which include the straight- line method, the diminishing balance method and the units of production method. However, a depreciation method that is based on revenue is not appropriate (effective for annual	Similar to IFRS.
Change in method of depreciation	Requires retrospective re-computation of depreciation and any excess or deficit on such re-computation is required to be adjusted in the period in which such change is affected. Such a change is treated as a change in accounting policy and its effect is quantified and disclosed.	Changes in depreciation method are considered as change in accounting estimate and applied prospectively.	Similar to IFRS.
Presentation of capital advances	Schedule II requires capital advances to be presented separately under the head 'Long-term loans and advances', as part of non-current assets.	No specific guidance though usually included in capital-work-in-progress.	Similar to IFRS.
Routine sale of some properties	Not specifically provided.	Entities might routinely sell items of property, plant and equipment that they have previously held for rental to others. The proceeds from the sale of such assets should be recognised as revenue in accordance with IAS 18,1FRS 15 (for annual period beginning 1.1.17).	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Changes in Existing Decommissioning, Restoration and Similar Liabilities	Not specifically provided.	Provisions for decommissioning, restoration and similar liabilities that have previously been recognized as part of the cost of an item of property, plant and equipment are adjusted for changes in the amount or timing of future costs and for changes in market-based discount rates.	Similar to IFRS.
Stripping Costs in the Production phase of a surface mine	Not specifically provided.	Waste removal costs that are incurred in surface mining activity during the production phase of the mine ('production stripping costs'). It addresses recognition of production stripping costs as an asset and measurement (initial and subsequent) of that stripping activity asset.	Similar to IFRS.
Leases — Source Standard	**AS 19— Leases**	**IAS 17— Leases** **IFRIC 4 — Determining Whether an Arrangement Contains a Lease** **SIC 15 — Operating Leases — Incentives** **SIC 27 — Evaluating the Substance of Transactions Involving the Legal Form of a Lease**	**Ind AS 17— Leases** **Ind AS 17—Appendix A — Operating Leases Incentives** **Ind AS 17— Appendix B — Evaluating the Substance of Transactions involving the Legal Form of a Lease** **Ind AS 17—Appendix C— Determining Whether an Arrangement Contains a Lease**
Interest in leasehold land	Leasehold land is recorded and classified as fixed assets.	• Recognised as operating lease or finance lease as per definition and classification criteria. **NB**: An important consideration in such determination is that land has an indefinite economic life. • A property interest in an operating lease may be classified as investment property in which case it should be accounted for as a finance lease and the fair value model should be applied for the asset recognised.	• Similar to IFRS • A property interest in an operating lease cannot be accounted for as investment property.

TOPIC	AS	IFRS	IND AS
Recognition of operating lease rentals	**Lease payments under an operating lease:** It should be recognised as an expense in the statement of profit and loss on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit. **Lease income from operating leases:** It should be recognised in the statement of profit and loss on a straight-line basis over the lease term, unless another systematic basis is more representative of the time pattern in which benefit derived from the use of the leased asset is diminished.	Similar to AS i.e. Indian GAAP.	Ind AS 17 contains a carve out for escalation of operating lease rentals that are in line with the expected general inflation.
Finance Lease - Initial direct costs of lessors for assets (other than those involving manufacturer or dealer lessors)	Either recognised immediately in the statement of profit and loss; or allocated against the finance income over the lease term.	Included in the measurement of the finance lease receivable and reduce the amount of income recognised over the ease term.	Similar to IFRS.
Finance Lease - Initial direct costs of lessors for assets (involving manufacturer or dealer lessors)	Recognised as expense at the inception of the lease.	Recognised as expense when selling profit is recognised, which is normally at the commencement of the lease term.	
Operating Leases— Initial direct costs of lessors for assets	Either deferred and allocated to income over the lease term (in proportion to the recognition of lease income); or are recognized as an expense in the statement of profit and loss in the period in which they are incurred.	Added to the carrying amount of the leased asset and recognised as an expense over the lease term on the same basis as lease income.	Similar to IFRS.
Determining as to whether an arrangement contains a lease	Not specifically covered. Payments under such arrangements are recognised in accordance with the nature of expense incurred,	Arrangements that do not take the legal form of a lease but fulfillment of which is dependent on the use of specific assets and which convey the rights to use the assets are accounted for as lease.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Operating Leases — Incentives	Not specifically covered.	Lease incentives (such as rent-free period) for operating leases are recognised by both the lessor and the lessee as a reduction of rental income and expense, respectively, over the lease term. Moreover, these are recognised on a straight-line basis unless another systematic basis is more representative of the time pattern over which the benefit of the leased asset is diminished for the lessor/time pattern of the lessee's benefit from the use of the leased asset (for the lessee).	Similar to IFRS.
Evaluation of a series of transactions Involving the Legal Form of a Lease	Not specifically covered.	A series of transactions that involves the legal form of a lease and the economic effect can only be understood with reference to the series as a whole, is accounted for as a single transaction	Similar to IFRS.
Employee Benefits — Source Standard	**AS 15 (Revised 2005> — Employee Benefits**	**IAS 19 — Employee Benefits (2011)**	**Ind AS 19 * Employee Benefits**
Distinction between short-term and other long-term employee benefits	The distinction between short-term and other long-term employee benefits depends on whether they fall wholly due within 12 months after the end of the period in which the employees render the related service.	The distinction between short-term and other long-term employee benefits depends on whether those benefits are expected to be settled wholly before twelve months after the end of the annual reporting period. Short-term employee benefits are recognised as an expense in the period in which the employee renders the related service. Unpaid short-term benefit liability is measured at an undiscounted amount.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Short-term compensated absences	Short-term employee benefits include short-term compensated absences where the absences are expected to occur within 12 months after the end of the period in which the employees render the related service.	Short-term employee benefits include paid annual leave and paid sick leave if it is expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related services.	Similar to IFRS.
Actuarial valuation	Similar to IFRS, except that detailed actuarial valuation to determine present value of the benefit obligation is carried out at least once every three years and fair value of plan assets are determined at each balance sheet date.	Detailed actuarial valuation to determine the present value of the net defined benefit liability (asset) is performed with sufficient regularity so that the amounts recognised in the financial statements do not differ materially from the amounts that would have been determined at the end of the reporting period. IAS 19 does not specify sufficient regularity.	Similar to IFRS.
Actuarial gains and losses	All actuarial gains and losses should be recognised immediately in the statement of profit and loss,	Actuarial gains and losses representing changes in the present value of the defined benefit obligation resulting from experience adjustment and effects of changes in actuarial assumptions are recognised in other comprehensive income and not reclassified to profit or loss in a subsequent period.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Discount rate	Market yields at the balance sheet date on government bonds are used as discount rates. The currency and term of the government bonds should be consistent with the currency and estimated term of the post-employment benefit obligations.	Post-employment benefit obligations (both funded and unfunded) are discounted using a discount rate determined by reference to market yields at the end of the reporting period on high quality corporate bonds. In countries where there is no deep market in such bonds, the market yields on government bonds denominated in that currency should be used.	Post-employment benefit obligations (both funded and unfunded) should be discounted using a discount rate determined by reference to market yields at the end of the reporting period on government bonds. However, subsidiaries. associates, joint ventures and branches domiciled outside India should use a rate determined by reference to market yields on high quality corporate bonds at the end of the reporting period. In case, such subsidiaries, associates, joint ventures and branches are domiciled in countries where there is no deep market in such bonds, the market yields (at the end of the reporting period) on government bonds of that country should be used. The currency and term of the government bonds or corporate bonds should be consistent with the currency and estimated term of the post-employment benefit obligations.
Defined benefit plans	The changes in defined benefit liability (surplus) has the following components: a) Service cost — recognised in profit or loss; b) Interest cost — recognised in profit or loss; c) The expected return on any plan assets — recognised in profit or loss; d) Net actuarial gains and losses — recognised in profit or loss.	The change in the defined benefit liability (asset) has the following components: a) Service cost — recognised in profit or loss; b) Net interest cost (i.e. time value) on the net defined benefit deficit! (asset) — recognised in profit or loss; c) Remeasurement including i) changes in fair value of plan assets that arise from factors other than time value and ii) actuarial gains and losses on obligations — recognised in other comprehensive income.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Termination benefits	Termination benefits are recognised as a liability and an expense when, and only when: • the enterprise has a present obligation as a result of a past event; • it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and • a reliable estimate can be made of the amount of the obligation.	A termination benefit liability is recognised at the earlier of the following dates: • when the entity can no longer withdraw the offer of those benefits — additional guidance is provided on when this occurs in relation to an employees decision to accept an offer of benefits on termination and as a result of an entity's decision to terminate an employee's employment; • when the entity recognises costs for a restructuring under IAS 37 Provisions, Contingent Liabilities and Contingent Assets which involves the payment of termination benefits.	Similar to IFRS.
Past service cost and curtailments	Past service cost is recognised as under: • As an expense on a straight-line basis over the average period until the benefits become vested. • If benefits already vested, recognised as an expense immediately. Entities recognise a curtailment when it occurs. However, when a curtailment is linked with a restructuring, it is accounted for at the same time as the related restructuring.	Past service cost (includes curtailments) is recognised as an expense at the earlier of the following dates: • when the plan amendment or curtailment occurs; and • when the entity recognises related restructuring costs or termination benefits.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Actuarial assumptions for Administration costs	The expected and actual return on plan assets is arrived at after deducting expected administrative costs, other than those included in the actuarial assumptions used to measure the defined benefit obligation. But AS 15 does not specify which costs should be included in those actuarial assumptions.	In determining the return on plan assets, an entity deducts the costs of managing the plan assets and any tax payable by the plan itself, other than tax included in the actuarial assumptions used to measure the defined benefit obligation. Other administration costs are not deducted from the return on plan assets.	Similar to IFRS.
Employee benefits contributions from employees or third parties to defined benefit plans	Not specifically provided.	Provides guidance on accounting for contributions from employees or third parties to defined benefit plans, which are linked to service- both dependent and independent of the number of years of service.	Similar to IFRS.
The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction	Not specifically provided.	Addresses when refunds or reductions in future contributions are regarded as available for recognition of an asset; how minimum funding requirements may affect the availability of reductions in future contributions and when minimum funding requirement may give rise to a liability. It also deals with prepayments of a minimum funding requirement.	Similar to IFRS.
Government Grants - Source Standard	**AS 12 — Accounting for Government Grants**	**IAS 20 — Accounting for Government Grants and Disclosure of Government Assistance**	**Ind AS 20 — Accounting for** **Government Grants and Disclosure of Government Assistance**
Regarding Government assistance	Not specifically provided.	Deals with both government grants and disclosure of government assistance.	Similar to IFRS.
Regarding Forgivable loans	Not specifically provided.	Treated as government grants when there is a reasonable assurance that the entity will meet the terms for forgiveness of the loan.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Government loans with below market rate of interest	Not specifically provided.	Government loans with below market rate of interest should be accounted for as government grant. It is measured as the difference between the initial carrying amount of the loan determined in accordance with IFRS 9 and the proceeds received.	Similar to IFRS.
Recognition of Government Grants	Two broad approaches may be followed — the capital approach or the income approach. **Government grants in the nature of promoters' contribution:** Credited directly to shareholders' funds. **Grants related to revenue:** Recognised in the statement of profit and loss on a systematic and rational basis over the periods necessary to match them with the related costs. **Grants relating to non-depreciable assets:** Credited to capital reserve. It such grants require fulfilment of some obligation, such grants should be credited to income over the period over which the cost of meeting the obligation is charged to income. Grants related to depreciable assets are either treated as deferred income and transferred to the statement of profit and loss in proportion to depreciation, or deducted from the cost of the asset.	Government grants are not directly credited to shareholders' interests. Government grants are recognized as income to match them with expenses in respect of the related costs for which they are intended to compensate on a systematic basis. **Government grants related to assets:** Presented in the statement of financial position either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.	Similar to IFRS. **Grants related to assets** (including non-monetary grants at fair value): Should be presented in the balance sheet only by setting up the grant as deferred income.

TOPIC	AS	IFRS	IND AS
Non-monetary government grants	If the asset is given by the Government at a discounted price, the asset and the grant is accounted at the discounted purchase price, Non-monetary grants free of cost are accounted for at nominal values.	The asset and the grant may be accounted at fair value. Alternatively, these can be recorded at nominal amount.	The asset and the grant should be accounted at fair value.
Repayment of grants relating to fixed assets	• Recognised either by increasing the carrying amount of the asset or reducing the deferred income or capital reserve, as appropriate, by the amount repayable. If the carrying amount of the asset is increased, depreciation on the revised carrying amount is provided prospectively over the residual useful life of the asset. • • Classified as an extraordinary item.	• Recognised either by increasing the carrying amount of the asset or reducing the deferred income by the amount repayable. • Cumulative depreciation that would have been recognised in profit or loss to date in the absence of grant should be recognised immediately in profit or loss. • Prohibited to be classified as an extraordinary item.	• Recognised by reducing the deferred income balance by the amount repayable. • Prohibited to be classified as an extraordinary tern.
Foreign Exchange - Source Standard	**AS 11 The Effects of Changes in Foreign Exchange Rates**	**IAS 21 — The Effects of Changes in Foreign Exchange Rates**	**Ind AS 21 - The Effects of Changes in Foreign Exchange Rates**
Functional and presentation currency	Foreign currency is a currency other than the reporting currency which is the currency in which financial statements are presented. There is no concept of functional currency.	Functional currency is the currency of the primary economic environment in which the entity operates. Foreign currency is a currency other than the functional currency. Presentation currency is the currency in which the financial statements are presented.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Exchange differences	There is a limited period irrevocable option for corporate entities to capitalise exchange differences on long-term foreign currency monetary items incurred for acquisition of depreciable capital assets and to amortise exchange differences on other long-term foreign currency monetary items over the life of such items but not beyond the stipulated date. Exchange differences on monetary items that in substance, form part of net investment in a non-integral foreign operation, are recognised in 'Foreign Currency Translation Reserve' both in the separate and consolidated financial statements and recognised as income or expense at the time of disposal of that operation.	Exchange differences arising on translation or settlement of foreign currency monetary items are recognised in profit or loss in the period in which they arise, Exchange differences on monetary items, that in substance, form part of net investment in a foreign operation, are recognised in profit or loss in the period in which they arise in the separate financial statements and in other comprehensive income in the consolidated financial statements and reclassified from equity to profit or loss on disposal of the net investment.	Similar to IFRS. However, an entity may continue the policy adopted for exchange differences arising from translation of long-term foreign currency monetary items recognized in the financial statements for the period ending immediately before the beginning of the first Ind AS financial reporting period as per previous GAAR
Translation in the consolidated financial statements	Translation of financial statements of a foreign operation to the reporting currency of the parent/ investor depends on the classification of that operation as integral or non-integral. In the case of an integral foreign operation, monetary assets are translated at closing rate. Non-monetary items are translated at historical rate if they are valued at cost. Non-monetary items which are carried at fair value or other similar valuation are reported using the exchange rates that existed when the values were determined. Income and expense items are translated at historical/average rate. Exchange differences are taken to the statement of profit and loss.	Assets and liabilities should be translated from functional currency to presentation currency at the closing rate at the date of the statement of financial position; income and expenses at actual/average rates for the period; exchange differences are recognised in other comprehensive income and accumulated in a separate component of equity. These are reclassified from equity to profit or loss (as a reclassification adjustment) when the gain or loss on disposal is recognised.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
	For non-integral foreign operations, closing rate method should be followed (i.e. all assets and liabilities are to be translated at closing rate while profit and loss account items are translated at actual/ average rates). The resulting exchange difference is taken to reserve and is recycled to profit and loss on the disposal of the non-integral foreign operation. Treatment for disposal does not depend on whether control over a foreign subsidiary is lost or not. Even if control is lost, only proportionate amount of the reserve is recycled to statement of profit and loss.	Treatment of disposal depends on whether control is lost or not. Thus, if control is lost, the exchange difference attributable to the parent is reclassified to profit or loss from foreign currency translation reserve in other comprehensive income.	
Scoping for derivatives	AS 11 is applicable to exchange differences on all forward exchange contracts including those entered into to hedge the foreign currency risk of existing assets and liabilities and is not applicable to the exchange difference arising on forward exchange contracts entered into to hedge the foreign currency risks of future transactions in respect of which firm commitments are made or which are highly probable forecast transactions.	Foreign currency derivatives that are not within the scope of IAS 39 (e.g. some foreign currency derivatives that are embedded in other contracts) are within the scope of IAS 21. In addition, AS 21 applies when an entity translates amounts relating to derivatives from its functional currency to its presentation currency.	Similar to IFRS.
Forward exchange contracts	Forward exchange contracts not intended for trading or speculation purposes: (i) Any premium or discount arising at the inception of a forward exchange contract is amortised as expense or income over the life of the contract.	Accounted for as a derivative.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
	(ii) Exchange differences on such a contract are recognised in the statement of profit and loss in the reporting period in which the exchange rates change. Exchange difference on a forward exchange contract is the difference between (a) the foreign currency amount of the contract translated at the exchange rate at the reporting date, or the settlement date where the transaction is settled during the reporting period, and (b) the same foreign currency amount translated at the latter of the date of inception of the forward exchange contract and the last reporting date. Forward exchange contract intended for trading or speculation purposes: The premium or discount on the contract is ignored and at each balance sheet date, the value of the contract is marked to its current market value and the gain or loss on the contract is recognised.		
Change in functional currency	Change in reporting currency is not dealt with, though reason for change is required to be disclosed,	Change in functional currency is applied prospectively. The fact of change in functional currency and the reason for the change in functional currency should be disclosed.	Similar to IFRS. Additionally, the date of change in functional currency is also required to be disclosed.

TOPIC	AS	IFRS	IND AS
Borrowing Costs - Source Standard	**AS 16 Borrowing Costs**	**IAS 23 Borrowing Costs**	**Ind AS 23 Borrowing Costs**
Scope	N.A.	Borrowing costs need not be capitalised in respect of (a) qualifying assets measured at fair value (e.g. biological assets) (b) inventories that are manufactured, or otherwise produced, in large quantities on a repetitive basis (even if they are otherwise qualifying assets). This is an option.	Similar to IFRS.
Components of borrowing costs	No reference to effective interest rate.	Description of specific components are linked to effective interest rate.	Similar to IFRS.
Related Party Disclosures - Source Standard	**AS 18 — Related Party Disclosures**	**IAS 24 Related Party Disclosures**	**Ind AS 24— Related Party Disclosures**
Related party	Parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.	A related party is a person or entity that is related to the entity that is preparing its financial statements (reporting entity): a) A person or a close member of that person's family is related to a reporting entity if that person: i) has control or joint control of the reporting entity; ii) has significant influence over the reporting entity; or iii) is a member of the key management personnel of the reporting entity or of a parent of the reporting entity. b) An entity is related to a reporting entity if any of the following conditions apply: i) The entity and the reporting entity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
		ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member). iii) Both entities are joint ventures of the same third party. iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity. v) The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity. vi) The entity is controlled or jointly controlled by a person identified in a). vii) A person identified in a) i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity). viii) The entity, or any member of a group of which it is a part, provides key management personnel services to the reporting entity or to the parent of the reporting entity (this is effective for annual periods beginning on or after 1 July 2014).	

TOPIC	AS	IFRS	IND AS
Close member of the family	The term'close member of the family' is not defined. Instead the term "relative" has been defined in relation to an individual as the spouse, son, daughter, brother, sister, father, mother who may be expected to influence, or be influenced by, that individual in his/her dealings with the reporting enterprise.	Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity and include: a) that person's children and spouse or domestic partner; b) children of that person's spouse or domestic partner; and c) dependants of that person or that person's spouse or domestic partner.	Similar to IFRS with the inclusion of father, mother, brother and sister in the definition of close members of the family.
Post-employment benefit plans	Post-employment benefit plans are not included as related parties.	Related party includes post-employment benefit plans for the benefit of employees of the reporting entity or any entity that is related to the reporting entity.	Similar to IFRS.
Exemptions	Disclosure requirements do not apply if providing such disclosures would conflict with an enterprise's duties of confidentiality as specifically required in terms of a statute or by any regulator or similar competent authority. Also, no disclosure is required in the financial statements of a state-controlled enterprise as regards related party relationships with other state-controlled enterprises and transactions with such enterprises.	Some minimum disclosures should be made by government-related entities.	Disclosures which conflict with confidentiality requirements of statute/ regulations are not required to be made.
Items to be disclosed	If an entity has related party transactions during the period covered by the financial statements, the enterprise should disclose the volume of transactions either as an amount or as an appropriate proportion and amounts or appropriate proportions of outstanding items.	If an entity has related party transactions during the period covered by the financial statements, the amount of such transactions and the amount of outstanding balances including commitments need to be disclosed.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Key management personnel	Compensation of key management personnel is disclosed in total as an aggregate of all items of compensation except when a separate disclosure is necessary for the understanding of the effects of related party transactions on the financial statements.	Compensation of key management personnel is disclosed in total and separately for a) short-term employee benefits; b) postemployment benefits; c) other long-term benefits; d) termination benefits; and e) share-based payments.	Similar to IFRS.
Investments in Associates and Joint Ventures — Source Standard	**AS 23 — Accounting for Investments in Associates in Consolidated Financial Statements**	**IAS 28 (Revised 2011) Investments in Associates and Joint Ventures**	**Ind AS 28 — Investments in Associates and Joint Ventures**
Significant influence	Significant influence is the power to participate in the financial and/ or operating policy decisions of the investee but not control over those policies,	Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.	Similar to IFRS
Potential voting rights	Potential voting rights are not considered in assessing significant influence,	The existence and effect of potential voting rights that are currently exercisable or convertible, including potential voting rights held by another entity, are considered when assessing significant influence.	Similar to IFRS
Equity method	As per AS 23, equity method is applicable only when the entity has subsidiaries and prepares consolidated financial statements. However, as per Companies Act, 2013, consolidated financial statements should be prepared, even if an entity has only associates and/or joint ventures but has no subsidiaries. For financial year ending 31 March 2015, if a company does not have any subsidiaries, but only has associates and/or joint ventures, then the company would not have to prepare consolidated financial statements in respect of such associates and/ or joint ventures. (Refer the topic 'Consolidated Financial Statements - scope').	Even if consolidated financial statements are not prepared (e.g. because the investor has no subsidiaries) equity accounting is used. IFRS 5 is applied to an investment, or a portion of an investment in an associate that meets the criteria to be classified as held for sale.	Similar to IFRS

TOPIC	AS	IFRS	IND AS
Scope	Currently there is no exemption for investments made by venture capital organisations, mutual funds, unit trusts and similar entities from applying the equity method.	Investments by venture capital organisations, mutual funds, unit trusts and similar entities including investment-linked insurance funds are exempted from applying equity method, if an election is made to measure such investments at FVTPL in accordance with IFRS 9 or IAS 39 where the entity is yet to apply IFRS 9. If this election is made, certain disclosure requirements have to be complied with. IAS 28 provides exemptions from applying the equity method similar to exemptions provided in IFRS O — Consolidated Financial Statements (Refer the topic 'Consolidated Financial Statements - scope')	Similar to IFRS.
Share of losses	Loss in excess of the carrying amount of investment is not recognised, unless the investor has incurred obligations or made payments on behalf of the associate to satisfy obligations of the associate that the investor has guaranteed or to which the investor is otherwise committed.	Losses recognised in excess of the interest in the investment are not recognised. The 'interest' is the carrying amount of investment determined using the equity method together with any long-term interest that, in substance, form part of the entity's net investment in the associate. Losses recognised using the equity method in excess of the entity's investment in ordinary shares are applied to the other components of the entity's interest in an associate in the reverse order of their seniority (i.e. priority in liquidation). After the entity's interest is reduced to zero, additional losses are provided for, and a liability is recognised, only to the extent that the entity has incurred legal or constructive obligations or made payments on behalf of the associate.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Transactions between investor and the associate	Unrealised profits and losses resulting from transactions between the investor (or its consolidated subsidiaries) are eliminated to the extent of the investors interest in the associate. Unrealised losses should not be eliminated if and to the extent the cost of the transferred asset cannot be recovered.	Investor's share in the gains or losses resulting from upstream and downstream transactions involving assets that do not constitute a 'business' as defined in IFRS 3 between the investor (including its consolidated subsidiaries) and its associate are eliminated. When downstream transactions provide evidence of impairment, the losses are recognised in full. When upstream transactions provide evidence of impairment, the investor should recognise its share of loss. Gain or loss resulting from a downstream transaction involving assets that constitute a 'business' as defined in IFRS 3 between the investor (including its consolidated subsidiaries) and its associate is recognised in full in the investor's financial statements.	Similar to IFRS.
Disposals	Not specifically provided for.	When an investor dis4ntinues the use of the equity method (for example, as a result of a change in ownership), the investment retained is remeasured to its fair value, with the gain or loss recognised in profit or loss. Thereafter, IFRS 9 or IAS 39 is applied to the remaining holding unless the investment becomes a subsidiary in which case the investment is accounted for in accordance with IFRS 3.	Similar to IFRS.
Goodwill	Goodwill arising on the acquisition of an associate by an investor should be included in the carrying amount of investment in the associate but should be disclosed separately.	Goodwill (i.e. excess of the cost of the investment over the investor's share of the net fair value of the associate's identifiable assets and liabilities) is included in the carrying amount of the investment.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Capital reserve/negative goodwill	Capital reserve arising on the acquisition of an associate by an investor should be included in the carrying amount of investment in the associate but should be disclosed separately.	Any excess of the investor's share of net fair value of the associate's identifiable assets and liabilities over the cost of investments is included as income in the determination of the investor's share of associate's profit or loss in the period in which the investment is acquired.	Any excess of the investor's share of the net fair value of the associate's identifiable assets and liabilities over the cost of the investment is recognised directly in equity as capital reserve in the period in which the investment is acquired.
Uniform accounting policies	If not practicable to use uniform accounting polices while applying the equity method, that fact should be disclosed together with a brief description of the differences between the accounting policies.	Uniform accounting policies should be followed while applying the equity method. No exception is provided.	Uniform accounting policies to be followed unless impracticable to do so.
Reporting date	The maximum difference between the reporting date of the associate and that of the parent is not specified.	The difference between the reporting date of the associate and that of the investor should be no more than three months.	Similar to IFRS.
Separate financial statements of the investor	At cost less impairment loss, if any, as per AS 13 — Accounting for Investments.	Either at cost or as an investment in accordance with IFRS 9 or IAS 39 (if the entity is yet to apply IFRS 9) or using the equity method as described in IAS 28, Investments in Associates and Joint Ventures. (The option to use the equity method will be applicable for annual periods beginning on or after 1 January 2016.)	Similar to IFRS, except that equity method is not permitted in the separate financial statements.
Reporting in Hyperinflationary Economies — Source Standard	**There is no equivalent standard.**	**IAS 29 Financial Reporting in Hyperinflationary Economies** **IFRIC 7 — Applying the Restatement Approach under IAS 29**	**Ind AS 29 Financial Reporting in Hyperinflationary Economies** **Ind AS 29 Appendix A - Applying the Restatement Approach under md AS 29**
Concept of Hyperinflationary	N. A.	Generally an economy is hyperinflationary when the cumulative inflation rate over 3 years is approaching or exceeds 100%.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Basic principle	N. A.	Financial statements should be stated in terms of the measuring unit current at the end of the reporting period. Comparative figures for prior period(s) should be restated into the same current measuring unit.	Similar to IFRS.
Disclosure	N. A.	The following disclosures are required: - the fact that the financial statements and the corresponding figures for previous periods have been restated for the changes in the general purchasing power of the functional currency and, as a result, are stated in terms of the measuring unit current at the end of the reporting period; - whether the financial statements are based on a historical cost approach or a current cost approach; and - the identity and level of the price index at the end of the reporting period and the movement in the index during the current and the previous reporting period.	Similar to IFRS. However, there is an additional disclosure required regarding duration of the hyperinflationary situation existing in the economy.
Restatements	N. A.	Restatements are made by applying a general price index. Items such as monetary items that are already stated at the measuring unit at the end of the reporting period are not restated. Other items are restated based on the change in the general price index between the date those items were acquired or incurred and the end of the reporting period. A gain or loss on the net monetary position is included in net income. It should be disclosed separately.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Applying the Restatement approach under IAS 29	There is no equivalent standard.	When the economy of an entity's functional currency becomes hyperinflationary, IAS 29 is applied as if the economy was always hyperinflationary.	Similar to IFRS.
Financial Instruments: Presentation — Source Standard	**AS 31 Financial Instruments: Presentation**	**IAS 32 Financial Instruments: Presentation**	**Ind AS 32 Financial Instruments: Presentation**
Classification of financial liabilities	Financial instruments are classified based on legal form — redeemable preference shares will be classified as equity. Preference dividends are always recognised similar to equity dividend and are never treated as interest expense.	Financial instruments are classified as a liability or equity according to the substance of the contractual arrangement, (and not its legal form), and the definition of financial liabilities and equity instruments. Dividends on financial instruments classified as financial liability is recognised as an interest expense in the statement of profit or loss and other comprehensive income. Hence if preference shares meet the definition of financial liability, the dividend is treated as an interest expense.	Similar to IFRS,
Treasury shares	Acquiring own shares is permitted only in limited circumstances. Shares repurchased should be cancelled immediately and cannot be held as treasury shares.	Cost of treasury shares is deducted from equity and resales of treasury shares are equity transactions. Costs of issuing or reacquiring equity instruments are accounted for as a deduction from equity, net of any related income tax benefit.	Similar to IFRS,
Offsetting Financial Instruments:	There are no offset rules. However, in practice the rules under IFRS are applied,	A financial asset and financial liability can only be offset if the entity currently has a legally enforceable right to set off the recognized amounts and intends to either settle on a net basis, or to realize the asset and settle the liability simultaneously.	Similar to IFRS,

TOPIC	AS	IFRS	IND AS
Classification of convertible debts	Currently, the entire instrument is classified as debt based on its legal form and any interest expense is recognised based on the coupon rate. Premium on redemption of the debt is recognised in securities premium to the extent available.	Split the instrument into liability and equity component / conversion option as an embedded derivative depending on the contractual terms of the financial instrument at issuance.	Similar to IFRS except for conversion option embedded in a foreign currency convertible bond under certain situations.
conversion option embedded in foreign currency convertible bonds	Not specifically provided for.	Conversion option to acquire fixed number of equity shares for fixed amount of cash in entity's functional currency only is treated as equity. Thus, a conversion option embedded in foreign currency convertible bonds is treated as embedded derivative, and accordingly fair valued through profit or loss at every reporting period end.	Conversion option to acquire fixed number of equity shares for fixed amount of cash in any currency (entity's functional currency or foreign currency) is treated as equity and accordingly is not required to be remeasured at fair value at every reporting date.
Puttable instruments etc.	Not specifically provided for.	Puttable instruments and instruments that impose an obligation to deliver pro rata share of net assets only on liquidation, that a) are subordinate to all other class of instruments and b) meet additional criteria as laid down in the standard, should be classified as equity instruments. This also triggers some disclosures to be made as required by IAS 1.	Similar to IFRS
Classification of rights issue	Not specifically provided for.	Rights, options or warrants to acquire a fixed number of an entity's own equity instruments for a fixed amount of any currency are equity instruments, if the entity offers such options, etc. pro rata to all of its existing owners of the same class of its non-derivative equity instruments.	Similar to IFRS

TOPIC	AS	IFRS	IND AS
Earnings Per Share — Source Standard	**AS 20 — Earnings Per Share**	**IAS 33 — Earnings Per Share**	**Ind AS 33 Earnings Per Share**
Applicability	Applicability of the standard is not linked to the listing status of an entity.	Applicable to the separate and consolidated financial statements of an entity/ group with a parent: • Whose ordinary shares or potential ordinary shares are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or • That files, or is in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing ordinary shares in a public market.	Ind AS 33 is applicable to companies that have issued ordinary shares to which Ind ASs noticed under the Companies Act apply.
Disclosure in separate financial statements	AS 20 requires disclosure of basic and diluted EPS information both in the separate and consolidated financial statements of the parent.	When an entity presents both separate and consolidated financial statements, EPS is required to be presented only in the consolidated financial statements. An entity may disclose EPS in its separate financial statements voluntarily.	EPS is required to be presented in both, consolidated as well as separate financial statements.
Disclosure of EPS from continuing and discontinued operations	No separate disclosure for EPSfrom continuing and discontinuing operations is required.	The statement of comprehensive income will present basic and diluted earnings per share from continuing operations and if applicable, basic and diluted earnings per share from discontinued operations. EPS from discontinued operations may alternatively be disclosed in the notes.	Similar to IFRS.
Additional disclosures	Certain additional disclosures that are required under IFRS are not required under the AS.	Disclosure is required for instruments (including contingently issuable shares) that could potentially dilute basic earnings per share in the future, but were not included in the calculation of diluted earnings per share because they are anti-dilutive for the periods presented.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Extraordinary items	EPS with and without extraordinary items is to be presented.	EPS with and without extraordinary items is not required to be presented (since IAS 1 prohibits the disclosure of items as extraordinary).	Similar to IFRS.
Mandatorily convertible instrument	Not specifically provided.	Ordinary shares to be issued upon conversion of a mandatorily convertible instrument are included in the calculation of basic EPS from the date the contract is entered into.	Similar to IFRS.
Contingently issuable shares	Not specifically provided.	Ordinary shares that are issuable solely after a passage of time are not treated as contingently issuable shares because passage of time is a certainty.	Similar to IFRS.
Contingently returnable shares	Not specifically provided.	Outstanding ordinary shares that are contingently returnable are not treated as outstanding and are ignored in the calculation of basic EPS until the shares are no longer subject to recall.	Similar to IFRS.
Items of income or expense debited or credited to securities premium account/other reserves	Not specifically provided. The ICAI has made a limited revision to AS 20 which will require that for purpose of calculating basic earnings per share, the net profit or loss for the period attributable to equity shareholders should be the net profit or loss for the period after adjusting the amount in respect of an item of income or expense which is debited or credited to share premium account / reserves, that is otherwise required to be recognised in the statement of profit and loss in accordance with Accounting Standards.	Not specifically provided.	Where any item of income or expense which is otherwise required to be recognised in profit or loss in accordance with Indian Accounting Standards is debited or credited to securities premium account/ other reserves, profit or loss from continuing operations should be adjusted by the amount in respect thereof for the purpose of calculating basic earnings per share.

TOPIC	AS	IFRS	IND AS
Interim Financial Reporting — Source Standard	**AS 25 — Interim Financial Reporting**	**IAS 34— Interim Financial Reporting**	**Ind AS 34 — Interim Financial Reporting**
Statutory requirement for an enterprise to prepare and present certain information at an interim date	A statute governing an enterprise or a regulator may require an enterprise to prepare and present certain information at an interim date which may be different in form and/ or content as required by AS 25. In such a case, the recognition and measurement principles as laid down in AS 25 are applied in respect of such information, unless otherwise specified in the statute or by the regulator.	It is not specifically provided as to when a statute requires an enterprise to prepare and present certain information at an interim date in a specific format.	Similar to IFRS.
Interim Reporting and Impairment	AS 28 does permit the reversal of goodwill in certain circumstances. This would be equally applicable to the interim financial statements. Reversal of impairment of investments is permitted in AS 13 and hence the same is equally applicable for interim financial statements.	Where an entity has recognized an impairment loss in an interim period in respect of goodwill, that impairment loss is not reversed in subsequent interim financial statements nor in annual financial statements.	Similar to IFRS.
Impairment of Assets — Source Standard	**AS 28 Impairment of Assets AS 26 — Intangble Assets**	**IAS 36 Impairment of Assets**	**Ind AS 36 — Impairment of Assets**
Regarding goodwill	AS 28 requires goodwill to be tested for impairment using the bottom-up/ top-down approach under which the goodwill is, in effect, tested for impairment by allocating its carrying amount to each cash-generating unit or smallest group of cash-generating units to which a portion of that carrying amount can be allocated on a reasonable and consistent basis.	Allocated to cash generating units that are expected to benefit from the synergies of business combination. Allocated to the lowest level at which goodwill is internally monitored by management which should not be larger than an operating segment before aggregation of segments as defined in IFRS 8.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Frequency of impairment test for goodwill and intangibles	Goodwill and other intangibles are tested for impairment only when there is an indication that they may be impaired. AS 26 *Intangible Assets* requires intangible assets that are not available for use and intangible assets that are amortised over a period exceeding ten years to be assessed for impairment at least at each financial year end even if there is no indication that the asset is impaired.	Goodwill, intangible assets not yet available for use and indefinite life intangible assets are required to be tested for impairment at least on an annual basis or earlier if there is an impairment indication.	Similar to IFRS.
Reversal of impairment loss for goodwill	Impairment loss for goodwill is reversed if the impairment loss was caused by a specific external event of an exceptional nature that is not expected to recur, and subsequent external events have occurred that reverse the effect of that event.	Impairment loss recognised for goodwill is prohibited from reversal in a subsequent period. Goodwill impaired in an interim period is not subsequently reversed in subsequent interim or annual financial statements.	Similar to IFRS.
Provisions, Contingent Assets and Contingent Liabilities — Source Standard	**AS 29 — Provisions, Contingent Liabilities and Contingent Assets**	**IAS 37 - Provisions, Contingent Liabilities and Contingent Assets**	**Ind AS 37 — Provisions Contingent Liabilities and Contingent Assets**
Recognition of provisions	Provisions are not recognised based on constructive obligations though some provisions may be needed in respect of obligations arising from normal practice, custom and a desire to maintain good business relations or to act in an equitable manner.	A provision is recognised only when a past event has created a legal or constructive obligation, an outflow of resources is probable, and the amount of the obligation can be estimated reliably. A constructive obligation is an obligation that derives from an entity's actions where, by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Discounting	Discounting of liabilities is not permitted and provisions are carried at their full values.	When the effect of time value of money is material, the amount of provision is the present value of the expenditure expected to be required to settle the obligation. The discount rate is a pre-tax rate that reflects the current market assessment of the time value of money and risks specific to the liability.	Similar to IFRS.
Contingent assets	Contingent assets are neither recognised nor disclosed in the financial statements. They are usually disclosed as part of the report of the approving authority (viz. Board of Directors report).	Contingent assets are notrecognised, but disclosed in the financial statements when an inflow of economic benefits is probable.	Similar to IFRS.
Restructuring cost	Requires recognition based ongeneral recognition criteria forprovisions i.e. when the entity has a present obligation as a result of past event and the liability is considered probable and can be reliably estimated.	Requires provisions on the basis of constructive obligations. A constructive obligation to restructure arises only when an entity has a detailed formal plan for the restructuring and has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.	Similar to IFRS.
Intangible Assets — Source Standard	**AS 26 — Intangible Assets**	**IAS 38 - Intangible Assets**	**Ind AS 38 — Intangible Assets**
Measurement	Intangible Assets are measured only at cost.	Intangible assets can be measured either cost or revalued amounts.	Similar to IFRS.
Useful Life	The useful life may not be indefinite. There is a presumption that the useful life of an intangible asset will not exceed ten years from the date when the asset is available for use.	The Useful life may be finite or indefinite.	Similar to IFRS.
Goodwill	Goodwill arising on amalgamation in the nature of purchase is to be amortised over a period not exceeding five years (as per AS 14).	Not amortised but subject to annual impairment test or more frequently whenever there is an impairment indication.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Regarding prepayments for advertising and promotional activities	Payment for the delivery of goods or rendering of services made in advance are considered as prepayment assets.	Recognition of a prepayment asset for advertising or promotional expenditure would be permitted only up to the point at which the entity has the right to access the goods or up to the receipt of services. Mail order catalogues specifically identified as a form of advertising and promotional activity to be expensed.	Similar to IFRS.
Revenue based amortisation model	Not specifically provided.	IAS 38 provides a rebuttable presumption that revenue is not an appropriate basis for amortisation of an intangible asset. This presumption can be rebutted only in two limited circumstances: (i) the intangible asset is expressed as a measure of revenue; and (ii) revenue and consumption of the intangible asset are highly correlated.	Similar to IFRS. However, a carve-out has been made in Ind AS 101 and Ind AS 38, which will allow entities to continue using the accounting policy adopted for amortisation of intangible assets arising from service concession arrangements related to toll roads recognised in the financial statements for the period ending immediately before the beginning of the first Ind AS reporting period.
Investment Property: Source Standard	**No standard on investment property. Investments covered by AS 13: Accounting for Investments.**	**IAS 40: Investment Property**	**Ind AS 40: Investment Property**
Definition and Scope	AS 13 defines investment property as an investment in land or buildings that are not intended to be occupied substantially for use by, or in the operations of, the investing enterprise,	Investment property is land or building (or part thereof) or both held (whether by owner or by a lessee under a finance lease) to earn rentals or for capital appreciation or both. IAS 40 does not apply to owner- occupied property or property that is being constructed or developed on behalf of third parties or property held for sale in the ordinary course of business, or property that is leased to another entity under a finance lease.	Similar to IFRS provisions.

TOPIC	AS	IFRS	IND AS
Measurement	Classified as long-term investments and measured at cost less impairment.	Investment property is measured initially at cost. Transaction costs are included in the initial measurement. Investment properties can subsequently be measured using the cost or the fair value model, with changes in fair value recognised in profit or loss.	Investment properties are measured using the cost model. Fair value model is not permitted. Detailed disclosures pertaining to fair value have to be given.
Agriculture - Source Standard	**There is no equivalent standard.**	**IAS 41 — Agriculture**	**Ind AS 41 — Agriculture**
Scope	N.A.	Applies to biological assets (with the exception of bearer plants that are used in the production or supply of agricultural produce and which will not be sold as agriculture produce and government grants related to these biological assets). Does not apply to land related to agricultural activity, intangible assets related to agricultural activity, and government grants related to bearer plants. However, it does apply to produce growing on bearer plants.	Similar to IFRS.
Measurement	N.A.	All biological assets are measured at fair value less costs to sell, unless fair value cannot be reliably measured. Any change in the fair value of biological assets during a period is reported in profit or loss. Exception to fair value model: If there is no active market at the time of recognition in the financial statements, and no other reliable measurement method, then the cost model is used for the specific biological asset only. The biological asset is then measured at depreciated cost less any accumulated impairment losses. However, fair value measurement stops at harvest.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
		Agricultural produce is measured at fair value less estimated costs to sell at the point of harvest. Because harvested produce is a marketable commodity, there is no 'measurement reliability exception for produce.	
First Time Adoption — Source Standard	**There is no equivalent standard under Indian GAAP. A first time preparer will have to comply with the measurement and disclosure requirements of all the Indian standards that are applicable to the enterprise.**	**IFRS 1 — First Time Adoption of International Financial Reporting Standards**	**Ind AS 101 — First Time Adoption of Indian Accounting Standards**
Date of transition	N.A.	The date of transition is the beginning of the earliest period for which an entity presents full comparative information under IFRS in its first IFRS financial statements. Entities are required to present at least one year comparatives.	Similar to IFRS.
Choice of previous GAAP	N.A.	Previous GAAP is the basis of accounting that a first-time adopter used immediately before adopting IFRS.	Previous GAAP is the basis of accounting that a first-time adopter used for its reporting requirement in India immediately before adopting Ind AS
Exemption to consider previous GAAP carrying value of property, plant and equipment as deemed cost	N.A.	There is no exemption permitting previous GAAP carrying value of property, plant and equipment as deemed cost under IFRS (except for certain specific oil and gas assets, and rate regulated assets).	Entities have an option to use previous GAAP carrying values of property, plant anti equipment as on the date of transition as deemed cost under md AS. A similar exemption is available for intangible assets and investment properties.
Regarding Non-current assets held for sale and discontinued operations	N.A.	No exemption in respect of non-current assets held for sale and discontinued operations.	Provides transitional relief while applying Ind AS 105 — Non-current Assets Held for Sale and Discontinued Operations. Under Ind AS 101, an entity may use the transitional date circumstances to measure such assets or operations at the lower of carrying value and fair value less cost to sell.

TOPIC	AS	IFRS	IND AS
Regarding Lease classification	N.A.	No exemption.	Ind AS 101 provides transitional relief to use transition date facts and circumstances for lease arrangements which includes both land and building elements to assess the classification of each element as finance or an operating lease. Also, if there is any land lease newly classified as finance lease then the first time adopter may recognise assets and liability at fair value on the transition date: any difference between those fair values is recognised in retained earnings.
Regarding Business combinations	N.A.	A first time adopter can claim exemption by not applying IFRS 3 retrospectively to past business combinations. If such exemption is availed, any intangible asset recognised under previous GAAP that does not qualify for recognition under AS 38 — Intangible Assets, should be reclassified as part of goodwill.	Similar to IFRS, except that Ind AS provides that such amounts could be adjusted against capital reserve to the extent such adjustment amount does not exceed the balance available in capital reserve.
Treatment of exchange differences	N.A.	No additional exemption is provided.	An additional exemption has been provided with regard to exchange differences arising from translation of long-term foreign currency monetary items. An entity may continue the policy adopted for accounting for exchange differences arising from translation of such long-term foreign currency monetary items recognised in the financial statements for the period ending immediately before beginning of the first Ind AS financial reporting period as per the previous GAAP.

TOPIC	AS	IFRS	IND AS
Amortisation of intangible assets arising from service concession arrangements	N.A.	No exemption is provided.	An exemption has been provided which will allow entities to continue using the accounting policy adopted for amortisation of intangible assets arising from service concession arrangements related to toll roads recognised in the financial statements for the period ending immediately before the beginning of the first Ind AS reporting period.
Share-based Payment - Source Standard	**There is no equivalent standard. However the ICA! has issued a Guidance Note on Accounting for Employee Share-based Payments. This guidance note deals only with employee share-based payments.** **The SEBI has also issued the SEBI (Share Based Employee Benefits) Regulations, 2014 which requires that the Guidance Note on Accounting for Employee Share-based Payments or Accounting Standards as may be prescribed by the ICAI, including the disclosure requirements prescribed therein, should be followed while accounting for share based schemes.**	**IFRS 2 — Share-based Payment (covers share-based payments both for employees and non-employees and transactions involving receipt of goods and services)**	**Ind AS 102 — Share-based Payment (covers share-based payments both for employees and non-employees and transactions involving receipt of goods and services)**
Recognition	Similar to IFRS.	Recognise as an expense over the vesting period. Goods and services in a share- based payment transaction are recognised when goods are received or as services are rendered. A corresponding increase in equity is recognised if goods and services were received in an equity-settled share-based payment transaction or a liability if these were received in a cash-settled share-based payment transaction.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Measurement	The guidance note permits the use of either the intrinsic value method or the fair value method for determining the costs of benefits arising from employee share-based compensation plans. The guidance note recommends the use of the fair value method, Under the intrinsic value method, the cost is the difference between the market price of the underlying share on the grant date and the exercise price of the option. The fair value method is based on the fair value of the option at the date of grant. The fair value is estimated using an option-pricing model (for example, the Black-Scholes or a binomial model) that takes into account as of the grant date the exercise price and expected life of the option, the current price in the market of the underlying stock and its expected volatility, expected dividends on the stock, and the risk-free interest rate for the expected term of the option. Where an enterprise uses the intrinsic value method, it should also disclose the impact on the net results and EPS — both basic and diluted — for the accounting period, had the fair value method been used.	For equity settled share-based transactions with non-employees, goods and services received and the corresponding increase in equity is measured at the fair value of the goods and services received. If the fair value of the goods and services cannot be estimated reliably, then the value is measured with reference to the fair value of the equity instruments granted, measured at the date the entity obtains the goods or the counterparty renders the service. In case of equity settled transactions with employees and others providing similar services, grant date fair value of the equity instrument should be used. Different valuation techniques may be applied.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Group entities	The Guidance Note on Accounting for Employee Share-based Payments applies to transfer of shares or stock options of the parent of an entity or shares or stock options of another entity in the same group to the employees of the entity.	IFRS 2 provides guidance on accounting for share-based payment transactions among group entities.	Similar to IFRS.
Business Combinations - Source Standard	**AS 14— Accounting for Amalgamations**	**IFRS 3 - Business Combinations**	**Ind AS 103 — Business Combinations**
Scope	There is no comprehensive standard dealing with all business combinations. Guidance for amalgamations is contained in AS 14. AS 21 deals with investments in subsidiaries and AS 10 deals with a demerged unit acquired in a slump sale.	Applies to a transaction or other event in which an acquirer obtains control of one or more businesses, IFRS 3 does not apply to: i) The formation of a joint arrangement in the financial statements of the joint arrangement itself ii) Combinations of entities or business under common control iii) Acquisition of an asset or group of assets that do not constitute a business.	Similar to FRS except that Ind AS 103 contains guidance on common control transactions.
Acquisition date	With respect to legal mergers under AS 14 involving merger of one or more entities into another entity, the appointed date may be defined under the Scheme of Amalgamation, which can be any date as determined by the Transferor/ Transferee Company. The effective date as per scheme of amalgamation will be the date of filing of Court order sanctioning the scheme with statutory authorities. In case the appointed date is prior to the effective date, the amalgamation is accounted on the effective date with effect from the appointed date as per scheme of amalgamation.	The date on which the acquirer obtains control of the acquired entity is the acquisition date.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Pooling of interests and Purchase method	Amalgamations in the nature of purchase are accounted for by recording the identifiable assets and liabilities of the acquiree either at the fair values or at book values, Amalgamations in the nature of merger are accounted under the pooling of interests method. Under the pooling of interests method, the assets, liabilities and reserves of the transferor company are recorded by the transferee company at their existing carrying amounts (after making the adjustments required for conflicting accounting policies). Identifiable assets and liabilities of subsidiaries acquired by purchase of shares which are not amalgamations are recorded in the consolidated financial statements at the carrying amounts stated in the acquired subsidiary's financial statements on the date of acquisition.	All business combinations, other than those between entities under common control, are accounted for using the purchase method. An acquirer is identified for all business combinations, which is the entity that obtains control of the other combining entity. Pooling of interests method to record business combinations within the scope of IFRS 3 is prohibited.	Common control transactions are included in the scope; and additional guidance is provided. The additional guidance provides that business combination transactions between entities under common control should be accounted for using the 'pooling of interests' method.

TOPIC	AS	IFRS	IND AS
Combination of entities under common control	N.A.	Does not apply to combination of entities or businesses under common control.	Ind AS 103 includes accounting for combination of entities or businesses under common control. Common control business combinations will include transactions, such as transfer of subsidiaries or businesses, between entities within a group. Businesses combinations involving entities or businesses under common control should be accounted for using the pooling of interests method. This involves the following: • The assets and liabilities of the combining entities are reflected at their carrying amounts. • No adjustments are made to reflect fair values, or recognise any new assets or liabilities. The only adjustments that are made are to harmonise accounting policies. • The financial information in the financial statements in respect of prior periods should be restated as if the business combination had occurred from the beginning of the preceding period in the financial statements, irrespective of the actual date of the combination. However, if business combination had occurred after that date, the prior period information should be restated only from that date.

TOPIC	AS	IFRS	IND AS
			• The balance of the retained earnings appearing in the financial statements of the transferor is aggregated with the corresponding balance appearing in the financial statements of the transferee. Alternatively, it is transferred to General Reserve, if any. • The identity of the reserves should be preserved and should appear in the financial statements of the transferee in the same form in which they appeared in the financial statements of the transferor. • Difference, if any, between the amount recorded as share capital issued plus any additional consideration in the form of cash or other assets and the amount of share capital of the transferor should be transferred to capital reserve and should be presented separately from other capital reserves with disclosure of its nature and purpose in the notes.
Non-controlling interest	At the time of acquisition, minority interests in the net assets consist of the amount of equity attributable to minorities at the date on which investment in the acquiree is made. This is determined on the basis of information contained in the financial statements of the acquiree as on the date of investment.	At the date of acquisition, an entity may elect to measure, on a transaction by transaction basis, the non-controlling interest at (a) fair value or (b) the non-controlling interest's proportionate share of the fair value of the identifiable net assets of the acquiree.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Measurement of goodwill	Any excess of the amount of the consideration over the value of the net assets of the transferor company acquired by the transferee company is recognised in the transferee company's financial statements as goodwill arising on amalgamation. If the amount of the consideration is lower than the value of the net assets acquired, the difference is recognised as capital reserve, a component of shareholders' equity.	Goodwill is measured as the difference between: • the aggregate of a) the acquisition-date fair value of the consideration transferred; b) the amount of any non-controlling interest and c) in a business combination achieved in stages, the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree; and • the net of the acquisition-date fair values of the identifiable assets acquired and the liabilities assumed. If the above difference is negative, the resulting gain is recognised as a bargain purchase in profit or loss.	Similar to IFRS. However, any gain on bargain purchase is recognised in other comprehensive income and accumulated in equity as capital reserve. If there is no clear evidence of the underlying reason for classification of the business combination as a bargain purchase, the resulting gain is recognised directly in equity as capital reserve.
Writing-off goodwill	Goodwill arising on amalgamation in the nature of purchase is amortised over a period not exceeding five years.	Goodwill is not amortised but tested for impairment on an annual basis or more frequently if events or changes in circumstances indicate impairment.	Similar to IFRS.
Business combinations achieved in stages	Covered in AS 21. If two or more investments are made over a period of time, the equity of the subsidiary at the date of investment is generally determined on a step-by-step basis; however, if small investments are made over a period of time and then an investment is made that results in control, the date of the latest investment, as a practicable measure, may be considered as the date of investment.	For business combinations achieved in stages, if the acquirer increases an existing equity interest so as to achieve control of the acquiree, the previously-held equity interest is remeasured at acquisition-date fair value and any resulting gain or loss is recognised in profit or loss.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Contingent consideration	Where the scheme of amalgamation provides for an adjustment to the consideration contingent on one or more future events, the amount of the additional payment should be included in the consideration if payment is probable and a reasonable estimate of the amount can be made. In all other cases, the adjustment should be recognised as soon as the amount is determinable.	Consideration for the acquisition includes the acquisition-date fair value of contingent consideration. The obligation to pay contingent consideration should be classified as a liability or as equity, as appropriate. The right to return of previously transferred consideration should be classified as an asset, if specified conditions are met. Changes in contingent consideration which are measurement period adjustments are recognised as an adjustment against the original accounting for the acquisition (and so may impact goodwill or bargain purchase gain). Contingent consideration classified as equity is not subsequently remeasured and its subsequent settlement is accounted within equity. Contingent consideration that is classified as an asset or a liability (whether financial asset! financial liability or non-financial asset/non-financial liability) should be measured at fair value at each reporting date with changes in fair value recognised in profit or loss. Changes to contingent consideration resulting from events after the acquisition date are recognised in profit or loss.	Similar to IFRS.
Acquisition related costs	Not specifically provided.	Acquisition related costs (viz. finder's fee, due diligence costs, etc.) are accounted for as expenses in the period in which the costs are incurred and the services are received.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Initial accounting for a business combination determined provisionally	Not specifically provided.	If the initial accounting for a business combination can be determined only provisionally by the end of the first reporting period, the combination is accounted for using provisional values. Adjustments to provisional values relating to new information about facts and circumstances that existed at the acquisition date are permitted within one year of the acquisition date. Such adjustments are made retrospectively as if those adjustments had been made at the acquisition date. No adjustments can be made after one year except to correct an error in accordance with IAS 8.	Similar to IFRS.
Insurance Contracts — Source Standard	**No equivalent standard.**	**IFRS 4— Insurance Contracts.** **The IASB is developing a comprehensive IFRS for insurance contracts to replace IFRS 4— insurance Contracts,**	**Ind AS 104 — Insurance Contracts**
Insurance Contracts	No standard existed.	Applicable to insurance and reinsurance contracts and to discretionary participation features in insurance contracts. The insurer is required at the end of each reporting period to make a liability adequacy test to assess whether its recognised insurance liabilities are adequate. If test shows carrying amount of its liabilities are inadequate, the deficiency is recognised in profit or loss. Reinsurance assets are tested for impairment. Insurance liabilities may not be offset against related reinsurance assets.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Non-current Assets Held for Sale and Discontinued Operations - Source Standard	**AS 24 — Discontinuing Operations** **AS 10 — Accounting for Fixed Assets**	**IFRS 5 Non-current Assets Held for Sale and Discontinued Operations** **IFRIC 17 — Distributions of Non-cash Assets to Owners**	**Ind AS 105 — Non-current Assets field for Sale and Discontinued Operations** **Ind AS 10 Appendix A— Distributions of Non-cash Assets to Owners**
Recognition, measurement and presentation	No specific standard exists. **NB**: AS 10 deals with assets held for disposal. Items of fixed assets that have been retired from active use and are held for disposal are stated at the lower of their net book value and net realisable value and are shown separately in the financial statements. Any expected loss is recognised immediately in the statement of profit and loss.	Non-current assets to be disposed of are classified as held for sale when the asset is available for immediate sale and the sale is highly probable. Depreciation ceases on the date when the assets (individually or as part of a disposal group) are classified as held for sale. Non-current assets classified as held for sale are measured at the lower of its carrying value and fair value less costs to sell. Non-current assets classified as held for sale, and the assets and liabilities in a disposal group classified as held for sale, are presented separately in the statement of financial position.	Similar to IFRS.
Non-cash assets held for distribution to owners	AS 24 has no specific guidance related to non-cash assets held for distribution to owners,	Non-cash assets are to be classified as 'held for distribution to owners' when the transaction is highly probable, taking into account probability of shareholders' approval, if required in the jurisdiction. Such assets are measured at the lower of carrying amount and fair value less costs to distribute.	Similar to IFRS.
Classification	An operation is classified as discontinuing at the earlier of (a) binding sale agreement for sale of the operation, and (b) on approval by the board of directors of a detailed formal plan and announcement of the plan.	An operation is classified as discontinued when it has either been disposed of or is classified as held for sale.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Distributions of Non-cash Assets to Owners	Not specifically provided.	An entity should measure the dividend payable at the fair value of the net assets to be distributed. The liability should be remeasured at each reporting date and at settlement, with changes recognized directly in equity. The difference between the dividend paid and the carrying amount of the net assets distributed should be recognized in profit or loss and should be disclosed separately. Additional disclosures should be made, if the net assets being held for distribution to owners meet the definition of a discontinued operation. If shareholders have a choice of receiving either a non-cash asset or a cash alternative, the liability should be measured considering both the fair value of each alternative and management's assessment of the probabilities of each outcome. IFRIC 17 applies to pro rata distributions of non-cash assets (all owners are treated equally) but does not apply to common control transactions.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Presentation of Discontinued Operations	Under AS 24, the profit and loss before tax is presented as a single section which includes continuing and discontinuing operation. The presentation provides separate disclosure for continuing operation before tax, income tax related to continuing operations, profit or loss from continuing operations after tax. A similar disclosure is made for discontinuing operations. The requirement under Schedule III to the Companies Act, 2013 is different, with the statement of profit and loss being effectively divided into two sections — continuing operations and discontinuing operations. The following details are required to be presented on the face of the statement of profit and loss as per Schedule III for discontinuing operations: • Profit / (loss) from discontinuing operations • Tax expense of discontinuing operations • Profit / (loss) from discontinuing operations (after tax)	The statement of comprehensive income is effectively divided into two sections — continuing operations and discontinued operations, with the entity presenting as a single amount in the statement of comprehensive income, the sum of the post- tax profit or loss from discontinued operations for the period and the post-tax gain or loss arising on the disposal of discontinued operations (or on the reclassification of the assets and liabilities of discontinued operations as held for sale). Detailed disclosure of revenue, expenses, pre-tax profit or loss and related income taxes is required either in the notes or in the statement of comprehensive income in a section distinct from continuing operations.	Similar to IFRS.
Exploration for and Evaluation of Mineral Resources — Source Standard	**No equivalent standard. However, there is a Guidance Note on Accounting for Oil and Gas Producing Activities**	**IFRS 6 Exploration for and Evaluation of Mineral Resources**	**Ind AS 106— Exploration for and Evaluation of Mineral Resources**

TOPIC	AS	IFRS	IND AS
Measurement	As per the guidance note, there are two alternative methods for accounting for acquisition, exploration and development costs, viz, the *Successful Efforts Method* or the *Full Cost Method*. The guidance note recommends the Successful Efforts Method, though full cost method is also permitted.	Exploration and evaluation assets are measured at cost or revaluation *Less* accumulated amortization and impairment loss. An entity determines the policy specifying which expenditure is recognised as exploration and evaluation assets.	Similar to IFRS.
Impairment	AS 28 *Impairment of Assets* is applicable irrespective of the method of accounting used,	IAS 36 *Impairment of Assets* is applicable. However an entity should determine an accounting policy for allocating exploration and evaluation assets to cash-generating units or groups of cash-generating units for the purpose of assessing such assets for impairment. Each cash-generating unit or group of units to which an exploration and evaluation asset is allocated should not be larger than an operating segment determined in accordance with IFRS 8 — Operating Segments.	Similar to IFRS.
Disclosures	Not specifically provided.	The standard requires disclosure of information that identifies and explains the amounts recognised in the financial statements arising from the exploration for and evaluation of mineral resources.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Financial Instruments: Disclosures - Source Standard	**AS 32 Financial Instruments: Disclosures Note that this standard has not been notified under the Companies (Accounting Standards) Rules, 2006. For the current status an the applicability of AS 32, see the caption 'Financial Instruments — primary literature. Since the above mentioned standard is not yet mandatory, the differences discussed below are based on the existing Indian Standards and generally accepted accounting practices.**	**IFRS 7 — Financial Instruments:**	**Ind AS 107 Financial Instruments: Disclosures**
Disclosures	Currently there are no detailed disclosure requirements for financial instruments. However, the ICAI has issued an Announcement in December 2005 requiring the following disclosures to be made in respect of derivative instruments in the financial statements: • Category-wise quantitative data about derivative instruments that are outstanding at the balance sheet date; • The purpose, viz., hedging or speculation, for which such derivative instruments have been acquired; and • The foreign currency exposures that are not hedged by a derivative instrument or otherwise.	Requires disclosure of information about the significance of financial instruments on financial information and performance. These include: Disclosure relating to financial assets and financial liabilities by category; special disclosures when the fair value option is used. Fair value disclosures must be made separately for each class of financial assets and financial liabilities in way that permits it to be compared with its carrying amount. Requires enhanced disclosures when an asset is transferred but not derecognised and requires some disclosures for assets that are derecognised but the entity continues to have a continuing exposure to the assets after the derecognition.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
		Requires disclosures on offsetting of financial assets and liabilities to evaluate the effect or potential effect of netting arrangements on the entity's financial position. Requires disclosure of information about the nature and extent of risks arising from financial instruments: • qualitative disclosures about exposures to each type of risk and • how those risks are managed; and quantitative disclosures about exposures to each type of risk, separately for credit risk, liquidity risk and market risk (including sensitivity analysis). Requires disclosures relating to performance in the period, including information about recognised income, expenses, gains and losses, interest income and expenses, fee income and impairment losses. Requires disclosures on reclassifications, allowance of credit losses, defaults and breaches, pledges of assets, collaterals and information on hedge accounting, including risk management strategy.	

TOPIC	AS	IFRS	IND AS
Operating Segments - Source Standard	**AS 17 — Segment Reporting**	**IFRS 8— Operating Segments**	**Ind AS 108 — Operating Segments**
Scope	The applicability of the standard is not linked to the listing status of an entity.	IFRS 8 is applicable to the separate and consolidated financial statements of an entity/ group with a parent: • Whose debt or equity instruments are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or • That files, or is in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market,	Ind AS 108 is applicable to companies to which Ind ASs notified under the Companies Act apply.
Determination of segments	AS 17 requires an enterprise to identify two sets of segments viz. Business and Geographical, using a risks and rewards approach.	Operating segments are identified based on the financial information that is regularly reviewed by the chief operating decision maker in deciding how to allocate resources and in assessing performance.	Similar to IFRS.
Measurement	Segment information is prepared in conformity with the accounting policies adopted for preparing and presenting the financial statements of the enterprise as a whole. Segment revenue, segment expense, segment result, segment asset and segment liability have been defined.	Segment profit or loss is reported on the same measurement basis as that used by the chief operating decision maker. There is no definition of segment revenue, segment expense, segment result, and segment asset or segment liability nor does it require segment information to be prepared in conformity with the accounting policies adopted for the entity's financial statement.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Reconciliation	A reconciliation is presented between the information disclosed for reportable segments and the aggregated information in the enterprise's financial statements.	Requires reconciliation of segment performance measures with the corresponding amounts reported in the financial statements. A reconciliation of the total of the segments' assets and total of the segments' liabilities to the entity's assets and the entity's liabilities respectively should only be provided if the segment assets and segment liabilities are regularly provided to the chief operating decision-maker.	Similar to IFRS.
Aggregation criteria	Not specifically provided.	Two or more operating segments may be aggregated into a single operating segment if the aggregation is consistent with the principles laid down in the standard. The judgements made in applying the aggregation criteria for operating segments need to be disclosed.	Similar to IFRS.
Entity wide disclosures	Disclosures are required based on the classification of segments as primary or secondary. The levels of disclosure requirements for secondary reporting format are less detailed than those required for primary, reporting formats.	Requires disclosure of a) external revenues from each product or service; b) revenues from customers in the country of domicile and from foreign countries; c) geographical information on non-current assets located in the country of domicile, and foreign countries. Information on major customers including total revenues from each major customer is disclosed if revenue from each customer is 1 0% or more of total segment revenues. The entity need not disclose the identity of such customers.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Financial Instruments - Source Standard	**AS 13 — Accounting for Investments** **AS 30 — Financial Instruments: Recognition and Measurement.** **Though AS 30 (not yet notified) was to become mandatory for certain enterprises for accounting periods commencing on or after 1 April 2011 with earlier adoption permitted, the ICAI has reconsidered the status of AS 30 and has issued a clarification on the applicability of the same. As per the clarification, to the extent of accounting treatments covered by any of the existing notified accounting standards (for e.g. AS 11, AS 13, etc.) or in cases where relevant regulatory authority has prescribed specific regulatory requirements, the existing accounting standards/ prescribed regulatory requirements would continue to prevail aver AS 30. Subject to the above, in other cases, preparers of financial statements are encouraged to follow the principles enunciated in the accounting treatments contained in AS 30.** **This announcement is applicable to accounting periods commencing on or after 1 April 2011 and is also valid for AS 31 and AS 32.** **The ICAI has also issued an exposure draft of Guidance Note on Accounting for Derivative Contracts, which will supersede AS 30 to the extent of guidance covered for accounting for derivatives within the scope of the Guidance Note. Pending finalisation, the discussion below does not include contents of the aforesaid exposure draft of the Guidance Note.**	**IFRS 9 (2014) Financial Instruments issued in July 2014, is IASS's replacement of IAS 39 Financial Instruments: Recognition and Measurement. The version of IFRS 9 issued in July 2014 supersedes all previous versions and is mandatory for periods beginning on or after 1 January 2018 with early adoption permitted.** **IFRIC 16— Hedges of a Net Investment in a Foreign Operation.** **IFRIC 19— Extinguishing Financial Liabilities with Equity Instruments**	**Ind AS 109— Financial Instruments** **Ind AS 109— Appendix C — Hedges of a Net Investment in a Foreign Operation** **Ind AS 109—Appendix 0— Extinguishing Financial** **Liabilities with Equity** **Instruments** **Ind AS 109 will be applicable as at the date of transition to md AS.**

TOPIC	AS	IFRS	IND AS
General recognition principle	There is no definition of financial instrument.	An entity should recognise a financial asset or a financial liability in its statement of financial position when, and only when, the entity becomes party to the contractual provisions of the instrument. A financial instrument is a contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.	Similar to IFRS.
Initial measurement	No specific guidance.	All financial instruments are initially measured at fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. Trade receivables that do not have a significant financing component should initially be measured at transaction price as defined in IFRS 15.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Classification and subsequent measurement of financial assets	Per AS 13, investments are classified as long-term or current. A current investment is an investment that is by its nature readily realisable and is intended to be held for not more than one year from the date on which such investment is made. A long-term investment is an investment other than a current investment. Accordingly, the assessment of whether an investment is long-term has to be made on the date the investment is made. Long-term investments are carried at cost less provision for diminution in value, which is other than temporary. Current investments are carried at lower of cost and fair value. Loans are measured at cost less valuation allowance.	All financial assets are classified as measured at amortised cost or measured at fair value. Where assets are measured at fair value, gains and losses are either recognised entirely in profit or loss, (FVTPL), or recognised in other comprehensive income (FVTOCI). A debt instrument that is held within a business model to collect contractual cash flows and the contractual terms of which give rise on specified dates, to cash flows that are solely payments of principal and interest on the principal amount outstanding must be measured at amortised cost. However if the debt instrument is held within a business model whose objective is achieved both by collecting contractual cash flows and selling financial assets, it must be measured at FVTOCI.	Similar to IFRS.
Classification and subsequent measurement of financial assets (continued)		IFRS 9 provides an option to irrevocably designate, at initial recognition, financial assets as measured at FVTPL if doing so eliminates an accounting mismatch. Equity instruments should be classified as FVTPL. IFRS 9 provides an option to irrevocably designate, at initial recognition, equity instruments which are neither held for trading nor are contingent consideration arising from business combination, to measure subsequent changes in fair value in other comprehensive income. The dividend from such investments is recognised in profit or loss.	

TOPIC	AS	IFRS	IND AS
Classification and subsequent measurement of financial liabilities	No specific guidance.	There are two measurement categories for financial liabilities — FVTPL and amortised cost. Financial liabilities held for trading are subsequently measured at FVTPL and all other financial liabilities are measured at amortised cost using the effective interest method. An entity may, at initial recognition, irrevocably designate a financial liability as measured at FVTPL if doing so eliminates an accounting mismatch, or a group of financial liabilities or financial assets and financial liabilities is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy.	Similar to IFRS.
Changes in fair value of financial liabilities due to changes in credit risk	No specific guidance.	Gains and losses on financial liabilities designated as at FVTPL are required to be split into the amount of change in fair value attributable to changes in credit risk of the liability, presented in other comprehensive income, and the remaining amount presented in profit or loss.	Similar to IFRS.
Changes in fair value of financial liabilities due to changes in credit risk (continued)		Amounts presented in other comprehensive income should not be subsequently transferred to profit or loss, the entity may only transfer the cumulative gain or loss within equity.	

TOPIC	AS	IFRS	IND AS
Reclassification	Investments can be reclassified from long-term to current; such transfers are made at the lower of cost and carrying value at the date of transfer. In case of current Investments reclassified as long-term, the transfers are made at lower of cost and fair value as at the date of transfer.	Reclassification is required when an entity changes its business model for managing financial assets. An entity should not reclassify any financial liability. IFRS 9 does not allow reclassification: • For equity investments measured at FVTOCI, or • Where the fair value option has been exercised in any circumstance for a financial assets or financial liability.	Similar to IFRS.
Derecognition of financial assets and securitization	There is no current equivalent standard.	Derecognition of financial assets is permitted only upon: • expiry of the contractual rights to the cash flows from the financial assets; • transfer the financial assets. An asset is transferred if either the entity has transferred the contractual rights to receive the cash flows, or the entity has retained the contractual rights to receive the cash flows from the asset, but has assumed a contractual obligation to pass those cash flows under an arrangement that meets certain specified conditions.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Derecognition of financial assets and securitization (continued)		Once an entity has determined that the asset has been transferred, it would need to evaluate the extent to which it retains the risks and rewards of ownership of the financial asset. If substantially all the risks and rewards have been retained, derecognition of the asset is precluded. If risks and rewards have neither been substantially transferred nor retained, an assessment is made whether control has been retained by the transferor. If the entity does not control the asset then derecognition is appropriate; however if the entity has retained control of the asset, then the assets continue to be recognised to the extent of continuing involvement.	
Derecognition of financial liabilities	There is no current equivalent standard,	A financial liability should be removed from the balance sheet when it is extinguished, that is when the obligation specified in the contract is discharged or cancelled or has expired.	Similar to IFRS.
Financial Instruments modification	There is no current equivalent standard	When contractual cash flows of financial assets are renegotiated! modified, and such renegotiation / modification does not result in derecognition, the gross carrying amount of the financial asset is recalculated as the present value of the renegotiated or modified contractual cash flows discounted at the financial asset's original effective interest rate and a modification gain or loss is recognised in profit or loss. Any costs or fees incurred are adjusted to the carrying amount of the modified financial asset and are amortised over the remaining term of the modified financial asset.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
		In case of financial liabilities, a substantial modification of the terms should be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The difference between the carrying amount of a financial liability extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, should be recognised in profit or loss.	
Impairment of financial assets	An enterprise should assess the provision for doubtful debts at each period end which, in practice, is based on relevant information such as • past experience, • actual financial position and • cash flows of the debtors. Different methods are used for making provisions for bad debts, including: • the ageing analysis, • an individual assessment of recoverability. Impairment losses recognised in profit or loss for equity investments are reversed through profit or loss (as per AS 13). For banks and financial service entities, the Reserve Bank of India has laid down specific provisioning norms based on the age of the outstanding.	The impairment model in IFRS 9 is based on expected credit losses and it applies equally to debt instruments measured at amortised cost or FVTOCI (the loss allowance is recognised in other comprehensive income and not reduced from the carrying amount of the financial asset), lease receivables, contract assets within the scope of IFRS 15 and certain written loan commitments and financial guarantee contracts. Expected credit losses (with the exception of purchased or original credit-impaired financial assets) are required to be measured through a loss allowance at an amount equal to: i) the 12 month expected credit losses or ii) lifetime expected credit losses if credit risk has increased significantly since initial recognition of the financial instrument. With respect to trade receivables or contract assets within the scope of IFRS 15, loss allowance is measured at lifetime expected credit losses.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
		For lease receivables within the scope of IAS 17, an entity can elect to always measure loss allowances at an amount equal to lifetime expected credit losses. Interest revenue is calculated by applying the effective interest rate to the amortised cost (which is the gross carrying amount minus loss allowance) for credit — impaired financial assets while for all other instruments, it is calculated based on the gross carrying amount.	
derivatives and embedded derivative	Currently there is no equivalent standard on derivatives except for certain forward exchange contracts within the scope of AS 11. For entities not following AS 30, an ICAI announcement requires such entities to recognise losses in respect of all outstanding derivative contracts not covered by AS 11 by marking them to market as at the balance sheet date. Under AS 30, embedded derivatives would be separately accounted for at FVTPL if it is not closely related to the host financial asset.	All derivatives are measured at fair value. An embedded derivative is a component of a hybrid contract that also includes a non-derivative host, with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative. A derivative that is attached to a financial instrument but is contractually transferable independently of that instrument, or has a different counterparty, is not an embedded derivative, but a separate financial instrument. If the host is an asset within the scope of IFRS 9, the embedded derivative is not separated from the host and classification and measurement principles as applicable to the financial asset is applied to the entire hybrid contract.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
hedged accounting	Currently, there is no notified Accounting Standard on hedge accounting. Based on an ICAI clarification, to the extent there are no accounting treatments covered by any of the existing notified accounting standards, entities are encouraged to follow the principles enunciated in the accounting treatments contained in AS 30: Hedge accounting principles included in AS 30 are similar to IAS 39 principles.	Application of hedge accounting is a choice. If certain eligibility and qualification criteria are met, hedge accounting allows an entity to reflect risk management activities in the financial statements by matching gains or losses on financial hedging instruments with losses or gains on the risk exposures they hedge.	Similar to IFRS.
designation of hedging instruments	AS 30 permits entities to designate derivative instruments (or portions thereof) as hedging instruments, except for certain written options. In addition, exclusively for hedges of foreign currency risk, AS 30 permits entities to designate non-derivative financial instruments as hedging instruments.	Under IFRS 9, a financial instrument's eligibility as a hedging instrument depends on whether the financial instrument is measured at FVTPL, not on whether it is a derivative instrument. Therefore, the IFRS 9 hedge accounting model permits entities to designate a derivative instrument (except for certain written options), as well as a non-derivative financial instrument that is measured at FVTPL, as a hedging instrument for all types of risks, not just foreign-currency risk.	Similar to IFRS.
qualifying hedged items	AS 30 permits entities to designate recognised assets or liabilities, firm commitments, highly probable forecast transactions, and net investments in foreign operations as hedged items. In addition, for financial assets and financial liabilities, entities may designate certain risk components of the asset or liability (e.g. interest-rate risk, foreign-currency risk) as the hedged item, provided that the risk is separately identifiable and reliably measurable. However, for non-financial assets and non-financial liabilities, AS 30 prohibits the designation of risk components (other than foreign- currency risk).	IFRS 9 hedge accounting model permits entities to also designate risk components of non-financial assets and liabilities as hedged items as long as certain criteria are met (e.g. the risk component is separately identifiable and can be reliably measured). IFRS 9 also expands the list of eligible hedged items by allowing entities to designate as a hedged item an aggregated exposure (i.e. the combination of an eligible hedged item and a derivative instrument) as well as certain group and net exposures (e.g. a net interest rate exposure), which were generally not eligible as hedged items under IAS 39.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
hedge accounting — accounting for options, forwards, and foreign currency derivatives	Under AS 30, an entity can exclude the time value of an option contract and the forward element of a forward contract when designating such contracts as hedging instruments. AS 30 requires that changes in the excluded components (i.e. the time value component of the option and the forward element of the forward) always be recognised in profit or loss.	Under the IFRS 9 hedge accounting model, the appropriate accounting for the time value component of an option that has been excluded from the designated hedging relationship depends on whether the hedged item is transaction-based (e.g. a hedge of a forecast transaction) or time-period-based (e.g. a hedge of changes in the fair value of a recognised asset, such as inventory, over a period). For hedges of transaction-based items, the time value of the option contract, to the extent that it is related to the hedged item, would initially be deferred in CCI. Subsequently, the amount deferred in accumulated other comprehensive income (AOCI) would be 1) included in the initial cost or carrying amount of a recognised nonfinancial asset or nonfinancial liability arising from the hedged transaction or 2) reclassified into earnings as the hedged item affects earnings if the hedged transaction does not result in recognition of a nonfinancial asset or liability.	

TOPIC	AS	IFRS	IND AS
		For hedges of time-period-based items, the time value of the option contract is also initially deferred in CCI to the extent that it is related to the hedged item. However, instead of recognising the option cost at the time the hedged item is recognised in the statement of comprehensive income, an entity releases the time value component from AOCI into earnings by using a systematic and rational basis (possibly a straight-line approach) over the period during which the hedging relationship could affect earnings. This approach is consistent with certain constituents' views that the time value of an option is a cost of hedging (i.e. a cost incurred to protect against unfavorable changes).	
hedge accounting forward contracts and foreign currency derivatives	AS 30 requires changes in the fair value of the excluded forward element to be recognised in profit or loss. Entities not applying hedge accounting under AS 30, as per AS 11 premium/discount on a forward exchange contract meant for hedging foreign currency risk of existing monetary items will be recognised in the statement of profit and loss over the life of the forward exchange contract. The foreign exchange gain/loss on the forward exchange contracts as well as on the existing monetary items will be recognised in the statement of profit and loss in the period in which they arise.	Under the IFRS 9 hedge accounting model, an entity may elect to account for the forward element of a forward contract that is excluded from the designated hedging relationship similarly to how the time value component of an option contract that is excluded from a hedging relationship is accounted for (see above). Alternatively, an entity can elect to account for changes in the excluded forward element in profit or loss in a manner consistent with the approach under IAS 39.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
qualifying criteria for applying hedge accounting	To qualify for hedge accounting under AS 30, the hedging instrument must be highly effective at achieving offsetting changes in fair value or cash flows attributable to the hedged risk both prospectively and retrospectively. To be highly effective, the level of offset must be between 80 percent and 125 percent. Entities must perform quantitative effectiveness tests on an ongoing basis to demonstrate that the hedging relationship qualifies for hedge accounting.	In order to qualify for hedge accounting, the hedge relationship must meet the following effectiveness criteria at the beginning of each hedged period: • There is an economic relationship between the hedged item and the hedging instrument • The effect of credit risk [from either the hedged item or hedging instrument] does not dominate the value changes that result from that economic relationship. • The hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the entity actually hedges and the quantity of the hedging instrument that the entity actually uses to hedge that quantity of hedged item [(unless the weightings of the hedged item and hedging instrument would create hedge ineffectiveness that would be inconsistent with the purpose of hedge accounting)]	Similar to IFRS.
qualifying criteria for applying hedge accounting (continued)		The IFRS 9 hedge accounting model requires entities to perform a hedge effectiveness assessment only prospectively. However, entities must still measure and recognise hedge ineffectiveness at the end of each reporting period.	

TOPIC	AS	IFRS	IND AS
Basis adjustments	Under AS 30, if an entity's hedge of a forecast transaction results in the recognition of a non-financial asset or liability, the entity could choose to 1) reclassify the effective portion of the cash flow hedge recorded in an appropriate equity account to profit or loss when the hedged item affects earnings or 2) include the amount recorded in the equity account in the initial cost or carrying amount of the non-financial item.	Under IFRS 9, an entity must remove the amount from CCI and include it in the initial cost or carrying amount of the non-financial item.	Similar to IFRS.
Modifying a hedging relationship	Under AS 30, when an entity changes a hedging relationship, it would generally have to discontinue hedge accounting for the existing hedging relationship and redesignate a new hedging relationship that reflects the desired change.	Under IFRS 9, when an entity's hedging relationship no longer satisfies the hedge ratio criterion but its risk management objective remains the same for that hedging relationship, the entity must adjust the hedge ratio so that it meets the hedging criteria prospectively. Such a "rebalancing" would not trigger discontinuation of the entire hedging relationship.	Similar to IFRS.
Discontinuing a hedging relationship	Under AS 30, a hedging relationship is discontinued when 1) the hedging instrument expires or is sold or terminated, 2) the hedging relationship no longer meets the qualifying criteria, 3) the entity revokes the hedge designation, or (4) the forecast transaction in a cash flow hedge is no longer expected to occur.	An entity discontinues hedge accounting prospectively only when the hedging relationship (or a part of a hedging relationship) ceases to meet the qualifying criteria (after any rebalancing). This includes instances when the hedging instrument expires or is sold, terminated or exercised.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Hedges of a net investment in a foreign operation	No specific guidance.	A parent may designate as a hedged risk, only the foreign exchange differences arising from a difference between its own functional currency and that of its foreign operation. The hedging instrument for the hedge of a net investment in a foreign operation may be held by any entity or entities within the group. On derecognition of a foreign operation, IFRS 9 must be applied to determine the amount that needs to be reclassified to profit or loss from the foreign currency translation reserve in respect of the hedging instrument, while AS 21 must be applied in respect of the hedged item.	Similar to IFRS.
Extinguishing financial liabilities with equity Instruments	No specific guidance.	If a debtor issues equity instruments to a creditor to extinguish all or part of a financial liability, those equity instruments are consideration paid'. This is accounted for as an extinguishment of the financial liability, and accordingly the debtor should derecognise the financial liability fully or partly. The debtor should measure the equity instruments issued to the creditor at fair value, unless fair value is not reliably determinable, in which case the equity instruments issued are measured at the fair value of the liability extinguished. The debtor recognises in profit or loss the difference between the carrying amount of the financial liability (or part) extinguished and the fair value of the equity instruments issued.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Separate and Consolidated Financial Statements - Source Standard	**AS 21 — Consolidated Financial Statements**	**IAS 27 Separate Financial Statements** **IFRS 10 Consolidated Financial Statements** **IFRS 12 Disclosure of Interests in Other Entities**	**Ind AS 27 Separate Financial Statements** **Ind AS 110 — Consolidated Financial Statements** **Ind AS 112— Disclosure of Interests in Other Entities**
Scope	AS 21 does not specify entities that are required to present consolidated financial statements. The accounting standard is required to be followed if consolidated financial statements are presented. The Companies Act 2013 requires a company having one or more subsidiaries, to prepare a consolidated financial statement of the company and of all the subsidiaries in the same form and manner as that of its own. The term 'subsidiary' includes an associate company and joint venture. For financial year ending 31 March 2015, if a company does not have any subsidiaries, but only has associates and/ or joint ventures, then the company would not have to prepare consolidated financial statements in respect of such associates and/or joint ventures. Preparation of consolidated financial statements will not be applicable to an intermediate wholly owned subsidiary, except if its immediate parent is a company incorporated outside India. Further if a company has subsidiary or subsidiaries incorporated outside India only, it need not present consolidated financial statements for the financial year beginning on or after 1 April 2014.	A parent is required to prepare consolidated financial statements in which they consolidate their investments in subsidiaries in accordance with IFRS 10. A subsidiary is an entity that is controlled by another entity (known as the parent). A parent need not prepare consolidated financial statements if it meets all the following conditions: a) it is a wholly-owned subsidiary or a partially-owned subsidiary and all its other owners have not objected to the entity not presenting consolidated financial statements; b) its debt or equity instruments are not traded in a public market c) it did not file, nor is it in the process of filing, its financial statements for the purpose of issuing any class of instruments in a public market; and d) its ultimate or any intermediate parent produces consolidated financial statements that are available for public use and comply with IFRS5	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
	Equity listed companies are required to present consolidated financial statements in addition to separate financial statements of the parent in terms of the Listing Agreement with the Stock Exchanges and the SEBI Guidelines,	The Standard contains an exemption for an entity that meets the definition of investment entity to measure all its subsidiaries at fair value through profit and loss except that a subsidiary that provides services that relate to the investment entity's investment activities should be consolidated.	
investment entity	Not applicable.	A parent should determine whether it is an investment entity. An investment entity is an entity that i) obtains funds from one or more investors for the purpose of providing those investor(s) with investment management services; ii) commits to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and iii) measures and evaluates the performance of substantially all of its investments on a fair value basis.	Similar to IFRS.
investment property measurement by investment entities	No specific guidance.	One of the criteria to qualify as an investment entity is to measure and evaluate the performance of substantially all of its investments on a fair value basis. Accordingly, an investment entity would need to account for any investment property using the fair value model in IAS 40 — Investment Property.	Similar to IFRS, except that since Ind AS 40— Investment Property requires all investment properties to be measured at cost initially and cost less depreciation subsequently, the requirement for investment entities to measure investment property using the fair value model has been deleted.

TOPIC	AS	IFRS	IND AS
Definition of control	Control is: a) the ownership, directly or indirectly through subsidiary(ies), of more than one-half of the voting power of an enterprise; or b) control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise so as to obtain economic benefits from its activities. Therefore a mere ownership of more than 50% of equity shares is sufficient to constitute control under Indian GAAP, whereas this is not necessarily so under IFRS.	Control is based on whether an investor has 1) power over the investee 2) exposure, or rights, to variable return from its involvement with the investee; and 3) the ability to use its power over the investee to affect the amounts of the returns.	Similar to IFRS.
Dual control	In a rare situation, when an enterprise is controlled by two enterprises — one which controls by virtue of ownership of majority of the voting power and the other which controls, by virtue of an agreement or otherwise, the composition of the board of directors, the first mentioned enterprise will be considered as subsidiary of both the controlling enterprises and therefore, both the enterprises will need to consolidate the financial statements of that enterprise.	Only one entity can have control (as distinct from joint control) over another entity. Therefore, when two or more entities each hold significant power, and exposure, or rights to variable returns, certain factors are reassessed to determine which party has control. ERS 10 includes guidance on assessment of control, including protective rights; delegated power; de facto control; and de facto agency arrangements.	Similar to IFRS.
Potential voting rights	Potential voting rights are not considered in assessing control.	Potential voting rights are considered only if the rights are substantive. For a right to be substantive, the holder must have the practical ability to exercise that right.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Exclusion of subsidiaries, associates and joint ventures	Excluded from consolidation, equity accounting or proportionate consolidation if the subsidiary; investment; interest was acquired with intent to dispose of in the near future (which, ordinarily means not more than 12 months, unless a longer period can be justified based on facts and circumstances of the case) or if it operates under severe long-term restrictions which significantly impair its ability to transfer funds to the parent! investor/venturer.	Consolidated financial statements include all subsidiaries and equity-accounted associates and joint ventures. No exemption for 'temporary control', 'different lines of business' or 'subsidiary/ associate/ joint venture that operates under severe long-term funds transfer restrictions'.	Similar to IFRS.
Uniform accounting policies	If not practicable to use uniform accounting policies in the preparation of consolidated financial statements, that fact should be disclosed together with the proportions of the items in the consolidated financial statements to which different accounting policies have been applied.	Consolidated financial statements should be prepared using uniform accounting policies.	Similar to IFRS.
Reporting dates	The difference between the reporting date of the subsidiary and that of the parent should be no more than six months,	The difference between the reporting date of the subsidiary and that of the parent should be no more than three months.	Similar to IFRS.
Non-controlling interests	Minority interests are presented in the consolidated balance sheet separately from liabilities and the equity of the parent's shareholders,	Non-controlling interests are presented in the consolidated statement of financial position within equity, separately from the equity of the owners of the parent.	Similar to IFRS.
Allocation of losses to non-controlling interests	Excess of loss applicable to minority over the minority interest in the equity of the subsidiary and any further losses applicable to minority are adjusted against majority interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses.	Profit or loss and each component of other comprehensive income should be attributable to the owners of the parent and to the non-controlling interests. The total comprehensive income should be attributable to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Disposals	No specific guidance.	If a parent loses control of a Similar subsidiary, the parent: • derecognises the assets and liabilities of the former subsidiary from the consolidated statement of financial position; • recognises any investment retained in the former subsidiary at its fair value when control is lost and subsequently accounts for it and for any amounts owed by or to the former subsidiary in accordance with relevant IFRSs. That fair value is regarded as the fair value on initial recognition of a financial asset in accordance with IFRS 9/IAS 39 or, when appropriate, the cost on initial recognition of an investment in an associate or Joint venture. • recognises the gain or loss associated with the loss of control attributable to the former controlling interest. If a parent loses control of a subsidiary that does not contain a business in a transaction with an associate or a joint venture, gains or losses resulting from those transactions are recognised in the parent's profit or loss only to the extent of the unrelated investors' interests in that associate or joint venture. (Added by Sale or Contribution of Assets between an Investor and its Associate or Joint Venture amendments, effective from 1 January 2016).	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Separate Financial Statements — accounting for investments in subsidiaries in separate financial statements of the parent	Accounted for at cost less impairment loss.	Accounted for either at cost or in accordance with IFRS 9 or IAS 39 where the entity is yet to apply IFRS 9 or using the equity method as described in IAS 28, investments in Associates and Joint Ventures (The option to use the equity method will be applicable for annual periods beginning on or after 1 January 2016 retrospectively in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. Earlier application is permitted.)	Equity method is not permitted in separate financial statements.
disclosure of nature and risk associated withinterest in other entities	There is no equivalent standard. AS 21, AS 23 and AS 27 require certain minimum disclosures in respect of subsidiaries, investments in associates and investments in joint ventures respectively.	IFRS 12 requires disclosures for the following broad categories: • significant judgements and assumptions such as how control, joint control and significant influence has been determined; • when a parent determines that it is an investment entity, the significant judgements and assumptions made in such determination; • interests in subsidiaries including details of the structure of the group, risk associated with consolidated structured entities, restrictions on use of assets and settlement of liabilities, changes in ownership levels, non-controlling interests in the group, etc.; • interest in joint arrangements and associates—the nature, extent and financial effects of interest in joint arrangements and associates (including names, details and summarised financial information) and risks associated with such entities;	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
		• interest in unconsolidated subsidiaries (in the case of investment entity parent)-name, principal place of business (and country of incorporation, if different from principal place of business, proportion of ownership interest held and, if different, proportion of voting rights held, nature of significant restrictions on the ability of the unconsolidated subsidiary to transfer funds to the investment entity parent etc. • interest in unconsolidated structured entities (other than unconsolidated subsidiaries controlled by an investment entity parent)-the nature and extent of interest in unconsolidated structured entities and the nature of, and changes in, the risk associated with its interest in unconsolidated structured entities.	
Interests in Joint Arrangements - Source Standard	**AS 27 — Financial Reporting of Interests in Joint Ventures**	**IFRS 11 — Joint Arrangements** **IAS 28 Investments in Associates and Joint Ventures**	**Ind AS 111 Joint Arrangements** **Ind AS 28 - Investments in Associates and Joint Ventures**
Joint control	Joint control is the contractually agreed sharing of control over an economic activity, However, where an enterprise by a contractual arrangement establishes joint control over an entity which is a subsidiary of that enterprise within the meaning of AS 21, the entity is consolidated under AS 21 by the said enterprise, and is not treated as a joint venture.	Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Classification	AS 27 identifies three broad types of joint ventures — jointly controlled operations, jointly controlled assets and jointly controlled entities.	IFRS 11 classifies joint arrangements into two types — joint operations and joint ventures depending upon the rights and obligations of the parties to the arrangement. An entity assesses its rights and obligations by considering the structure and legal form of the arrangement, the terms agreed by the parties in the contractual arrangement and, when relevant, other facts and circumstances. A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement (i.e. joint operators) have rights to the assets, and obligations for the liabilities, relating to the arrangement. A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement (i.e. joint venturers) have rights to the net assets of the arrangement.	Similar to IFRS.
Scope	There is no exemption for investments made by venture capital organisations, mutual funds, unit trusts and similar entities from applying the proportionate consolidation method.	The scope exemption applicable for investments in associates under AS 28 is equally applicable for a venturer's interest in a joint venture. (Refer the topic 'Investments in Associates and Joint Ventures — scope').	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Unit of account	No specific guidance.	IFRS 11 acknowledges that the framework agreement governing the parties might set out that the parties establish different joint arrangements to deal with specific activities that form part of the agreement and the rights and obligations differ when undertaking the different activities dealt with in the framework agreement. Consequently, joint operations and joint ventures can coexist when the parties undertake different activities that form part of the same framework agreement.	Similar to IFRS.
Separate financial statements of the venturer	Interest in a jointly controlled entity should be accounted for as an investment in accordance with AS 13 — Accounting for Investments. For jointly controlled operations, the venturer should recognise the assets that it controls and liabilities that it incurs and the expenses it incurs and its share of income that it earns from the joint venture in separate (as well as consolidated) financial statements. For jointly controlled assets, a venturer recognises its share of jointly controlled assets, liabilities, expenses, any liabilities it has incurred, any income from the sale or use of its share of output of the joint venture and any expenses which it has incurred in respect of its interest in the joint venture, in separate (as well as consolidated) financial statements.	Joint operations: a joint operator recognises the assets it controls, and expenses and liabilities it incurs, and its share of income earned, in both its separate and consolidated financial statements. In the separate financial statements, interests in joint ventures are accounted for either at cost or as investments in accordance with IFRS 9 or IAS 39 or using the equity method. (The option to use the equity method will be applicable for annual periods beginning on or after 1 January2016).	Similar to IFRS, except that the equity method is not permitted in the separate financial statements.

TOPIC	AS	IFRS	IND AS
Consolidated financial statements of the venture	As per AS 27, proportionate consolidation method is applicable only when the entity has subsidiaries and prepares consolidated financial statements. However, as per the Companies Act, 2013, consolidated financial statements should be prepared even if an entity has only associates and/or joint ventures but has no subsidiaries. For financial year ending 31 March2015, if a company does not have any subsidiaries, but only has associates and/or joint ventures, then the company would not have to prepare consolidated financial statements in respect of such associates and/ or joint ventures. (Refer the topic 'scope'). In the consolidated financial statements, interests in jointly controlled entities to be accounted using proportionate consolidation only. Equity method is not permitted.	Joint operations: a joint operator recognises the assets it controls, and expenses and liabilities it incurs, and its share of income earned, in both its separate and consolidated financial statements. A joint venturer applies the equity method, as described in IAS 28. Even if consolidated financial statements are not prepared (e.g. because the venturer has no subsidiaries), the equity method is used to account for joint ventures. IFRS 5 is applied to an investment, or a portion of an investment in a joint venture that meets the criteria to be classified as held for sale.	Similar to IFRS.
Share of losses	Loss pertaining to one or more investors in a jointly controlled entity may exceed their interests in the equity of the jointly controlled entity. Such excess, and further losses are recognised by the venturers in proportion of their shares in the venture, except to the extent that the investors have a binding obligation to, and are able to, make good the losses.	The treatment applicable for an entity's share of losses of an associate is equally applicable to an entity's share of losses of a joint venture. (Refer the topic 'Investments in Associates and Joint Ventures — share of losses').	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Disposals	On the date of discontinuation of use of proportionate consolidation, the Cost of investments is the venture share of net assets of the jointly controlled entity as at the date of discontinuation adjusted with carrying value of the relevant goodwill/capital reserve. Such investments are accounted in accordance with AS 13 — Accounting for Investments.	When the investment ceases to be a joint venture and becomes a financial asset, the retained interest in the former joint venture is measured at fair value in accordance with IFRS 9 or IAS 39 (if the entity is yet to apply IFRS 9). The difference between the fair value of retained interest together with any proceeds from disposing of a part interest in the joint venture and the carrying amount of the investment at the date the equity method was discontinued is recognised in profit or loss. When an entity discontinues the use of the equity method, it should account for all amounts previously recognised in other comprehensive income in relation to that investment on the same basis as would have been required if the investee had directly disposed of the related assets or liabilities. If an investment in a joint venture becomes an investment in an associate, the entity continues to apply equity method and does not remeasure the retained interest.	Similar to IFRS.
Goodwill	Goodwill arising on the proportionate consolidation of the jointly controlled entity (i.e. excess of the cost to the venturer of its interest in the jointly controlled entity over its share of net assets of the jointly controlled entity) is separately disclosed in the consolidated financial statements.	Goodwill (i.e. excess of the cost of the investment over the entity's share of the net fair value of the joint venture's identifiable assets and liabilities) is included in the carrying amount of the investment.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Capital reserve/negative goodwill	When the cost to the venturer of its interest in a jointly controlled entity is less than its share of the net assets of the jointly controlled entity, at the date of acquisition the difference is treated as capital reserve in the consolidated financial statements.	Any excess of the entity's share of net fair value of the joint venture's identifiable assets and liabilities over the cost of investments is included as income in the determination of the investor's share of joint venture's profit or loss in the period in which the investment is acquired.	Any excess of the entity's share of the net fair value of the joint venture's identifiable assets and liabilities over the cost of the investment is recognised directly in equity as capital reserve in the period in which the investment is acquired.
Uniform accounting policies	If not practicable to use uniform accounting polices while applying the proportionate consolidation method, that fact should be disclosed together with proportions of items in the consolidated financial statements to which different accounting policies have been applied.	Uniform accounting policies should be followed while applying the equity method. No exception is provided.	Similar to IFRS.
Reporting date	The difference between the reporting date of the jointly controlled entity and that of the venturer should be no more than six months.	The difference between the reporting date of the joint venture and that of the venturer should be no more than three months.	Similar to IFRS.
Accounting for acquisitions of interest in joint operations	No specific guidance.	The acquisition of an interest in a joint operation in which the activity constitutes a business should be accounted for using the principles of IFRS 3 — Business Combination. This requirement applies to annual periods beginning on or after 1 January 2016 on a prospective basis to acquisitions of interests in joint operations occurring from the beginning of the first period in which the amendments are applied.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Accounting for acquisitions of interests in joint operations in the case of common control transactions	No specific guidance.	Similar to IFRS 3 — Business Combinations, IFRS 11 scopes out business combinations,	Acquisition accounting does not apply to acquisition of interest in a joint operation in which the activity of the joint operation constitutes a business as defined in Ind AS 103, when the parties sharing joint control, including the entity acquiring the interest in the joint operation, are under the common control of the same ultimate controlling party or parties both before and after the acquisition. For such transactions, refer to the topic 'Business Combinations — combination of entities under common control'.
Fair Value - Source Standard	**No equivalent standard existed**	**IFRS 13 Fair value measurements**	**Ind AS 113 — Fair value measurements**
Applicability	N. A.	Applies when another IFRS requires or permits fair value measurements or disclosures about fair value measurements (and measurements such as fair value less cost to sell).	Similar to IFRS.
Definition of Fair value	N. A.	Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.	Similar to IFRS.
Classification and Disclosure	N. A.	Requires with some exceptions, classification of these measurements into a 'fair value hierarchy' based on the nature of inputs: Level 1: Quoted prices in active markets for identical assets and liabilities that the entity can access at the measurement date; Level 2: Inputs other than quoted market prices included within Level 1 that are observable for the asset liability, either directly or indirectly; Level 3: Unobservable inputs for the asset or liability.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
		Requires various disclosures depending on the nature of the fair value measurement (e.g. whether it is recognised in the financial statements or merely disclosed) and the level in which it is classified.	
Regulatory Deferral Accounts - Source Standard	**Guidance Note on Accounting for Rate Regulated Activities (revised)* (effective for accounting periods beginning on or after 1 April 2015)**	**IFRS 14— Regulatory Deferral Accounts (effective for annual periods beginning on or after 1 January 2016. Earlier application is permitted)**	**Ind AS 114 Regulatory Deferral Accounts**
Scope, recognition and presentation	The Guidance Note should be applied by an entity to its operating activities (all or only a portion) that meet the following criteria: • the regulator establishes the price the entity must charge its customers for the goods or services the entity provides and that price binds the customers; and • the price established by regulation is designed to recover the specific costs the entity incurs in providing the regulated goods or services and to earn a specified return (which could be a minimum or range and need not be a fixed or guaranteed return).	IFRS 14— Regulatory Deferral Accounts is designed as a limited scope Standard to provide an interim, short-term solution for rate-regulated entities which are first-time adopters of IFRS to continue to account, with some limited changes, for regulatory deferral account balances in accordance with its previous GMP, both on initial adoption of IFRS and in subsequent financial statements, until such time as the IASB completes its comprehensive project on rate regulated activities, Regulatory deferral account balances arise when an entity provides goods or services to customers at a price or rate that is subject to rate regulation.	Similar to ERS. However a clarification is provided in and AS 114 that the Guidance Note on Accounting for Rate Regulated Activities issued by ICAI would be considered as previous GAAP. A clarification is included in Ind AS 114 that an entity subject to rate regulation coming into existence after Ind AS coming into force or an entity whose activities become subject to rate regulation subsequent to preparation and presentation of first Ind AS financial statements should be permitted to apply the requirements of previous GAAP in respect of such rate regulated activities.

TOPIC	AS	IFRS	IND AS
		Entities which are eligible to apply IFRS 14 are not required to do so, and so can choose to apply only the requirements of IFRS 1 — First-time Adoption of International Financial Reporting Standards when first applying IFRS5. The election to adopt IFRS 14 is only available on the initial adoption of IFRSs, meaning an entity cannot apply IFRS 14 for the first time in financial statements subsequent to those prepared on the initial adoption of IFRS5. However, an entity that elects to apply IFRS 14 in its first IFRS financial statements must continue to apply it in subsequent financial statements.	
Scope, recognition and presentation (continued)	A regulatory lability is recognised when: • an entity has a present obligation as a result of a past event; • it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and • a reliable estimate can be made of the amount of the obligation. On initial recognition and at the end of each subsequent reporting period, an entity should measure a regulatory asset or regulatory liability at the best estimate of the amount expected to be recovered or refunded or adjusted as future cash flows under the regulatory framework, with changes in the expectation being recorded as a change in an accounting estimate.	IFRS 14 provides an exemption from paragraph 11 of IAS 8 - Accounting Policies, Changes in Accounting Estimates and Errors, which requires an entity to consider the requirements of IFRSs dealing with similar matters and the requirements of the Conceptual Framework when setting its accounting policies. The effect of the exemption is that eligible entities can continue to apply the accounting policies used for regulatory deferral account balances under the basis of accounting used immediately before adopting IFRS ('previous GMP') when applying IFRSs, subject to the presentation requirements of IFRS 14.	

TOPIC	AS	IFRS	IND AS
	A regulatory asset or regulatory liability should not be discounted to its present value. An entity should present regulatory assets and regulatory liabilities as current/non-current, as the case may be, in the balance sheet, separately from other assets and liabilities. No offsetting is permitted and separate line items should be presented in the balance sheet for the total of all regulatory assets and the total of all regulatory liabilities. A separate line item is also required to be presented under tax expense for the deferred tax expense/saving related to regulatory account balances. Additional specific disclosures are also required.	Regulatory deferral account balances, and movements in them, are presented separately in the statement of financial position and statement of profit or loss and other comprehensive income, and specific disclosures are required. Regulatory deferral account balances are not classified between current and non-current, but are separately disclosed using subtotals.	
Revenue from Contract with customers — primary literature	**No comprehensive equivalent standard, The following deal with revenue recognition;** **AS 9 Revenue Recognition** **AS 7 — Construction Contracts** **Guidance Note on Accounting for Real Estate Transactions (Revised 2012)** **Guidance Note on Accounting for Dot-corn Companies**	**IFRS 15- Revenue from Contracts with Customers (effective from Annual period beginning on or after 1 January 2017 with earlier application permitted)** **IFRIC 12 — Service Concession Arrangements** **SIC 29 — Service Concession Arrangements: Disclosures** **IFRS 15 supersedes the following standards and interpretations:** • **IAS 11 — Construction Contracts** • **IAS 18 Revenue,** • **IFRIC 13 Customer Loyalty Programmes,** • **IFRIC 15 Agreements for the construction of Real Estate,** • **IFRIC 18 Transfer of Assets from Customers** • **SIC-31 — Barter Transactions Involving Advertising Services**	**Ind AS 115— Revenue from Contracts with Customers** **Ind AS 115 —Appendix C — Service Concession Arrangements** **IndAS 115 —Appendix D — Service Concession Arrangements: Disclosures**

TOPIC	AS	IFRS	IND AS
Scope	AS 7 deals with construction contracts and AS 9 deals with the recognition of revenue arising in the course of ordinary activities of the entity — sale of goods, rendering of services and use by others of entity resources yielding interest, royalties and dividend. AS 9 scopes out revenue from lease agreements, insurance contracts, revenue arising from government grants, and other similar subsidies.	IFRS 15 applies to contract with a customer and establishes principles on reporting the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with customer. A contract is an agreement between two or more parties that creates enforceable rights and obligations, and can be either written, oral or implied by an entity's customary business practices. **It also scopes out non-monetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers.**	Similar to IERS.
Definition	As per AS 9, revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities from the sale of goods, from the rendering of services, and from the use by others of enterprise resources yielding interest, royalties and dividends.	Revenue is defined as income arising in the course of an entity's ordinary activities. Income is defined as increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in an increase in equity, other than those relating to contributions from equity participants.	Similar to IFRS.
Recognition	AS 9 requires recognition of revenue when (i) there is transfer significant risks and rewards of ownership (ii) no significant uncertainty exists regarding the amount of consideration and (iii) at the time performance, it s not unreasonable to expect ultimate collection.	The core principle under IFRS 15 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the considerations to which the entity expects to be entitled in exchange for those goods or services.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
	Revenue from sale of goods is recognized when seller has transferred the property in goods to the buyer for a consideration — which in most cases results in or coincides with transfer of significant risks and rewards of ownership. Revenue from service transactions is usually recognized as the services are performed either by the proportionate completion method or by the completed service contract method.	To achieve that core principles, the following steps are applied: 1) Identify the contract(s) with a customer. 2) Identify the performance obligations in the contract (account for a 'distinct' good or service). 3) Determine the transaction price. 4) Allocate the transaction price to the performance obligations in the contract. 5) Recognise revenue when the entity satisfies a performance obligation.	
Identification contracts	Under AS 7, a construction contract specifically negotiated for the construction of the asset or a combination of assets that are closely interrelated or interdependent in terms of design, technology, and function of their ultimate purpose or use. AS 9 does not have similar guidance.	A contract falls within the scope of IFRS 15, when all the following conditions are met: a) The contract has commercial substance (that is, the risk, timing, or amount of future cash flows is expected to change as a result of the contract) b) The parties to the contract have approved the contract c) Each party's rights regarding the goods or services to be transferred can be identified d) Payment terms can be identified for the goods or services to be transferred e) The parties are committed to perform their respective obligations and they intend to enforce their respective contractual rights f) It is probable that the entity will collect the consideration to which it expects to be entitled.	Similar to IERS.

TOPIC	AS	IFRS	IND AS
Contract modification	Under AS 7, construction of an additional asset is treated as a separate contract if the asset differs significantly in design, technology, or function, or the price of the asset is negotiated without regard to the original contract price. Variation and claims are part of the original contract revenue, unless the above treatment of construction of the additional asset as a separate contract applies. Claims, variations are included in contract revenue only when the probability of customer accepting! approving the claim or variation is established and amount of revenue can be reliably measured. Similar guidance not available in AS 9.	Contract modification is treated as a separate contract if the modification results in 1) addition of 'distinct goods or services' and 2) a change in consideration that reflects the entity's stand-alone selling price for such additional promised goods or services. If modification does not meet the criteria to be accounted for as a separate contract, determination needs to be made on whether to account for modification as 1) termination of the original contract and creation of a new contract (i.e. allocate the amount of consideration not yet recognised to the remaining performance obligation) or 2) as if it were part of the original contract (i.e. update the transaction price, measure progress toward complete satisfaction of the performance obligation, and record a cumulative catch-up adjustment to revenue). Accordingly change orders and claims (price adjustments, or changes in scope) need to be assessed if 1) customer has approved any change in scope or price, or 2) it has enforceable rights to considerations, and accordingly apply contract modification guidance.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Unilateral right of termination	No guidance included.	A contract does not exist if the contract provides for a unilateral enforceable right to terminate a wholly unperformed contract without compensating the other party (or parties). Any considerations received on such arrangements from the customer are recorded as a liability and recognised as revenue only when there is no remaining obligation to the customer and the amount is not refundable or the contract has been terminated and the consideration received from the customer is non-refundable.	Similar to IFRS.
Identify the performance obligation	Under AS 7, if a contract covers a number of assets, the construction of each asset is treated as a separate construction contract when separate proposals have been submitted, each asset is subject to separate negotiations and costs and revenues of each asset can be identified. Similar guidance does not exist in AS 9.	IFRS 15 requires evaluation of performance obligations — to account for 'distinct' goods or services (or a bundle of distinct goods or services, or a series of distinct goods or services — i.e. a separate unit of account) based on the following criteria: a) The customer can benefit from the goods or services either on its own or together with other resources that are readily available to the customer, b) Promise to transfer the good or services to the customer is separately identifiable from other promises in the contract (that is, the goods or services is distinct within the context of the contract). A good or service that does not meet these criteria would be combined with other goods or services in the contract until the criteria are met.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Variable considerations, contingent considerations	Under AS 7, incentive payments are included in contract revenue when the contract is sufficiently advanced that it is probable the specified performance standards will be met or exceeded and the amount of the incentive payments can be measured reliability. No similar guidance in AS 9.	Variable considerations (including potentially contingent considerations) are only included in the transaction price to the extent that it is probable that the amount of cumulative revenue recognised would not be subject to a significant future revenue reversal when such estimates are revised. Variable considerations are estimated using either 1) an expected value which is a sum of probability-weighted amounts in a range of possible consideration amounts. An expected value may be appropriate if there are a large number of contracts with similar characteristics, or 2) most likely amount in a range of possible consideration amounts. Most likely amount is appropriate when the contract has only two possible outcomes (for example, an entity either achieves a performance bonus or does not).	Similar to IFRS. However under Ind AS 115, penalties should be accounted for as per the 5ubstance of the contract. Where the penalty is inherent in the determination of transaction price, it should form part of variable consideration, otherwise the same should not be considered for determining the consideration and the transaction price should be considered as fixed.
Time value of money	Revenue is not adjusted for the time value.	Transaction price is adjusted for the time value of money when a significant financing component exists.	Similar to IFRS.
Allocating the transaction price	No guidance provided.	The transaction price is allocated to each performance obligation identified in the contract on the basis of a relative stand-alone selling price determined at contract inception.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
		The stand-alone selling price is the price at which an entity would sell a promised good or service separately to a customer (the best evidence being the observable price at which the good or service is separately sold in similar circumstances and to similar customers. If not directly observable, estimation methods are used e.g. cost plus margin method, residual approach, competitor pricing).	
Satisfaction of performance obligation	Under AS 9, revenue from sale of goods is recognised when seller has transferred the property in goods to the buyer for a consideration — which in most coincides with transfer of significant risks and rewards of ownership. Revenue from service transactions is usually recognised as the services are performed either by the proportionate completion method or by the completed service contract method. Under AS 7, contract revenue and contract costs to be recognised as revenue or expenses by reference to the percentage of completion method if the outcome of the contract can be estimated reliably; else, revenue should be recognised only to the extent of contract costs incurred of which recovery is probable.	Revenue is recognised as 'control' of the goods or services underlying the performance obligation is transferred to the customer. The control-based model differs from the risk-and-rewards model. Entities need to determine whether control is transferred over time. If not, it is transferred at a point in time. For each performance obligation satisfied over time, revenue is recognised by measuring the progress towards complete satisfaction (by using either output or input methods) and only if it can reasonably measure its progress towards completion; else, revenue should be recognised only to the extent of contract costs incurred of which recovery is probable.	Similar to IFRS.

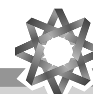
TOPIC	AS	IFRS	IND AS
Contract costs	Capitalization of contract cost is not permitted.	IFRS 15 contains criteria for determining when to capitalise costs associated with obtaining and fulfilling a contract. Specifically entities are required to capitalise recoverable incremental costs of obtaining a contract (e.g. sales commissions). Such costs capitalised would be amortised in a manner consistent with the pattern of transfer of the goods or services to which the asset is related (i.e. as the related revenue is recognised). All capitalized costs assets would be subject to impairment testing if any impairment indicator exists.	Similar to IFRS.
Disclosure	AS 7 requires disclosure of contract revenue recognised, methods used to recognise revenue, methods used to determine stage of completion, aggregate amount of cost incurred and recognised profits, amount of advances received and amount of retentions. AS 9 requires disclosure of circumstances when revenue recognition has been postponed pending resolution of significant uncertainties.	Cohesive set of disclosure requirements including both qualitative and quantitative information about the nature, amount, timing and uncertainty of revenue and cash flows from contracts with customers. Specifically, information about: • revenue recognised from contracts with customers, including the disaggregation of revenue into appropriate categories • contract balances, including the opening and closing balances of receivables, contract assets and contract liabilities;	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
	As per Schedule III, in the case of a company other than a finance company, revenue from operations should disclose separately in the notes to accounts the following: • sale of products • sale of services • other operating revenues Less: Excise Duty Turnover (Net) In the case of a finance company, revenue from operations should include revenue from: • interest; and • other financial services	• performance obligations, including when the entity typically satisfies its performance obligations and the transaction price that is allocated to the remaining performance obligations in a contract; • significant judgements, and changes in judgements, made in applying the requirements to those contracts; and • assets recognised from the costs to obtain or fulfill a contract with a customer.	
non-cash considerations	No specific guidance.	If a customer promises consideration in a form other than cash, the non-cash consideration is measured at fair value; if fair value cannot be estimated, by reference to the stand-alone selling price of the goods or services.	Similar to IFRS.
Application guidance	No specific guidance.	The standard includes application guidance for specific transactions such as i) sale with a right of return ii) warranties, iii) principal versus agent considerations, iv) customer options for additional goods or services, v) non-refundable upfront fees, vi) bill and hold arrangements, and viii) customer unexercised rights ix) Licensing, x) Repurchase agreements.	Similar to IFRS.

TOPIC	AS	IFRS	IND AS
Scope	No specific guidance. The CAI has issued an exposure draft of Guidance Note on Accounting for Service Concession Arrangements, which is similar to IFRIC 12.	Prescribes accounting by private sector operators involved in provision of public sector infrastructure assets and services. Under service concession arrangements, the grantor specifies the services to be provided to the public, controls the infrastructure and the price to be charged to the public by the operator.	Similar to IFRS.
Recognition	No specific guidance. The CAI has issued an exposure draft of Guidance Note on Accounting for Service Concession Arrangements, which is similar to IFRIC 12.	Depending on the terms of the arrangement: • a financial asset is recognised where an operator has the unconditional right to receive cash or other financial asset from the grantor over the life of the arrangement; or • an intangible asset is recognised where the operator receives cash directly from the public and where future cash flows vary depending on the usage of the infrastructure; or • both a financial asset and an intangible asset are recognised where the operators return is provided partly by a financial asset and partly by an intangible asset.	Similar to IFRS.

Study Note - 2

ACCOUNTING OF BUSINESS COMBINATIONS & RESTRUCTURING



This Study Note includes

2.1 Introduction

2.2 Concept of Business Combination

2.3 Relevant Terminologies Related to Business Combination

2.4 Types of Merger

2.5 Method of Accounting

2.6 Scheme of Reconstruction

2.7 Demerger – Cocept

2.8 Reverse Merger

2.9 External Reconstruction

2.10 Notes and Disclosure Relating to Business Combination

2.11 Business Combination of Entities under Common Control

2.1 INTRODUCTION

In today's global business environment, companies – both new and existing, face immense competition for their survival. Moreover, the companies have to ensure a steady growth. The growth can be achieved by a company through the regular 'organic' process by increase in its scale of operations, by diversification and capturing higher market share. But many companies today adopt an indirect route that happens to be 'inorganic' in nature. One of the best ways for a company through grow via the indirect route is by merging with another company or acquiring other companies.

2.2 CONCEPT OF BUSINESS COMBINATION

Business Combination is a transaction or an event in which an acquirer obtains control of one or more businesses. (e.g. acquisition of shares or net assets, legal mergers, reverse acquisitions).

A Business Combination can be structured in a number of ways for legal, taxation and other reasons, which include but are not limited to:

(a) one or more subsidiaries become subsidiaries of an acquirer or the net assets of one or more businesses are legally merged into the acquirer; or

(b) one combining entity transfers its net assets, or its owners transfer their equity interests, to another combining entity or its owners;

(c) all of the combining entities transfer their net assets, or the owners of those entities transfer their equity interests to a newly formed entity (sometimes referred to as a roll-up or put together transaction); or

(d) a group of former owners of one of the combining entities obtain control of the combined entity.

The accounting for all forms of business combinations are accounted for as per the provisions set out in Indian Accounting Standard (Ind AS) 103 **Business Combinations**.

An entity shall determine whether a transaction or other event is a business combination by applying the definition in this Indian Accounting Standard, which requires that the assets acquired and liabilities assumed constitute a business. If the assets acquired are not a business, the reporting entity shall account for the transaction or other event as an asset acquisition.

Objective & Scope of Ind AS 103:

Objective: The objective of this Indian Accounting Standard (Ind AS) is to improve the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements about a business combination and its effects.

Scope: This Ind AS applies to a transaction or other event that meets the definition of a business combination. This standard does not apply to the following:

- The accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself.
- Acquisition of an asset or group of assets that is not a business.
- A combination of entities or businesses under common control.

2.3 RELEVANT TERMINOLOGIES RELATED TO BUSINESS COMBINATION

Business: As per Ind AS 103, the term 'Business' refers to an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs or other economic benefits directly to investors or other owners, members or participants.

Business Combination: As per Ind AS 103, Business Combination refers to a transaction or other event in which an acquirer obtains control of one or more businesses. Transactions sometimes referred to as 'true mergers' or 'mergers of equals' are also business combinations as that term is used in this Indian Accounting Standard.

Acquiree: The business or businesses that the acquirer obtains control of in a business combination.

Acquirer: The entity that obtains control of the acquiree.

Acquisition Date: The date on which the acquirer obtains control of the acquiree.

Control: The power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Equity Interests: For the purposes of this Indian Accounting Standard, equity interests is used broadly to mean ownership interests of investor-owned entities and owner, member or participant interests of mutual entities.

Fair Value: The amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Goodwill: An asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognised.

Identifiable: An asset is identifiable if it either: (a) is separable, ie capable of being separated or divided from the entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable asset or liability, regardless of whether the entity intends to do so; or (b) arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

Intangible Asset: An identifiable non-monetary asset without physical substance.

Mutual Entity: An entity, other than an investor-owned entity, that provides dividends, lower costs or other economic benefits directly to its owners, members or participants. For example, a mutual insurance company, a credit union and a co-operative entity are all mutual entities.

Non-Controlling: The equity in a subsidiary not attributable, interest directly or indirectly, to a parent.

Owners: For the purposes of this Indian Accounting Standard, owners is used broadly to include holders of equity interests of investor-owned entities and owners or members of, or participants in, mutual entities.

2.4 TYPES OF MERGERS

Merger is a process in which either two or more companies unifies into another existing company or any one or more companies may form a new company to take over the business of two or more existing companies.

Mergers may be broadly classified as follows:

1. **Cogeneric Mergers**

   It happens within same industries and taking place at the same level of economic activity - exploration, production or manufacturing. It may be wholesale distribution or retail distribution to the ultimate consumer. The Cogeneric mergers are of two types:

   (a) **Horizontal merger:**

   - This class of merger is a merger between business competitors who are manufacturers or distributors of the same type of products or who render similar or same type of services for profit i.e. they are in the same stage of business cycle.
   - It involves joining together of two or more companies which are producing essentially the same products or rendering same or similar services or their products and services directly competing in the market with each other.
   - It is a combination of two or more firms in similar type of production/distribution line of business.

   (b) **Vertical merger:**

   - It occurs between firms which are complementary to each other, e.g. one of the companies is engaged in the manufacture of a particular product and the other is established and expert in the marketing of that product.
   - In this merger the two companies merge and control the production and marketing of the product.

   Types of vertical merger:

   Vertical merger may take the form of forward or backward merger.

   A vertical may result into a smooth and efficient flow of production and distribution of a particular product and reduction in handling and inventory costs. It may also pose a monopolistic trend in the industry.

   Forward-looking merger: When a company combines with the customer, it is known as forward merger.

   Backward merger: When a company combines with the supplier of material, it is called a backward merger.

2. **Conglomerate merger:**

   This type of merger involves coming together of two or more companies engaged in the different industries and/or services. Their businesses or services are neither horizontally nor vertically related to each other. They lack any commonality either in their product, or in the rendering of any specific type of service to the society. This is the type of merger of companies which are neither competitors, nor complementaries nor suppliers of a particular raw material nor consumers of a product or consumable. In this, the merging companies operate in unrelated markets no functional economic relationship.

   The conglomerate merger may be of three types:

   (a) Product extension merger

   (b) Market extension merger

   (c) Pure conglomerate merger

2.5 METHODS OF ACCOUNTING

As per paragraph 4 of Ind AS 103, an entity shall account for each business combination by applying the **Acquisition Method**.

Ind AS 103 requires mandatory use of purchase method of accounting for business combination except for common control transaction. It also mandates recording of all assets acquired and liabilities assumed to be recorded at fair value.

The application of the Acquisition Method involves the following steps:

- **Identification of the acquirer**: For each business combination, one of the combining entities shall be identified as the acquirer. The guidance in Ind AS 27 Consolidated and Separate Financial Statements shall be used to identify the acquirer—the entity that obtains control of the acquiree.
- **Determination of date of acquisition**: The acquirer shall identify the acquisition date, which is the date on which it obtains control of the acquiree. The date on which the acquirer obtains control of the acquiree is generally the date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree—the closing date. However, the acquirer might obtain control on a date that is either earlier or later than the closing date. For example, the acquisition date precedes the closing date if a written agreement provides that the acquirer obtains control of the acquiree on a date before the closing date. An acquirer shall consider all pertinent facts and circumstances in identifying the acquisition date.
- **Recognition and Measurement of Assets, Liabilities and Non-controlling Interests (NCI)**: As of the acquisition date, the acquirer shall recognise, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree.

Recognition Conditions

To qualify for recognition as part of applying the acquisition method, the identifiable assets acquired and the identifiable liabilities assumed must meet the definitions of assets and liabilities in the Framework for the Preparation and Presentation of Financial Statements issued by the Institute of Chartered Accountants of India at the acquisition date.

In addition, to qualify for recognition as part of applying the acquisition method, the identifiable assets acquired and liabilities assumed must be part of what the acquirer and the acquiree (or its former owners) exchanged in the business combination transaction rather than the result of separate transactions.

The acquirer's application of the recognition principle and conditions may result in recognising some assets and liabilities that the acquiree had not previously recognised as assets and liabilities in its financial statements.

Classifying or designating identifiable assets acquired and liabilities assumed in a business combination

At the acquisition date, the acquirer shall classify or designate the identifiable assets acquired and liabilities assumed as necessary to apply other Indian Accounting Standards subsequently. The acquirer shall make those classifications or designations on the basis of the contractual terms, economic conditions, its operating or accounting policies and other pertinent conditions as they exist at the acquisition date. In some situations, Indian Accounting Standards provide for different accounting depending on how an entity classifies or designates a particular asset or liability.

Measurement Principle

The acquirer shall measure the identifiable assets acquired and the liabilities assumed at their acquisition-date fair values.

For each business combination, the acquirer shall measure at the acquisition date components of non-controlling interest in the acquiree that are present ownership interests and entitles their holders to a proportionate share of the entity's net assets in the event of liquidation at either: (a) fair value; or (b) The present ownership instruments' proportionate share in the recognised amounts of the acquiree's identifiable net assets.

All other components of non-controlling interests shall be measured at their acquisition-date fair values, unless another measurement basis is required by Indian Accounting Standards.

Exceptions to the recognition or measurement principles

- This Indian Accounting Standard provides limited exceptions to its recognition and measurement principles.
- Exception to the recognition principle: Contingent Liabilities.
- Exception to the measurement principle: Reacquired Rights, Share-based payment transactions, Assets held for sale.
- Exception to the recognition and measurement principle: Income Taxes, Employee benefits, Indemnification Assets.

Recognition and Measurement of Goodwill or a Bargain Purchase:

The acquirer shall recognise goodwill as of the acquisition date measured as the excess of (a) over (b) below:

(a) the aggregate of:

(i) the consideration transferred measured in accordance with this Indian Accounting Standard, which generally requires acquisition-date fair value (see paragraph 37);

(ii) the amount of any non-controlling interest in the acquiree measured in accordance with this Indian Accounting Standard; and

(iii) in a business combination achieved in stages, the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree.

(b) the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed measured in accordance with this Indian Accounting Standard.

- In a business combination in which the acquirer and the acquiree (or its former owners) exchange only equity interests, the acquisition date fair value of the acquiree's equity interests may be more reliably measurable than the acquisition-date fair value of the acquirer's equity interests. If so, the acquirer shall determine the amount of goodwill by using the acquisition-date fair value of the acquiree's equity interests instead of the acquisition-date fair value of the equity interests transferred. To determine the amount of goodwill in a business combination in which no consideration is transferred, the acquirer shall use the acquisition-date fair value of the acquirer's interest in the acquiree determined using a valuation technique in place of the acquisition-date fair value of the consideration transferred.
- **Initial Accounting of Business Combination:** If initial accounting of BC could be done only on provisional measurement at the end of the reporting period, adjustments to provisional measurement based on new information as to facts and circumstances that existed at the acquisition date are allowed within one year of the acquisition date retrospectively as if the adjustments have been made at the acquisition date except to correct error under Ind AS 8.
- **Subsequent measurement and accounting**: Usually, subsequent to the date of a business combination an acquirer measures and accounts for assets acquired and liabilities assumed or incurred in accordance with other applicable IFRSs.
- **Business combination achieved in stages (Step Acquisition)**: An acquirer sometimes obtains control of an acquiree in which it held an equity interest immediately before the acquisition date. This is referred to as step acquisition · Obtaining control triggers re-measurement of previous investments (equity interests). The acquirer remeasures its previously held equity interest in the acquiree at its acquisition-date fair value. Any resulting gain/loss is recognised in profit or loss.
- **Business combination without transfer of consideration**: The acquisition method of accounting for a business combination also applies even when no consideration is transferred.

- Such circumstances include:
  - The acquiree repurchases a sufficient number of its own shares for an existing investor (the acquirer) to obtain control;
  - Minority veto rights lapse that previously kept the acquirer from controlling an acquiree in which the acquirer held the majority voting rights;
  - The acquirer and the acquiree agree to combine their businesses by contract alone.

AS -14: Accounting for Amalgamations

- Accounting Standard – 14 as prescribed by the Institute of Chartered Accountants of India deals with accounting for amalgamation and treatment for resulting goodwill or reserves.
- AS-14 classifies amalgamation into two type's viz.: Amalgamation in nature of merger; and Amalgamation in nature of purchase.

Methods of Accounting: As per AS-14, there are two recognised methods of accounting for amalgamations, namely:

1. Pooling of Interest Method (applicable in case of Amalgamation in nature of merger);
2. Purchase Method (applicable in case of Amalgamation in nature of purchase)

Pooling of Interest Method (Amalgamation in the nature of merger)

The assets, liabilities and reserves of the transferor company are to be recorded at their existing carrying amounts and in the same form as it was appearing in the books of the transfer or transferor company.

The identity of the reserves of the transferor company is to be kept intact in the balance sheet of the transferee company.

Difference between the amounts of share capital issued plus any other additional consideration paid by the transferee company and the amount of the share capital of the transferor company should be adjusted in Reserves.

Purchase Method (Amalgamation in nature of purchase)

The assets and the liabilities of the transfer or company are to be recorded at their existing carrying amounts or, alternatively, the consideration should be allocated to individual assets and liabilities on the basis of air values at the date of amalgamation while preparing the financial statements of the transferee company.

The identity of the reserves of the transferor company other than the statutory reserves is not preserved. The identity of the statutory reserves is preserved in the same form and is recorded in the books of the transferee company by a corresponding debit to the amalgamation adjustment A/c.

Excess or shortfall of consideration over the value of net assets acquired should be credited/ debited as capital reserve/goodwill, as the case may be.

It is appropriate to amortize goodwill over a period of not exceeding 5 years unless a longer period is justified.

Meaning of Purchase Consideration:

- Purchase consideration represents consideration paid by the transferee company(s) to shareholders (equity and preference) in any form viz., cash, shares, debentures etc.
- According to AS-14, it is aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the **shareholders** of the transferor company.
  - Shareholders means both equity and preference shareholders.
  - Payment to any other party like Debenture holders, other creditors and any amount of expenses of dissolution borne by the Transferee company will not come in Purchase Consideration.

Entries to close the books of Transferor Company:

1. **For transfer of Assets:**

Realisation A/c……………… ………..……..	Dr.	With the book value of assets
To All Assets A/c		

2. **For transfer of External liabilities:**

All External Liabilities A/c…………………………	Dr.	With book value of external liabilities
To Realisation A/c		

3. **For the due entry for purchase consideration:**

Transferee Company A/c …………	Dr.	With the aggregate amount of purchase consideration
To Realisation A/c		

4. **For transfer of internal liabilities:**

Equity Share Capital A/c ……………….…..….	Dr.
Reserve & Surplus A/c ...…………………………...	Dr.
To Equity Share Holder A/c	

5. **For transfer of accumulated loss:**

Equity Share Holder A/c………………………..…	Dr.
To Profit & Loss A/c	

6. **For receiving of purchase consideration:**

Equity shares in transferee Company A/c………………	Dr.
Preference shares in transferee Company A/c………..	Dr.
Debenture in transferee Company A/c………………….	Dr.
Cash A/c………………………………………………………..	Dr.
To Transferee Company A/c	

Note: It may be noted that issue price of securities is to be noted here.

7. **For the amount payable to Preference share Holder:**

Preference Share Capital A/c…………………..….	Dr.	
Realisation A/c……………………………….….…….	Dr.	[Excess amount payable]
To Pref. Share Holder A/c		
To Realisation A/c		[Deficit amount]

8. **For payment to pref. shareholders:**

Pref. Share Holder A/c ……………………….……...	Dr.
To Bank A/c	
To Shares in Transferee Company A/c	
To Debenture in Transferee Company A/c	

9. For realisation of assets not taken over:

Bank A/c ………………………………….……….. Dr.

To Realisation A/c

10. For settlement of Liabilities not taken over

Realisation A/c……..…………………………….. Dr.

To Bank A/c

11. For transfer of realisation profit:

Realisation A/c .………………………………….. Dr.

To Equity Share Holder A/c

12. For settlement of account of share holders:

Equity share Holders A/c …………………….. Dr.

To Shares in Transferee Company A/c

To Debenture in Transferee Company A/c

To Cash A/c

Opening entries in the books of Transferee Company:

1. For purchase consideration payable:

Business Purchase A/c ………………………………. Dr. Purchase Consideration

To Liquidator of Transferor Company A/c

2. For incorporation of Assets and liabilities:

Debtors A/c…………………………………………………. Dr.

Stock A/c……………………………………………..…. Dr.

Bank A/c………………………………………………..….. Dr.

Goodwill A/c (bal fig)..……………..…………..……….… Dr.

To Capital Reserve A/c (bal. fig.)

To Creditors A/c

To Business Purchase A/c

3. For incorporation of Statutory Reserve:

Amalgamation Adjustment A/c…………………. Dr.

To Statutory Reserve A/c

4. For discharge of purchase consideration:

Liquidator of Transferor Company A/C………………. Dr.

Discount on Issue of Securities A/C………………….. Dr

To Bank A/C

To Equity Share Capital A/C

To Preference Share Capital A/C

To Debentures A/C

To Securities Premium A/C

Accounting for investment in subsidiary:

Accounting for investment in subsidiary can be of any one of the following five categories:

1. Transferor company holding shares in transferee company
2. Transferee company holding shares in transferor company
3. Transferor company holding shares in another transferor company
4. Transferor company holding shares in transferee and vice versa [Cross holding]
5. Transferor company holding shares in another transferor company and vice versa [Cross holding]

2.6 SCHEME OF RECONSTRUCTION

The need for reconstruction arises when a company has accumulated losses or when a company finds itself over capitalized which means either that the value placed on assets is too much as compared to their earning capacity or that the profits as a whole are insufficient to pay a proper dividend. Apart from clarity, wide acceptance and justice, there construction scheme must take in to account the following:-

The fundamental basis of any proposals is the earning power of the company. Even the interest to debenture holders cannot be paid unless the company's activities are profitable. A very careful estimate should, therefore, be made of the profits expected by the company in the future. Unless the profits are sufficient to meet all the expenses including adequate depreciation, interest to debenture holders and other creditors, preference dividend, and a reasonable return to the equity shareholder, it would be useless to process with any reconstruction scheme because, otherwise, the need for reconstruction will soon arise again.

Assuming that adequate profits can be expected, the reconstruction scheme should not adversely affect the rights of preference shareholders (not to speak of creditors and debenture holders)unless it is absolutely necessary. Suppose, the profits are such that after paying dividends to preference shareholders little remains for equity shareholders: the preference shareholder may be persuaded to accept a sacrifice either by reduction of capital or by reduction in the rate of dividend or both because the alternative to such acceptance of sacrifice may be the liquidation of the company (in which case, due to forced sale, the asset may not realize much and the preference shareholder may not be able to get back what they have invested). If the company is in very bad position, even the debenture holders may be prevailed upon to accept a reduction of their claims. But, so far as is possible, contractual and legal rights and priorities should be maintained.

The equity share holder will naturally have to bear the brunt of the losses and sacrifice. This is not as bad as it sounds because (a) the equity shareholders realize from the very beginning that if losses occur they have to bear them before anybody else can be called upon to do so, and (b) they must have already known that the value of their holding is small due to absence of dividend. The market price of share is related to dividend and not to the face or nominal value of the share. It really does not matter, therefore, whether the nominal value of an equity share is ₹1 or ₹100 or ₹1,000 as long as it is not 0. (This does matter in case of preference share holders and debenture holders whose earnings depend on the nominal value). In fact, are construction scheme may be beneficial to the equity share holders by enabling the payment of a dividend on such shares. On this ground, it would be unjust to ask the preference shareholders to accept a sacrifice when the equity share holders improve their position.

There is, however, one important right which the equity shareholders enjoy. This is control over the affairs of the company. The equity share holders will not easily give up this rite, and hence there construction scheme should keep this in mind. The equity share holder may not agree to the conversion of preference share or debenture into equity share even if the holders of preference shares or debenture are willing to accept lower security for their holdings. The equity share holders may agree to this only if there is a threat of the company being wound up (in which case they will lose almost all). It should also be noted that without the consent of the parties their liability cannot be increased. For instances, fully paid shares cannot be converted into partly paid shares without the consent of the shareholders.

The requirements of the working capital must not be overlooked. Cash may require to pay certain dissenting creditor or even to pay arrears of preference dividend. Generally, therefore, a company under reconstruction will have to raise funds to enable it to pay off such dissenters and to carry on its work smoothly. Which of the various parties are willing to subscribe more shares will have to be seen. The equity shareholders will like to consolidate their position by buying more shares. Sometimes, outsiders are willing to subscribe to the shares but they will generally prefer to do so if they are given a controlling share.

Steps:

(1) First of all the total amounts to be written off should be as certained. This would mean totaling up the debit balance of the Profit and Loss account, all fictitious assets like goodwill, preliminary expenses, discount on shares or debentures, any fall in value of assets ,any increase in liabilities and arrears of dividends on cumulative preference shares. If the value of any share can be legitimately increased the amount of loss would then be reduced accordingly. The other way to get at the same figure would be to add up the present value as a going concern, of all the assets and deduct there from the amount of liabilities and also the arrears of dividend on cumulative preference shares. What is left is "net assets". The share capital compared with net assets will show how much amount is to be written off.

(2) The question now arises as to who is to bear the loss. If the net assets are more than the preference share capital, it is obvious the whole of the loss will have to be borne by the equity shareholders. The nominal value of the equity shares should be reduced by a sufficient margin to cover the loss. If the net assets are not sufficient to cover the preference share capital (or if the net assets are just sufficient), the preference share holder will have to accept a sacrifice, although their sacrifice will be smaller than that of the equity share holders. (Equity share holders should not be completely wiped off). If the future earning power of the company permits, the dividend rate should be increased so that, in terms of rupees, the dividend remains unchanged. Thus if 10.5% preference share of ₹100 are converted into preference share of ₹75 each, rate of dividend should be raised to 14%, if possible. In both cases, then the dividend will be ₹ 10.5 per share.

(3) Payment of arrears of dividend (question arises only in case of cumulative preference shares) in cash immediately may present difficulties. In such a case a good method is to issue deposit certificates. This is preferable to issuing shares because (a) it will not upset the voting power and (b) the certificate can be redeemed as soon as opportunity arises. The rate of interest need not be heavy, but of course, it will depend on the future earning capacity of the company.

(4) Debenture holders and other creditors are affected by the reconstruction scheme only if the total assets in the company are insufficient to cover even the liabilities (although they are concerned is necessary to any scheme that may be formulated). In such an eventuality, the creditors (including debenture holders) will have to accept sacrifice unless they think that by sending the company into liquidation we will be able to realize substantial portion of their claims. The share holders, both preference and equity will have to accept a heavy reduction in the value of share but they cannot be expected to agree to complete wiping of the shares, in which case they will have no interest in keeping the company going. In short, the whole scheme should broadly depend upon the expected earning power and upon the position as it likely to obtain if the company is sent to liquidation.

Internal vs. External Reconstruction: Having decided who is to bear how much sacrifice of loss and having settled the broad details of the scheme, and important question remains to be decided. Will the reconstruction be internal or external? Internal reconstruction means that the scheme will be carried out by liquidating the existing company and incorporating immediately another company (with the name only slightly changed such as AB Ltd., to take over the business of the outgoing company. There are advantages in both, but generally internal reconstruction is preferred. The advantages in its favour are:-

(a) Creditors, specially bank over draft and debenture holders, may continue where as they may not if the company is formally liquidated which will involve payment of claims to out siders, If they do not continue, the company may suffer from want of financial assistance. This is, however, only academic since no reconstruction scheme, even internal, will be really formulated without the consent of the bank, debenture holders. etc.

(b) The company will be able to set off its past losses against future profits for income-tax purposes.

This will materially reduce the income-tax liability depending on the losses suffered during the preceding eight years. Losses can be carried forward for eight years provided the business is carried on. The business will technically end when the company is liquidated. Hence, in case of external reconstruction, losses cannot be carried forward for income tax purposes.

The arguments in favour of external reconstruction are as under:-

(a) External reconstruction may be the only way to bring about speedy reconstruction because sometimes a few people hold up the scheme by delaying tactics by means of legal objections.

(b) It may help in raising more finance by issuing to the existing shareholders partly paid shares in the new company. It should be remembered that in internal reconstruction fully paid up shares unless every share holder gives his assent in writing. This may prove cumbersome. However, if share holders are willing to accept partly paid shares in the new company, there is not much reason why they should refuse to buy new shares under a scheme of internal reconstruction.

Legal position as regards external reconstruction:

Sec 319 of the Companies Act permits the liquidator of a company to transfer the whole or any part of the company's business or property to another company and receive from the transferee company for distribution among the shareholders of the company under liquidation. The liquidator must obtain the sanction of the company by a special solution. Any sale of arrangement in pursuance of this section is binding on the members of the transferor company.

But a share holder who has not voted for the special resolution may, within seven days of the resolution, serve a notice on the liquidator expressing his dissent and requiring the liquidator either,(a) to abstain from carrying the resolution in to effect, or (b) to purchase his interest at a price to be determined by agreement or by arbitration.

2.7 DEMERGER – CONCEPT

- The term "demerger" has been defined in the Income-tax Act, 1961. The definition of the term under the IT Act refers back to the provisions of sections 230 to 232 of the Companies Act, 2013, though an exception has been made in case of foreign companies. We know by now that the said sections 230 to 232 deal with a scheme of compromise or/and arrangement duly approved by the company or companies in question and further approved by the Tribunal. The IT Act has made provisions removing certain tax disabilities, often referred to in appropriately in our view, as tax incentives for demerger, to the companies' involved in a demerger and to their shareholders. To avoid some of the disabilities under the Income-tax Act, it is essential that a demerger squarely falls within the definition of the term "demerger" under section 2(19AA) of the IT Act. Section 2(19AA) reads as follows:
- "Demerger", in relation to companies, means the transfer, pursuant to a scheme of arrangement under sections 230 to 232 of the Companies Act, 2013, by a demerged company of its one or more under takings to any resulting company in such a manner that—

  (i) All the property of the under taking, being transferred by the demerged company, immediately before the demerger becomes the property of the resulting company by virtue of the demerger;

  (ii) All the liabilities relatable to the under taking, being transferred by the demerged company, immediately before the demerger becomes the liabilities of the resulting company by –virtue of the demerger;

  (iii) The property and the liabilities of the under taking or under takings being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger;

  (iv) The resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis;

  (v) The share holders holding not less than three – fourths in value of the shares in the demerged company (other than shares already held there in immediately before the demerger, or by a nominee for, the

resulting company or, its subsidiary) become shareholders of the resulting company or companies by virtue of the demerger, otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company;

(vi) The transfer of the under taking is on a going concern basis;

(vii) The demerger is in accordance with the conditions, if any, notified under sub –section (5) of section 72 A by the Central Government in this behalf.

Explanation 1. For the purposes of this clause "undertaking" shall include any part of an under taking or a unit or division of an under taking or a business activity taken as a whole but does not include individual assets or liabilities or any combination thereof not constituting a business activity.

Explanation 2. For the purposes of this clause the liabilities referred to in sub-clause (ii) shall include —

(a) the liabilities which arise out of the activities or operations of the undertaking;

(b) the specific loans or borrowings (including debentures) raised, incurred and utilized solely for the activities or operations of the undertaking; and

(c) in cases, other than those referred to in clause (a) or clause (b), so much of the amounts of general or multipurpose borrowings, if any, of the demerged company as stand in the same proportion which the value of the assets transferred in a demerger bears to the total value of the assets of such demerged company immediately before the demerger.

Explanation 3. For determining the value of the property referred to in sub-clause (iii), any change in the value of assets consequent to their revaluation shall be ignored.

Explanation 4. For the purposes of this clause, the splitting up or there construction of any authority or a body constituted or established under a Central, State – or Provincial Act, or a local authority or a public sector company, into separate authorities or bodies or local authorities or companies, as the case may be, shall be deemed to be a demerger if such split up or reconstruction fulfils such conditions as may be notified in the Official Gazette by the Central Government.

Other related definitions:

Definition of 'demerged company'

Section 2 (19AAA)" demerged company " means the company whose under taking is transferred, pursuant to a demerger, to a resulting company;

Definition of 'resulting company'

Section 2(41A) "resulting company" means one or more companies (including a wholly owned subsidiary there of] to which the under taking of the demerged company is transferred in a demergerand, the resulting company in consideration of such transfer of undertaking, issues shares to the share holders of the demerged company and includes any authority or body or local authority or public sector company or a company established, constituted or formed as a result of demerger.

2.8 REVERSE MERGER

- **A Reverse merger** - at times also referred to as a reverse takeover (RTO) – is a way by which a private company can become a public company and take advantage of the greater financing options available to public companies.

  The reverse merger is an alternative to the traditional IPO (Initial Public Offering) as a method for going public. Reverse takeovers have historically been used by businesses that wish to start trading in a very short time. A reverse merger is a complex method that a private company uses to become a publicly traded corporation.

- Reverse mergers happen when a public company that is no longer actively involved in business and has limited assets (called a Shell Company or Shell Corporation) joins or merges, with a private company. The

private company buys most of the outstanding shares of the shell company, gaining control and seating its own board of directors. The resulting merged business entity becomes a new operating company and may change its name to better reflect the newly merged company's business purpose.

- A reverse merger refers to an arrangement where private company acquires a public company, usually a shell company, in order to acquire the status of a public company. Also known as a reverse takeover, it is an alternative to the traditional initial public offering (IPO) method of floating a public company. It is an easier way that allows private companies to change their type while avoiding the complex regulations and formalities associated with an IPO. Also, the degree of ownership and control of the private stakeholders increases in the public company. It also leads to combining of resources there by giving greater liquidity to the private company.
- Reverse takeovers are one way for a company to go public. Companies interested in going public can go public without the use of Shell Corporation. Our firm takes companies public directly. The going public process is attractive to businesses because after becoming a publicly traded company, the business can use its stock as currency to buy assets and other businesses. Many companies will use the stock of their public company to trade for advertising. Raising capital of ten becomes easier to accomplish as a public company because investors now have a clear exit strategy.
- Reverse merging is the joining together of a public company and a private company. This can speed up the process to become a public company. It is still required by SEC (Securities and Exchange Commission) Form 8 K to provide some of the information that would be in an SEC registration statement.
- Many company directors and officers don't recognize there are other ways for a private company to become publicly traded, outside of doing a traditional IPO (Initial Public Offering) or a reverse merger.
- As a strategy to go public it is not necessary to do a reverse merger. You can do a direct registration of your company. Many of the benefits best owed upon public companies also apply to companies created through a direct registration, to include:
  - The greater choice of financial opportunities available to public companies.
  - An exit strategy for the company directors and founders.
  - Investors are more compelled to invest in a company with a clear exit strategy.
  - The ability to use the company stock as currency to acquire other businesses (M&A).

2.9 EXTERNAL OF RECONSTRUCTION

- Reconstruction means reorganization of a company's financial structure. In reconstruction of a company, usually the assets and liabilities of the company are revalued, the losses suffered by the company are written off by a deduction of the paid-up value of shares and /or varying of the rights attached to different classes of shares and compounding with the creditors. It may be done without liquidating the company and forming a new company in which case the process is called internal reconstruction. However, there may be external reconstruction in which case the undertaking being carried on by the company is transferred to a newly started company consisting substantially of the same shareholders with a view to the business of the transferor company being continued by the transferee company. An attempt is made that the newly started company has a sound financial structure and a good set off assets and liabilities recorded in the books of the transferee company at their fair values.
- From the point of view of an accountant, external reconstruction is similar to amalgamation in the nature of purchase; the books of the transferee company are closed and in the books of the transferee company, the purchase of the business is recorded.
- But otherwise external reconstruction and amalgamation differs as follows:

  (i) In external reconstruction, only one company is involved where as in amalgamation, there are at least two existing companies which amalgamate.

(ii) In external reconstruction, a new company is certainly formed where as in amalgamation a new company may be formed or in the alternative one of the existing companies may take over the other amalgamating company or companies and no new company may be formed.

(iii) The objective of the external reconstruction is to reorganize the financial structure of the company, on the other hand, the objective of the amalgamation is to cut competition and reap the economies of larger scale.

2.10 NOTES AND DISCLOSURE RELATING TO BUSINESS COMBINATION

- The acquirer shall disclose information that enables users of its financial statements to evaluate the nature and financial effect of a business combination that occurs either:
  (a) during the current reporting period; or
  (b) after the end of the reporting period but before the financial statements are approved for issue.
- To meet the above mentioned objective the acquirer shall disclose the following information for each business combination that occurs during the reporting period:
  (a) the name and a description of the acquiree.
  (b) the acquisition date.
  (c) the percentage of voting equity interests acquired.
  (d) the primary reasons for the business combination and a description of how the acquirer obtained control of the acquiree.
  (e) a qualitative description of the factors that make up the goodwill recognised, such as expected synergies from combining operations of the acquiree and the acquirer, intangible assets that do not qualify for separate recognition or other factors.
  (f) the acquisition-date fair value of the total consideration transferred and the acquisition-date fair value of each major class of consideration, such as: (i) cash; (ii) other tangible or intangible assets, including a business or subsidiary of the acquirer;(iii) liabilities incurred, for example, a liability for contingent consideration; and (iv) equity interests of the acquirer, including the number of instruments or interests issued or issuable and the method of determining the fair value of those instruments or interests.
  (g) for contingent consideration arrangements and indemnification assets: (i) the amount recognised as of the acquisition date; (ii) a description of the arrangement and the basis for determining the amount of the payment; and (iii) an estimate of the range of outcomes (undiscounted) or, if a range cannot be estimated, that fact and the reasons why a range cannot be estimated. If the maximum amount of the payment is unlimited, the acquirer shall disclose that fact.
  (h) for acquired receivables: (i) the fair value of the receivables; (ii) the gross contractual amounts receivable; and (iii) the best estimate at the acquisition date of the contractual cash flows not expected to be collected.The disclosures shall be provided by major class of receivable, such as loans, direct finance leases and any other class of receivables.
  (i) the amounts recognised as of the acquisition date for each major class of assets acquired and liabilities assumed.
  (j) for each contingent liability recognised in accordance with paragraph 23, the information required in paragraph 85 of Ind AS 37 Provisions, Contingent Liabilities and Contingent Assets. If a contingent liability is not recognised because its fair value cannot be measured reliably, the acquirer shall disclose: (i) the information required by paragraph 86 of Ind AS 37; and (ii) the reasons why the liability cannot be measured reliably.
  (k) the total amount of goodwill that is expected to be deductible for tax purposes.

(l) for transactions that are recognised separately from the acquisition of assets and assumption of liabilities in the business combination in accordance with paragraph 51: (i) a description of each transaction; (ii) how the acquirer accounted for each transaction; (iii) the amounts recognised for each transaction and the line item in the financial statements in which each amount is recognised; and (iv) if the transaction is the effective settlement of a preexisting relationship, the method used to determine the settlement amount.

(m) the disclosure of separately recognised transactions required by (l) shall include the amount of acquisition-related costs and, separately, the amount of those costs recognised as an expense and the line item or items in the statement of profit and loss in which those expenses are recognised. The amount of any issue costs not recognised as an expense and how they were recognised shall also be disclosed.

(n) in a bargain purchase (see paragraphs 34–36A): (i) the amount of any gain recognised in other comprehensive income in accordance with paragraph 34; (ii) the amount of any gain directly recognised in equity in accordance with paragraph 36A;and (iii) a description of the reasons why the transaction resulted in a gain in case of (i) above.

(o) for each business combination in which the acquirer holds less than 100 per cent of the equity interests in the acquiree at the acquisition date: (i) the amount of the non-controlling interest in the acquiree recognised at the acquisition date and the measurement basis for that amount; and (ii) for each non-controlling interest in an acquiree measured at fair value, the valuation techniques and key model inputs used for determining that value.

(p) in a business combination achieved in stages: (i) the acquisition-date fair value of the equity interest in the acquiree held by the acquirer immediately before the acquisition date; and (ii) the amount of any gain or loss recognised as a result of remeasuring to fair value the equity interest in the acquiree held by the acquirer before the business combination and the line item in the statement of profit and loss in which that gain or loss is recognised.

(q) the following information: (i) the amounts of revenue and profit or loss of the acquiree since the acquisition date included in the consolidated statement of profit and loss for the reporting period; and (ii) the revenue and profit or loss of the combined entity for the current reporting period as though the acquisition date for all business combinations that occurred during the year had been as of the beginning of the annual reporting period. If disclosure of any of the information required by this subparagraph is impracticable, the acquirer shall disclose that fact and explain why the disclosure is impracticable. This Indian Accounting Standard uses the term 'impracticable' with the same meaning as in Ind AS 8 Accounting Policies, Changes in Accounting Estimates and Errors.

- The acquirer shall disclose information that enables users of its financial statements to evaluate the financial effects of adjustments recognised in the current reporting period that relate to business combinations that occurred in the period or previous reporting periods.
- In this regard, the following disclosures should be made.The acquirer shall disclose the following information for each material business combination or in the aggregate for individually immaterial business combinations that are material collectively:

(a) if the initial accounting for a business combination isincomplete for particular assets, liabilities, non-controlling interests or items of consideration and the amounts recognised in the financial statements for the business combination thus have been determined only provisionally: (i) the reasons why the initial accounting for the business combination is incomplete; (ii) the assets, liabilities, equity interests or items of consideration for which the initial accounting is incomplete; and (iii) the nature and amount of any measurement period adjustments recognised during the reporting period.

(b) for each reporting period after the acquisition date until the entity collects, sells or otherwise loses the right to a contingent consideration asset, or until the entity settles a contingent consideration liability or the liability is cancelled or expires: (i) any changes in the recognised amounts, including any differences arising upon settlement; (ii) any changes in the range of outcomes (undiscounted) and the reasons for those changes; and (iii) the valuation techniques and key model inputs used to measure contingent consideration.

(c) for contingent liabilities recognised in a business combination, the acquirer shall disclose the information required by paragraphs 84 and 85 of Ind AS 37 for each class of provision.

(d) a reconciliation of the carrying amount of goodwill at the beginning and end of the reporting period showing separately: (i) the gross amount and accumulated impairment losses at the beginning of the reporting period. (ii) additional goodwill recognised during the reporting period, except goodwill included in a disposal group that, on acquisition, meets the criteria to be classified as held for sale in accordance with Ind AS 105 Noncurrent Assets Held for Sale and Discontinued Operations. (iii) adjustments resulting from the subsequent recognition of deferred tax assets during the reporting period. (iv) goodwill included in a disposal group classified as held for sale in accordance with Ind AS 105 and goodwill derecognised during the reporting period without having previously been included in a disposal group classified as held for sale. (v) impairment losses recognised during the reporting period in accordance with Ind AS 36. (Ind AS 36 requires disclosure of information about the recoverable amount and impairment of goodwill in addition to this requirement.) (vi) net exchange rate differences arising during the reporting period in accordance with Ind AS 21 The Effects of Changes in Foreign Exchange Rates. (vii) any other changes in the carrying amount during the reporting period. (viii) the gross amount and accumulated impairment losses at the end of the reporting period.

(e) the amount and an explanation of any gain or loss recognised in the current reporting period that both: (i) relates to the identifiable assets acquired or liabilities assumed in a business combination that was effected in the current or previous reporting period; and (ii) is of such a size, nature or incidence that disclosure is relevant to understanding the combined entity's financial statements.

2.11 BUSINESS COMBINATIONS OF ENTITIES UNDER COMMON CONTROL

DEFINITIONS

The following terms are used in this Appendix with the meaning specified:

- **Transferor** means an entity or business which is combined into another entity as a result of a business combination.
- **Transferee** means an entity in which the transferor entity is combined.
- **Reserve** means the portion of earnings, receipts or other surplus of an entity (whether capital or revenue) appropriated by the management for a general or a specific purpose other than provision for depreciation.
- **Common control business combination** means a business combination involving entities or businesses in which all the combining entities or businesses are ultimately controlled by the same party or parties both before and after the business combination, and that control is not transitory.

COMMON CONTROL BUSINESS COMBINATION

- Common control business combinations will include transactions, such as transfer of subsidiaries or businesses, between entities within a group.
- The extent of non-controlling interests in each of the combining entities before and after the business combination is not relevant to determining whether the combination involves entities under common control. This is because a partially-owned subsidiary is nevertheless under the control of the parent entity.
- The fact that one of the combining entities is a subsidiary that has been excluded from the consolidated financial statements of the group in accordance with Ind AS 27 is not relevant to determining whether a combination involves entities under common control.
- An entity can be controlled by an individual, or by a group of individuals acting together under a contractual arrangement, and that individual or group of individuals may not be subject to the financial reporting requirements of Ind ASs. Therefore, it is not necessary for combining entities to be included as part of the same consolidated financial statements for a business combination to be regarded as one having entities under common control.

- A group of individuals are regarded as controlling an entity when, as a result of contractual arrangements, they collectively have the power to govern its financial and operating policies so as to obtain benefits from its activities, and that ultimate collective power is not transitory.

METHOD OF ACCOUNTING FOR COMMON CONTROL BUSINESS COMBINATIONS

- Business combinations involving entities or businesses under common control shall be accounted for using the pooling of interests method.
- The pooling of interest method is considered to involve the following:
  - (i) The assets and liabilities of the combining entities are reflected at their carrying amounts.
  - (ii) No adjustments are made to reflect fair values, or recognise any new assets or liabilities. The only adjustments that are made are to harmonise accounting policies.
  - (iii) The financial information in the financial statements in respect of prior periods should be restated as if the business combination had occurred from the beginning of the earliest period presented in the financial statements, irrespective of the actual date of the combination. However, if business combination had occurred after that date, the prior period information shall be restated only from that date.
- The consideration for the business combination may consist of securities, cash or other assets. Securities shall be recorded at nominal value. In determining the value of the consideration, assets other than cash shall be considered at their fair values.
- The balance of the retained earnings appearing in the financial statements of the transferor is aggregated with the corresponding balance appearing in the financial statements of the transferee. Alternatively, it is transferred to General Reserve, if any.
- The identity of the reserves shall be preserved and shall appear in the financial statements of the transferee in the same form in which they appeared in the financial statements of the transferor. Thus, for example, the General Reserve of the transferor entity becomes the General Reserve of the transferee, the Capital Reserve of the transferor becomes the Capital Reserve of the transferee and the Revaluation Reserve of the transferor becomes the Revaluation Reserve of the transferee. As a result of preserving the identity, reserves which are available for distribution as dividend before the business combination would also be available for distribution as dividend after the business combination. The excess, if any, between the amount recorded as share capital issued plus any additional consideration in the form of cash or other assets and the amount of share capital of the transferor is recognised as goodwill in the financial statements of the transferee entity; in case of any deficiency, the same shall be treated as Capital Reserve.

DISCLOSURE

The following disclosures shall be made in the first financial statements following the business combination:

(a) names and general nature of business of the combining entities;

(b) the date on which the transferor obtains control of the transferee;

(c) description and number of shares issued, together with the percentage of each entity's equity shares exchanged to effect the business combination; and

(d) the amount of any difference between the consideration and the value of net identifiable assets acquired, and the treatment thereof.

[A] Computation of Purchase Consideration

Illustration 1.

The Oil Shell Ltd. was incorporated on1st April 2016 for the purpose of acquiring P Ltd., Q. Ltd., and R Ltd.

The Balance sheet of these companies as on 31st March 2016 are as follows:

(₹)

Particulars	PLtd. ₹	QLtd. ₹	RLtd. ₹
Assets			
Tangible Fixed assets - at cost less depreciation	50,00,000	40,00,000	30,00,000
Goodwill		6,00,000	
Other Assets	20,00,000	28,00,000	8,50,000
Total	**70,00,000**	**74,00,000**	**38,50,000**
Liabilities			
Issued Equity Share Capital (shares of ₹10 each)	40,00,000	50,00,000	25,00,000
Profit and Loss A/c	15,00,000	11,00,000	6,00,000
10% Debentures	7,00,000		4,00,000
Sundry Creditors	8,00,000	13,00,000	3,50,000
Total	**70,00,000**	**74,00,000**	**38,50,000**

Average annual profits before debentures interest (April 2014 to March 2016 inclusive)	9,00,000	12,00,000	5,00,000
Professional valuation of tangible assets on 31st March 2016	62,00,000	48,00,000	36,00,000

1. The directors in their negotiations agreed that:
   - (i) the recorded goodwill of Q Ltd. is valueless;
   - (ii) the "Other assets" of P Ltd. are worth ₹3,00,000;
   - (iii) the valuation of 31st March 2016 in respect of tangible Fixed assets should be accepted.
   - (iv) these adjustments are to be made by the individual company before the completion of the acquisition.
2. The acquisition agreement provided for the issue of 12% Unsecured Debentures to the value of the net assets of companies P Ltd., Q Ltd. and R Ltd., and for the issuance of ₹100 nominal value equity shares for the capitalized average profit of each acquired company in excess of net assets contributed. The capitalisation rate is established at 10%.

You are required to:

(i) Compute Purchase Consideration.

(ii) Discharge of Purchase Consideration.

Solution:

Computation of Purchase Consideration

WN#1: Consideration in the form of 12% Debentures

Particulars	P Ltd.		Q Ltd.		R Ltd.	
	(₹)	(₹)	(₹)	(₹)	(₹)	(₹)
A. **Assets**						
i. Tangible Fixed Assets (as valuation)	62,00,000		48,00,000		36,00,000	
ii. Other Assets (as per directors negotiation)	3,00,000	65,00,000	28,00,000	76,00,000	8,50,000	44,50,000
B. **Liabilities**						
i. Sundry Creditors	8,00,000		13,00,000		3,50,000	
ii. 10% Debentures	7,00,000	(15,00,000)	__	(13,00,000)	4,00,000	(7,50,000)
C. **Net Assets (A-B)**		50,00,000		63,00,000		37,00,000
D. 12% Debentures to be issued.		50,00,000		63,00,000		37,00,000

WN#2: Consideration in the form of Equity Shares

Particulars	P Ltd. ₹	Q Ltd. ₹	R Ltd. ₹
a. Average annual profit before debenture interest (given)	9,00,000	12,00,000	5,00,000
b. Debenture interest (on 10% Debentures)	70,000	—	40,000
c. Profit after debentures interest (a-b)	8,30,000	12,00,000	4,60,000
d. Capitalisation rate	10%	10%	10%
e. Capitalised average profit(c/d)	83,00,000	1,20,00,000	46,00,000
f. Net Assets takeover (WN # 1(c))	50,00,000	63,00,000	37,00,000
g. Excess of capitalised average profit over net assets taken over (e-f)	33,00,000	57,00,000	9,00,000

WN#3: Summary of Purchase Consideration

Particulars	P Ltd. ₹	Q Ltd. ₹	R Ltd. ₹
a. 12% Debentures of Oil Shell Ltd. each @ ₹100/- [WN # 1(d)	50,00,000	63,00,000	37,00,000
b. Equity shares of ₹100 each of Oil Shell Ltd. [WN # 2(g)	33,00,000	57,00,000	9,00,000
c. Total Consideration	**83,00,000**	**1,20,00,000**	**46,00,000**

Illustration 2.

The extracts of Trial Balance of Sukh Ltd. and Sari Ltd. As on 31.03.2015 are as under:

Particulars	Sukh Ltd.		Sari Ltd.	
	Debit (₹)	Credit (₹)	Debit (₹)	Credit (₹)
Equity Share Capital (in shares of ₹100 each)		24,00,000		12,00,000
8% Preference Share Capital (in shares of ₹100 each)		8,00,000		
10% Preference Share Capital (in shares of ₹100 each)				4,00,000
Reserves		30,00,000		24,00,000
Current Liabilities		18,00,000		10,00,000
Fixed Assets	55,00,000		30,00,000	
Current Assets	25,00,000		20,00,000	
Total	80,00,000	80,00,000	50,00,000	50,00,000

A. The following information is provided for the year 2014-15:

Particulars	Sukh Ltd. (₹)	Sari Ltd. (₹)
(a) Profit before tax	10,64,000	4,80,000
(b) Taxation	4,00,000	2,00,000
(c) Preference Dividend	64,000	40,000
(d) Equity Dividend	2,88,000	1,92,000

B. The equity shares of both the companies are quoted in the market. Both the companies are carrying on similar manufacturing operations.

C. Sukh Ltd. purposes to absorb Sari. Ltd. as on 31.03.2015. The terms of absorption are as under:

(a) Preference shareholders of Sari Ltd. will receive 8% preference shares of Sukh Ltd. sufficient to increase the income of preference shareholders of Sari Ltd. by 10%.

(b) The equity shareholders of Sari Ltd. will receive equity shares of Sukh Ltd. on the following basis:

(i) The equity shares of Sari Ltd. Will be valued by applying to the earning per share of Sari Ltd. 75% of price earnings ratio of Sukh Ltd. based on the results of 2014-15 of both the companies.

(ii) The market price of equity shares of Sukh Ltd. is ₹300 per share.

(iii) The number of shares to be issued to the equity shareholders of Sari Ltd. will b based on the above market value.

(iv) In addition to equity shares, 8% preference shares of Sukh Ltd. will be issued to the equity shareholders of Sari Ltd. to make up for the loss in income arising from the above exchange of shares based on the dividends for the year 2014-15.

D. For the next two years, no increase in the rate of equity dividend is expected. You are required to calculate purchase consideration.

Solution:

Calculation of Purchase Consideration

A. Preference Shareholders Consideration:

Particulars	₹
Present Income of 10% Preference Share Capital = 10% on ₹4,00,000	40,000
Income Required in future (Present income + 10% increment) = 40,000 + (40,000 x 10%)	44,000
Amount of 8% preference shares to maintain the above Income = (₹44,000/8%)	5,50,000

B. Equity Shareholders Consideration

(i) Consideration by way of equity shares

Valuation of shares of Sari Ltd. (12,000 x ₹180) = ₹21,60,000

No. of equity shares to be issued ₹21,60,000/ ₹300 = 7,200

(a) Share capital (7,200 x ₹100) = ₹7,20,000

(b) Share Premium (7,200 x ₹200) = ₹14,40,000

(ii) Consideration by way of preference shares:

(a)	Current Equity dividend from Sari Ltd	₹1,92,000
(b)	Less: Expected equity dividend (₹ 2,88,000 / ₹ 24,00,000) × ₹7,20,000	₹86,400
(c)	Loss in income	₹1,05,600
(d)	Value of 8% preference shares to be issued (₹1,05,600/8%)	₹13,20,000

C. Total Purchase Consideration= ₹(5,50,000+21,60,000+13,20,000) = ₹40,30,000.

Working Notes:

Computation of EPS:

Particulars	**Sukh Ltd. (₹)**	**Sari Ltd. (₹)**
Profit Before Tax	10,64,000	4,80,000
Less: Tax	4,00,000	2,00,000
Profit After Tax	6,64,000	2,80,000
Less: Preference Dividend	64,000	40,000
Profit Available to Equity Shareholders	6,00,000	2,40,000
No. of Equity Shares .	24,000	12,000
EPS	25	20

P/E ratio of Sukh Ltd.= Market Price/ EPS = ₹300/₹25 = 12 times

75% of P/E ratio = (12 x 0.75) = 9 times Value per share of Sari Ltd. = EPS x P/E ratio = (₹20 x 9) = ₹180

Illustration 3.

Tom Ltd. holds 45% of the paid up share capital of Bee Ltd. The shares were acquired at market price of Rs.18 per share. The balance 55% shares of Bee Ltd. are held by a foreign collaborating company. A memorandum of understanding has been entered into with the foreign company providing for the following:

(i) The shares held by foreign company will be sold to Torn Ltd. The price per share will be calculated by capitalizing the yield at 20%. Yield, for this purpose, would mean 50% of the average of pre-tax profits for last 3 years, which were ₹ 35 lakhs, ₹40 lakhs and ₹45 lakhs.

(ii) The actual cost of the shares to the foreign company was 6,00,000. The profit that would accrue to them would be taxable at an average rate of 25%. The tax payable will be deducted Iron the proceeds and Tom Ltd. will pay it to government.

(iii) Out of the net consideration, 50% wouid be remitted to be foreign company immediately and the balance will be an unsecured loan repayable after three years. The above agreement was approved by all concerned for being given effect to on 01.04.2015.

The total assets of Bee Ltd as on 31 .03.2015 were ₹1,10,00,000. It was decided to write down fixed assets by ₹2,10,000. Current Liabilities of Bee Ltd. as on the same date were 40,00,000. The paid- up sha.re capital of Bee Ltd. was ₹20,00,000 divided into 2,00,000 equity shares of 10 each.

Required:

(1) Compute purchase consideration.

(2) Prepare statement showing discharge of purchase consideration, and

(3) Find out Goodwill/Capital Reserve to Tom Ltd. on acquiring wholly the shares of Bee Ltd.

Solution:

1. Calculation of Purchase Consideration

(a)	Yield of Bee Ltd: $\left[\frac{35+40+45}{3} \times \frac{50}{100}\right]$	₹20 lakhs
(b)	Price per share of Bee Ltd: Capitalized yield [₹ 20,00,000 x 100/20]	₹100 Lakhs
	No. of shares	2,00,000
	Price per share	₹50
(c)	Purchase consideration for 55% shares in Bee Ltd (2,00,000 shares x 55/1 00 x 50)	₹55 Lakhs

2. Statement showing discharge of Purchase Consideration

Particulars	**Amount (₹)**
Payment to Government (as tax) on behalf of Foreign Company [₹55 Lakhs-₹6 Lakhs] x 25/100	12,25,000
Payment to Foreign Company i.e. @ 50% of (₹55,00,000 -₹1 2,25,000)	21,37,500
Unsecured. Loan owed to Foreign Company (repayable after 3 years)	21,37,500
Total Purchase Consideration	55,00,000

3. Calculation of Goodwill/ Capital Reserves:

Particulars	Amount (₹)
Net Assets Acquired	
Total Assets	1,10,00,000
Less: Fixed Assets written down	(2,10,000)
Less: Current Liabilities	(40,00,000)
Amount of Net Assets Acquired	67,90,000
Less: P.C. Paid	
To Foreign Company	55,00,000
To own cost of investment	16,20,000
Goodwill	3,30,000

Illustration 4.

ANKIT LTD. agreed to absorb SHRIJA LTD. on March .31, 2015 whose summarized Balance Sheet Stood as follows:

(Amount in ₹ '000')

Equity and liabilities	Amount (₹)	Assets	Amount (₹)
Share Capital:		Fixed Assets	2,100
2,40,000 shares of ₹10 each fully paid	2,400	Investments.	
Reserves & Surplus:		Current Assets, Loans and Advances;	
General Reserve	300	Stock in Trade	300
Secured Loan	---	Sundry Debtors	600
Unsecured Loan	---		
Current Liabilities & Provisions:	300		
Sundry Creditors	3,000		3,000

The Consideration was agreed to be paid as follows:

(i) A payment in cash of ₹5 per share in SHRIJA LTD., and

(ii) The issue of shares of ₹10 each in ANKIT LTD. on the basis of two equity shares (valued at ₹15) and one 10% cum-preference share (valued at ₹10) for every five shares held in SHRLIA LTD. The, whole of the share capital consists of shareholding in exact multiple of five, except .the following, holdings:

A	348
B	228
C	216
D	84

Other Individuals 24 (Twenty four members holding one share each)

It was agreed that ANKIT LTD. will pay in cash for fractional shares equivalent at agreed value of share in SHRIJA LTD. i.e. ₹65 for five shares of ₹50 paid.

Required:

Prepare a statement showing the purchase consideration receivable by shareholders in shares and cash.

Solution:

1. Analysis of Fractional Holdings and Exchange of Shares:

Name of Shareholder	Shares held	Exchangeable In Multiples of five	Exchange in Equity Shares	Exchange in Preference Shares	Non exchangeable
A	348	345	345 x 2/5 = 138	345 x115 =69	3
B	228	225	225 x 2/5 = 90	225 x115 45	3
C	216	215	215 x 2/5 =86	215x1/5=43	1
D	84	80	80 x 2/5 = 32	80x1/5=16	4
O	24	---	---	---	24
Total	900	865	346	173	35

2. Computation of Shares Exchangeable

Particulars	Shares in Shrija Ltd.	Equity shares of Ankit Ltd.	Preference Shares of Ankit Ltd.
Fractional	900	346	173
Holding (as, per Table 1.) Other Holdings	2,40,000 – 900	2,39,100 x 2/5	2,39,100 x 1/5
	= 2,39,100	= 95,640	= 47,820
Total	2,40,000	95,986	47,993

3. Cash Payment for Fractional Holding: There are 35 shares in Shrija Ltd, which are not capable of exchange into Equity and Preference shares of Ankit Ltd. Hence, they will be paid cash as 350 x 65/50= 455

4. Statement showing Purchase Consideration:

Particulars	₹
95,986 Equity Shares at ₹15 each	14,39,790
47,993 Preference Shares at ₹10 each	4,79,930
Cash for 2,39,965 shares @ ₹5	11,99,825
Cash for 35 shares fractional holding non exchangeable	455
Total	31,20,000

Illustration 5.

X Ltd. agreed to takeover Y Ltd. as on 1 October, 2015. No Balance Sheet of Y Ltd. was prepared on that date:

Summarised Balance Sheets of X Ltd. and Y Ltd. as at 31st March, 2015 were as follows:

Liabilities	X Ltd (₹)	Y Ltd (₹)	Assets	X Ltd (₹)	Y Ltd (₹)
Equity of ₹10 each fully paid	20,00,000	15,00,000	Fixed assets	15,50,000	12,60,000
Reserves and Surplus:			Current Assets:		
Reserve	3,90,000	3,40,000	Stock	5,35,500	3,81,500
Profit & Loss A/c	3,30,000	1,60,000	Debtors	3,49,500	2,31,000
Creditors	85,000	75,000	Bank	3,40,000	1,80,000
			Miscellaneous Expenditure:		
			Preliminary Expenses	30,000	22,500
Total	28,05,000	20,75,000	Total	28,05,000	20,75,000

Additional information available:

(i) For the six months period from 15th April 2015, X Ltd. and Y Ltd. made profits of ₹ 5,40,000 and ₹ 3,60,000 respectively, after writing off depreciation @ 10% per annum on their fixed assets.

(ii) Both the companies paid on 1 August 2015, equity dividends of 10%. Dividend tax at 15% was paid, by each of them on such payments.

(iii) Goodwill of Y Ltd. was valued at ₹1,68,900 on the date of takeover. Stock of Y Ltd., subject to an abnormal item of 8,500 to be fully written off, would be appreciated 'by 20% for purpose of takeover.

(iv) X Ltd. would issue to Y Ltd.'s shareholders fully paid equity shares of ₹10 each, on the basis of the comparative intrinsic values of the shares on the date of takeover.

You are required to:

(1) Calculate Purchase consideration payable by X Ltd.

(2) Calculate Number of shares to be issued by X Ltd. to Y Ltd.

(3) Ascertain closing bank balance which will appear in the Balance Sheet of X Ltd. (After absorption of Y Ltd.).

Solution:

1. Computation of cash and bank balance of the Companies as on 1st October

Particulars	**X Ltd. (₹)**	**Y Ltd.(₹)**
Balance as on 1st April	3,40,000	1,80,000
Add: Net Profit during the 6 months	5,40,000	3,60,000
Add: Depreciation for 6 months (15,50,000 x 10% x 6/12) & (12,60,000 x 10% x 6/12)	77,500	63,000
Total of above	9,57,500	6,03,000
Less: Dividend paid	2,00,000	1,50,000
Less: Dividend distribution Tax @15%	30,000	22,500
Balance as on 30th September	7,27,500	4,30,500

2. Computation of Net Assets of X Ltd and V Ltd. as on 1st October

Particulars	**X Ltd. (₹)**	**Y Ltd. (₹)**
Goodwill (at agreed value)	---	1,68,900
Fixed Assets (Book Value- Depreciation @10% for 6 months)	14,72,500	11,97,000
Debtors	3,49,500	2,31,000
Stock (including appreciation @ 20%)	5,35,500	4,47,600
Cash and Bank balances as computed above	7,27,500	4,30,500
Total Assets	30,85,000	24,75,000
Less: Creditors	85,000	75,000
Value of Net Assets as per books as on 1st October	30,00,000	24,00,000
No: of equity shares	2,00,000	1,50,000
Intrinsic value per share	₹15	₹16

So, purchase consideration payable by X Ltd. will be ₹24,00,000.

3. Calculation of Number of shares to be issued by X Ltd. to Y Ltd —

Number of shares to be issued by X Ltd. to Y Ltd. = ₹24,00,000/₹15 per shares = 1,60,000 shares.

Illustration 6.

Gold Ltd. agreed to absorb Silver Ltd. on 31st March, 2014, whose Balance Sheet stood as follows:

Liabilities	₹	Assets	₹
1,60,000 equity shares of ₹100 each fully paid up	1,60,00,000	Fixed Assets	1,40,00,000
Reserves and Surplus:		Current Assets,	
General Reserve	20,00,000	Loans & Advances:	
Current Liabilities and Provisions:		Stock in trade	20,00,000
Sundry Creditors	20,00,000	Sundry Debtors	40,00,000
Total	2,00,00,000		2,00,00,000

The consideration was agreed to be paid as follows:

(i) A payment in cash of ₹ 50 per share in Silver Ltd. and

(ii) The issue of shares of ₹100 each in Gold Ltd., on the basis of four equity shares (valued at ₹150 each) and two 9% cumulative preference shares (valued at ₹100 each) for every ten shares held in Silver Ltd.

It was agreed that Gold Ltd. will pay cash for fractional shares equivalent at agreed value of shares in Silver Ltd. i.e., ₹1,300 paid for ten shares of ₹1,000. The whole Share capital consists of shareholdings in exact multiple of ten, except the following holdings:

	No. of Shares held	
Anal	232	
Bimal	152	
Chinu	144	
Debu	56	
Other individuals	16	(eight members holding two shares each)
	600	

Prepare a statement showing the purchase consideration receivable by above shareholders in shares and cash.

Solution:

Statement of Purchase Consideration:

	Particulars	₹	₹
(a)	In Shares:		
	(i) 63,988 equity shares@ ₹150 each	95,98,200	
	(ii) 31,994 preference shares @ ₹100 each	31,99,400	1,27,97,600
(b)	In Cash (W.N.3)		80,02,400
	Total		**2,08,00,000**

Working Notes:

1. Statement of consideration paid for fraction shares

	Particulars	Anal	Bimal	Chinu	Debu	Others	Total
(a)	Holding of shares	232	152	144	56	16	600
(b)	Non-exchangeable shares (payable in cash)	2	2	4	6	16	30
(c)	Exchangeable shares (a-b)	230	150	140	50	-	570
(d)	Above shares						
	(i) In equity shares (4:10)	92	60	56	20	-	228
	(ii) In preference shares (2:10)	46	30	28	10	-	114

2. Number of shares to be issued

(a) Exchangeable shares:

= Total Shares- Non exchangeable shares

= 1,60,000 - 30 = 1,59,970

(b) Equity shares to be issued (4 shares for every 10 shares)

= 1,59,970/10 x 4

= 63,988

(c) Preference shares to be issued (2 shares for every 10 shares)

= 1,59,970/10x2

= 31,994

3. Cash to be paid

Particulars	₹
1,59,970 shares @ ₹ 50 each	79,98,500
Consideration for non-exchangeable shares (30 x ₹100) x ₹1,300/₹1,000	3,900
Total	80,02,400

4. Statement of Purchase Consideration:

Particulars	₹	₹
A. In shares:		
(i) 63,998 Equity Shares @ ₹150 each	95,99,700	
(ii) 31,994 9% Preference Shares of ₹100 each	31,99,400	127,99,100
B. In Cash (WN#3)		80,02,400
Total (A+B)		**2,08,01,500**

[B] Purchase Consideration & Drafting of Balance Sheet

Illustration 7.

The summarised Balance Sheets of A Ltd. and B Ltd. as on 31st March, 2015 are given below. B Ltd. was merged with A Ltd. with effect from 31st March, 2015 and the merger was in the nature of purchase:

Summarised Balance Sheets as on 31.03.2015

Liabilities	A Ltd. (₹)	B Ltd. (₹)	Assets	A Ltd. (₹)	B Ltd. (₹)
Share Capital:			Fixed assets	10,00,000	4,50,000
Equity Shares of ₹ 10 each	8,00,000	3,00,000	Investments (Non-trade)	1,50,000	50,000
General Reserve	3,00,000	2,00,000	Stock	1,60,000	50,000
Profit & Loss A/c	2,50,000	80,000	Debtors	80,000	90,000
12% Debentures	2,00,000	1,00,000	Advance Tax	60,000	30,000
Sundry Creditors	50,000	50,000	Cash and Bank Balance	2,30,000	1,10,000
Provision For Taxation			Preliminary Expenses	20,000	--
Total	17,00,000	7,80,000	Total	17,00,000	7,80,000

A Ltd. would issue 12% Debentures to discharge the claims of the debenture holders of B Ltd. at par. Non-trade investments of A Ltd. fetched @ 20% while those of B Ltd. fetched @ 12%. Profit (Pre-tax) by A Ltd. and B Ltd. during 201 2-13, 2013-14 and 2014-15 were as follows:

Year	A Ltd. (₹)	B Ltd. (₹)
2012-13	6,00,000	2,00,000
2013-14	7,00,000	2,50,000
2014-15	5,00,000	1,50,000

Goodwill may be calculated on the basis of capitalisation method taking 20% as the pre-tax normal rate of return. Purchase consideration is discharged by A Ltd. on the basis of intrinsic value per share.

Prepare Balance Sheet of A Ltd. after merger as per revised Schedule III .

Solution:

1. Calculation of Net Assets (Closing Capital Employed)

Particulars	A Ltd. (₹)	B Ltd. (₹)
Sundry Assets as per Balance Sheet	17,00,000	7,80,000
Less: Preliminary Exps.	20,000	---
Less: Non -Trade Investment	1,50,000	50,000
Less: Creditors	60,000	50,000
Less: 12% Debentures	2,00,000	1,00,000
Less: Provisions for Taxations	90,000	50,000
Net Capital Employed	11,80,000	5,30,000

2. Calculation of goodwill:

Particulars	A Ltd. (₹)	B Ltd. (₹)
Total of profits for the 3 years	18,00,000	6,00,000
Simple Average Profits	6,00,000	2,00,000
Less: Non -Trade Investment	30,000	6,000
Average income from capital employed	5,70,000	1,94,000
Capitalized value of Average Profits = Average Income from capital employed/20%	28,50,000	9,70,000
Net Capital Employed (From Table 1)	11,80,000	5,30,000
Goodwill	16,70,000	4,40,000

3. Calculation of Intrinsic value

Particulars	A Ltd. (₹)	B Ltd. (₹)
Net Capital Employed	11,80,000	5,30,000
Add: Non Trade Investment	1,50,000	50,000
Add: Goodwill	16,70,000	4,40,000
Total	30,00,000	10,20,000
No. of shares	80,000	30,000
Intrinsic value Per Share	₹ 37.50	₹34
Capitalized value of Average Profits average Income from capital employed/20%	28,50,000	9,70,000
Net Coital Employed (From Table 1)	11,80,000	5,30,000
Goodwill	16,70,000	4,40,000

4. Calculation of Purchase Consideration

Purchase Consideration = 30,000 shares at ₹ 34 per share = ₹1 0,20,000 Discharged By A Ltd.: = By issue of its own 27,200 shares of 10 @ ₹ 37.50.

Balance Sheet of A Ltd.

as at 1st April 2015

	Particulars	Note No.	Amount (₹)
I.	**Equity and Liabilities**		
	1. Shareholders' Funds		
	(a) Share Capital	1	10,72,000
	(b) Reserves and Surplus	2	12,78,000
	2. Non-Current Liabilities : 12% Debentures		3,00,000
	(₹ 200000 + ₹ 100000)		
	3. Current Liabilities		
	(a) Creditors (60,000 + 50,000)		1,10,000
	(b) Provision for Tax		1,40,000
	Total		29,00,000
II.	**Assets**		
	1. Non-Current Assets		
	(a) Fixed Assets		
	(i) Tangible Assets		14,50,000
	(ii) Intangible Assets -Goodwill		4,40,000
	(b) Non-current investment (1,50,000 ÷ 50,000)		2,00,000
	2. Current Assets	3	8,10,000
	Total		29,00,000

[Relevant Notes]

1. Share Capital

Particulars	Amount (₹)
Authorized, issued, subscribed and paid up capital of 1,07,200 Equity Shares of ₹10 each(of the above 27,200 shares were issued to vendors for non cash consideration)	10,72,000
Total	**10,72,000**

2. Reserves and Surplus

Particulars	Amount (₹)
Securities Premium (@ ₹ 27.5 on 27,200 shares)	7,48,000
Profit & Loss A/c	3,00,000
General Reserve	2,50,000
Total	12,98,000
Less: Preliminary Expenses (assumed) written off	(20,000)
Total	**10,72,000**

3. Other Current Assets

	Particulars	Amount (₹)
(a)	Stock [1,60,000 + 50,000]	2,10,000
(b)	Sundry Debtors [80,000 + 90,000]	1,70,000
(c)	Advance Tax [60,000 + 30,000]	90,000
(d)	Cash and Bank [2,30,000 +1,10,000]	3,40,000
Total		**8,10,000**

Illustration 8.

X Ltd. and Y Ltd. were amalgamated on and from 1 April, 2014. A new company Z Ltd. was formed to take over the business of the existing companies. The summarised Balance Sheets of X Ltd. and Y Ltd. as on 31 March, 2014 are given below:

(₹in Lakhs)

Liabilities	X Ltd. ₹	Y Ltd. ₹	Assets	X Ltd. ₹	Y Ltd. ₹
Share Capital			Fixed Assets:		
Equity shares of ₹ 100 each	800	750	Land and Building	550	400
12% Preference shares of ₹100 each	300	200	Plant and Machinery	350	250
Reserves and Surplus:			Investments	150	50
Revaluation Reserve	200	150	Current Assets, Loans and Advances:		
General Reserve	170	150	Stock	350	250
Profit and Loss Account	50	30	Sundry Debtors	250	300
Secured Loans:			Bills Receivables	50	50
10% Debentures (₹100 each)	60	30	Cash and Bank	300	200
Current Liabilities and Provisions:					
Sundry Creditors	270	120			
Bills payables	150	70			
Total	2,000	1,500	Total	2,000	1,500

Additional Information:

(1) 10% Debenture holders of X Ltd., and Y Ltd., are discharged by Z Ltd., issuing such number of its 15% Debentures of ₹100 each, so as to maintain the same amount of interest.

(2) Preference shareholders of the two companies are issued equivalent number 15% preference shares of Z Ltd., at a price of ₹150 per share (face value of ₹100).

(3) Z Ltd. will issue 5 equity shares for each equity share of X Ltd. and 4 equity shares for each equity share of Y Ltd. The shares are to be issued ₹30 each, having a face value of ₹10 per share.

Prepare the Balance Sheet of Z Ltd. as on 1 April, 2014 in the revised Schedule III format, after amalgamation has been carried out on the basis of amalgamation in the nature of purchase.

Solution:

1. Computation of Purchase Consideration (₹in lakhs)

Particulars	X Ltd.(₹)	Y Ltd.(₹)
Preference Share Holders : 3,00,000 shares of ₹150 each	450	
: 2,00,000 shares of ₹ 150 each		300
Equity Share Holders : 5 x 8,00,000 shares of ₹ 30 each	1,200	
: 4 x 7,50,000 shares of ₹ 30 each		900
Total	1,650	1,200

2. Computation of Securities Premium (₹ in lakhs)

Particulars	Share Capital	Securities premium	Total
Preference Share Capital = (3,00,000 + 2,00,000) = 5,00,000 shares	₹100 each = 500	At ₹50 each = 500	750
Equity Share Capital = (40,00,000 + 30,00,000) = 70,00,000 shares	₹10 each = 700	At ₹20 each = 1,400	2100
Total		1,650	

3. Issue of Debentures (₹ in lakhs)

Particulars	X Ltd.	Y Ltd.	Total
15% debentures for 10% old debentures	[₹60 x 10%/15%]=₹40	[₹30 x 10%/15%] = ₹20	₹60

4. Computation of Goodwill / Capital Reserve (₹ in lakhs)

Particulars	X Ltd.	Y Ltd.
Purchase Consideration	1,650	1,200
Less: Net assets taken over	1,540	1,290
Goodwill	110	
Capital Reserve		90
Net Goodwill	(110-90) = 20	

Balance Sheet of Z Ltd.
(As at 1st April 2014)

(₹ in lakhs)

	Particulars	Note No.	Amount (₹ in Lakhs)
I.	EQUITY AND LIABILITIES		
	(1) Shareholders' Funds		
	(a) Share Capital	1	1,200
	(b) Reserves and Surplus (Securities Premium)		1,650
	(2) Non-current Liabilities: Long term Borrowings	2	60
	(3) Other Current Liabilities	3	610
	Total		**3,520**
II.	ASSETS		
	(1) Non-current Assets		
	(a) Fixed Assets		
	(i) Tangible Assets	4	1,550
	(ii) Intangible Assets(Goodwill)		20
	(b)Non-current investment	5	200
	(2) Current Assets Other Current Assets	6	1,750
	Total		**3,520**

[Relevant Notes]

1. Share Capital

Particulars	Amount (₹ in Lakhs)
Authorized, issued, subscribed and paid up capital:	
(a) 70,00,000 equity shares of ₹10each	700
(b) 5,00,000 preference shares of ₹100 each	500
Total	1,200

2. Non Current Liabilities

Particulars	Amount (₹ in Lakhs)
15% Debentures of ₹100	60
Total	60

3. Other Current Liabilities

Particulars	Amount (₹ in Lakhs)
Sundry Creditors (270 + 120)	390
Bills payable (150 + 70)	220
Total	610

4. Tangible Assets:

Particulars	Amount (₹ in Lakhs)
(a) Plant and Machinery [350 + 250]	600
(b) Land and Building [550 + 4001]	950
Total	1,500

5. Non Current Investments

Particulars	Amount (₹ in Lakhs)
Investment [150+50]	200
Total	200

6. Other Current Assets

Particulars	Amount (₹ in Lakhs)
(a) Stock [350 + 250]	600
(b) Sundry Debtors [250 + 300]	550
(c) Bills receivable [50 + 50]	100
(d) Cash and Bank [300 + 200]	500
Total	1,750

[C] Accounting in the Books of Vendor/ Transferor Company

Illustration 9.

The following is the summarized position of assets and liabilities of Moonlite Ltd. as on 31st March, 2016:

Liabilities	₹	Assets	₹
Share Capital	20,00,000	Patents & trademarks	1,90,000
General reserve	1,40,000	Factory land and building	10,00,000
P & L A/c	85,000	Vehicles	2,10,000
Plant replacement reserve	1,00,000	Inventories	4,20,000
Provision for unexpired Warranties	20,000	Sundry debtors	4,80,000
Sundry creditors	55,000	Cash in hand	30,000
		Cash at bank	70,000
	24,00,000		24,00,000

Notes:

(1) Share capital consists of 20,000 equity shares of ₹100 each, fully paid up.

(2) A customer has lodged a claim for 5,000 towards defective parts purchased from the company, which Moonlite Ltd. has decided to meet from the provision for warranties.

Moonlite Ltd. is taken over by Sunshine Ltd. as at the, closure, of business hours on 31.03.2008. All assets and liabilities (excepting cash) are taken over. Land and building are valued at ₹ 12.00,000 prior to the acquisition. Expenses of absorption amount to ₹60,000 which are borne by Moonlite Ltd. and Sunshine Ltd. in the ratio of 4: 6.

Show the journal entries in the books of Moonlite Ltd., assuming that entire sale consideration of 30 lacs was met by Sunshine Ltd. in the form of equity shares of ₹10 each in their company.

Solution:

Books of Moonlight Ltd.

Journal

Particulars		Dr (₹ in Crore)	Cr. (₹ in Crore)
Factory Land & Building A/c	Dr.	2,00,000	
To Revaluation Reserve A/c			2,00,000
(Being the Revaluation of the factory Land & Building)			
Provision for Unexpired Warranties A/c	Dr.	5,000	
To Compensation to Customer A/c			5,000
(For meeting the claim of a customer for defective part)			
Realization A/c	Dr.	25,70,000	
To Patent & Trademarks A/c			1,90,000
To Factory Land & Building A/c			12,00,000
To Vehicles A/c			2,10,000
To Intangibles A/c			4,20,000
To Sundry debtors A/c			4,80,000
To Cash at bank A/c			70,000
(Being transferring the various Assets to realization A/c on acquisition of company Sunshine Ltd.)			
Provision for Unexpired Warranties A/c.	Dr.	15,000	
Sundry Creditors A/c	Dr.	55,000	
To Realization A/c			70,000
(Being transferring the provision for warranties and the sundry creditors' to realization A/c)			
Realization A/c	Dr.	24,000	
To Cash A/c			24,000
(Being the expenses of Liquidation of ₹60,000, 40% of which is borne by Moonlight Ltd.)			
Sunshine Ltd. A/c	Dr.	30,00,000	
To Realization A/c			30,00,000
(Being the consideration due from Sunshine Ltd. As per agreement dated…..)			
Shares in Sunshine Ltd. A/c	Dr.	30,00,000	
To Sunshine Ltd.			30,00,000
(Being receipt of shares from Sunshine Ltd. for meeting the absorption terms)			
Share Capital A/c	Dr.	20,00,000	
General Reserve A/c	Dr.	1,40,000	
Profit & Loss A/c	Dr.	85,000	
Plant Replacement Reserve A/c	Dr.	1,00,000	
Revaluation Reserve A/c	Dr.	2,00,000	
Realization A/c	Dr.	4,76,000	
To Sundry Shareholders A/c			30,01,000
(Being the above are transferred to Shareholders Account)			
Shareholders A/c	Dr.	30,01,000	
To Share in Sunshine Ltd. A/c			30,00,000
To Cash A/c			1,000
(Being payment to the shareholders Moonlight Ltd. of their Dues)			

[D] Accounting in the Books of Acquirer/Transferee Company

Illustration 10.

On 1st April, 2014 Hero Ltd. was incorporated with an authorised capital of ₹1,000 lakhs. It issued to its promoters equity capital of ₹ 50 lakhs which was paid for in full. On that day it purchased the running business of Vijay Ltd. for ₹ 200 lakhs and allotted at par equity capital of ₹ 200 lakhs in discharge of the consideration. The net assets taken over from Vijay Ltd. were valued as follows : Fixed assets ₹ 150 lakhs, inventory ₹ 10 lakhs, customers' dues ₹ 70 lakhs and Creditors ₹ 30 lakhs.

Hero Ltd. carried on business and the following information is furnished to you:

a. Summary of cash/bank transactions for year ended 31 st March, 2015.

		(₹ in Lakhs)
Equity capital raised :		
Promotors (as shown above)	50	
Others	250	300
Collections from customers		4,000
Sale proceeds of Fixed assets (cost ₹18 crores)		20
Less :		4,320
Payment to suppliers	2,000	
Payment for employees	700	
Payment for expenses	500	3,200
Investments in Upkar Ltd.		100
Payments to suppliers of Fixed assets :		
Instalment due	600	
Interest	50	3,200
Tax payment		270
Dividend		50
Closing cash/bank balance		50

b. On 31st March, 2015 Hero Ltd.'s assets and liabilities were.

	₹ in Lakhs
Inventory at cost	15
Customers' dues	400
Prepaid expenses	10
Advances to suppliers	40
Amounts due to suppliers of goods	260
Amounts due to suppliers of Fixed assets	750
Outstanding expenses	30

c. Depreciation for the year under :

i. Companies Act, 2013	₹ 180 Lakhs
ii. Income tax Act, 1961	₹ 200 Lakhs

d. Provide for tax at 35% of "total income". There are no disallowables for the purpose of income taxation, provision for tax is to be rounded off.

i. Revenue statement for the year ended 31st March, 2015 and

ii. Balance Sheet as on 31st March, 2015 from the above information.

Solution:

WN # 1 : *Computation of purchase consideration*

	₹ in Lakhs
Fixed Assets	150
Inventory	10
Customer's Dues	70
Less: Creditors	(30)
Purchase consideration	**200**

IN THE BOOKS OF HERO LTD.

- Nature of Amalgamation - Purchase Method
- Method of Accounting - Purchase Method

(₹ in Lakhs)

	Particulars		Debit	Credit
1.	**For Business Purchase :**			
	Business Purchase A/c	Dr.	200	
	To Liquidator of Vijay Ltd. A/c			200
2.	**Incorporation of assets and liabilities taken over :**			
	Fixed Assets A/c	Dr.	150	
	Inventory A/c	Dr.	10	
	Customer's dues A/c	Dr.	70	
	To Creditors A/c			30
	To Business Purchase A/c			200
	Note : There is no goodwill or Capital reserve arising.			
3.	**Discharge of Consideration :**			
	Liquidator of Vijay Ltd. A/c	Dr.	200	
	To Equity Share Capital A/c			200

Debtors / Customers Account

Dr. *Cr.*

Particulars	Amount (₹)	Particulars	Amount (₹)
To Business Purchase	70	By Bank	4,000
To Sales [balance c/d]	4,330	By Balance c/d	400
	4,400		**4,400**

Suppliers Account

Dr. *Cr.*

Particulars	Amount (₹)	Particulars	Amount (₹)
To Bank *	1,960	By Business Purchase	30
To Balance c/d	260	By Purchase [balance c/d]	2,190
	2,220		**2,220**

* Payment to suppliers

Amount	2,000
Less: Advances	40
	1,960

Fixed assets Accounts (Suppliers) *₹ in lakhs*

Dr. *Cr.*

Particulars	Amount (₹)	Particulars	Amount (₹)
To Bank A/c	650	By Fixed assets A/c (Bal. fig.)	1,350
To Balance c/d	750	By Interest A/c	50
	1,400		**1,400**

Fixed assets Accounts *₹ in lakhs*

Dr. *Cr.*

Particulars	Amount (₹)	Particulars	Amount (₹)
To Business Purchase A/c	150	By Bank A/c	20
To Profit and Loss A/c	2	By Balance c/d	1,482
To Suppliers A/c	1,350		
	1,502		**1,502**

Expenses Accounts *₹ in lakhs*

Dr. *Cr.*

Particulars	Amount (₹)	Particulars	Amount (₹)
To Bank A/c	500	By Profit and Loss A/c	520
To Outstanding expenses A/c	30	(Balancing Figure)	
		By Balance c/d (prepaid)	10
	530		**530**

Revenue Statement for the year ended 31.3.15

Particulars		***Amount***	**₹ in Lakhs** ***Amount***
a)	Sales		4,330
b)	Less: Expenditure		
	Stock taken over	10	
	Add: Purchases	2,190	
		2,200	
	Less : Closing Stock	15	
	Inventory consumed	2,185	
	Expenses	520	
	Employee Cost	700	(3,405)
	Profit before Interest depreciation and Tax		925
	Less: Interest		(50)
Profit before depreciation and Tax			875
Less: Depreciation as per Companies Act, 2013			(180)
			695
Add: Profit on sale of Fixed assets			2
	Profit before tax		697
Less: Provision for tax *			236.25
	Profit After Tax		460.75
Less: Dividend			(50)
	Balance Carried forward to Balance Sheet.		**410.75**

* Calculation of Tax provision

Particulars	***₹ in lakhs***
Profit before Tax.	697
Less: Profit and Loss on sale of Fixed assets	(2)
Add: Depreciation as per Companies Act	180
Less: Depreciation as per IT Account	(200)
Adjusted Profit before tax	675
Less: Tax @ 35%	236.25
	438.75

Name of the Company: Hero Ltd.				
Balance Sheet as at 31.03.2015				
Ref No.		**Particulars**	**Note No.**	**As at 31st March, 2015**
				(₹ in lakhs)
	I.	**Equity and Liabilities**		
	1	**Shareholders' funds**		
		(a) Share capital	1	500.00
		(b) Reserves and surplus	2	410.75
	2	**Share application money pending allotment**		Nil
	3	**Non-current liabilities**		
		(a) Other Long term liabilities	3	750.00
	4	**Current Liabilities**		
		(a) Trade payables	4	260.00
		(b)Other current liabilities	5	30.00
		(c) Short-term provisions	6	236.25
		Total		2,187.00
	II.	**Assets**		
	1	**Non-current assets**		
		(a) Fixed assets		
		(i) Tangible assets	7	1,302.00
		(b) Non-current investments	8	100.00
		(c) Long-term loans and advances	9	270.00
	2	**Current assets**		
		(a) Inventories		15.00
		(b) Trade receivables	10	400.00
		(c) Cash and cash equivalents	11	50.00
		(d) Short-term loans and advances	12	40.00
		(e) Other current assets	13	10.00
		Total		2,187.00

Note : Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

(Note: Amount due to supplier of Fixed Assets assumed to be for more than 12 months, hence treated as long term borrowings. (Without interest).

(₹ in Lakhs)

Note 1. Share Capital	31.03.15
Authorised Capital:Equity Shares of ₹5 each	1,000
Issued,subscribed and fully paid up capital Existing 300+ Issued 200 (of the above, shares worth ₹200 crores were issued for a consideration other than cash)	500.00
Total	500.00

RECONCILATION OF SHARE CAPITAL		
FOR EQUITY SHARE :-	**As at 31st March, 2015**	
	Nos	**Amount (₹)**
Opening Balance as on 01.04.14		300.00
Add: Fresh Issue (Incld Bonus shares, Right shares, split shares, shares issued other than cash)		200.00
		500.00
Less: Buy Back of shares		-
		500.00

Note 2. Reserves and Surplus	31.03.15
Profit and loss A/c	410.75
Total	410.75

Note 3. Other Long-term Liabilities	31.03.15
Amount due to suppliers of fixed assets	750
Total	750

Note 4. Trade Payables	31.03.15
Creditors	260
Total	260

Note 5. Other Current Liabilities	31.03.15
Outstanding expenses	30
Total	30

Note 6. Short Term Provisions	31.03.15
Provision for tax	236.25
Total	236.25

Note 7. Tangible assets	31.03.15
Fixed assets less: depreciation (1,482 – 180)	1,302
Total	1,302

Note 8. Non Current Investments	31.03.15
Investment in Upkar Ltd.	100
Total	100

Note 9. Long term Loans and Advances	31.03.15
Advance Tax	270
Total	270

Note 10. Trade receivables	31.03.15
Dcustomers Due	400
Total	400

Note 11. Cash and cash equivalents	31.03.15
Cash and Bank	50
Total	50
Note 12. Short term loans and advances	31.03.15
Advance to suppliers	40
Total	40

Note 13. Other Current assets	31.03.15
Prepaid expenses	10
Total	10

[E] Accounting in the event of Inter-Company Investment

Illustration 11.

The summarized Balance Sheet of A Ltd. and B Ltd. as at 31st March, 2014 were as under:

	A Ltd. (₹)	**B Ltd.** (₹)
Fully paid up equity shares of ₹ 10 each	20,00,000	12,00,000
Share Premium Account	4,00,000	—
General Reserve	5,20,000	5,00,000
Profit and Loss Account	3,60,000	3,20,000
10% Debentures	10,00,000	—
Secured Loan	6,00,000	6,00,000
Sundry Creditors	—	3,40,000
	48,80,000	29,60,000
Land and Buildings	18,00,000	9,00,000
Plant and Machinery	10,00,000	7,60,000
Investments (10,000 shares in B Ltd.)	1,60,000	—
Stock	10,40,000	7,00,000
Debtors	8,20,000	5,20,000
Bank	60.000	80,000
	48,80,000	29,60,000

The companies agree on a scheme of amalgamation on the following terms:

(a) A new Company AB Ltd. is to be formed.

(b) AB Ltd. to take over all assets and liabilities of the existing companies.

(c) For the purpose of amalgamation, the shares of the existing companies are to be valued as under:

A Ltd. — ₹ 18 per share

B Ltd. — ₹ 20per share

(d) A contingent liability of A Ltd. of ₹ 1,20,000 is to be treated as real liability.

(e) The shareholders of A Ltd. and B Ltd. are to be paid by issuing sufficient number of shares of AB Ltd. at par.

(f) The shares of AB Ltd. are to be of ₹10 each.

Required:

(i) Show the computation of the number of shares AB Ltd. will issue to the shareholders of the existing companies;

(ii) Pass the journal entries to close the books of A Ltd. and

(iii) Prepare the opening balance sheet of AB Ltd.

[Ignore liquidation and formation expenses]

Solution:

(i) Calculation of number of shares to be issued

	A Ltd. (₹)	B Ltd. (₹)
Existing Shares	2,00,000	1,20,000
Less: Held by A Ltd.	-	10.000
	2,00,000	1,10,000
Agreed Value per Share	18	20
Total Agreed Value	36,00,000	22,00,000
No of shares to be issued of ₹10 each	3,60,000	2,20,000
Total no. of shares to be Issued of ₹10		**5,80,000**

(ii)

Books of A Ltd.

Journal

Particulars		**Dr(₹)**	**Cr. (₹)**
Realization A/c	Dr.	48,80,000	
To Land & Building A/c			18,00,000
To Plant & Machinery A/c			10,00,000
To Stock A/c			10,40,000
To Debtors A/c			8,20,000
To Investment A/c			1,60,000
To Bank A/c			60,000
(Being Assets transferred to Realization A/c)			
Profit & Loss A/c	Dr.	1,20,000	
To Creditors A/c			1,20,000
(Being Contingent Liability treated as real liability)			
10% Debentures A/c	Dr.	10,00,000	
Creditors A/c	Dr.	5,20,000	
To Realization A/c			15,20,000
(Being Liabilities transferred to Realization A/c)			
AB Ltd. A/c	Dr.		
To Realization A/c		36,00,000	
(Being the Purchase Consideration Accounted for)			36,00,000

Particulars		Dr. (₹)	Cr. (₹)
Share in AB Ltd. A/c	Dr.		
To AB Ltd.		36,00,000	
(Being the Purchase Consideration Received)			36,00,000
Share Capital A/c	Dr.	20,00,000	
Share Premium A/c	Dr.	4,00,000	
General Reserve A/c	Dr.	6,00,000	
Profit& Loss A/c	Dr.	2,40,000	
Relization A/c	Dr.	3,60,000	
To Shareholders A/c			32,40,000
(Being Transfer of ledger balances)			
Shareholders A/c	Dr.	36,00,000	
To Shares in AB Ltd.			36,00,000
(Being closure of Shareholders A/c)			

(iii)

Balance Sheet of AB Ltd.

as on 1st April, 2014

	Particulars	Note No.	(₹)
I.	**Equity and Liabilities**		
	1. Shareholders' Funds		
	(a) Share capital	1	58,00,000
	(b) Reserves and Surplus		-
	2. Non-current Liabilities		
	10% Debenture		10,00,000
	Secured loan		6,00,000
	3. Current Liabilities		
	Sundry creditors		9,80,000
	Total		**83,80,000**
II	Assets		
	1. Non-current Assets Fixed assets		
	(a) Tangible assets	2	44,60,000
	(b) Intangible assets		7,00,000
	2. Current assets		
	Stock		17,40,000
	Debtors		13,40,000
	Bank		1,40,000
	Total		**83,80,000**

Notes to Account

Note - 1 Share Capital	As on 1st April 2014 (₹)
Equity shares of ₹10 each issued for consideration other than cash	58,00,000

Notes to Account

Note -2 Tangible Assets	As on 1st April 2014 (₹)
Land and Building	27,00,000
Plant and Machinery	17,60,000
Total	44,60,000

Purchasing Company holding shares in Selling Company

Illustration 12:

The following are the Balance Sheets of Good Ltd. and Bad Ltd. as on 31.03.2016:

	Good Ltd. (₹in crores)		**Bad Ltd. (₹ in crores)**	
Sources of Funds:				
Share Capital:				
Authorised		25		5
Issued and Subscribed Equity Shares of ₹ 10 each fully paid		12		5
Reserves and surplus		88		10
Shareholders Fund		100		15
Unsecured loan from Good Ltd.		---		10
		100		25
Funds employed in Fixed Assets cost		80		40
Less: Depreciation		60		34
Written down value		20		6
Investments at Cost:				
30 lakhs equity shares of ₹10.each of Bad Ltd.		3		---
Long term loan to Bad Ltd.		10		
Current Asset: (Less Current Liabilities)	200		134	---
	(-)133	67	(-)115	19
		100		25

On that day Good Ltd. absorbed Bad Ltd. The Members of Bad Ltd. are to get one equity share of Good Ltd. issued at a premium of ₹ 2 per share for every five equity share held by them in Bad Ltd. The necessary approvals are obtained;

You are asked to pass Journal entries in the books of the two companies to give effect to the above.

Solution:

Books of Bad Ltd.

Journal

Particulars		Dr. (₹ in Crore)	Cr. (₹ in Crore)
Realization A/c	Dr.	174.00	
To Fixed A/c			40.00
To Current Assets A/c			134.00
(Being the Assets taken over by Good Ltd. transferred to Realization A/c)			
Provision for Depreciations A/c	Dr.	34.00	
Current Liabilities A/c	Dr.	115.00	
Unsecured Loan from Good Ltd. A/c	Dr.	10.00	
To Realization A/c			159.00
(Being the transferred of liabilities and provision to Realization A/c)			
Good Ltd. A/c	Dr.	1.20	
To Realization A/c (Being P.C Credited o Realization A/c)			1.20
Equity Shareholders A/c	Dr.	13.80	
To Realization A/c			13.80
(Being loss on Realization transferred to Equity shareholders A/c)			
Equity Share Capital A/c	Dr.	5.00	
Reserves and Surplus A/c	Dr.	10.00	
To Equity Shareholders A/c			15.00
(Being the amount of share capital and reserve transferred to equity shareholders A/c)			
Equity Shareholders (Good Ltd.) A/c	Dr.	0.72	
To Good Ltd. A/c			0.72
(Being 3/5th of the considerations due from Good Ltd. adjusted against the amount due to Good Ltd.)			
Equity Shares of Good Ltd. A/c	Dr.	0.48	
To Good Ltd. A/c			0.48
(Being the receipts of 4 lacs Equity Shares of ₹10 each at ₹12 per Share for allotment of outside shareholders)			
Equity Shareholders A/c	Dr.	0.48	
To Equity Share of Good Ltd. A/c			0.48
(Being the distributions of equity shares received from Good Ltd. to Shareholders)			

Books of Good Ltd.

Journal

Particulars		Dr. (₹ in Crore)	Cr. (₹in Crore)
Business Purchase A/c	Dr.	1.20	
To Liquidator of Bad Ltd. A/c			1.20
(Being the amount of P.C)			
Fixed Assets A/c	Dr.	6.00	
Current Assets A/c	Dr.	134.00	
To Current Liabilities A/c			115.00
To Unsecured Loan (from Good Ltd.) A/c			10.00
To Business Purchase A/c			1.20
To Capital Reserve A/c			13.80
(Being. the assets and liabilities taken over and the difference transferred to Capital Reserve A/c)			
Liquidator of Bad Ltd. A/c	Dr.	0.72	
Capital Reserve A/c	Dr.	2.28	
To Investment in Equity Shares of Bad Ltd. A/c			3.00
(Being cancellation of entries and the resultant loss recovered)			
Liquidator of Bad Ltd. A/c	Dr.	0.48	
To Equity Share Capital A/c			0.40
To Security Premium A/c			0.08
(Being the allotment to outside Shareholders at a premium of ₹ 2 per Share)			
Unsecured Loan (From Good Ltd.) A/c	Dr.	10.00	
To Loan to Bad Ltd. A/c			10.00
(Being the cancellations of unused loan)			

Working Notes

	(₹ in Crores)
Purchase Considerations	0.48
(50 lacs/5) x ₹12 = 1.20 i.e., 10 lacs	
Equity Shares of ₹12 each belonging to Good Ltd. 3/5 x 1.20	0.72
Payable to other equity shareholders	0.48
Number of equity shares of ₹ 10 each to be issued 48 lacs /12	4 lcas

Illustration 13:

The summarized balance sheets of X Ltd. and its subsidiary Y Ltd. as on 31.03.2015 are as follows:

Particulars	X Ltd (₹)	Y Ltd (₹)
Shares of ₹10 each	1,00,00,000	20,00,000
Reserves and surplus	1,40,00,000	60,00,000
Secured loans	49,00,000	-----
Current liabilities	60,00,000	20,00,000
	3,49,00,000	1,00,00,000
Fixed assets	1,29,01,000	35,00,000
Investment in Y Ltd. shares	7,39,000	----
Sundry debtors	70,00,000	10,00,000
Inventories	60,00,000	50,00,000
Cash and bank	82,60,000	5,00,000
	3,49,00,000	1,00,00,000

X Ltd. holds 76% of the paid-up capital of Y Ltd. The balance shares in Y Ltd. are held by a foreign collaborating company. A memorandum of understanding has been entered into with the foreign company providing for the following:

(a) The shares held by the foreign company will be sold to X Ltd. The price per share will be calculated by capitalizing the yield at 16%. Yield. For this purpose, would mean 40% of the average of pre-tax profits for the last 3 years, which were ₹35 lakh. ₹44 lakh and ₹65 lakh respectively.

(b) The actual cost of shares to the foreign company was 2,40,000 only. The profit that would accrue to them would be taxable at an average rate of 30%. The tax payable will be deducted from the proceeds and X Ltd. will pay it to the Government.

(c) Out of the net consideration, 50% would be remitted to the foreign company immediately and the balance will be Unsecured loan repayable after one year.

The Board of X Ltd. also decided that X Ltd. would absorb Y Ltd. simultaneously by writing down the fixed assets of Y Ltd. by 5%. The balance sheet figures included a sum of 1,50,000 due by Y Ltd. to X Ltd.

The entire arrangement was approved by all concerned for giving effect to on 01.04.2015.

Required:

Show the Balance Sheet of X Ltd. as it would appear after the above arrangement is put through on 01.04.2015:

Solution:

Balance Sheet of X Ltd. as at April 1, 2015

	Particulars	Note No.	₹
I	Equity and Liabilities		
	1. Shareholders' Funds		
	(a) Share Capital	1	100.00
	(b) Reserves and Surplus	2	182.06
	2. Non-current Liability		49.00
	3. Current Liabilities		
	Unsecured Loan		10.44
	Provisions		78.50
	Total		420.00

II	Assets		
	Non-current Assets		
	1. Fixed Assets		
	(a) Tangible assets		162.26
	2. Non-current Investment		110.00
	3. Current Assets		
	Debtors		78.5
	Cash at bank		69.24
	Total		420.00

Notes to Accounts

(₹ in Lakhs)

Note-1.Share Capital	**As on 1st April, 2008**
Authorised issued and subscribed capital	
1 crore equity shares of ₹10each	100.00
Note -2 Reserves and Surplus	**As on 1st April, 2008**
Capital Reserve	42.06
Other Reserve	140.00
Total	182.06

Working Notes: 1 Computation of Purchase Consideration

Yield of V Ltd. = 40% of (35 + 44 + 65)/3	₹19.20 Lakhs
Price per Share of V Ltd. (19.20 Lakhs÷16%)÷2 Lakhs shares	₹60.00
Purchase consideration (24% of 2,00,000 shares x ₹ 60	₹28.80 Lakhs

Discharge of Purchase Consideration

Tax payable by X Ltd. (Deduction from Purchase Consideration) on the capital gain of the foreign collaborator:

Purchase consideration	28.80 Lakhs
Less: Cost of acquisition	(2.40) Lakhs
Capital Gain	26.40 Lakhs
Tax at 30%	7.92 Lakhs

Net Purchase consideration payable = 28.80 Lakhs — 7.92 Lakhs = Rs.20.88Lakhs

Mode of Payment	
Immediately 50% i.e.	10.44 Lakhs
Unsecured Loan 50% i.e.	10.44 Lakhs

Working Notes: 2 Computation of Capital reserve

Fixed Assets of Y Ltd. at 95% of book value (+) Net current Assets of V Ltd. (-) Existing Investment in V Ltd. shares (-) Purchase Consideration = ₹ (95% of 35+45-7.39-28.80) = ₹ 42.06 Lakhs

Working Notes: 3 Cash & Bank Balances

= ₹ [82.60 + 5 -10.44 - 7.92]

= ₹69.24 Lakhs

Illustration 14:

The following are the Balance Sheets of Bat Ltd. and Ball Ltd. as on 31st March, 2010.

(₹in crores)

	Bat Ltd.		Ball Ltd.	
Sources of funds:	(₹)	(₹)	(₹)	(₹)
Share Capital:				
Authorised		25		5
Issued and Subscribed: Equity shares of ₹10 each fully paid		12		5
Reserves and surplus		88		10
Shareholders funds		100		15
Unsecured loan from Bat Ltd	.	-		10
		100		25
Funds employed:				
Fixed assets: Cost		70		30
Less: Depreciation		50		24
Written down value		20		6
Investments at cost:				
30 lakhs equity shares of₹ 10 each of Ball Ltd.		3		-
Long-term loan to Ball		10		-
Current assets				
Less: Current liabilities	100		34	
	33	67	15	19
		100		25

On that day Bat Ltd. absorbed Ball Ltd. The members of Ball Ltd. are to get one equity share of Bat Ltd. issued at a premium of ₹ 2 per share for every five equity share held by them in Ball Ltd. The necessary approvals are obtained.

You are asked to pass journal entries in the book of Ball Ltd. to give effect to the above.

Solution:

Books of Bat Ltd.

Journal

Particulars		Dr.	Cr.
		₹	₹
Business Purchase A/c To Liquidator of Ball Ltd. A/c (Being the amount of purchase consideration agreed under approved scheme of amalgamation) (See W. N. 1)	Dr.	1.2	1.2
Fixed Assets A/c	Dr.	6.00	
Current Assets A/c	Dr.	34.00	
To Current Liabilities A/c			15.00
To Unsecured Loan (from Bat Ltd.) A/c.			10.00

To Business purchases Account A/c			1.20
To Capital Reserve			13.80
(Being the assets and liabilities taken over and the surplus transferred to capital reserve)			
Liquidator of Ball Ltd. A/c	Dr.	0.72	
Capital Reserve A/c	Dr.	2.28	
To Investments in Equity Share of Ball Ltd. A/c			3.00
(Being the allotment of outside shareholders of Ball Ltd. cancelled and the resultant loss recorded			
Liquidator of Ball Ltd. A/c	Dr.	0.48	
To Equity Share Capital A/c			0.40
To Securities premium A/c -			0.08
(Being the allotment of outside shareholders of Ball Ltd.			
4 Lakhs equity share of ₹10 each at a premium of ₹ 2 per share)			
Unsecured loan (from ball Ltd.) A/c	Dr.	10.00	
Dr. To Loan to Ball Ltd. A/c			10.00
(Being the cancellation of unsecured loan given to Ball Ltd.)			

Working Note:

W.N. 1

Purchase Consideration $\frac{50\text{ Lakhs}}{5} = ₹10$		
i.e. 10 Lakhs equity shares at ₹ 12 per share	1.20	
Less: Belonging to Bat Ltd. $\left(\frac{3}{5}\times 120\right)$	0.72	
Payable to other equity shareholders	0.48	
Number of equity share of ₹10 each to be issued	$\frac{48\text{ Lakhs}}{12}$	4 Lakhs

Selling Company holding shares in Purchasing Company

Illustration 15.

Following are the extract Balance sheets of two companies, B Ltd. and D Ltd. as at March 31, 2015.

Liabilities	B Ltd.	D Ltd.	Assets	B Ltd.	D Ltd.
	₹	₹		₹	₹
Equity Share Capital:			Sundry Assets	7,50,000	3,50,000
(Shares of ₹ 10 each)	5,00,000	3,00,000	10,000 Shares in		
Reserve	1,00,000	55,000	B Ltd.	—	1,00,000
Creditors	1,50,000	95,000			
Total	**7,50,000**	**4,50,000**	**Total**	**7,50,000**	**4,50,000**

B Ltd. was to absorb D Ltd. on the basis of intrinsic value of the shares, the purchase consideration was to be discharged in the form of fully paid shares, entries to be made at par value only. A sum of ₹ 20,000 is owed by B Ltd. to D Ltd. Also included in the stocks of B Ltd. ₹ 30,000 goods supplied by D Ltd. cost plus 20%. Give Journal entires in the books of both the Companies and prpeared a Balance Sheet after absorption.

Solution:

Part I: In the Books of D Ltd.

	Particulars		*Debit* ₹	*Credit* ₹
1.	Realisation A/c	Dr.	3,50,000	
	To Sundry Assets A/c			3,50,000
	[Being the assets taken over by B Ltd. transferred to Realisation A/c]			
2.	Creditors A/c	Dr.	95,000	
	To Realisation A/c			95,000
	[Being Creditors taken over by B Ltd. transferred Realisation A/c]			
3.	B Ltd. A/c	Dr.	2,12,500	
	To Realisation A/c			2,12,500
	[Being purchase consideration (WN # 2) receivable]			
4.	Shares in B Ltd. A/c	Dr.	2,12,500	
	To B Ltd. A/c			2,12,500
	[Being discharge of purchase consideration]			
5.	Shareholders A/c	Dr.	42,500	
	To Realisation A/c			42,500
	[Being realisation loss transferred to Shareholder A/c]			
6.	Share Capital A/c	Dr.	3,00,000	
	Reserves A/c	Dr.	55,000	
	To Shareholders A/c			3,55,000
	[Being Share capital and Reserves transferred to Shareholders A/c]			
7.	Shareholders A/c	Dr.	3,12,500	
	To Shares in B Ltd.			3,12,500
	[Being the settlement to shareholders for the amount due]			

Calculation of Purchase consideration - Net Assets Method

WN # 1: ***Intrinsic value of share***

	Particulars	*B Ltd* (₹)	*D Ltd.* (₹)
(a)	Sundry Assets	7,50,000	3,50,000
(b)	Investments in B Ltd. 10,000 shares @ ₹ 12 each	—	1,20,000
(c)	Creditors	(1,50,000)	(95,000)
(d)	Net Assets	6,00,000	3,75,000
(e)	No. of shares outstanding	50,000	30,000
(f)	Intrinsic Value of shares [d ÷ e]	12	12.5

WN # 2: *Purchase Consideration*

	Particulars	*Amount (₹)*
(a)	No. of shares of D Ltd.	30,000
(b)	Value of shares @ ₹ 12.50	₹ 3,75,000
(c)	No. of shares issuable based on intrinsic value of ₹ 12 (3,75,000 ÷ 12)	31,250
(d)	No. of shares held by D Ltd.	(10,000)
(e)	Net shares to be issued	21,250
(f)	Total consideration at par (21,250 x ₹ 10)	₹ 2,12,500

Part - II : *In the books of B Ltd.*

- Nature of Amalgamation - Merger
- Method of Accounting - Pooling of Interest

	Particulars		*Debit (₹)*	*Credit (₹)*
1.	For Purchase Consideration Due:			
	Business Purchase A/c	Dr.	2,12,500	
	To Liquidator of D Ltd.'s A/c			2,12,500
2.	a. For of assets and liabilities taken over			
	i. Aggregate consideration to share holders of Selling Company			
	* Shares already held by D Ltd. 1,00,000			
	* Shares now issued 2,12,500			
	ii. Paid up capital of D Ltd. 3,12,500			
	(3,00,000)			
	iii. Excess 12,500			
	iv. Above excess to be adjusted against reserves of D Ltd. 12,500			
	v. Balance of reserves to be incorporated 42,500 (55,000 - 12,500)			
	b. Assets A/c	Dr.	3,50,000	
	To Creditors A/c			95,000
	To Reserves A/c			42,500
	To Business Purchase A/c			2,12,500
3.	Discharge of Purchase consideration			
	Liquidator of D Ltd.'s A/c	Dr.	2,12,500	
	To Equity Share Capital A/c			2,12,500
4.	Others			
	a. Cancellation of Inter company owings			
	Creditors A/c	Dr.	20,000	
	To Sundry Assets A/c			20,000
	b. Adjusted of Stock Reserve			
	Reserve A/c	Dr.	5,000	
	To Stock Reserve			5,000

Name of the Company: B Ltd.					
Balance Sheet as at 31.03.2015 (After absorption)					
Ref No.		**Particulars**	**Note No.**	**After**	**Before**
				₹	₹
	I.	**Equity and Liabilities**			
	1	**Shareholders' funds**			
		(a) Share capital	1	7,12,500	
		(b) Reserves and surplus	2	1,37,500	
	2	**Share application money pending allotment**		Nil	
	3	**Non-current liabilities**		Nil	
	4	**Current Liabilities**			
		(a) Trade payables	3	2,25,000	
		Total		10,75,000	
	II.	**Assets**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	4	10,75,000	
	2	**Current assets**		Nil	
		Total		10,75,000	

Note : Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

(₹)

Note 1. Share Capital	**After**	**Before**
A. Authorised Capital B. Issued,and paid up Capital Eqity Share Capital(Share of ₹10 each)[out of which 21,250 shares were issued for consideration other than cash)	7,12,500	
Total	7,12,500	

RECONCILATION OF SHARE CAPITAL

FOR EQUITY SHARE :-	**After**		**Before**	
	Nos	**Amount (₹)**	**Nos**	**Amount (₹)**
Opening Balance as on 01.01.14	50,000	5,00,000	NIL	NIL
Add: Fresh Issue (Incld Bonus shares, Right shares, split shares, shares issued other than cash)	21,250	2,12,500	NIL	NIL
	71,250	7,12,500	NIL	NIL
Less: Buy Back of shares	-	-	-	-
	71,250	7,12,500	-	-

Note 2. Reserves and Surplus	After	Before
Reserve (1,00,000 + 42,50,000 - 5,000)	10,75,000	
Total	10,75,000	

Note 3. Trade Payables	After	Before
Creditors	2,25,000	
Total	2,25,000	

Note 4. Tangible assets	After	Before
Sundry Assets (7,50,000+3,50,000-20,000-5,000)	10,75,000	
Total	10,75,000	

Cross Holding of Shares

Illustration 16.

The following are the Balance Sheets of BEE Ltd. And DEE Ltd. as on 31 .03.2014

	BEE Ltd. (₹)	DEE Ltd. (₹)
Equity and Liabilities:		
Shareholders' Funds:		
Share Capital:		
Equity shares of 100 each fully paid	90,00,000	30,00,000
Reserves and Surplus:		
General Reserve	8,00,000	6,00,000
Profit and Loss A/c	14,68,000	60,000
Non-Current Liabilities:		
14% Debentures	—	18,00,000
Current Liabilities:		
Trade payables	12,00,000	5,40,000
Total	1,24,68,000	60,00,000
Assets:		
Non-Current Assets:		
Tangible Assets	60,00,000	3,00,000
Non-Current Investments (at cost):		
6,000 shares in DEE Ltd.	9,00,000	—
18,000 shares in BEE Ltd.	—	30,00,000
Current Assets:		
Inventories	28,80,000	12,60,000
Trade Receivables	17,40,000	9,00,000
Cash and Cash equivalents	9,48,000	5,40,000
Total	1,24,68,000	60,00,000

Inventories of BEE Ltd. include goods worth ₹ 6,00,000 purchased from DEE Ltd. which made a profit of 20% on selling price. As on 31.03.2014, BEE Ltd. absorbs DEE Ltd. on the basis of the intrinsic value of the shares of both companies as on 31.03.2014. Before absorption, BEE Ltd. has declared a dividend of 12%. Dividend tax is 10%.

You are required to calculate:

(i) No. of shares to be issued to DEE Ltd.

(ii) Purchase consideration payable by BEE Ltd.

(iii) Capital Reserve/Goodwill which will appear in the Balance Sheet of BEE Ltd.

Solution:

Computation of Net Assets excluding Inter-Company Investments

Particulars	BEE Ltd. (₹)	DEE Ltd. (₹)
Tangible Assets	1,15,68,000	30,00,000
Dividend Receivable [18,000 shares x 100 x 12%]	---	2,16,000
Total Assets [A]	**1,15,68,000**	**32,16,000**
Current Liabilities	12,00,000	5,40,000
Proposed Dividend	10,80,000	---
Dividend Tax	1,08,000	---
14% Debentures	---	18,00,000
Total Liabilities [B]	**23,88,000**	**23,40,000**
Net Assets [A-B]	**91,80,000**	**8,76,000**

2. Intrinsic value of Equity Shares

Let 'a' as the intrinsic value (Net Assets including Inter Company Investments) of Equity Shares of BEE Ltd. and 'b' as the intrinsic value of Equity Shares of DEE Ltd.

a = 91,80,000+1/5b….. (1) b = 8,76,000+ 1/5a….. (2)

or, b = 8,76,000 + 1/5(91,80,000 + 1/5b)

or, b = ₹8,76,000 + 18,36,000 + b/25

or, b-b125 = 27,12,000

or, b = 27,12,000 x 25/24 = ₹ 28,25,000

Putting the value of b in equation (1), we get, a = 91,80,000 + 1/5 x 28,25,000 = 97,45,000

Intrinsic value of shares of BEE Ltd. = 97,45,000/90,000 = ₹108.28 Intrinsic value of shares of DEE Ltd.

= 28,25,000/30,000 = 94.167 approximately

3. Calculation of purchase consideration payable by BEE Ltd.

Value of Shares held by Outsiders in DEE Ltd.	= 24,000 x 94.167 = 22,60,000 (approx)
Shares to be issued by BEE Ltd. based on Intrinsic Value	= 22,60000 /1 08.28 20,872 Shares
Less: Shares held by DEE Ltd.	= 18,000 shares
Number of Shares to be issued	= 2,872 shares
Purchase consideration(2872 Shares x 1.08.28)	= 3,10,980

4. Calculation of Capital Reserve / Goodwill

Particulars	₹
Assets taken over:	32,16,000
Less: Liabilities	23,40,000
Net Assets taken over	8,76,000
Less: Purchase Consideration	3,10,980
Capital Reserve	5,65,020

Illustration 17:

The following are the Balance Sheet of A Ltd. and B Ltd. as on 31st March, 2014.

	₹ in Crores	**₹ in Crores**
Liabilities		
Share capital:		
Equity Share of ₹ 10 each	4,00,000	2,00,000
10% Preference Shares of ₹10 each	2,00,000	1,00,000
Reserves and Surplus	2,00,000	1,00,000
12% Debentures	3,00,000	2,00,000
Sundry creditors	1,50,000	1,60,000
Total	12,50,000	7,60,000
Assets		
Fixed Assets	6,00,000	3,00,000
Stock	2,00,000	1,00,000
Debtors	3,00,000	2,00,000
Cash at bank	80,000	90,00,00
Investments in:		
4000 equity shares of B Ltd.	70,000	—
5000 equity shares of A Ltd.	—	70,000
Total	12,50,000	7,60,000

Fixed Assets of A Ltd. and B Ltd. are to be revalued at 15% and 10% respectively above book values. Stock and debtors 'of B Ltd. are to be taken over by A Ltd. at 5% less than their book values. While both the companies have 'already paid preference dividends, they are, yet to pay 10% equity dividends.

After the above transactions are given effect to, A Ltd. will absorb B Ltd. on the following terms:

(i) 6 equity shares of ₹ 10 each will be issued by A Ltd. at par against 4 equity shares of B Ltd

(ii) 10% Preference Share of B Ltd. will be paid off at 10% discount by issue of 10% Preference Shares of 100 each of A Ltd. at par.

(iii) 20,000 to be paid by A Ltd. to B Ltd. for liquidation expenses.

(iv) 12% debenture holders of B Ltd. are to be paid off at 4% premium by 12% debentures in A Ltd. issued at a discount of 20%.

Prepare:

(i) a statement of Purchase consideration payable by A Ltd., and

(ii) a Balance Sheet of A Ltd. after its absorption of B Ltd. (Schedules are not required)

Solution:

(i) Statement of Purchase Consideration Payable by A Ltd.

Payment To	Payment in	Working	Amount (₹)
Equity Shareholder	Equity Share	[16,000 x 6/4 5,000] x 10	1,90,000
10% Pref. Shareholder	10% pref. shares	1,00,000 x 90%	90,000
Total Purchase Consideration			2,80,000

(ii) Balance Sheet of A Ltd. (after absorption of B Ltd.) as on March, 2014

	Particulars	Note No.	Amount (₹)
I.	**EQUITY AND LIABILITIES**		
	(1) Shareholders'. Funds		
	(a) Share Capital	1	8,80,000
	(b) Reserves and Surplus	2	2,34,000
	(2) Non-Current Liabilities		
	(a) Long Term Borrowing	3	5,60,000
	(3) Current Liabilities '		
	(a) Trade Payables – Sundry creditors	4	3,10,000
	Total		**19,84,000**
II	Assets		
	(1) Non Current Assets		
	(a) Tangible-Fixed Assets (6,00,000 x 15% + 3,00,000 x 10%)		10,20,000
	(b) Intangible-Goodwill		28,000
	(c) Other non-current assets	5	52,000
	(2) Current Assets		
	(a) Stock (2,00,000 + 1,00,000 x 95%)		2,95,000
	(b) Trade Receivable		4,90,00
	(c) Cash and Cash Equivalent (W.N.1)		99,000
	Total		**19,84,000**

[Relevant Notes]

1. Share Capital

Particulars	₹
59,000 ie. (40,000 +19,00,000) Equity Shares of ₹ 10 each (out of which 19,000 equity shares has been issued for consideration other than cash)	5,90,000
29,000 10% Preference Shares of ₹ 10 each	2,90,000
Total Share Capital	8,80,000

2. Reserves and Surplus

Particulars	₹
Revaluation Reserve (6,00,000 x 15%)	90,000
Other Reserve (W. Note-3)	1,44,000
Total	2,34,000

3. Long Term borrowing

Particulars	₹
12% Debentures 3,00,000 + [(2,00,000 x 104%)/0.80]	5,60,000
Total	5,60,000

4. Trade Payables

Particulars	₹
Sundry Creditors (1,50,000 + 1,60,000)	3,10,000
Total	3,10,000

5. Other Non—current Assets

Particulars	₹
Discount on issue of Debentures [2,00,000 x 104% (20/80)]	52,000
Total	52,000

W.N. 1: Calculation of closing balance of Cash

Particulars	**A Ltd. (₹)**	**B Ltd. (₹)**
Balance as per B/S	80,000	90,000
(-) Dividend Paid @ 10%	(40,000)	(20,000)
+ Dividend received from each other	4,000	5,000
(-) Expenses of Liquidation	(20,000)	---
Total (₹ 99,000)	24,000	

W.N 2: Calculation of Goodwill / Capital Reserve

Purchase Consideration		2,80,000
Investment		70,0000
Less: Net Assets taken over		
F.A.	3,30,000	
Stock	95,000	
Debtors	1,90,000	
Cash at Bank	75,000	
(-) Debenture	(2,08,000)	
(-) Creditor	(1,60,000)	(3,22,000)
Goodwill		28,000

W.N. 3: Calculation of other Reserve

Reserve as per B/S	2,00,000
Less: Dividend Declared	(40,000)
Less: Expenses on Liquidation	(20,000)
Add: Dividend from B Ltd.	4,000
Total	1,44,000

Chain Holding of Shares

Illustration 18.

The following are the summarized Balance Sheet of A Ltd. and B Ltd.

(₹)

Liabilities	*A Ltd.*	*B Ltd.*	*Assets*	*A Ltd.*	*B Ltd.*
Equity Share Capital A/c	32,000	28,000	Sundry assets	42,000	33,000
Profit and Loss A/c	5,000	—	Shares in B Ltd.	20,000	—
Creditors	15,000	6,000	Profit and Loss A/c	—	1,000
Loan - C Ltd.	10,000	—			
	62,000	**34,000**		**62,000**	**34,000**

Note : Loan from C Ltd. assumed to be of less that 12 months, hence treated as short terms borrowings (ignoring interest)

The whole of the shares of A Ltd. are held by C Ltd. and the entire Share capital of B Ltd. is held by A Ltd.

A new company Z Ltd. is formed to acquire the sundry assets and liabilities of A Ltd. and B Ltd. For the purpose, the sundry assets of A Ltd. are revalued at ₹ 30,000 and those of B Ltd. at ₹ 20,000.

Show the journal entries and prepare necessary ledgers A/c to close the books of A Ltd. and B Ltd.

Solution:

In the Books of A Ltd.

(₹)

	Particulars		*Debit*	*Credit*
1.	Realisation A/c	Dr.	62,000	
	To Sundry Assets A/c			42,000
	To Investment in B Ltd. A/c			20,000
	[Being sundry assets and shares in B Ltd. transferred to Realisation A/c on sale of business of A Ltd.]			
2.	Creditors A/c	Dr.	15,000	
	Loan (C Ltd.) A/c	Dr.	10,000	
	To Realisation A/c			25,000
	[Sundry creditors and loans transferred to Realisation A/c on sale of business to Z Ltd.]			
3.	Z Ltd. A/c	Dr.	5,000	
	To Realisation A/c			5,000
	[Amount of purchase consideration receivable from Z Ltd.]			
4.	Shares in Z Ltd. A/c	Dr.	5,000	
	To Z Ltd. A/c			5,000
	[Amount of purchase consideration received as shares of B Ltd.]			
5.	Shares in Z Ltd. A/c	Dr.	14,000	
	To Realisation A/c			14,000
	[Amount of shares in Z Ltd. received against investment in Z Ltd.]			
6.	Shareholders (C Ltd.) A/c	Dr.	18,000	
	To Realisation A/c			18,000
	[Loss on realisation transferred to Shareholders A/c]			

7.	Equity Share Capital A/c Dr. Profit and Loss A/c Dr. To Realisation A/c [Balance of Share capital and Profit and Loss A/c transfer to Share holder A/c]	32,000 5,000	 37,000
8.	Shareholders (C Ltd.) A/c Dr. To Shares in Z Ltd. A/c [Amount payable to shareholders discharged by issue of shares in Z Ltd. (14,000÷5,000)]	19,000	 19,000

In the Books of B Ltd.

	Particulars	***Debit***	***Credit***
1.	Realisation A/c Dr. To Sundry Assets A/c [Being Sundry Assets and Shares in B Ltd. transferred to Realisation account on sale of business to Z Ltd.]	33,000	 33,000
2.	Creditors A/c Dr. To Realisation A/c [Sundry Creditor is transferred to Realisation A/c on sale of Business to Z Ltd.]	6,000	 6,000
3.	Z Ltd. A/c Dr. To Realisation A/c [Amount of purchase consideration receivable from Z Ltd. on transfer sundry assets, creditor and Loan vide agreement dated.....]	14,000	 14,000
4.	Equity Share Capital A/c Dr. To Shareholders (A Ltd.) A/c [Being amount of Share capital transferred to Shareholder A/c]	28,000	 28,000
5.	Shareholders A/c Dr. To Realisation A/c To Profit and Loss A/c [Loss on realisation and Profit and Loss A/c debit balance transferred to Share holders A/c]	14,000	 13,000 1,000
6.	Shares in Z Ltd. A/c Dr. To Z Ltd. A/c [Amount of purchase consideration received in shares of Z Ltd.]	14,000	 14,000
7.	Shareholders (A Ltd.) A/c Dr. To Shares in Z Ltd. [Amount payable to shareholders discharged by issue of shares in Z Ltd.]	14,000	 14,000

WN # 1 : Calculation of Purchase Consideration (Net Assets Method) (₹)

Particulars	***A Ltd.***	***B Ltd.***
Value of net assets	30,000	20,000
Creditors	(15,000)	(6,000)
Loans from C Ltd.	(10,000)	—
Purchase Consideration	**5,000**	**14,000**

In the Books of B Ltd. :

Realisation Account

Dr. ***Cr.***

Particulars	Amount (₹)	Particulars	Amount (₹)
To Sundry Assets	33,000	By Creditors A/c	6,000
		By A Ltd. (Purchase Consideration)	14,000
		By Shareholders (A Ltd.) A/c (Loss on Realisation)	13,000
	33,000		**33,000**

Shareholders (A Ltd.) Account

Dr. ***Cr.***

Particulars	Amount (₹)	Particulars	Amount (₹)
To Realisation A/c	13,000	By Share Capital A/c	28,000
To Profit and Loss A/c	1,000		14,000
To Shares in Z Ltd. A/c	14,000		13,000
	28,000		**28,000**

In the Books of A Ltd. :

Realisation Account

Dr. ***Cr.***

Particulars	Amount (₹)	Particulars	Amount (₹)
To Sundry Assets	42,000	By Creditors A/c	15,000
To Investments in B Ltd.	20,000	By Loan (Z Ltd.)	10,000
		By A Ltd. A/c (Purchase	5,000
		consideration)	14,000
		By Shares in A Ltd.	18,000
		By Shareholders A/c (Loss on Realisation)	
	62,000		**62,000**

Sundry Shareholders (A Ltd.) Account

Dr. ***Cr.***

Particulars	Amount (₹)	Particulars	Amount (₹)
To Realisation A/c	18,000	By Share Capital A/c	32,000
To Shares in Z Ltd. (14,000 from B Ltd. 5,000 from Z Ltd.)	19,000	By Profit and Loss A/c	5,000
	37,000		**37,000**

[G] Internal Reconstruction

Illustration 19.

The following is the Balance Sheet as at 31st March, 2014 of Hospital Ltd.

Liabilities	₹	Assets	₹
Share Capital:		Fixed Assets (including	
8,500 Equity Shares of		goodwill of ₹1 ,00,000)	11,80,000
₹100 each fully paid up	8,50,000	Investments	40,000
4,000 Cumulative		Stock in Trade	2,75,000
Preference Shares of ₹ 100		Trade Debtors	1,50,000
each fully paid up	4,00,000	Bank Balances	65,000
Securities Premium	20,000		
General Reserve	60,000		
Trade Creditors	3,80,000		
	17,10,000		17,10,000

Contingent liability:

Preference Dividends in arrears ₹ 60,000.

The Board of Directors of the company decided upon the following scheme of reconstructions, which was duly approved by all concerned and put into effect from 1st April, 2014.

(i) The Preference Shares are to be converted into 12% unsecured debentures of ₹ 100 each with regard to 70% of the dues (inducing arrears of dividends) and for the balance Equity Shares of ₹ 50 paid up would be issued. The authorized Capital of the company permitted the issue of additional shares.

(ii) Equity Shares would be reduced to share of ₹ 50 each paid up.

(iii) Since goodwill has no value, the same is to be written of the fully.

(iv) The market value of investments are to be reflected at ₹60,000.

(v) Obsolete items in Stock of ₹ 75,000 are to be written off. Bad Debts to the. extent of 5% of the total debtors would be provided for. Fixed assets to be written down by ₹ 1,80,000.

The company carried on trading, for six months upto 30th September 2014, and made a net profit of ₹1,00,000 after writing off depreciation at 25% p.a. on the revised value of fixed assets. The half yearly working resulted in an increase of Sundry Debtors by ₹80,000, stock by ₹70,000 and Cash by ₹ 50,000.

You are required to show the Journal entree for giving effect to the above arrangement and also draw the Balance Sheet of the company as at 30th September, 2014.

Solution:

Books of Hopeful Ltd.

Journal

Particulars		Dr. (₹)	Cr. (₹)
Cumulative Preference Share Capital A/c	Dr.	4,00,000	
Capital Reduction A/c	Dr.	60,000	
To Cumulative Preference Shareholders A/c			4,60,000
(Being Cumulative preference shares and Preference Shareholders A/c)			
Cumulative Preference Shareholders A/c	Dr.	4,60,000	
To 12% Unsecured Debentures A/c			3,22,000
To Equity Share Capital A/c			1,38,000
(Being the issue of 12% Unsecured Debentures and 2,760 Equity Shares of ₹ 100 each issued as ₹ 50 paid up)			
Equity Share Capital A/c	Dr.	4,25,000	
To Capital Reduction A/c			4,25,000
(Being the entry for reducing every share of ₹ each as ₹ 50 paid up, 8,500 Equity shares @ ₹50 per share.)			
Investments A/c	Dr.	20,000	
Capital Reduction A/c (Balancing figure)	Dr.	3,42,500	
To Goodwill A/c			1,00,000
To Stock A/c			75,000
To Fixed Assets A/c			1,80,000
To Provision for doubtful debts			7,500
(Being the change in value of assets)			
Capital Reduction A/c	Dr.	22,500	
To Capital Reserve A/c			22,500
(Being transfer of Capital Reduction A/c balance to Capital Reserve)			

Balance Sheet of Hopeful Ltd.

as at 30.09.14

	Particulars		Note No.	₹ (in Lakh)
I.	**Equity and Liabilities**			
	1.	**Shareholders' Funds**		
		(a) Share Capital	1	5,63,000
		(b) Reserves and Surplus	2	2,02,500
	2.	**Non Current Liabilities**		
		12% Unsecured Debenture		3,22,000
		Current Liabilities		3,67,500
		Total		14,55,000
II.	**Assets**			
	1.	**Non Current Assets**		
		Fixed Assets		
		Tangible Assets	3	7,87,500
		Other Non Current Assets		60,000
	2.	**Current Assets**	4	6,07,500
		Total		14,55,000

Note - 1 Share Capital	As on 30th September 2014
Authorized, issued subscribed and paid up capital 11,260 equity shares of ₹50 each	5,63,000

Note - 2 Reserves and Surplus	As on 30th September 2014
Securities Premium	20,000
Capital Reserve	22,500
General Reserve	60,000
Profit and Loss A/c	1,00,000
Total	**2,02,500**

Note - 3 Tangible Assets		As on 30th September 2014
Fixed Assets	9,00,000	
Less: Depreciation	1,12,500	7,87,500

Note - 4 Current Assets		As on 30th September 2014
Stock in trade	(2,75,000-75,000+70,000)	2,70,000
Trade Debtors	2,30,000	
Less: Provision for doubtful debt	7,500	2,22,500
Cash and Bank Balance		1,15,000
Total		**6,07,500**

Working Notes :-

1. No. of equity shares issued to cumulative preferences Shareholders — 2,760

No. of shares held by Equity Shareholders — 8,500

11,260

2. Calculation of Cash Balance:

Opening cash balance as on 31.03.2014	65,000
Add: Changes in cash balance (as given in question)	50,000
	1,15,000

3. Calculation or Creditors:

Profit and Loss upto 30.09.2014	1,00,000
Add: Depreciation (Non - cash item)	1,12,500
Cash from operations (A)	**2,12,500**

Change in Current Assets

Debtors	+80,000
Stock	+70,000
Cash	+50,000
Cash out flow (B)	**2,00,000**
Decrease in Creditors:	
Excess of (A) over (B)	-12500
Add: Opening balance of Creditor	3,80,000
Closing creditor (30.09.12)	**3,67,500**

Illustration 20:

The following are the Balance Sheet of Rito Ltd. and Arima Ltd. as on March 31, 2013.

(Amounts in ₹ lakh)

Liabilities	RITO LTD.	ARIMA LTD.	Liabilities	RITO LTD.	ARIMA LTD.
Share Capital:			Fixed Assets-net of deprecation	810	255
Equity Shares of ₹ 100 each fully paid up	600	300	Investments (including investment in Arima Ltd.)	210	-
			Debtors	120	45
Reserves & Surplus	240	-	Cash at Bank	75	-
10% Debentures	150	-	Accumulated loss	-	240
Loans from Banks	75	135	Profit & Loss A/c		
Bank Overdrafts	-	15			
Sundry Creditors	90	90			
Proposed Dividends	60	-			
	1,215	**540**		**1,215**	**540**

It was decided that Arima Ltd. will acquire the business of Rito Ltd. for enjoying the benefits of carry forward of business loss. The following scheme has been approved for the merger:

(i) Arima Ltd. will reduce its shares to ₹10 per share and then consolidate ₹ 10 such shares into one share of ₹100 each (New Shares).

(ii) Banks agreed to waive the loan of ₹18 lakh of Arima Ltd.

(iii) Shareholders of Rito Ltd. will be given one (new) shares of Arima Ltd. in exchange of every share held in Rito Ltd.

(iv) Sundry Creditors of Arirna Ltd. includes ₹ 30 lakh payable to Rito Ltd.

(v) After merger the proposed dividend of Rito Ltd. will be paid to Shareholders of Rito Ltd.

(vi) Rito Ltd. will cancel 20% holding of Arima Ltd. investment which was held at a cost of ₹75 lakh.

(vii) Authorised Capital of Arima Ltd. will be raised accordingly to carry out the scheme.

Required:

Pass necessary entries in the books of Arima Ltd. and prepare Balance Sheet (after merger) as on March 31, 2013.

Solution:

Arima Ltd.

Calculation Purchase Consideration

Particulars	₹	₹
Rito Ltd. 6,00,000 Equity Shares will be issued:		6,00,000
One Share (new) for each Share by Arima Ltd.		
Less: Already held by Rito Ltd.		
20% of 3,00,000 =	60,000	
Shares converted into New Shares		6,000
Number of Shares to be issued by Arima Ltd. to Rita Ltd.		5,94,000
Total purchase Consideration	₹ 594 Lakh	

Books of Arima Ltd.

Journal **(₹ in Lakhs)**

Particulars		Dr. Amount (₹)	Cr. Amount (₹)
Equity Share Capital A/c (₹ 100)	Dr.	300	
To Equity Share Capital A/c (₹ 10)			30
To Reconstruction A/c			270
(Being reduction in share capital)			
Equity Share Capital A/c (₹10 each)	Dr.	30	
To Equity Share Capital A/c (₹ 100)			30
(Being consolidation of share)			
Loan from Banks	Dr.	18	
To Reconstruction A/c			18
(Being waiver of loan by Bank)			
Reconstruction A/c. (₹ 100)	Dr.	288	
To Profit and Loss A/c			240
To Capital Reserve A/c			48
(Being adjustment for accumulated loan)			
Business Purchase A/c	Dr.	594	
To Liquidator of Rito Ltd. A/c			594
(Being purchase consideration for Rito Ltd.)			

Fixed Assets A/c	Dr.	810	
Other Investments A/c	Dr.	135	
Sundry Debtors A/c	Dr.	120	
Cash at Bank A/c	Dr.	75	
Reserves A/c	Dr.	69	
To Sundry Creditors A/c			90
To 10% Debentures A/c			150
To Loan from Banks A/c			75
To Proposed Dividend A/c			60
To Business Purchase A/c			594
To Reserves A/c			240
(Being entry on acquiring of Assets / Liabilities of Rito Ltd.)			
Proposed. Dividend A/c	Dr.	60	
To Bank A/c			60
(Being payment of Proposed dividend to shareholders of Rito Ltd.)			
Liquidator or Rito A/c	Dr.	594	
To Equity Share Capital A/c (of Arima Ltd.)			594
(Discharge of purchase Consideration in the Form of equity Shares of Arima Ltd.)			
Sundry Creditors A/c.	Dr.	30	
To Sundry Debtors A/c (Cancellation of Inter Company ownings.)			30

	Particulars		Note No.	As on 31st March 2013 (₹)
I.	**Equity and Liabilities**			
	1.	Shareholders' Funds		
		(a) Share Capital	1	624
		(b) Reserves and Surplus	2	219
	2.	Non Current Liabilities		
		10% Debenture		150
		Loan from banks [75+135-18]		192
	3.	Current Liabilities		
		Bank overdraft		15
		Sundry creditors		150
		Total		1,350
II.	**Assets**			
	1.	Non-Current Assets		
		Fixed Assets		1,065
		Non-current Investment [210-75]		135
	2.	Current Assets		
		Sundry Debtors		135
		Cash at Bank [75-60]		15
		Total		1,350

Note - 1 Share Capital	As on 31st March 2013 (₹)
Authorized, issued subscribed and paid up capital 6,24,000 equity shares of ₹10 each	624

Note - 2 Reserves and Surplus	As on 31st March 2013 (₹)
Capital Reserve	48
General Reserves (240-69)	171
Total	219

Illustration 21.

The business of P Ltd. was being carried on continuously at losses. The following are the extracts from the Balance Sheet of the Comapny as on 31st March, 2015.

Balance Sheet as on 31st March, 2015

Liabilities	Amount ₹	*Assets*	Amount ₹
Authorised, Issed and		Goodwill	50,000
Subscribed Capital :		Plant	3,00,000
30,000 Equity Shares of ₹ 10 each fully paid	3,00,000	Loose Tools	10,000
2,000 8% Cumulative Pref. Shares of ₹ 100 each fully paid	2,00,000	Debtors	2,50,000
Securities Premium	90,000	Stock	1,50,000
Unsecured Loan (From Director)	50,000	Cash	10,000
Sundry creditors	3,00,000	Bank	35,000
Outstanding Expenses	70,000	Preliminary Expenses	5,000
(including Directors' remuneration ₹20,000)		Profit & Loss Account	2,00,000
	10,10,000		**10,10,000**

Note : 1) Dividends on Cumulative Preference Shares are in arrears for 3 years.

2) Unsecured loans (from director) is assumed to be of less than 12 months hence, treated as short term borrowings. (ignoring interest)

The following scheme of reconstruction has been agreed upon and duly approved by the Court.

1. Equity shares to be converted into 1,50,000 shares of ₹ 2 each.
2. Equity shareholders to surrender to the Company 90 per cent of their holding.
3. Preference shareholders agree to forego their right to arrears to dividends inconsideration of which 8 percent Preference Shares are. to be converted into 9 per cent Preference Shares.
4. Sundry creditors agree to reduce their claim by one fifth in consideration of their getting shares of ₹ 35,000 out of the surrendered equity shares.
5. Directors agree to forego the amounts due on account of unsecured loan and Director's remuneration.
6. Surrendered shares not otherwise utilised to be cancelled.

7. Assets to be reduced as under :

Goodwill by	₹ 50,000
Plant by	₹ 40,000
Tools by	₹ 8,000
Sundry Debtors by	₹ 15,000
Stock by	₹ 20,000

8. Any surplus after meeting the losses should be utili sed in writing down the value of the plant further.
9. Expenses of reconstruction amounted to ₹ 10,000.
10. Further 50,000 Equity shares were issued to the existing members for increasing the working capital. The issue was fully subscribed and paid-up.

A member holding 100 equity shares opposed the scheme and his shares were taken over by the Director on payment of ₹ 1,000 as fixed by the Court.

You are required to pass the journal entries for giving effect to the above arrangement and also to draw up the resultant Balance Sheet of the Company.

Solution:

Particulars		***Debit*** ₹	***Credit*** ₹
a. Sub Division of Shares			
Equity Share Capital (₹10 each) A/c	Dr.	3,00,000	
To Equity Share Capital (₹ 2 each) A/c			3,00,000
b. Surrender of Shares			
Equity Share Capital (₹ 2) A/c	Dr.	2,70,000	
To Shares Surrendered A/c			2,70,000
c. Conversion of Preference Share Capital			
8% Cumulative Preference Share Capital A/c	Dr.	2,00,000	
To 9% Cumulative Preference Share Capital A/c			2,00,000
d. Surrendered shares issued to creditors under reconstruction scheme			
Shares Surrendered A/c	Dr.	35,000	
To Equity Share Capital A/c			35,000
e. Expenses Paid			
Expenses A/c	Dr.	10,000	
To Bank A/c			10,000
f. Cancellation of unissued surrendered shares			
Shares Surrendered A/c	Dr.	2,35,000	
To Capital Reduction A/c			2,35,000
g. Amount sacrificed by Directors			
Unsecured Loan A/c	Dr.	50,000	
Sundry Creditors A/c	Dr.	60,000	
Outstanding Expenses A/c	Dr.	20,000	
To Capital Reduction A/c			1,30,00

h.	Assets Written off			
	Capital Reduction A/c	Dr.	3,65,000	
	To Goodwill A/c			50,000
	To Loose tools A/c			8,000
	To Sundry debtors A/c			15,000
	To Stock - in - trade A/c			20,000
	To Profit and Loss A/c			2,00,000
	To Preliminary expenses A/c			5,000
	To Expenses A/c			10,000
	To Plant A/c			57,000
i.	Issue of Shares			
	Applications received			
	Bank A/c	Dr.	1,00,000	
	To Share Application A/c			1,00,000
	Allotment of Shares			
	Share Application A/c	Dr.	1,00,000	
	To Share Capital A/c			1,00,000
	(Being 50000 equity shares of ₹ 2 each issued as fully paid as per Board's Resolution dated...)			

Note 1 : a. Cancellation of Preference dividend need not be journalised; on cancellation it cease to be contingent liability and hence no further disclosure.

b. Preference shareholders have to forego policy rights presently enjoyed at par with Equity Shareholders.

Note 2 : The transfer of 100 shares by the dissentient shareholders to the director concerned need not be journalised.

Note 3 : It has been assumed that the share premium account is to be kept infact since the scheme is silent about it.

Name of the Company: P Ltd.					
Balance Sheet as at 31.03.2015					
Ref No.		**Particulars**	**Note No.**	**As at 31st March, 2015**	**As at 31st March, 2014**
				₹	₹
	I.	**Equity and Liabilities**			
	1	**Shareholders' funds**			
		(a) Share capital	1	3,65,000	
		(b) Reserves and surplus	2	90,000	
	2	**Share application money pending allotment**		Nil	
	3	**Non-current liabilities**		Nil	
	4	**Current Liabilities**			
		(a) Trade payables	3	2,40,000	
		(b)Other current liabilities	4	50,000	
		Total		7,45,000	

	II.	Assets			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	5	2,43,000	
	2	**Current assets**			
		(a) Inventories	6	1,32,000	
		(b) Trade receivables	7	2,35,000	
		(c) Cash and cash equivalents	8	1,35,000	
		Total		7,45,000	

Note: Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

		(₹)
Note 1. Share Capital	**As at 31st March, 2015**	**As at 31st March, 2014**
Particulars	**Amount (₹)**	**Amount (₹)**
Authorised : 1,50,000 equity shares of ₹ 12 each fully paid up	3,00,000	
2,000 8% cumulative preferrence shares of ₹ 100 each	2,00,000	
	5,00,000	
Issued, Subscribed and Paidup Subscribed Capital : 82,500Equity shares of ₹ 2 each fully paid up (of the above 17,500 shares have been issued other than cash under the scheme of reconstruction)	1,65,000	
2,000 9 % Cumulative Pref. Shares of ₹ 100 each fully paid up	2,00,000	
Total	3,65,000	

RECONCILIATION OF SHARE CAPITAL				
FOR EQUITY SHARE :-	**As at 31st March, 2015**		**As at 31st March, 2014**	
	Nos	**Amount (₹)**	**Nos**	**Amount (₹)**
Opening Balance as on 01.04.14	82,500	165,000,000	NIL	NIL
Add: Fresh Issue (Incld Bonus shares, Right shares, split shares, shares issued other than cash)			NIL	NIL
	82,500	165,000,000	NIL	NIL
Less: Buy Back of shares	-	-	-	-
	82,500	165,000,000	NIL	NIL

Note 2. Reserves and Surplus	**As at 31st March, 2015**	**As at 31st March, 2014**
Securities Premium	90,000	
Total	90,000	

Note 3. Trade Payables	**As at 31st March, 2015**	**As at 31st March, 2014**
Sundry creditors	2,40,000	
Total	2,40,000	

Note 4. Other Current Liabilities	**As at 31st March, 2015**	**As at 31st March, 2014**
Outstanding Expenses	50,000	
Total	50,000	

Note 5. Tangible assets		**As at 31st March, 2015**	**As at 31st March, 2014**
Plant	₹ 3,00,000		
less: Amount written off under the sceme of reconstruction	₹57,000	2,43,000	
Total		2,43,000	

Note 6. Inventories	**As at 31st March, 2015**	**As at 31st March, 2014**
Stock-in trade	1,30,000	
Loose tools	2,000	
Total	1,32,000	

Note 7. Trade receivables	**As at 31st March, 2015**	**As at 31st March, 2014**
Debtors	2,35,000	
Total	2,35,000	

8. Cash and Cash Equivalents	**As at 31st March, 2015**	**As at 31st March, 2014**
Cash at Bank	1,25,000	
Cash in Hand	10,000	
Total	1,35,000	

[H] DEMERGER

Illustration 22.

AB Ltd. has 2 divisions-A and B. Division A has been making constant profit, while Division B has been suffering losses. The Division wise Balance Sheet as on 31 March, 2014 are as follows:

	₹ in Lakhs		
	Division A	**Division B**	**Total**
Fixed assets: cost (Tangible)	500	1,000	1,500
Less: Depreciation	450	800	1,250
Written Down Value (i)	50	200	250
Current Assets:	400	1,000	1,400
Less : Current Liabilities	50	800	850
Net Current Assets (ii)	350	200	550
Total (i) + (ii)	400	400	800
Financed by:			
Loan	---	600	600
Capital: Equity Shares of 10 each	50	---	50
Reserves and Surplus	350	(200)	150
Total	400	400	800

Division B along with its assets and liabilities was sold for 50 lakhs to X Ltd., a new company which issued 2 lakhs equity shares of ₹10 each at a premium of ₹15 per share to the members of B Division in full settlement of the consideration in proportion to their shareholding in the company. Assuming that there are no other transactions, You are required to:

(i) Show journal entries in the books of AB Ltd.

(ii) Prepare the Balance Sheet of AB Ltd. after the entries made in (i) above.

(iii) Show journal entries in the books of X Ltd. (iv) Prepare the Balance Sheet of X Ltd.

In both the cases, Balance Sheets to be prepared Under the Scheduled III format.

Solution:

(i) Books of AB Ltd.

Journal

Date	Particulars		₹	₹
31.03.2014	X Ltd. A/c	Dr.	50	
	Current Liability A/c	Dr.	800	
	Accumulated Depreciation A/c	Dr.	800	
	Loan A/c	Dr.	600	
	To Fixed Assets A/c			1,000
	To Current Assets A/c			1,000
	To Capital Reserve A/c (Bal Fig.)			250
	(Being net assets transferred under scheme of demerger)			
31.03.2014	Equity Shares in X Ltd. A/c	Dr.	50	
	To X Ltd,. A/c			50
	(Being consideration received)			

Note: Division B was sold to X Ltd. The consideration received for transfer was equity shares of X Ltd. of 10 each fully paid, issued at a premium of ₹15.

The value of consideration = 2,00,000 shares x (10 + 15) = ₹ 50,00,000

(ii) Balance Sheet of AB Ltd. as on 31st March, 2014.

Ref. No.	Particulars	Note No.	Amount
I.	**EQUITY AND LIABILITIES**		**(₹ in Lakhs)**
	(1) Shareholders' Funds		
	(a) Share capital	1	50
	(b) Reserves, and Surplus	2	400
	(150 + Capital Reserve 200)		
	(2) Current Liabilities	3	50
	Total		500
II	**ASSETS**		
	(1) Non-current Assets		
	(a) Fixed Assets (500 - Dep. 450)	4	50
	(b) Non current investment	5	50
	(2) Current Assets	6	400
	Total		500

[Relevant Notes]

1. Share Capital

Particulars	Amount (₹ in Lakhs)
Authorized, issued, subscribed and paid up capital:	
5,00,000 equity shares of ₹10 each fully paid	50
Total	50

2. Reserves and Surplus

Particulars	Amount (₹ in Lakhs)
Capital Reserve	250
Profit and Loss (existing)	150
Total	400

3. Other Current Liabilities

Particulars	Amount (₹ in Lakhs)
Current Liabilities	50
Total	50

4. Tangible Assets

Particulars	Amount (₹ in Lakhs)
Fixed Assets less Depreciation (400 - 350)	50
Total	50

5. Non Current Investments

Particulars	Amount (₹ in Lakhs)
Investment in X Ltd.	50
Total	50

6. Other Current Assets

Particulars	Amount (₹ in Lakhs)
Current Assets	400
Total	400

(iii) Books of X Ltd.

Journal

Date	Particulars		₹	₹
31.03.2014	Fixed Assets A/c	Dr.	200	
	Current Assets A/c	Dr.	1,000	
	Goodwill A/c (Sal. Fig.)	Dr.	250	
	To Current Liability A/c			800
	To Loan A/c			600
	To Purchase Consideration			500
	(Being sundry assets and liabilities taken over.)			
31.03.2014	Purchase .Consideration A/c	Dr.	50	
	To Equity Share Capital A/c			20
	To Securities Premium A/c			30
	(Being purchase consideration settled.)			

(v) Balance Sheet of X Ltd. as on 31st March, 2014

Ref. No.		Particulars	Note No.	As at 31st March, 2012
I.	**EQUITY AND LIABILITIES**			**(₹ in Lakhs)**
	1.	Shareholders' Funds		
		(a) Share capital		20
		(b) Reserves, and Surplus		30
		(Securities Premium)		
	2.	Non- current Liabilities		
		(a) Loan		600
		(b) Current Liabilities		800
		Total		**1,450**
II.	**ASSETS**			
		Non-current Assets		
		(a) Fixed Assets (1,000 - Dep. 800)		200
		(b) Goodwill		250
		Current Assets		1,000
		Total		**1,450**

[I] REVERSE MERGER

Illustration 23.

The following are the Extracted Balance sheets of AB Ltd. and XY Ltd. as on 31.03.2015.

(₹ '000)

Liabilities	***AB Ltd.*** ₹	***XY Ltd.*** ₹	***Assets***	***AB Ltd.*** ₹	***XY Ltd.*** ₹
Share capital:			Fixed assets		
Equity Shares of ₹ 100	2,000	1,000	(net of depreciation)	2,700	850
each fully paid up			Investments	700	–
Reserves and surplus	800	–	Sundry Debtors	400	150
10% Debentures	500	–	Cash and Bank	250	–
Loan from Financial			Profit and Loss A/c	–	800
Institutions	250	400			
Bank Overdraft	–	100			
Sundry creditors	300	300			
Proposed Dividend	200	–			
Total	**4,050**	**1,800**	**Total**	**4,050**	**1,800**

Note: Loan from financial institution is assumed to be of more than 12 months (ignoring interest) hence treated as long term borrowings.

It was decided that XY Ltd. will acquire the business of AB Ltd. for enjoying the benefit of carry forward of business loss. After acquisition, XY Ltd. will be renamed as Z Ltd. The following scheme has been approved for the merger.

i. XY Ltd. will reduce its shares to ₹ 10 and then consolidate 10 such shares into one share of ₹ 100 each (New Share).

ii. Financial institutions agreed to waive 15% of the loan of XY Ltd.

iii. Shareholders of AB Ltd. will be given one new share of XY Ltd. in exchange of every share held in AB Ltd.

iv. AB Ltd. will cancel 20% holdings of XY Ltd. Investments were held at ₹ 250 thousands.

v. After merger, the proposed dividend of AB Ltd. will be paid to the shareholders of AB Ltd.

vi. Authorised Capital of XY Ltd. will be raised accordingly to carry out the scheme.

vii. Sundry creditors of XY Ltd. includes payables to AB Ltd. ₹ 1,00,000.

Pass the necessary entries to implement the scheme in the books of AB Ltd. and XY Ltd. and prepare a Balance Sheet of Z Ltd.

Solution:

Part - I Purchase consideration

WN # 1 : Shareholding of AB Ltd. in XY Ltd.

Particulars	Amount ₹
a. Original Share capital of XY Ltd. [10,000 equity shares of ₹ 100 each]	10,00,000
b. Share capital of XY Ltd. after reduction [10,000 equity shares of ₹ 10 each]	1,00,000
c. Share capital of XY Ltd. after reconsolidation [1000 equity shares of ₹ 100 each]	1,00,000
d. Holding of AB Ltd in XY Ltd.	20%
e. Value of holding of AB Ltd in XY Ltd. [200 equity shares of ₹ 100 each]	20,000

WN # 2 : Purchase consideration

a. No. of equity shares of AB Ltd. (20,00,000 ÷ 100)	20,000
b. Exchange ratio	1:1
c. No. of equity shares to be given by XY Ltd. to AB Ltd.	20,000
d. Less : No. of Equity shares held by AB Ltd. in XY Ltd.	200
e. No. of shares now to be given	19,800
f. Purchase consideration (19,800 equity shares of ₹ 100 each)	19,80,000

Part - II : Journal entries in the books of AB Ltd.

(₹ '000)

Particulars		Debit	Credit
1. a. Transfer to realisation account of all Assets taken over except investment held by selling company in purchasing company			
Realisation A/c	Dr.	3,800	
To Fixed assets A/c			2,700
To Investments [700 - 250] A/c			450
To Sundry Debtors A/c			400
To Cash and Bank A/c			250
b. Transfer to realisation account of all liabilities taken over			
10% Debentures A/c	Dr.	500	
Loan from financial institations A/c	Dr.	250	
Sundry Creditors A/c	Dr.	300	
Proposed Dividend A/c	Dr.	200	
To Realisation A/c			1250

2. Purchase consideration			
a. Due entry			
XY Ltd. A/c	Dr.	1,980	
To Realisation A/c			1,980
b. Receipt			
Shares in XY Ltd. A/c	Dr.	1,980	
To XY Ltd. A/c			1,980
3. Transfer of realisation loss to share holders			
Equity shareholders A/ c	Dr.	570	
To Realisation A/c			570
4. Transfer of Share capital and Reserves and surplus to equity share holders			
Share capital A/c	Dr.	2,000	
Reserves and surplus A/c	Dr.	800	
To Equity shareholders			2,800
5. Settlement to share holders by transfer of purchase consideration now received and shares already held by AB Ltd. in XY Ltd.			
Equity shareholders A/c	Dr.	2,230	
To Equity shares of XY Ltd.			2,230

Part. III. Journal entries in the books of XY Ltd.

(₹ '000)

Particulars		Debit	Credit
1. Reduction of Share capital			
Equity Share Capital (₹ 100) A/c	Dr.	1,000	
To Equity Share Capital (₹ 10) A/c			100
To Reconstruction A/c			900
2. Consolidation of equity shares of ₹10 each to ₹ 100 each			
Equity Share Capital (₹ 10) A/c	Dr.	100	
To Equity Share Capital (₹ 100) A/c			100
3. Waiver of loan by financial institution			
Loan from financial institution A/c	Dr.	60	
To Reconstruction A/c			60
4. Write off the debit balance of Profit and Loss A/c by utilising Reconstruction A/c and balance of Reconstruction A/c transferred to Capital reserve			
Reconstruction A/c	Dr.	960	
To Profit and Loss A/c			800
To Capital Reserve A/c			160

Entries relating to Amalgamation **:**

- Nature of Amalgamation - Merger
- Method of Accounting - Pooling of Interest Method

(₹ '000)

Particulars			Debit	Credit
1. For Purchase Consideration Due				
Business Purchase A/c		Dr.	1,980	
To Liquidator of AB Ltd. A/c				1,980
2. For assets and liabilities taken over				
Purchase consideration now paid	1,980			
Shares already held by AB Ltd.	250			
Total consideration	2,230			
Less: Paid-up Share capital of AB Ltd.	2,000			
Excess Purchase Consideration Paid	230			
This excess is to be adjusted against reserves of AB Ltd.				
Reserves of AB Ltd. 800				
Less: Excess as above 230				
Balance to be incorporated 570				
Fxed assets (net of depreciation) A/c		Dr.	2,700	
Investment A/c		Dr.	450	
Sundry Debtors A/c		Dr.	400	
Cash and Bank A/c		Dr.	250	
To Reserves and Surplus A/c				570
To Debentures A/c				500
To Loan from financial institutions A/c				250
To Sundry Creditors A/c				300
To Proposed Dividend A/c				200
To Business Purchase A/c				1,980
3. Discharge of purchase consideration				
Liquidator of AB Ltd. A/c		Dr.	1,980	
To Equity Share capital of XY Ltd. A/c				1,980
4. Payment of proposed divided to shareholders of AB Ltd.				
Proposed Dividend A/c		Dr.	200	
To Bank A/c				200
5. Cancellation of inter company owings				
Sundry Creditors A/c		Dr.	100	
To Sundry Debtors A/c				100

Name of the Company: Z Ltd.					
Balance Sheet as at 31st March, 2015 (and Reduced)					
Ref No.	**Particulars**		**Note No.**	**As at 31st March, 2015**	**As at 31st March, 2014**
				(₹ in '000)	**(₹ in '000)**
	I.	**Equity and Liabilities**			
	1	**Shareholders' funds**			
		(a) Share capital	1	2,080.00	
		(b) Reserves and surplus	2	730.00	
	2	**Share application money pending allotment**		Nil	
	3	**Non-current liabilities**			
		(a) Long-term borrowings	3	1,090.00	
	4	**Current Liabilities**			
		(a) Trade payables	4	500.00	
		(b) Other current liabilities	5	50.00	
		Total		4,450.00	
	II.	**Assets**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	6	3,550.00	
		(b) Non-current investments	7	450.00	
	2	**Current assets**			
		(a) trade receivables	8	450.00	
		Total		4450.00	

Note : Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

(₹ '000)

Note 1. Share Capital	**As at 31st March, 2015**	**As at 31st March, 2014**
A. Authosired, Issued, Subscribed and paid up:- Equity Shares of ₹ 100 each issued and Fully paid up (1,980+20+80)	2,080	
Total	2,080	

RECONCILATION OF SHARE CAPITAL

FOR EQUITY SHARE :-	**As at 31st March, 2015**		**As at 31st March, 2014**	
	Nos	**Amount (₹)**	**Nos**	**Amount (₹)**
Opening Balance as on 01.04.14	20.8	2,080.00	NIL	NIL
Add: Fresh Issue (Incld Bonus shares , Right shares, split shares, shares issued other than cash)	-	-	NIL	NIL
	20.8	2,080.00	NIL	NIL
Less: Buy Back of shares	-		-	-
	20.8	2,080.00	NIL	NIL

Note 2. Reserves and Surplus	**As at 31st March, 2015**	**As at 31st March, 2014**
General Reserve	160	
Capital Reserve	570	
Total	730	

Note 3. Long Term Borrowings	As at 31st March, 2015	As at 31st March, 2014
100% debentures Loan from Financial Institution	500 590	
Total	1090	

Note 4. Trade Payables	As at 31st March, 2015	As at 31st March, 2014
Creditors (600-100)	500	
Total	500	

Note 5. Other Current Liabilities	As at 31st March, 2015	As at 31st March, 2014
Bank Overdraft (200+100-250)	50	
Total	50	

Note 6. Tangible Assets	As at 31st March, 2015	As at 31st March, 2014
Fixed Assets net of depreciation (2,700+850)	3,550	
Total	3,550	

Note 7. Non-Current Investments	As at 31st March, 2015	As at 31st March, 2014
Investments (700-250)	450	
Total	450	

Note 8. Trade Receivables	As at 31st March, 2015	As at 31st March, 2014
Sundry Debtors (400+150-100)	450	
Total	450	

[J] EXTERNAL RECONSTRUCTION

Illustration 24.

A Ltd. is engaged in the manufacture of D and N. It has two wholly owned subsidiaries. B Ltd. and C Ltd. which have never traded. The draft financial statement of parent company shows:

Extracted Balance Sheet as on 31st March, 2015

Liabilities	₹	***Assets***	₹
Share Capital	40,000	Fixed Assets	21,400
Reserves and surplus	48,800	Investment in B Ltd.	10,000
Secured loan	12,000	Investment in C Ltd.	10,000
Sundry creditors	90,000	Current assets	
Owing to subsidiaries	20,000	Stock and Work-in-progress	43,400
Proposed dividend	4,000	Sundry debtors	9,360
		Cash at bank	36,400
	2,14,800		**2,14,800**

Note: Secured loan and owing to subsidiary is assumed to be not less than 12 months, hence treated as long term borrowings (ignoring interest).

Profit and Loss Account for the year ended 31st March, 2015

	₹
Net Profit	37,200
Less : Dividend Paid	4,000
Transfer to Reserve	33,200

The two managing directors Mr. Kali and Mr. Prem who own 40% and 60% respectively of the Share capital of A Ltd. will become individually concerned with B Ltd. and C Ltd. respectively in order to allow them to develop their own interests.

They have agreed to a scheme of reconstruction whereby the respective trade and assets apart from cash at bank and liabilities will be transferred to the two subsidiaries. The resulting inter-company debts will be waived and A Ltd. will be placed into liquidation. The liquidator will retain ₹ 5,200 of the cash at bank to meet the costs of liquidation and reorganisation and pay dividend. He will distribute the remaining cash at bank and shares in two subsidiaries to A Ltd's shareholders Mr. Kali and Mr. Prem.

As far as his cash distribution pool permits, each director will then purchase, at net assets value, those shares in his own company distributed by the liquidator to his former colleague. It has been agreed that B Ltd. will receive a first tranch of the assets of A Ltd. comprising stock and work in progress of ₹ 15,000. C Ltd. will take over the liability for the Secured Loan. The remainder of the net assets will be transferred to the subsidiary companies in the ratio of 75% to B Ltd. and 25% of C Ltd. with the group freehold property, included in the Fixed assets at ₹ 15,000 being revalued at the open market value of ₹ 42,000 and being transferred to C Ltd. as a part of its share.

You are required to :

a. Produce the proforma balance sheets of the two former subsidiary immediately after reorganisation.

b. Calculate the final share holdings in each of the two companies.

Solution:

Purchase Consideration:

Particulars	B Ltd. ₹	C Ltd. ₹
Stock in trade	15,000	—
Secured Loan	—	(12,000)
Remaining Net Assets in the Ratio of 75:25 (WN#1)	60,300*	20,100*
	75,300	**8,100**
Total Purchase Consideration	**₹ 83,400**	

WN # 1 : Net Asset Value :

Particulars		₹	₹
a.	Fixed Asset:	15,000	
	Add: Increase due to Revaluation	27,000	
	Others (21,400 – 15,000)	6,400	48,400
b.	Stock and Work-in-progress	43,400	
	Less: Separately taken by B Ltd.	15,000	28,400
c.	Sundry Debtors		93,600
d.	Total Assets (a+b+c)		1,70,400
e.	Sundry Creditors		(90,000)
f.	Net Assets		80,400
g.	B Ltd. Share (75% of Net Assets)		60,300
h.	A Ltd. Share (25% of Net Assets)		20,100

Shareholders Account

Dr. **Cr.**

	Kali (40%)	**Prem (60%)**		**Kali (40%)**	**Prem (60%)**
To Cash	12,480@	18,720@	By Share capital	16,000	24,000
To B Ltd.	33,360		By Reserve	19,520	29,280
To C Ltd.		50,040	By Realisation (Profit)	10,320#	15,480#
	45,840	**68,760**		**45,840**	**68,760**

Cash **(₹)**

Particulars	***Amount***
Opening balance	36,400
Retained by liquidator	(5,200)
Closing balance	31,200
Kalii's share [40% of (c)]	12,480
Prem's share [60% of (c)]	18,720

Realisation Profit

Particulars	***Amount***
Dividend	4,000
Revaluation on Fixed assets (42,000 – 15,000)	27,000
Liquidation expenses:	(5,200)
Net realisation profit	25,800
Kali [40% of (d)]	10,320
Prem [60% of (d)]	15,480

WN # 2 : Statement showing Goodwill or Capital Reserves

	Particulars	B Ltd. (₹)	C Ltd. (₹)
a.	Purchase Consideration	75,300	8,100
b.	Less: Net Assets as at the date of acquisition		
	representedby :	10,000	10,000
	- Share capital		
c.	Goodwill		**1,900**
d.	Capital Reserves	**65,300**	

Proforma Balance Sheet of B Ltd. as on 31st March, 2015.

Liabilities	Amount ₹	Assets	Amount ₹
Share Capital	10,000	Fixed Assets	6,400
Reserves and Surplus	65,300	Current Assets:	
Current liabilities		Stocks and Work-in-Progress	43,400
Creditors	68,100	Debtors	93,600
	1,43,400		**1,43,400**

Proforma Balance Sheet of C Ltd. as on 31st March, 2015.

Liabilities	Amount ₹	Assets	Amount ₹
Share Capital	10,000	Fixed assets	42,000
Secured Loan	12,000	Goodwill	1,900
Current liabilities	21,900		
	43,900		**43,900**

Illustration 25.

AB Ltd has 2 divisions - A and B. The draft Balance Sheet as at 31, March, 2015 was as under:

(₹ *in Crores*)

		A		B		Total
Fixed assets						
Cost		600		300		900
Depreciation		500		100		600
W.D.V.		100		200		300
Net Current Assets						
Current Assets	400		300		700	
Less: Current Liabilities	100	300	100	200	200	500
Total		**400**		**400**		**800**
Financed by:						
Loans		—		100		100
(Secured by a charge on Fixed assets)		—		100		100
Own funds:						
Equity capital						50
(Fully paid up ₹ 10 shares)						
Reserves and surplus						650
						700
Total		**400**		**400**		**800**

It is decided to form a new company B Ltd., to take over the assets and liabilities of B division.

According B. Ltd. was incorporated to take over at balance sheet figures, the assets and liabilities of that division. B Ltd. is to allot 5 crores equity shars of ₹ 10 each in the company to the members of AB Ltd., in full settlement of the consideration. The members of AB Ltd. are therefore to become members of B Ltd. as well without having to make any further investment.

a. You are asked to pass journal entries in relation to the above in the books of AB Ltd. and B. Ltd. Also show the Balance Sheets of the 2 companies as on the morning of 1st April, 2015, showing corresponding previous year's figures.

b. The directors of the 2 companies, ask you to find out the net asset value of equity shares pre and post demerger.

c. Comment on the impact of demerger on "shareholders wealth".

Solution:

Part I: In the Books of M/s. AB Ltd.

(₹ in Crores)

	Particulars		*Debit*	*Credit*
i.	Transfer of assets and liabilities of Division B to B Ltd.			
	(a) For Purchase Consideration Due:			
	A Ltd. A/c	Dr.	50	
	Loan funds A/c	Dr.	100	
	Curent liabilities A/c	Dr.	100	
	Povision for depreciation A/c	Dr.	100	
	Profit and Loss A/c (balancing figure)	Dr.	250	
	To Fixed Assets A/c			300
	To Current Assets A/c			300
ii.	Cancellation of balance in A Ltd. not receivable since consideration is paid to members of AB Ltd. in full			
	Reserves A/c	Dr.	50	
	To A Ltd.			50

Part II: In the Books of B Ltd.

(₹ in crores)

	Particulars		*Debit* ₹	*Credit* ₹
i.	For Purchase Consideration Due:			
	Business Purchase A/c	Dr.	50	
	To Shareholders of AB Ltd. A/c			
ii.	Assets and liabilities taken over			
	Fixed Assets A/c	Dr.	200	
	Current Assets A/c	Dr.	300	
	To Loan A/c			100
	To Current liabilities A/c			100
	To Capital Reserve (balancing figure)			250
	To Business Purchase A/c			50
iii.	Discharge of purchase consideration			
	Shareholders of AB Ltd.	Dr.	50	
	To Equity Share capital A/c			50

Part III: Balance Sheet of two companies after reorganisation.

Name of the Company: Y Ltd.							
Balance Sheet as at 01.04.2015							
				AB Ltd.		**B Ltd.**	
Ref No.	**Particulars**		**Note No.**	**As at 1st April, 2015**	**As at 31st March, 2015**	**As at 1st April, 2015**	**As at 31st March, 2015**
				(₹ **in Crore**)	(₹ **in Crore**)	(₹ **in Crore**)	(₹ **in Crore**)
	I.	**Equity and Liabilities**					
	1	**Shareholders' funds**					
		(a) Share capital	1	50.00	50.00	50.00	-
		(b) Reserves and surplus	2	350.00	650.00	250.00	-
	2	**Share application money pending allotment**		Nil	Nil	Nil	-
	3	**Non-current liabilities**					
		(a) Long-term borrowings	3	-	100.00	100.00	-
	4	**Current Liabilities**		Nil	Nil	Nil	-
		Total		400.00	800.00	400.00	-
	II.	**Assets**					
	1	**Non-current assets**					
		(a) Fixed assets					
		(i) Tangible assets	4	100.00	300.00	200.00	-
	2	**Current assets**					
		(a) Other current assets	5	300.00	500.00	200.00	-
		Total		400.00	800.00	400.00	

Note: Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

(₹ in Crores)

Note 1. Share Capital	**01.04.2015**		**31.03.2015**
	Before AB Ltd.	**After B Ltd.**	**Before AB**
Authorised, Issued, Subscribed and paid up Equity Share of ₹ 10 each fully paid	- 50.00	- 50.00	- 50.00
Total	50.00	50.00	50.00

Note 2. Reserve and Surplus	**01.04.2015**				**31.03.2015**	
	Before AB Ltd.		**After B Ltd.**		**Before AB**	
Capital Reserve	-			250.00	-	
Revenue Reserve		650.00	-		650.00	650.00
Less : Trf to B Ltd.	250.00					
Less : Cancel due frm B Ltd.	50.00					
		300.00				
Total		350.00	-	250.00		650.00

Note 3. Long Term Borrowings	**01.04.2015**		**31.03.2015**
	Before AB Ltd.	**After B Ltd.**	**Before AB**
Loan Funds	-	100.00	100.00
Total	-	100.00	100.00

Note 4. Tangible Assets	01.04.2015				31.03.2015	
	Before AB Ltd.		After B Ltd.		Before AB	
Fixed Assets	600.00	-	300.00	-	900.00	-
Less : Provision for Depreciation	500.00	-	100.00	-	600.00	-
Total	100.00	-	200.00	-	300.00	-

Note 5. Other Current Assets	01.04.2015		31.03.2015
	Before AB Ltd.	After B Ltd.	Before AB
Current Asset (Net)	300.00	200.00	500.00
Total	300.00	200.00	500.00

(₹ in Crores)

	A	*B*	*AB*
Value of total assets	800	400	400
Less: Loan funds	(100)	—	(100)
Net assets	700	400	300
Net assets belonging to Equity share holders after December		700	

Conclusion:

The impact on share holders wealth after reorganisation is Nil.

[K] Notes to Accounts & Related Disclosures

Illustration 26.

The following information has been extracted from the books of account of Hero Ltd. as at 31st March, 2015:

(₹ '000)

	Dr.	Cr.
Administration Expenses	480	
Cash at Bank and on Hand	228	
Cash Received on Sale of Fittings		10
Long Term Loan		70
Investments	200	
Depreciation on Fixtures, Fittings, Tools and Equipment		
(1st April, 2014)		260
Distribution Costs	102	
Factory Closure Costs	60	
Fixtures, Fittings, Tools and Equipment at Cost	680	
Profit & Loss Account (at 1st April, 2014)		80
Purchase of Equipment	120	
Purchases of Goods for Resale	1710	
Sales (net of Excise Duty)		3,000
Share Capital (1,00,000 shares of @ ₹10 each fully paid)		1,000
Stock (at 1st April, 2014)	140	
Trade Creditors		80
Trade Debtors	780	
	4,500	4,500

Additional Information:

(1) The stock at 31st March, 2015 (valued at the lower of cost or net realizable value) was estimated to be worth ₹ 2,00,000.

(2) Fixtures, fittings, tools and equipment all related to administration. Depreciation is charged at a rate of 20% per annum on cost. A full year's depreciation is charged in the year of acquisition, but no depreciation is charged in the year of disposal.

(3) During the year to 31st March, 2015, the Company purchased equipment of ₹ 1,20,000. It also sold some fittings (which had originally cost ₹ 60,000) for ₹ 10,000 and for which depreciation of ₹ 30,000 had been set aside.

(4) The average Income tax for the Company is 50%. Factory closure cost is to be presumed as an allowable expenditure for Income tax purpose.

(5) The company proposes to pay a dividend of 20% per Equity Share.

Prepare Hero Ltd.'s Profit and Loss Account for the year to 31st March, 2015 and Balance Sheet as at that date in accordance with the Companies Act, 2013 in the Vertical Form along with the Notes on Accounts containing only the significant accounting policies.

Solution:

Name of he Company : Hero Ltd.

Balance Sheet as at 31st March, 2015

(₹ In '000)

Ref No.		Particulars	Note No.	As at 31st March, 2015	As at 31st March, 2014
	I	**EQUITY AND LIABILITIES**			
	1	**Shareholder's Fund**			
		(a) Share capital	1	1,000	
		(b) Reserves and surplus	2	150	
	2	**Share application money pending allotment**		Nil	
	3	**Non-current liabilities**			
		(a) Long-term borrowings	3	70	
	4	**Current Liabilities**			
		(a) Other current liabilities	4	80	
		(b) Short-term provisions	5	470	
		Total (1+2+3+4)		1,770	
	II	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	6	362	
		(b) Non-current investments	7	200	
	2	**Current assets**			
		(a) inventories	8	200	
		(b) trade receivables	9	780	
		(c) Cash and cash equivalents	10	228	
		Total (1+2)		1,770	

Note: Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

		Note No.		As at 31st March, 2015	As at 31st March, 2014
I	REVENUE FROM OPERATION	11		3,000	
	Less: Excise duty				
				3,000	
II	OTHER INCOME				
III	TOTAL REVENUE(I+II)			3000	
IV	EXPENSES:				
	(a) Purchase of products for sale		1,710		
	(b) changes in inventories of finished goods, work-in-progress and products for sale (140-160)		(60)		
	(c) Depreciation and amortization expenses		148		
	(d) Other expenses	12	602		
	TOTAL EXPENSES			2,400	
V	PROFIT BEFORE EXCEPTIONAL AND EXTRAORDINARY ITEMS AND TAX (III-IV)			600	
VI	EXCEPTIONAL ITEMS			Nil	
VII	PROFIT BEFORE EXTRAORDINARY ITEMS AND TAX (V-VI)			600	
VIII	EXTRAORDINARY ITEMS			60	
IX	PROFIT BEFORE TAX FRON CONTINUING OPERATIONS (VII-VIII)			540	
X	Tax expenses:				
	(1) Current Tax			270	
	(2) deferred tax			-	
XI	PROFIT AFTER TAX FOR THE YEAR FROM CONTINUING OPERATION(IX-X)			270	
XII	Profit (loss) from discontinuing operations				
XIII	Tax expenses from discontinuing operations				
XIV	Profit(loss) from discontinuing operations (after tax) (XII-XIII)			Nil	
XV	PROFIT (LOSS) FOR THE PERIOD (XI+XIV)			270	
	Balance brought forward from previous year				
	Profit available for appropriation			80	
				350	
	Appropriation:				
	Proposed dividend		200		
	Transfer to General Reserve		30	230	
	Balance carried forward			120	
XVI	Earning per equity share:				
	(1) Basic				
	(2) Diluted				

(₹ In '000)

Note 1. Share Capital	**As at 31st March, 2015**	**As at 31st March, 2014**
Authorized, Issued, Subscribed and paid-up Share capital:-		
1,00,000 Equity share of ₹10 each	1,000	
Total	1,000	

RECONCILIATION OF SHARE CAPITAL

FOR EQUITY SHARE	**As at 31st March, 2015**		**As at 31st March, 2014**	
	Nos.	**Amount (₹)**	**Nos.**	**Amount (₹)**
Opening Balance as on 01.04.11 (Figure in '000)	100	1,000		
Add: Fresh Issue (Including Bonus shares, right shares, split shares, share issued other than cash)				
	100	1,000		
Less: Buy Back of share				
Total	100	1,000		

Note 2. Reserve & Surplus	**As at 31st March, 2015**	**As at 31st March, 2014**
General Reserve	30	
Profit and loss A/c	120	
Total	150	

Note 3. Long term borrowings	**As at 31st March, 2015**	**As at 31st March, 2014**
Long term loan	70	
Total	70	

Note 4. Trade Payables	**As at 31st March, 2015**	**As at 31st March, 2014**
Sundry Creditors	80	
Total	80	

Note 5. Short- term provisions	**As at 31st March, 2015**	**As at 31st March, 2014**
Proposed dividend (20% on ₹10,00,000)	200	
Provision for Taxation	270	
Total	470	

Note 6. Tangible Assets		**As at 31st March, 2015**	**As at 31st March, 2014**
Fixtures, Fittings, Tools and equipment at cost- Opening	680		
Add: Additions	120		
Less: Sale/ disposed	(30)		
Less: Depreciation (260+148)	(408)	362	
Total		362	

Note 7. Non Current Investments	As at 31st March, 2015	As at 31st March, 2014
Investments	200	
Total	200	

Note 8. Inventories	As at 31st March, 2015	As at 31st March, 2014
Stock	200	
Total	200	

Note 9.Trade Receivables	As at 31st March, 2015	As at 31st March, 2014
Trade Debtors (more than six months considered good) –	780	
Total	780	

Note 10. Cash and cash equivalents	As at 31st March, 2015	As at 31st March, 2014
Cash at Bank and on hand	228	
Total	228	

Note 11. Revenue from operation	As at 31st March, 2015	As at 31st March, 2014
Sales (net of Excise Duty)	3,000	
Total	3,000	

Note 12. Other Expenses	As at 31st March, 2015	As at 31st March, 2014
Administrative Expenses	480	
Distribution Expenses	102	
Loss on sale of Fixed Assets	20	
Total	602	

Notes on Accounts for the year ended 31st March, 2015

Significant Accounting Policies:

(a) Basis for preparation of financial statements: The financial statements have been prepared under the historical cost convention, in accordance with the generally accepted accounting principles and the provisions of the companies Act, 2013 as adopted consistently by the company.

(b) Depreciation: Depreciation on fixed assets is provided using the straight-line method, based on the period of five years. Depreciation on additions is provided for the full year but no depreciation is provided on assets sold in the year of their disposal.

(c) Investments: Investments are valued at lower of cost or net realizable value.

(d) Inventories: Inventories are valued at the lower of historical cost or the net realizable value.

Working Notes:

(₹ in thousands)

(1)	Fixtures, Fittings, Tools and Equipment		
	Gross Block		
	As on 1.4.2014	680	
	Add: Additions during the year	120	
		800	
	Less: Deductions during the year	60	
	As on 31.3.2015		740
	Depreciation		
	As on 1.4.2014	260	
	For the year (20% on 740)	148	
		408	
	Less: Deduction during the year	30	
	As on 31.3.2015		378
	Net block as on 31.3.2015		362
(2)	Provision for taxation		
	Profit as per profit and loss account		540
	Add back: Loss on sale of asset (short term capital loss)	20	
	Depreciation	148	
			168
			708
	Less: Depreciation under Income-tax Act		168
			540
	Provision for tax @ 50%		270
	It has been assumed that depreciation calculated under Income-tax Act amounts to ₹1,68,000)		
(3)	Provisions		
	(a) Provision for taxation		270
	(b) Proposed dividend (20% on ₹10,00,000)		200
			470

(4) In balance sheet, Reserves and Surplus represent general reserve ₹30,000 and profit and loss account ₹1,20,000.

Notes:

(1) The rate of interest on long term loan is not given in the question. Reasonable assumption may be made regarding the rate of interest and accordingly it may be accounted for.

(2) As per Companies (Transfer of Profits to Reserve) Rules, the amount to be transferred to the reserves shall not be less than 7.5% of the current profits since proposed dividend exceeds 15% but does not exceed 20% of the paid up capital. In this answer, it has been assumed that ₹30,000 have been transferred to General Reserve. The students may transfer any amount based on a suitable percentage not less than 7.5%.

(3) In the absence of details regarding factory closure costs, there costs are treated as extraordinary items in the above solution assuming that the factory is permanently closed. However, the factory may close for a short span of time on account of strikes, lockouts etc. and such type of factory closure costs should be treated as loss from ordinary activities. In that case also, a separate disclosure regarding the factory closure costs will be required as per para 12 of AS 5 (Revised) 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies.'

Illustration 27.

On 1st April, 2014 Zigzag Enterprises Ltd. was incorporated with an Authorised Capital of ₹ 50 lakhs. Its first accounts were closed on 31st March, 2015 by which time it had become a listed company with an issued subscribed and paid up Capital of ₹ 40 lakhs in 4,00,000 Equity Shares of ₹ 10 each. The company started off with two lines of business namely 'First Division' and 'Second Division', with equal asset base with effect from 1st April, 2015. The 'Third Division' was added by the company on 1st April, 2015. The following data is gathered from the books of account of Zigzag Enterprises Ltd:

Trial Balance as on 31st March, 2015.

(₹ in 000's)

	Dr.	Cr.
First Division sales	–	15,000
Cost of First Division sales	6,500	–
Second Division sales	–	20,000
Cost of sales of Second Division	10,750	–
Third Division Sales	–	3,750
Cost of sales of Third Division	2,250	–
Administration costs	5,000	–
Distribution costs	3,750	–
Dividend-Interim	3,000	–
Fixed Assets at cost	22,500	–
Accumulated Depreciation on Fixed Assets	–	3,750
Stock on 31st March, 2015	1,000	–
Trade Debtors	1,100	–
Cash at Bank	400	–
Trade Creditors	–	1,250
Equity Share Capital in shares of ₹ 10 each	–	10,000
Retained Profits	–	2,500
	56,250	56,250

Additional Information:

(a) Administration costs should be split between the Divisions in the ratio of 5 : 3 : 2.

(b) Distribution costs should be spread over the Divisions in the ratio of 3 : 1 : 1.

(c) Directors have proposed a Final Dividend of ₹ 20 lakhs.

(d) Some of the users of Third Division are unhappy with the product and have lodged claims against the company for damages of ₹ 18.75 lakhs. The claim is hotly contested by the company on legal advice.

(e) Fixed Assets worth ₹ 75 lakhs were added in the Third Division on 1.4.2015.

(f) Fixed Assets are written off over a period of 10 years on straight line basis in the books. However for Income tax purposes depreciation at 20% on written down value of the assets is allowed by Tax Authorities.

(g) Income tax rate may be assumed at 35%.

(h) During the year First Division has sold to Hitachi Ltd. goods having a sales value of ₹ 62.5 lakhs. Mr. Rydu, the Managing Director of Zigzag Enterprises Ltd. owns 100% of the issued Equity Shares of Hitachi Ltd. The sales made to Hitachi Ltd. were at normal selling price of Zigzag Enterprises Ltd.

You are required to prepare Profit and Loss Account for the year ended 31st March, 2015 and the Balance Sheet as at the date. Your answer should include notes and disclosures as per Accounting Standards.

Solution:

Name of the company : ZIG ZAG Ltd.

Balance Sheet as at 31st March, 2015

(₹ In crores)

Ref No.	Particulars		Note No.	As at 31st March, 2015	As at 31st March, 2014
	1	**EQUITY AND LIABILITIES**			
		(a) Share capital	1	10,000	
		(b) Reserves and surplus	2	3,800	
	2	**Share application money pending allotment**		Nil	
	3	**Non-current liabilities**			
		(a) Deferred tax liabilities (Net)	3	1,102.50	
	4	**Current Liabilities**			
		(a) Trade payables	4	1,250	
		(b) Short-term provisions	5	5,097.50	
		Total (1+2+3+4)		21,250	
	II	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	6	18,750	
	2	**Current assets**			
		(a) inventories	7	1,000	
		(b) trade receivables	8	1,100	
		(c) Cash and cash equivalents	9	400	
		Total (1+2)		21,250	

Name of the company : ZIG ZAG Ltd.

Profit and Loss Statement for the year ended 31st March, 2015

(₹ In crore)

		Note No.		As at 31st March, 2015	As at 31st March, 2014
I	REVENUE FROM OPERATION	10		38,750	
	Less: Excise duty				
				38,750	
II	OTHER INCOME			Nil	
III	TOTAL REVENUE(I+II)			38,750	
IV	EXPENSES:				
	(a) Cost of material consumed				
	(b) Purchase of products for sale				
	(C) changes in inventories of finished goods, work-in-progress and products for sale				

	(d) Cost of sale	11	19,500		
	(d) Employees cost/ benefits expenses				
	(e) Finance cost				
	(f) Depreciation and amortization expenses				
	(g) Other expenses	12	8,750		
	TOTAL EXPENSES			28,250	
V	PROFIT BEFORE EXCEPTIONAL AND EXTRAORDINARY ITEMS AND TAX (III-IV)			10,500	
VI	EXCEPTIONAL ITEMS			Nil	
VII	PROFIT BEFORE EXTRAORDINARY ITEMS AND TAX (V-VI)			10,500	
VIII	EXTRAORDINARY ITEMS			Nil	
IX	PROFIT BEFORE TAX FRON CONTINUING OPERATIONS (VII-VIII)			10,500	
X	Tax expenses:				
	(1) Current Tax		3,097.50		
	(2) deferred tax		577.50	3,675	
XI	PROFIT AFTER TAX FOR THE YEAR FROM CONTINUING OPERATION(IX-X)			6,825	
XII	Profit (loss) from discontinuing operations				
XIII	Tax expenses from discontinuing operations				
XIV	Profit(loss) from discontinuing operations (after tax) (XII-XIII)			Nil	
XV	PROFIT (LOSS) FOR THE PERIOD (XI+XIV)			6,825	
	Balance brought forward from previous year			1,975	
	Profit available for appropriation			8,800	
	Appropriation:				
	Proposed dividend			5,000	
	Balance carried forward			3,800	
XVI	Earning per equity share:			Nil	
	(1) Basic				
	(2) Diluted				

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note to the Accounts

(₹ In '000)

Note 1. Share Capital	**As at 31st March, 2015**	**As at 31st March, 2014**
Authorized Equity share capital of ₹10 each	15,000	
Issued, Subscribed and paid-up Share capital : 10,00,000 Equity share of ₹10 each fully paid	10,000	
Total	100	

RECONCILIATION OF SHARE CAPITAL

FOR EQUITY SHARE	As at 31st March, 2015		As at 31st March, 2014	
	Nos.	Amount (₹)	Nos.	Amount (₹)
Opening Balance as on 01.04.14	10,00,000	10,000		
Add: Fresh Issue (Including Bonus shares, right shares, split shares, share issued other than cash)				
	10,00,000	10,000		
Less: Buy Back of share				
Total	10,00,000	10,000		

Note 2. Reserve & Surplus	As at 31st March, 2015	As at 31st March, 2014
Retained profits	3,800	
Total	3,800	

Note 3. Deferred Tax Liability	As at 31st March, 2015	As at 31st March, 2014
Opening Deferred tax liability	525	
Add: Deferred tax liability during the year	577.50	
Total	1,102.50	

Note 4. Trade Payables	As at 31st March, 2015	As at 31st March, 2014
Trade Creditors	1,250	
Total	1,250	

Note 5. Short-term Provisions	As at 31st March, 2015	As at 31st March, 2014
Provision for Tax	3,097.50	
Proposed Dividend	2,000	
Total	5,097.5	

Note 6. Tangible Assets	As at 31st March, 2015	As at 31st March, 2014
Fixed Assets- Gross Block	22,500	
Less: Depreciation	3,750	
Total	18,750	

Note 7. Inventories	As at 31st March, 2015	As at 31st March, 2014
Stock	1,000	
Total	1,000	

Note 8. Trade receivables	As at 31st March, 2015	As at 31st March, 2014
Trade Debtor's	1,100	
Total	1,100	

Note 9.Cash and cash equivalents	As at 31st March, 2015	As at 31st March, 2014
Cash at bank	400	
Total	400	

Note 10. Revenue from operation	As at 31st March, 2015	As at 31st March, 2014
Sales (net of Excise Duty)	38,750	
Total	38,750	

Note 11. Cost of sale	As at 31st March, 2015	As at 31st March, 2014
First Division	6,500	
Second Division	10,750	
Third Division	2,250	
Total	19,500	

Note 12. Other expenses	As at 31st March, 2015	As at 31st March, 2014
Administration costs (2,500+1,500+1,000)	5,000	
Distribution cost (2,250+750+750)	3,750	
Total	8,750	

Notes to Accounts:

1. **Segmental Disclosures (Business Segments)**

(Figures in ₹ 000's)

	First Division	Second Division	Third Division	Total
Sales	15,000	20,000	3,750	38,750
Cost of Sales	6,500	10,750	2,250	19,500
Administration Cost (5:3:2)	2,500	1,500	1,000	5,000
Distribution Cost (3:1:1)	2,250	750	750	3,750
Profit/Loss	3,750	7,000	(250)	10,500
	15,000	20,000	3,750	38,750
Original cost of Assets (Equal Capital Base)	7,500	7,500	7,500	22,500
Depreciation @ 10% p.a. For the year ended 31.3.2014	750	750	NIL	1,500
For the year ended 31.3.2015	750	750	750	2,250

Note: Third division is a reportable segment as per assets criteria.

2. Tax computation

	(₹ in 000's)
Profit before tax for the year ended 31.3.2015	10,500
Add: Depreciation provided in the books (750 + 750 + 750)	2,250
	12,750
Less: Depreciation as per Income Tax Act (1,200 + 1,200 + 1,500)	3,900
Taxable Income	8,850
Tax at 35%	3,097.50

3. Deferred Tax liability (as per AS 22 on Accounting for Taxes on Income)

₹ '000

Opening Timing Difference on 1.4.2014		
WDV of fixed assets as per books	13,500	
WDV of fixed assets as per Income Tax Act	12,000	
Difference		1,500
Deferred Tax Liability @ 35% on 1,500		525
This has been adjusted against opening balance of retained profits.		
Current year (ended 31st March, 2015)	₹ '000	
Depreciation as per Books	2,250	
Depreciation as per Income Tax Act (1,200 + 1,200 + 1,500)	3,900	
Difference		1,650
Deferred Tax Liability @ 35% on 1,650 (to be carried forward)		577.50

4. **Contingent Liabilities not provided:** Company is contesting claim for damages for ₹ 18,75,000 and as such the same is not acknowledged as debts.

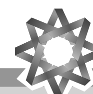
5. **Related Party Disclosure:** Para 3 of AS 18 lists out related party relationships. It includes individuals owning, directly or indirectly, an interest in voting power of reporting enterprise which gives them control or significant influence over the enterprises, and relatives of any such individual. In the instant case, Mr. Rydu as a managing director controls operating and financial actions of Zigzag Enterprise Ltd. He is also owning 100% share Capital of Hitachi Ltd. thereby exercising control over it. Hence, Hitachi Ltd. is a related party as per Para 3 of AS 18.

Disclosure to be made:

Name of the related party and nature of relationship	Hitachi Ltd. common director
Nature of the transaction	Sale of goods at normal commercial terms
Volume of the transaction	Sales to Hitachi Ltd. worth ₹62.50 lakhs.

Study Note - 3

CONSOLIDATED FINANCIAL STATEMENTS



This Study Note includes

3.1 Holding Company
3.2 Methods of Combination
3.3 Accounting Treatment
3.4 Treatment of Investment in Associate in Consolidated Financial Statement (AS-23)
3.5 Treatment of Investment in Joint Ventures in Consolidated Financial Statement (AS-27)
3.6 Preparation of Group Cash Flow Statement

3.1 HOLDING COMPANY

The tendency to combine in order to derive advantages of economics of scale as well as market power / monopoly power, firms may amalgamate – one firm may absorb another firm in which case their size increases and legal in a larger firm comes into existence. This implies dissolution of one or more existing firms. A legal procedure has to be followed for this purpose. However, Firms may continue without any dissolution by investing in the shares of another company and thereby, acquiring owner ship interest to the extent of the holding. If a company holds more than 51% of the issued share capital of another firm or controls composition of Board of Directors of another firm, the company holding the majority share is termed as holding company and the company whose shares are held is termed as subsidiary company.

A partly owned subsidiary is one in which the holding company (or the group) does not hold all the shares. The interest of shareholders outside the group is called '***Non-controlling interest'***.

While the wholly owned subsidiary is one where all the shares are owned by the holding company. From legal point of view both the companies continue to enjoy, separate legal entity but from the point of view of investor, lender as well as management, then, may very well be regarded as single entity. Legally accounts of these companies are complied separately but a more realistic picture will be presented if consolidated accounts especially with respect to published statements – income and position statements are also included in published reports. For this purpose inter – company transactions have to be eliminated from all stages and a single Profit and Loss Account and Balance Sheet compiled for the group as a whole. If a company is a subsidiary company, it is also deemed to be a subsidiary of the holding company.

3.2 METHODS OF COMBINATION

In order to be able to account for combinations, we must first explore some of the methods which may be used to affect them. Such methods may best be classified as to whether or not a group structure results from the combination. Let us take as an example: two companies L and M and assume that the respective Boards of Directors and owners have agreed to combine their business.

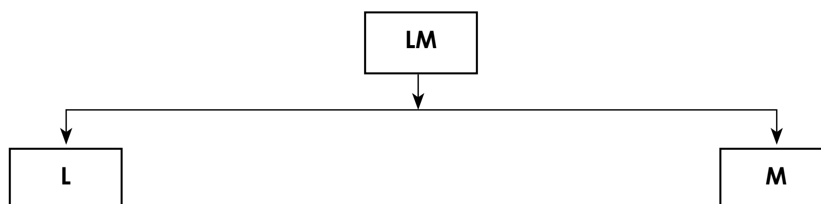
COMBINATIONS WHICH RESULTS IN A GROUP STRUCTURE

Two such combinations may be considered. In the first case, company L (say) may purchase the shares of Co. M (say) and there by acquire a subsidiary company, alternatively Co. M may purchase the shares of Co. L. The choice of consideration given in exchange for the shares acquired, will determine whether or not the old shareholders in what becomes the subsidiary Co., have any interest in the combined business. Thus, if Co. L issues shares in exchange for shares in Co. M the old share holders of Co. M have an interest in the resulting holding company and thereby in the group. Whereas, if Co. L pay cash for the shares in Co. M, the old shareholders in M take their cash and cease to have any, interest in the resulting group.

In the second case a new company L M (say) may be established to purchase the shares of both M Co. and L Co. Thus the shareholders in L and M may sell their shares to LM in exchange for shares in LM. The resulting group structure would be:-

HOLDING COMPANY

SUBSIDIARY COMPANY



The shareholders in LM would be the old shareholders in LM would be the old shareholders in the two separate companies and their respective interests would depend, as in the above examples, upon the valuation placed the two separate companies – which should in turn depend upon the bargaining between the two Boards of Directors.

It would be possible for LM Co. to issue not only shares but also loan stock in order to purchase shares in L Co. and M Co. It would be difficult for payment to be made in cash and LM Co. is a newly formed company, although it could, of course offer – shares or raise loan to obtain cash.

COMBINATIONS NOT RESULTING IN GROUP STRUCTURE

Again, two such combinations may be considered. First, instead of purchasing the shares of Co. M, Co. L may obtain control of the net assets of M by making a direct purchase of those net assets. The net assets would thus be absorbed into Co. L and Co. M would itself receive the consideration. This, in due course would be distributed to the share holders of M by its liquidator. Once again, the choice of consideration determines whether or not the old shareholders in Co. M have any interest in the enlarged Co. L, second, instead of one of the companies purchasing the net assets of the other, a new company may be formed to purchase the net assets of both the existing companies. Thus a new company LM may be formed to purchase the net assets of Co. L and Co. M. If payments is made by issue of shares in Co. LM these will be distributed by the respective liquidators so that the end result in one company, LM which own the net assets previously held by the separate companies and has as its shareholders the old shareholders in the two separate companies.

PREFERENCE FOR GROUP STRUCTURE

The above are methods of effecting combination between two or indeed more, companies. It appears that the majority of large business combination makes use of a group structure rather than a purchase of assets or net assets. Such a structure is advantageous in that separate companies enjoying limited liability as already in existence. It follows that names and associated Goodwill, of the original Companies are not lost and, in addition, that it is not necessary to renegotiate contractual agreement. All sorts of other factors will be important in practice, some example are the desire to retain staff, the impact of taxation and stamp duty, whether or not there is remaining non-controlling interest.

CHOICE OF CONSIDERATION

As discussed above, the choice of consideration will determine who is interested in the single business created by the combination and therefore be affected by the size of the companies and also by the intention of the parties to the combination and also by the conditions in the market securities and taxation system in force.

The main type of consideration are cash, loan stock, equity shares and some form of convertible securities, all sorts of combinations of these are possible.

3.3 ACCOUNTING TREATMENT

It seems to be intention of the Companies Act that the financial year of holding and subsidiary firm should end on the same date. Section129 of The Companies Act, 2013 requires that a holding company shall attach to its Balance Sheet the following documents:

- A copy of the Balance Sheet of the subsidiary.
- A copy of the Profit and Loss Account of the subsidiary.
- A copy of the board of Directors report and auditor's report.
- A statement of holding company's interest.

Accounting Standard AS–21 requires that holding company shall also present consolidated financial statement in addition to the separate financial statements as stated above. Student is advised to study AS–21 in this context. Consolidated Balance Sheet with respect to the consolidation process is carried out on a step by step basis so that common transaction are eliminated and the assets and liabilities of the entire group are presented in a single Balance Sheet and P/L Account at market prices.

The consolidation of the Balance Sheet is carried out in the following steps:

1. **Elimination of inter-company investments account:** a holding company by definition holds majority shares in the subsidiary company which appears as an investment on the assets side of the Balance Sheet of the holding company. In the context of subsidiary company it is part of issued capital on the liability side.

   As a first step in the consolidated process the investment account in the Balance Sheet of the holding company in the subsidiary company is eliminated and the assets (leaving a side fictitious assets or including an adjustment for them and all outside liabilities will be incorporated into the holding company's Balance Sheet as shown below :-

Extract Balance Sheet as at 31-03-2016

	H	S		H	S
Share Capital @₹ 10 each	20,000	10,000	Sundry Assets (Tangible)	20,000	10,000
Sundry Liabilities	10,000	5,000	Investments in S. Ltd. (1000 shares)	10,000	-
	30,000	15,000		30,000	10,000

Solution:

Name of the Company: H

Consolidated Balance Sheet as at 1st April, 2016

Ref No.	Particulars		Note No.	As at 1st April, 2015	As at 31st March, 2015
				₹	₹
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital		20,000.00	-
				20,000.00	-
	2	**Share application money pending allotment**		Nil	-
	3	**Non-current liabilities**		Nil	
				-	-

Ref No.	Particulars		Note No.	As at 1st April, 2015	As at 31st March, 2015
				₹	₹
	4	**Current liabilities**			
		(a) Other current liabilities	1	15,000.00	-
				15,000.00	-
		TOTAL (1+2+3+4)		35,000.00	-
	B	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	2	35,000.00	-
				35,000.00	-
	2	**Current assets**		Nil	
				-	-
		TOTAL (1+2)		35,000.00	-

Note: Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note 1. Other Current Liabilities

	Current Year	Previous Year
H	10,000.00	-
S	5,000.00	-
	15,000.00	-

Note 2. Tangible Assets

	Current Year	Previous Year
H	20,000.00	-
S	15,000.00	-
	35,000.00	-

In the above case the subsidiary firm is fully owned by the holding company and therefore the entire net assets of the subsidiary firm are in the ownership of the holding company and for the purpose consolidation they have been incorporated into Balance Sheet of the holding company. However, very often the holding company have holds only majority shares in which case the extent of the ownership interest (no. of shares held in the form of investments by the Holding company/ total issued capital of S limited in terms of number of shares) In the process of consolidated therefore, assets and liabilities should be incorporated only to the extent of ownership interest. However, this method is not allowed in practice as per convention.

2. **Determination of Minority Interest:** The shares of the subsidiary firm held by outsiders i.e. other than the Holding company are in aggregate termed as minority interest since majority shares are held by Holding company. As per I, even in case of partly owned subsidiary firm the entire assets and liabilities of the subsidiary companies are incorporated in the consolidated Balance Sheet and an additional calculation is made to determine the extent of minority interest in the assets of subsidiary firms and this is shown as additional liability in consolidated Balance Sheet. The claim of the majority (or outside) shareholders will consist of the face value of the shares held by them plus a proportional share in any increases in the value of assets of the company minus their portion of company's losses or decrease in the value of assets of the company.

Example 1.

From the following prepare a consolidated Balance Sheet as at 1st April, 2016

					(Figures in Rupees)
	H	S		H	S
Share Capital@ ₹10 each	20,000	10,000	Shares in S. Ltd.	80,000	
S. Liabilities	10,000	5,000	800 shares		
			Other assets (Tangible)	22,000	15,000
	30,000	15,000		30,000	15,000

H limited has acquired the shares on the closing Date of the Balance Sheet as on 31.3.2015.

Solution:

Name of the Company: H

Consolidated Balance Sheet as at 1st April, 2015

Ref No.	Particulars		Note No.	As at 1st April 2015	As at 31st March, 2015
				₹	₹
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital		20,000.00	-
				20,000.00	-
	2	**Minority Interest**		2,000.00	-
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**		Nil	
				-	-
	5	**Current liabilities**			
		(a) Other current liabilities	1	15,000.00	-
				15,000.00	-
		TOTAL (1+2+3+4+5)		37,000.00	-
	B	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	2	37,000.00	-
				37,000.00	-
	2	**Current assets**		Nil	
		TOTAL (1+2)		37,000.00	-

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note 1. Other Current Liabilities

	Current Year	Previous Year
H	10,000.00	-
S	5,000.00	-
	15,000.00	-

Note 2. Tangible Assets

	Current Year	Previous Year
H	22,000.00	-
S	15,000.00	-
	37,000.00	-

Net Assets available for distribution of Equity shareholders of S Limited =

(Assets - Liabilities) = (15000 - 5000) = ₹ 10000

Minority Interest = (10000*1/5) = 2000

(800/1000) = (4/5) Majority Interest

3. Goodwill, Capital Reserve / Cost of Control **–** In the Balance Sheet of subsidiary company when a company acquires shares there are likely to be accumulated Profit/Losses. These will not be incorporated into the consolidated Balance Sheet but with respect to the Holding companies cost of investment reflected on the assets side in the holding's company Balance Sheet a comparison will be carried out with the actual value of these investments. The subsidiary Co's Balance Sheet (paid up value of shares + accumulated profit or – accumulated losses = market value of the investment). The difference between the cost of acquisition of share and the market value determined above will be goodwill if cost of acquisition is less and accordingly goodwill A/c or capital reserve A/c will be incorporated into the consolidated Balance Sheet. This figure is also termed as cost of control since the holding company has a controlling investment in the subsidiary firm.

Example 2.

H Ltd. acquires 3/4 of the share capital of S Ltd. On 31-12-2016 whose extract Balance Sheets are as follows:

	H	S		H	S
Share Capital @ ₹ 10 each	20,000	10,000	Fixed assets (Tangible)	20,000	10,000
			Current assets	13,000	12,000
General Reserves	5,000	3,000	Shares in B Ltd. (3/4)	10,000	
P/L Account	3,000	2,000			
10% Debentures	10,000	5,000			
Sundry creditors	5,000	2,000			
	43,000	22,000		43,000	22,000

Required to compile consolidated Balance Sheet on 31-12-2016.

Solution:

In case of partly owned subsidiary firm the H Co's interests in the accumulated profit or loss the subsidiary firm is only to the extent of the ownership interest. The balance due to minority will be adjusted for the minority interest.

Cost of Control

Amount paid for shares in S Ltd. / cost of acquisition Of shares		₹ 10,000
Less: Paid up value in S Ltd. (3/4 of ₹ 10000)	7,500	
Share of General Reserve (3/4 of ₹ 3000)	2,250	
Share of P/L Account (3/4 of ₹ 2000)	1,500	
		11,250
Capital Reserve		1,250

Minority Interest

Paid up value	2,500
General Reserve (1/4)	750
P/L Account (1/4)	500
Minority Interest	3,750

Name of the Company: H Ltd.

Consolidated Balance Sheet as at 31st December, 2016

Ref No.		Particulars	Note No.	As at 31st December, 2015	As at 31st March, 2015
				₹	₹
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital		20,000.00	-
		(b) Reserves and surplus	1	9,250.00	-
				29,250.00	-
	2	**Minority Interest**		3,750.00	-
	3	**Share application money pending allotment**		Nil	-
	4	**Non-current liabilities**			
		(a) Long-term borrowings (10% debentures)	2	15,000.00	-
				15,000.00	-
	5	**Current liabilities**			
		(a) Trade payables	3	7,000.00	-
				7,000.00	-
		TOTAL (1+2+3+4+5)		55,000.00	-
	B	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	4	30,000.00	-
				30,000.00	-
	2	**Current assets**			
		(a) Other current assets	5	25,000.00	-
				25,000.00	-
		TOTAL (1+2)		55,000.00	-

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note 1. Resesrve & Surplus

	Current Year	Previous Year
General Reserve	5,000.00	-
P/L A/c	3,000.00	-
Capital Reserve	1,250.00	-
	9,250.00	-

Note 2. Long Term Borrowings

	Current Year	Previous Year
10% Debenture		
H	10,000.00	-
S	5,000.00	-
	15,000.00	-

Note 3. Trade Payable

	Current Year	Previous Year
H	5,000.00	-
S	2,000.00	-
	7,000.00	-

Note 4. Tangible Assets

	Current Year	Previous Year
H	20,000.00	-
S	10,000.00	-
	30,000.00	-

Note 5. Other Current Assets

	Current Year	Previous Year
H	13,000.00	-
S	12,000.00	-
	25,000.00	-

S Company Balance Sheet

(Net assets – Debentures – Creditors) = (22,000 - 5,000 - 2,000) = 15,000

= Net assets available for equity shareholders.

Minorities share in 15,000 = (1/4) * 15,000 = 3,750

(including paid up value of share capital and accumulated profits)

4. **Capital profit/ revenue profit:** The date of acquisition of shares by the holding company may not coincide with the closing of financial year i.e they may be acquired during the course of financial year. However, the published statements will be compiled only with respect to the closing date of financial year. In such a case, the date of acquisition of shares does not coincide with the date of Balance Sheet and accordingly adjustments have to be made. **The Profit and Loss of the subsidiary company prior to the date of acquisition are capital in nature while post dated profits are revenue in nature.** From the accounting point of view the pre – acquisition profits will be adjusted for in the cost of control extent of holding company's ownership interest while the post acquisition profit will be treated as revenue in nature and therefore in the closing Balance Sheet as shown in the Profit/Loss Account of the holding company. For this purpose in the absence of any further information it is perfumed that the subsidiary company earns uniformly throughout the year, for example, if the date of acquisition is in the middle of first year 1/2 the profit of the subsidiary company will be capital in nature, the other 1/2 as revenue , with respect to the minorities the treatment is identical for either share in capital or revenue profit which are added on, to the minority interest. In some cases in the analysis of profit additional adjustments have to be made before they are analysed into capital and revenue profit. **All accumulated profit except current year profit which has to be segregated into capital and revenue will be treated as capital profit.**

5. **Inter Company Transactions:** The holding and subsidiary firm may have centered into the following transaction and these common transactions will be eliminated while compiling the consolidated Balance Sheet.
   (a) The holding or the subsidiary firm may have granted loans (short term) to each other.
   (b) They may have sold goods on credit in which case the inter company transactions will be included in debtors and creditors.
   (c) The subsidiary or holding company may have drawn Bills of Exchange on each other in which case the common transaction will be included in Bills Payable/ Bills Receivable.

   In all the above cases where the companies were treated as separate entities, these transactions would appear on the liabilities side on the Balance Sheet of one and on the assets side of the other's Balance Sheet. However, when the entire group is being treated as a single entity it is undesirable to include common transaction and therefore they will be eliminated in the consolidated Balance Sheet from the liabilities as well as assets side.

6. **Contingent Liabilities:** A contingent liability appears as a footnote. This is on account of a liability which may or may not arise in the future. While preparing a consolidated Balance Sheet they may be categorized as external current liabilities or internal current liabilities. External liabilities between the holding and subsidiary firm and the outsiders. Internal current liabilities is on account of transactions between the firms belonging to the same group. The external liabilities continue unchanged for the same group while internal liabilities no longer appears as a footnote as it is generally incorporated on the liability side.

Example 3.

The following are the extract Balance Sheet of H & S Company as on 31-03-2016 (in ₹)

Liabilities	H	S	Assets	H	S
Share Capital @ ₹ 10 each	20,000	10,000	Fixed Assets (Tangible)	30,000	15,000
General Reserve	10,000	5,000	Current Assets	35,000	25,000
P/L A/c (1.4.14)	5,000	4,000	Shares in S Ltd. (8000)	10,000	
12% Debenture	20,000	10,000			
S. creditors	10,000	5,000			
Profit for the year	10,000	6,000			
	75,000	40,000		75,000	40,000

H Limited acquired shares in S Limited on 01-10-2015. S limited has a balance of ₹ 4000 in General Reserve on 01-04-2015. On the account fire goods costing ₹ 2000 of S Limited were destroyed in June, 2015. The loss has been charged to the Profit and Loss Account for the year.

Required to prepare a consolidated Balance Sheet.

Solution:

Working Notes:

1. Date of Acquisition: 01.10.2015
2. Holding Company Share: 800/1000 *100 = 80%
3. Minority Company Share: 200/1000*10 = 20%

Analysis of profit (of S)

Particulars	**Capital Profit**	**Revenue Profit**
General Reserve of 01.04.15	4000.00	-
Profit & Loss of 01.04.15	4000.00	-
Profit for the year prior to Transfer + General Reserve (6000+1000+2000)/2	4500.00	4500.00
	12500.00	4500.00
Less: Loss on fire in March	2000.00	-
	10500.00	4500.00
Holding Company's share (80%)	8400.00	3600.00
Minority Company's share (20%)	2100.00	900.00

Cost of Control:-

	Amount (₹)	**Amount (₹)**
Cost acquiring share	—	10000.00
Less: Nominal Value of shares (800*10)	8000.00	—
Share of Capital profits of H	8400.00	16400.00
Capital Reserve	—	**6400.00**

Minority Interest:

Nominal Value of share Capital (200*10)	2000.00
Share of Capital Profit	2100.00
Share of Revenue Profit	900.00
	5000.00

Name of the Company: H Ltd.

Consolidated Balance Sheet as at 31st March, 2016

Ref No.		Particulars	Note No.	As at 31st March, 2015 (₹)	As at 31st March, 2014 (₹)
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital		20,000.00	-
		(b) Reserves and surplus	1	35,000.00	-
				55,000.00	-
	2	**Minority Interest**		5,000.00	-
	3	**Share application money pending allotment**		Nil	-
	4	**Non-current liabilities**			
		(a) Long-term borrowings (10% debentures)	2	30,000.00	-
				30,000.00	-
	5	**Current liabilities**			
		(a) Trade payables	3	15,000.00	-
				15,000.00	-
		TOTAL (1+2+3+4+5)		105,000.00	-
	B	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	4	45,000.00	-
				45,000.00	-
	2	**Current assets**			
		(a) Other current assets	5	60,000.00	-
				60,000.00	-
		TOTAL (1+2)		105,000.00	-

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note 1. Resesrve & Surplus

	Current Year	Previous Year
General Reserve	10,000.00	-
P/L A/c	-	-
H	15,000.00	-
S	3,600.00	-
Capital Reserve	6,400.00	-
	35,000.00	-

Note 2. Long Term Borrowings

	Current Year	Previous Year
12% Debenture		
H	20,000.00	-
S	10,000.00	-
	30,000.00	-

Note 3. Trade Payable

	Current Year	Previous Year
H	10,000.00	-
S	5,000.00	-
	15,000.00	-

Note 4. Tangible Assets

	Current Year	Previous Year
H	30,000.00	-
S	15,000.00	-
	45,000.00	-

Note 5. Other Current Assets

	Current Year	Previous Year
H	35,000.00	-
S	25,000.00	-
	60,000.00	-

7. **Unrealized gains:** If goods have been sold by holding company to subsidiary company or vice versa, presumably they would be including a profit margin on the cost price. However, when the firms are treated as a single entity, stock or inventory should be valued at cost i.e excluding profits. The firm that has sold the goods must have credited the profit of account of the sales: therefore, profit or selling company has to be reduced and the stock account of the company that has purchased the goods also has to be reduced for which purpose the following entry is passed.

   Profit & Loss A/c (selling company) Dr.

   To stock company (purchasing company)

   (with the company of profit included in the inter

   company sales of goods that can be…..)

   By making a deduction for the inter company sale of goods, the adjustments is made only in relation to those goods that can still be traced in the inventories of the purchasing company. If the goods are not traceable no adjustments is required. A finer accounting analysis can be performed by taking into consideration extent of the ownership interest of the holding company in the subsidiary firm accordingly making the above entry to the extent of ownership interest. As per decision of the Institute Chartered Accountants, this method no longer followed and the total profit included in inventories (irrespective of it belonging to majority or minority) is deducted from both sides of the Balance Sheet.

8. **Revaluation of assets and Liabilities:** The Holding company may revalue the Assets and Liabilities of the subsidiary firm at the time of acquisition of shares in terms of market prices. In such a case the rate of revaluation is, assumed to be the same date as acquisition of shares. The profit or loss on revaluation is capital in nature and accordingly will be adjusted for in the analysis of profit under capital profits. The date of acquisition of shares as considered earlier also may not coincide with date of Balance Sheet in which case as stated earlier the current years profit has to be segregated between capital and revenue. Since the date of revaluation of assets is the date of acquisition of shares, a change in depreciation may be required on the revalued assets from the date of acquisition till the closing of Balance Sheet. For, presumably the Balance Sheet of the subsidiary company has been made or complied in terms of its original values. Information with respect to revaluation has to be explicitly stated by an agreement between the firms at the time of acquisition of majority share by the holding company.

Preference Shares

The Holding or Subsidiary Company may have Preference shares at the time of consolidation. The preference shares of the holding company continue as they are in the consolidated Balance Sheet. With respect to the Subsidiary firm if preference share capital has been issued there are 2 possibilities.

- All preference shares are held by the outsiders i .e. other than holding company i.e which case the paid up value of the preference shares of the Subsidiary company is added to the minority interest.
- It is possible that part whole of the preference. shares of the Subsidiary company is held by the Holding Company. In such a case the cost of acquiring of the preference shares (shown in the investment account in the assets side in the Balance Sheet of the holding company) is compared with the paid up value (shown in Balance Sheet of Subsidiary firm) and the difference if any, adjusted in the cost of control. (if preference shares are issued after date of acquisition the adjustments remain the same)

Arrears of preference dividends may be payable or outstanding at the time of consolidation of Balance Sheet and usually preference dividends are cumulative in nature. If the subsidiary company, has adequate profits, it is reasonable to assume that these dividends will be paid. The minorities shares will be added to Minority Interest while with respect to the holding company the treatment will differ in terms of the divided being paid out of pre acquisition or post acquisition profits or both.

In case the dividends are paid out of pre-acquisition profits (capital profit), the dividend due to the holding company will be adjusted for in the cost of control. In case post acquisitions revenue profits are employed, the dividend due to the holding company will be credited (added on) to the Profit and Loss Account of the holding company in the consolidated Balance Sheet. It is possible that a combination of both pre and post acquisition profit is employed for the purpose of making dividend payment in which case the dividend paid out of the capital profit will be adjusted for in the cost of control and the portion out of revenue profit will be adjusted for in the P/L Account of Holding company, the total being amount due to the holding company with respect to minorities no distinction is made between capital and revenue profit for the purpose of making dividend payment and the dividend payable to them will be added to minority interest.

Bonus Shares

The Subsidiary company may issue Bonus shares either at the time of acquisition of shares by the holding company or after the acquisition of shares by the Holding company. For issuing bonus shares, the accumulated profits in the Balance Sheet of the subsidiary company are employed. These profits may be capital or revenue in nature or a combination of both. At the time of bonus issue the share of the Holding company as well as the minorities increases proportionately (in terms of the ration of bonus issue) but the proportion of their ownership remains the same as before. If bonus shares are issued out of capital profits are adjusted accordingly and bonus shares transferred to cost of control. If bonus shares issued out of revenue profit of subsidiary company to that extent revenue profit stand capitalized and will affect capital reserve or goodwill as the case may be.

DIVIDEND ON EQUITY SHARES

The Subsidiary company may declare dividend on its equity shares and the following are the possibilities with respect to it.

a. **Intention to propose dividend:** In such a case since the proposal has not been approved in the meeting the intention may be ignored and no adjustment is required (in terms of calculation) with respect to this dividend intention.

b. **Proposed dividend:** It is possible that dividend has been proposed in a meeting on the closing date of the financial year but no notification of this fact has been made in the books of the Holding company. In such a case, the amount of dividend declared may be added to the profits of the Subsidiary company (assuming this has been deducted) and then the analysis of profits is performed in the usual manner. No adjustment is needed in the books of the Holding company.

c. **Dividends Payable:** In some cases, the dividends that have been declared by the Subsidiary firm may have been adjusted for in both the books i.e. the Subsidiary and Holding company. In this case adjustment is

made in the books of the Subsidiary company. In the books of the Holding company the dividend that are receivable fro the Subsidiary company will be credited to Profit and Loss Account of the Holding company (in terms of income receivable on investments).It is possible that these dividends have been paid by the subsidiary firm out of Capital profit, revenue profit, combination of both profit

(i) If dividend of subsidiary company have been declared totally out of capital profit, then it is incorrect that this capital income should stand credited to the revenue P/L Account of the holding company. Therefore one adjustment entry is made for remaining dividend from the P/L Account of the holding company and they are transferred to cost of control.

P/L Account (H Ltd.) Dr.

To Cost of control/Investment Account

With the amount of dividend receivable from the Subsidiary firm

(ii) If the dividend of the subsidiary firm have been declared out of Revenue profit then they should be credited to the P/L A/c. of the Holding Company and of they are already included therein as per our presumption, no adjustment is required.

(iii) The dividend receivable by Holding Company may be partly out of capital profit or out of revenue profit of Subsidiary company. The portion paid out of capital profit will be eliminated form P/L Account of Holding company and transferred to cost of control with respect to the portion of the dividend receivable out of revenue profit no adjustment is required. With respect to the minorities irrespective of the dividend declared by the Subsidiary company being payable out of capital profit or revenue profit will be added to minority interest.

d. Dividend paid: The Subsidiary company may have declared a dividend in the course of the financial year and this fact has been adjusted for in both the books and in fact the cash liability has already been met by subsidiary firm for the purpose of dividend payment. This implies there is no liability outstanding with respect to payment of dividends therefore no addition on account dividends has to be made to minority interest. With respect to Holding company has stated in point (iii) the dividend must have been credited to P/L Account out of capital profit, revenue profit are a combination from the subsidiary company's books. The portion out of capital profit stated earlier will be transferred from the P/L Account of the Holding company to the cost of control.

Share Premium:

The share premium account may appear in the Balance Sheet of the Holding company at the time of consolidation. It will continue as share premium account. However if the holding company has issued some of its own shares to the subsidiary company the share premium due on this share will be adjusted for in the cost of control. If share premium appears in the books of subsidiary company, it may be prior to the acquisition of shares by the holding company in which case it is treated as capital profit in the analysis of profit. However, the share premium arises after acquisition of share by H company it will continue as share premium in the consolidated Balance Sheet.

Preliminary Expenses:

If the Holding company has preliminary expenses they continue as such. If subsidiary company has preliminary expenses they may be treated as a capital loss in the analysis of profit or clubbed with preliminary expenses of Holding company.

Provision for Taxation:

Taxes are payable to outside agencies and provision for taxation with respect to holding and subsidiary company will be shown as such in the consolidated Balance Sheet.

Sale of Share:

The holding company may sell some of the share of the subsidiary company that it holds as investment. The P/L on such sale is transfer to cost of control. This changes the proportion of the Holding company and minority interest

and requires adjustment in calculation of cost of control, minority interest and an analysis of profit will have to be performed.

Purchase of shares in instalments:

The Holding company may acquire shares in the subsidiary firm not in once single instalment but in a number of instalments. If the earlier dates of the acquisition may be ignored. If however, shares have been acquired in major instalments, a step by step analysis of profit after taking into consideration the dates of acquisition will have to be performed in the analysis of profit between capital and revenue.

Debentures:

The subsidiary and the holding may have issued debentures at time of consolidation of Balance Sheet. These will be added and continued to appear in the debenture account in the consolidated Balance Sheet. However, if some portion of these debentures are held by the holding company or subsidiary company, this will be dedicated from the investment account on the asset side and the debentures account on the liabilities side at the time of consolidation.

Goodwill:

A goodwill account may appear in the books of Subsidiary and Holding at the time of consolidation. The aggregate goodwill be the total of these goodwill and will be adjusted for any goodwill or capital reserve that appear in the cost of control.

Interim Dividend:

When a dividend is paid in between an accounting year i.e, prior to completion of final accounts, it is termed as interim dividend. The general presumption with respect to this dividend is that it has been paid i.e, it has been adjusted for in the books of Holding and Subsidiary. No adjustment required with respect to minorities however, with respect to the Holding company, if capital profit have been employed for making dividend payment to the extent (wholly or partly) it will go to the cost of control from the P/L Account of Holding company.

Illustration 1. Analysis of Balances in Reserves

Following are the balances in various reserves of P. Ltd., subsidiary of V Ltd. as on the date of controlling acquisition and the date of consolidation -

Accounts	Date of Acquisition (₹)	Date of Consolidation (₹)
General Reserve	60,000	1,20,000
Profit and Loss Account	25,000	80,000
Capital Redemption Reserve	40,000	55,000
Securities Premium	45,000	45,000
Capital Reserve	5,000	25,000
Preliminary Expenses	5,000	1,000
Underwriting Commission	10,000	5,000

Additional information -

1. One year after the date of controlling acquisition, P. Ltd. had issued Bonus Shares for ₹ 60,000 utilizing the balances in Capital Reserve and Capital Redemption Reserve in full, and sourcing the balance from General Reserve. The Director's did not utilize the balance in Securities Premium for this purpose.
2. In the intervening period, Preference Share Capital had been redeemed at a Premium of ₹ 12,000. For statutory Compliance, a sum of ₹ 40,000 had been transferred to Capital Redemption Reserve and a further sum of ₹ 15,000 had been transferred upon redemption of Debentures, which were also redeemed at a Premium of ₹ 10,000.

3. To finance its redemption of Preference Capital, P Ltd. had issued Equity Capital at a Premium. The balance of ₹ 5,000 against Underwriting Commission is incurred in this regard.
4. The Company has been writing off balances in Underwriting Commission A/c and Preliminary Expenses against balance in Securities Premium Account. The balance in Preliminary Expenses as on consolidation date is the amount as on acquisition date not yet written off.
5. P. Ltd. had declared Equity and Preference Dividend of ₹ 20,000 out of its P&L A/c balance as on date of acquisition.

How would the above balances as on date of consolidation be analyzed and classified for the purposes of consolidation?

Solution:

1. General Reserve

Balance as on Consolidation ₹1,20,000

	Date of Acquisition	₹60,000	Acquisition to Consolidation
Less:	Bonus Issue (60,000 - trfd. from Cap. Res. 5,000 - trfd. from CRR 40,000)	₹15,000	(balancing figure) ₹ **75,000**
	Balance **Capital Reserve**	**45,000**	**Revenue Reserve**

2. Profit and Loss A/c

Balance as on Consolidation ₹80,000

	Date of Acquisition	₹25,000	Acquisition to Consolidation
Less:	Dividend out of this	₹20,000	(balancing figure) ₹ **75,000**
	Balance **Capital Reserve**	₹**5,000**	**Revenue Profit**

3. Capital Redemption Reserve

Balance as on Consolidation ₹55,000

	Date of Acquisition	₹40,000	Acquisition to Consolidation
Less:	Bonus Shares	₹40,000	(balancing figure) ₹ 55,000
	Balance Capital Profit	**NIL**	

Acquisition to Consolidation ₹ 55,000 is split into:

Redemption of Pref. Capital	Redemption of Debentures
₹ **40,000**	₹ **15,000**
Capital Redemption Reserve	**Capital Redemption Reserve**

4. Securities Premium

Balance as on Consolidation ₹45,000

	Date of Acquisition	₹45,000	Acquisition to Consolidation
Less:	Premium on Redemption of Pref. Capital	₹(12,000)	Premium on Fresh Issue of Capital
Less:	Premium on Redemption of Debentures	₹(10,000)	(balancing figure) ₹ **36,000**
Less:	Underwriting Commission and Prelim Exp. written off (10,000 + 4,000)	₹(14,000)	**Securities Premium**
	Balance **Capital Profit**	₹**9,000**	

5. Capital Reserve

Balance as on Consolidation ₹25,000

	Date of Acquisition	₹5,000	Acquisition to Consolidation
Less:	Bonus Shares	₹5,000	(balancing figure) ₹ **25,000**
	Balance Capital Profit	**NIL**	**Capital Reserve**

6. Preliminary Expenses

Balance as on Consolidation ₹1,000

	Date of Acquisition	₹5,000	Acquisition to Consolidation
Less:	Written off against Securities Prem.	₹4,000	(balancing figure) ₹ **NIL**
	Balance **Capital Profit**	₹**1,000**	**Preliminary Expenses**

7. Underwriting Commission

Balance as on Consolidation ₹5,000

	Date of Acquisition	10,000	Acquisition to Consolidation
Less:	Written off against Securities Prem.	10,000	₹ **5,000**
	Balance **Capital Profit**	**NIL**	**Underwriting Commission**

Summary

Accounts (1)	Balance on DOC (2) ₹	Considered Capital Profit (3) ₹	Balance considered as such (4) ₹
General Reserve	1,20,000	45,000	75,000
Profit and Loss Account	80,000	5,000	75,000
Capital Redemption Reserve	55,000	NIL	55,000
Securities Premium	45,000	9,000	36,000
Capital Reserve	25,000	NIL	25,000
Preliminary Expenses	1,000	1,000	NIL
Underwriting Commission	5,000	NIL	5,000

Note: In the course of consolidation, the amounts in Col. (3) and (4) shall be apportioned to Holding Company (P Ltd.) and Minority Interest (of V Ltd.) in the ration of their shareholding.

Illustration 2: Analysis of Reserves – Adjustment for Abnormal Loss, Dividend, etc.

A Ltd. Acquired 80% interest in B Ltd. On 01.10.2014. A Ltd is in the process of preparing its Consolidated Financial Statement as on 31.03.2016. The details of Profit and Loss A/c balances of B Ltd. Is as under –

- Balance on 01.04.2014 ₹ 6,000
- Profit for 2014-15 ₹ 10,000 (before Equity Dividend)
- Balance on 31.03.2016 ₹ 33,800

In Julyl 2014, B Ltd. Lost stocks costing ₹ 1,550 due to riots. The Insurance Company admitted a claim of ₹ 650 only.

In November 2015, A. Ltd. Received ₹ 9,600 as Dividend from B Ltd. In respect of the year ending 31.03.2015. B Ltd. has proposed a dividend of ₹ 15,000 for the year ending 31.03.2016.

During 2015-16, B Ltd. had purchased shares of Maya Ltd cum –dividend for ₹ 34,500. B Ltd. received a dividend of ₹ 7,500 on this investment, which was credited to its Profit and Loss Account. A provision for outstanding expenses of ₹ 1,700 provided during the year was considered excessive. The balance in Profit and Loss Account as on 31.03.2016 is after providing for the expenses.

Analyze the balance in Profit and Loss Account as Capital and Revenue for the purposes of Consolidation.

Solution:

Analysis of Profit and Loss Account

		₹
	Balance as given on 31.03.2016	33,800
Less:	Pre-Acqn. Dividend from Maya Ltd.	(7,500) (to credit Investment in Maya A/c)
Less:	Proposed Dividend for 2015-16	(15,000)
Add:	Excess Provision to be written back	1,700 (to debit Outstanding Expenses A/c)
	Corrected Balance as at 31.03.2016	**13,000**

01.04.2014	Profit for 2014-15		Dividend for 2014-15	Profit for 2015-16
₹ 6,000	Profit for 2014-15	10,000	Recd. By A 9,600 for 80%	₹ 9,000
Capital	Add: Abnormal Loss	900	Total Dividend = 9,600÷80 %	Revenue (bal. fig.)
Profit	Profit without abnormal losses	10,900	= (₹12,000)	(13,000 – Opg. 6,000 – Pft for 2014-16 10,000 + Dividend 12,000) (fig in '00)

	01.04.2014 to 01.10.2014	01.10.2014 to 31.03.2015	From Opg Bal. (bal. figure)	From Profit for 01.04.2014 to 01.10.2014	From Profit for 01.10.2014 to 31.03.2015
	5,450	5,450			
Less: Abnormal Loss	(900)	Revenue	(₹ 2,000)	(₹ 4,550)	(₹ 5,450)
Bal. Capital Profit	4,550		Capital	Capital	Revenue

Total Capital Profit: 6,000 + 4,550 – 2,000 – 4,550 = ₹ 4,000;

Total Revenue Profit: 9,000 + 5,450 – 5,450 = ₹ 9,000

Abnormal Loss = Stock Loss is Riots ₹ 1,550 (-) Insurance Claim received ₹ 650 = ₹ 900

Note:

- It has been assumed that the Profit arose evenly throughout the year.
- Dividend declared for 2014-15 = ₹ 12,000, but profit for 2014-15 is ₹10,000. So it is presumed that balance of ₹2,000 has been declared from the opening reserve.

Illustration 3: Cost of Investment - Share Split

A Ltd. acquired 5,000 Shares of S Ltd. at ₹ 48 per Share cum-dividend constituting 62.50% holding in the latter. Immediately after purchase, S Ltd. declared and distributed a dividend at ₹ 4 per Share, which S Ltd. credited to its Profit and Loss Account.

One year later, S Ltd. declared a Bonus of 1 fully paid Equity Share of ₹ 10 each for every 5 Shares held. Later on, S Ltd. proposed to raise funds and made a Rights Issue of 1 Share for 5 held at ₹ 36 per Share. A Ltd. exercised its right.

After some time, at its AGM, S Ltd. had decided to split its Equity Share of ₹ 10 into Two Equity Shares of ₹ 5 each. The necessary resolutions were passed and share certificates issued to all its existing shareholders.

To increase its stake in S Ltd. to 80%, A Ltd. acquired sufficient number of shares at ₹ 30 each.

Ascertain the Cost of Control as on 31st March if S's share in Capital Profits (duly adjusted for purchase in lots) as on that date was ₹ 3,15,000.

Solution:

1. Cost of Investment

	Particulars		Shares	₹
	Cost of First Acquisition	(5,000 x ₹ 48)	5,000	2,40,000
Less:	Pre-Acquisition Dividend	(5,000 × ₹ 4 per Share)	N.A.	(20,000)
	Corrected Cost of Investment		5,000	2,20,000
Add:	Bonus Shares	(1/5 × 5,000 Shares)	1,000	–
	Cost after Bonus Shares		6,000	2,20,000
Add:	Rights Shares	(1/5 x 6,000 Shares x ₹ 36)	1,200	43,200
	Cost after Rights Issue before Share Split		**7,200**	**2,63,200**
	Cost after share split (WN 1)	(2 Sh. for 1 for 7,200 Sh = 7,200 x 2)	14,400	2,63,200
Add:	Acquisition to increase holding to 80% (WN 2)	(4,032 x ₹ 30)	4,032	1,20,960
	Balance on date of Consolidation		**18,432**	**3,84,160**

Notes:

- **Share Split:** In case of Share Split, the Cost of Acquisition will not undergo any change. Only the number of Equity Shares and the face value will change. This is similar to adjustment for Bonus Issue. However, for Bonus Issue, the face value and paid up value of the share will be the same as the original share. In share split, the face value and paid up value will be lesser than that of the original shares.
- **Calculation of Number of Shares to be acquired to increase stake to 80%**

	Particulars			Shares
a.	Shares held before acquisition			14,400
b.	% of holding			62.5%
c.	Hence, Total Number of Shares of S Ltd.	(a ÷ b)	= (14,400 ÷ 62.50%)	23,040
d.	80% of above	(c x 80%)	= (23,040 x 80%)	18,432
e.	Number of Shares to be acquired	(d - a)	= (18,432 - 14,400)	4,032

2. Cost of Control

Particulars			₹
Cost of Investment	**(A)**	(from 1 above)	**3,84,160**
Nominal Value of Equity Capital		(18,432 x ₹ 5 per Share)	92,160
Share in Capital Profit			3,15,000
Total of Above	**(B)**		**4,07,160**
Capital Reserve (if B < A)	**(B-A)**		23,000

Illustration 4: Cost of Control - For different Investment Costs

C Ltd. has acquired 50,000 Shares of ₹ 10 each in A Ltd. constituting 62.5% of the latter's Equity. On the same day, C. Ltd. had also acquired 10,000 8% Preference Shares of ₹ 20 each.

The balances in Reserves of A Ltd. are -

Capital Reserve	₹ 60,000	(Fully Pre Acquisition)
Securities Premium	₹ 15,000	(Fully Post Acquisition)
General Reserve	₹ 78,000	(30% Pre Acquisition 70% Post Acquisition)
Profit and Loss A/c	₹ 90,000	(50% Pre Acquisition 50% Post Acquisition)

Ascertain the cost of control if total cost of investment is (a) ₹ 7,50,000; (b) ₹ 8,50,000; and (c) ₹ 10,00,000.

Solution:

1. Determination of Capital Profit

Reserve Account	Total (₹)	Pre Acquisition Capital Profit (₹)	Post Acquisition Revenue Profit (₹)
Capital Reserve	60,000	60,000	—
Securities Premium	15,000	—	15,000
General Reserve	78,000	23,400 (30% x ₹ 78,000)	54,600 (70% x ₹ 78,000)
Profit and Loss Account	90,000	45,000 (50% x ₹ 90,000)	45,000 (50% x ₹ 90,000)
Total	**₹ 2,43,000**	**₹ 1,28,400**	**₹ 1,14,600**
Share of C Ltd. (62.5% of above)		**₹ 80,250**	**₹ 71,625**

2. Cost of Control

Particulars		₹	₹	₹
Cost of Investment	**(A)**	**7,50,000**	**8,50,000**	**10,00,000**
Nominal Value of Equity Capital	(50,000 x ₹ 10)	5,00,000	5,00,000	5,00,000
Nominal Value of Preference Capital	(10,000 x ₹ 20)	2,00,000	2,00,000	2,00,000
Share in Capital Profit		80,250	80,250	80,250
Total of Above	**(B)**	**7,80,250**	**7,80,250**	**7,80,250**
Goodwill (if A > B)	**(A-B)**	**—**	**69,750**	**2,19,750**
Capital Reserve (if B < A)	**(B-A)**	**30,250**	**—**	**—**

Illustration 5: Cost of Control - for Ex-Dividend and Cum-Dividend Acquisition

D Ltd. has made the following investments in S Ltd. a few years before –

1. 6,000 Equity Shares of ₹ 10 each at ₹ 1,50,000.
2. 200 12% Preference Shares of ₹ 100 each at ₹ 30,000.
3. 500 10% Debentures at ₹ 95 per Debenture.

The Capital Profits of S Ltd. have been ascertained at ₹ 96,000.

Determine the cost of control, under the following situations –

1. Shares were purchased Cum-Dividend and Equity Dividend was declared at 20% and the dividends were
   (a) Credited to Profit and Loss Account
   (b) Credited to Investment Account
2. Shares were purchased Ex-Dividend and Equity Dividend was declared at 20% and the dividends were
   (a) Credited to Profit and Loss Account
   (b) Credited to the Investment Accounts

Solution:

1. Cost of Control

Particulars	Cum-Dividend		Ex-Dividend	
Credited to	**P&L A/c**	**Invt. A/c**	**P&L A/c**	**Invt. A/c**
Cost of Investment				
Equity Capital	1,50,000	1,50,000	1,50,000	1,50,000
Preference Capital	30,000	30,000	30,000	30,000
Total Cost of Investment	1,80,000	1,80,000	1,80,000	1,80,000
Adjustment for Dividend out of Pre–Acquisition Profits				
Less: Only for Cum Dividend Purchase				
Preference Dividend (12% x ₹ 20,000)	(2,400)	–	N.A.	N.A.
Equity Dividend (20% x ₹ 60,000)	(12,000)	–	N.A.	N.A.
Add: Only for Ex-Dividend Purchase				
Preference Dividend (12% x ₹ 20,000)	N.A.	N.A.	–	2,400
Equity Dividend (20% x ₹ 60,000)	N.A.	N.A.	–	12,000
Corrected Cost of Investment (A)	**1,65,600**	**1,80,000**	**1,80,000**	**1,94,400**
Nominal Value of Equity Capital (6,000 x ₹ 10)	60,000	60,000	60,000	60,000
Nominal Value of Pref. Capital (200 x ₹ 100)	20,000	20,000	20,000	20,000
Share in Capital Profit	96,000	96,000	96,000	96,000
Total of Above (B)	**1,76,000**	**1,76,000**	**1,76,000**	**1,76,000**
Goodwill (if A > B) (A - B)	**–**	**4,000**	**4,000**	**18,400**
Capital Reserve (if B < A) (B - A)	**10,400**	**–**	**–**	**–**

Note: Investment in Debentures are not considered for determining Cost of Control since as per AS 21, Cost of Control is required to be determined only to the extent of share in the Equity of the Subsidiary i.e. Shareholders Networth. Debentures are excluded in computing Shareholders Networth and hence should not be considered in the determining Cost of Control. Gain or Loss on elimination of mutually held Debentures in the consolidation process will be adjusted against Group Reserves.

Illustration 6: Minority Interest

X Ltd. acquired 75% of the Equity Shares of Y Ltd. From the following extract Balance Sheet as at 31st March of Y Ltd. and additional information furnished, determine Minority Interest in Y Ltd. as on Balance Sheet date

Liabilities	₹	Assets	₹
Share Capital:		**Fixed Assets:**	
Equity Capital (₹ 100)	20,00,000	(Net Block) (Tangible)	40,00,000
Reserves:		**Current Assets:**	
Securities Premium	3,00,000	Stock in Trade	20,00,000
General Reserve	7,00,000	Debtors	12,00,000
Profit and Loss Account	12,00,000	Other Current Assets	8,00,000
Current Liabilities:			
Creditors	14,00,000		
Bank Overdraft	24,00,000		
Total	**80,00,000**	**Total**	**80,00,000**

When X Ltd. acquired shares, balances in Reserves of Y Ltd. were as under - (a) Securities Premium ₹ 3,00,000; (b) General Reserve ₹ 1,00,000; (c) Profit and Loss Account ₹ 4,00,000.

Solution:

1. Basic Information

Company Status		Dates		Holding Status	
Holding Company	= X	**Acquisition:**	Not Available	Holding Company	= 75%
Subsidiary	= Y	**Consolidation:**	31st March	Minority Interest	= 25%

2. Analysis of Reserves and Surplus of Y Ltd.

(a) Securities Premium

Balance as per Balance Sheet ₹ 3,00,000

Balance on date of acquisition	Acquisition to Consolidation
₹ **3,00,000**	(balancing figure) ₹ **NIL**
Capital Profit	**Securities Premium**

(b) General Reserve

Balance as per Balance Sheet ₹ 7,00,000

Balance on date of acquisition	Acquisition to Consolidation
₹ **1,00,000**	(balancing figure) ₹ **6,00,000**
Capital Profit	**Revenue Reserve (General Reserve)**

(c) Profit and Loss Account

Balance as per Balance Sheet ₹ 12,00,000

Balance on date of acquisition	Acquisition to Consolidation
₹ **4,00,000**	(balancing figure) ₹ **8,00,000**
Capital Profit	**Revenue Profit (P&L A/c)**

3. Analysis of Net Worth of Y Ltd.

Particulars		Total	Share of X Ltd.	Minority Interest
		100%	75%	25%
(a) Equity Share Capital		**20,00,000**	15,00,000	5,00,000
(b) Capital Profits	Securities Premium	3,00,000		
	General Reserve	1,00,000		
	Profit & Loss Account	4,00,000		
	Total	**8,00,000**	6,00,000	2,00,000
(c) Revenue Reserves	General Reserve	**6,00,000**	4,50,000	1,50,000
(d) Revenue Profits	Profit & Loss A/c	**8,00,000**	6,00,000	2,00,000
Minority Interest				**10,50,000**

Illustration 7: Minority Interest - Investment in Preference Capital

J Ltd. acquired 60% of the Equity Shares and 35% of Preference Shares of K Ltd. The Extract Balance Sheet of K Ltd. as on 31st March is as under —

Liabilities		₹	Assets		₹
Share Capital:	Equity Capital (₹ 100)	3,75,000	**Fixed Assets:**	(Net Block - Tangible)	5,50,000
	Pref. Capital (₹ 100)	2,50,000	**Current Assets:**	Stock In Trade	1,70,000
Reserves:	Capital Reserve	37,500		Debtors	1,87,500
	General Reserve	1,70,000		Other Current Assets	67,500
	Profit and Loss Account	42,500	**Miscellaneous Expenditure:**		
Current Liabs:	Creditors	1,25,000		Preliminary Expenses	25,000
	Total	**10,00,000**		**Total**	**10,00,000**

When J Ltd. acquired shares, balances in Reserves of K Ltd. were as under – (a) Capital Reserve ₹ 20,000; (b) General Reserve ₹ 45,000; (c) Profit and Loss Account ₹ 67,500; (d) Preliminary Expenses ₹ 25,000.

Determine Minority Interest for the purpose of Consolidation.

Solution:

1. Basic Information

Company Status		Dates		Holding Status	
Holding Company	= J Ltd.	**Acquisition:**	Not Available	Holding Company	= 60%
Subsidiary	= K Ltd.	**Consolidation:**	31st March	Minority Interest	= 40%

2. Analysis of Reserves and Surplus of J Ltd.

(a) Capital Reserve

Balance as per Balance Sheet ₹ 37,500

Balance on date of acquisition	Acquisition to Consolidation
₹ **20,000**	(balancing figure) ₹ **17,500**
Capital Profit	**Capital Reserve**

(b) General Reserve

Balance as per Balance Sheet ₹ 1,70,000

Balance on date of acquisition	Acquisition to Consolidation
₹ **45,000**	(balancing figure) ₹ **1,25,000**
Capital Profit	**Revenue Reserve (General Reserve)**

(c) Profit and Loss Account

Balance as per Balance Sheet ₹ 42,500

Balance on date of acquisition	Acquisition to Consolidation
₹ **67,500**	(balancing figure) **(₹ 25,000)**
Capital Profit	**Revenue Profit (P&L A/c)**

(d) Preliminary Expenses

Balance as per Balance Sheet ₹ 25,000

Balance on date of acquisition	Acquisition to Consolidation
(₹ **25,000**)	(balancing figure) ₹ **NIL**
Capital Profit	**Preliminary Expenses**

3. Analysis of Net Worth of K Ltd.

	Particulars		**Total**	**Share of J. Ltd.**	**Minority Interest**
			100%	**60%**	**40%**
(a)	**Equity Share Capital**		**3,75,000**	2,25,000	1,50,000
(b)	**Pref. Share Capital**	**[35 : 65]**	**2,50,000**	87,500	1,62,500
(b)	**Capital Profits**	Capital Reserve	20,000		
		General Reserve	45,000		
		Profit & Loss Account	67,500		
		Preliminary Expenses	(25,000)		
	Total		**1,07,500**	64,500	43,000
(c)	**Capital Reserve**		**17,500**	10,500	7,000
(c)	**Revenue Reserves**	General Reserve	**1,25,000**	75,000	50,000
(d)	**Revenue Profits**	Profit & Loss A/c	**(25,000)**	(15,000)	(10,000)
	Minority Interest				**4,02,500**

Illustration 8: Elimination of Unrealized Profits – Stock Movement

From the following information determine the amount of unrealized profits to be eliminated and the apportionment of the same, if C Ltd. holds 75% of the Equity Shares of D Ltd. -

1. Sales by C Ltd. to D Ltd. -
   (a) Goods costing ₹ 5,00,000 at a profit of 20% on Sale Price. Entire stock were lying unsold as on the Balance Sheet date.
   (b) Goods costing ₹ 7,00,000 at a profit of 25% on Cost Price. 40% of the goods were included in closing stock of D.
2. Sales by D Ltd. to C Ltd. -
   (a) Goods sold for ₹ 7,50,000 on which D made profit of 25% on Cost. Entire stock were at C's godown as on the Balance Sheet date.
   (b) Goods sold for ₹ 9,00,000 on which D made profit of 15% on Sale Price. 70% of the value of goods were included in closing stock of C.

Solution:

Transaction	**Sale by C Ltd. (Holding) to D Ltd. (Subsidiary)**	
Nature of Transaction	Downstream Transaction	
Profit on Transfer	Cost ₹ 5,00,000 x Profit on Sale 20% ÷ Cost on Sale 80% = ₹ **1,25,000**	Cost ₹ 7,00,000 x Profit on Cost 25% = ₹ **1,75,000**
% of Stock included in Closing Stock	100%	40%
Unrealized Profits to be eliminated (transferred to Stock Reserve)	₹ 1,25,000 x 100% = ₹ **1,25,000**	₹ 1,75,000 x 40% = ₹ **70,000**
Share of **Majority** - Reduced from Group Reserves	100% x ₹ 1,25,000 = ₹ **1,25,000**	100% x ₹ 70,000 = ₹ **70,000**
Share of Minority	(Unrealized Profit on Downstream Transactions is fully adjusted against Group Reserves. Minority Interest is not relevant)	

Transaction	**Sale by D Ltd. (Subsidiary) to C Ltd. (Holding)**	
Nature of Transaction	Upstream Transaction	
Profit on Transfer	Sale ₹ 7,50,000 x Profit on Cost 25% ÷ Sale to Cost 125% = ₹ **1,50,000**	Sale ₹ 9,00,000* Profit on Cost 15% = ₹ **1,35,000**
% of Stock included in Closing Stock	100%	70%
Unrealized Profits to be eliminated (reduced from Closing Stock)	₹ 1,50,000 x 100% = ₹ **1,50,000**	₹ 1,35,000 x 70% = ₹ **94,500**
Share of Majority - Reduced from Group Reserves	Share of Majority 75% x Unrealized Profits ₹ 1,50,000 = ₹ **1,12,500**	Share of Majority 75% x Unrealized Profits ₹ 94,500 **= ₹ 70,875**
Share of Minority - Reduced from Minority Interest	Share of Minority 25% x Unrealized Profits ₹ 1,50,000 = ₹ **37,500**	Share of Minority 25% x Unrealized Profits ₹ 94,500 = ₹ **23,625**

Illustration 9: Elimination of Unrealized Profits - Transfer of Assets

In each of the following cases, ascertain (a) Unrealized Profits to be eliminated; (b) Unrealized Profits adjusted against Holding Company's Reserve and Minority Interest; and (c) balance in Asset Account as appearing in the Consolidated Balance Sheet –

(a) A Machine costing ₹ 3,50,000 has been sold by Z Ltd. to its subsidiary F Ltd. for ₹ 4,20,000. During the year F Ltd. has charged depreciation of ₹ 35,000 on the machinery. Z Ltd. holds 80% of the Equity of F Ltd. Machinery Account balance as appearing in the books of Companies - Z Ltd. ₹ 9,57,500; F Ltd. ₹ 6,85,000.

(b) C Ltd. sold 8 Workstations to its parent S Ltd. at ₹ 25,000 each. The total cost of the Workstations to C was ₹ 97,500. S holds 70% of the Equity Capital in C. The balances in the Asset Account "Computer and Peripherals" were – C ₹ 2,50,000; S ₹ 5,00,000. Depreciation at 30% was charged by S on the Workstations purchased from C.

Solution:

Sold by	**Z Ltd. (Holding Co.)**	**C Ltd. (Subsidiary Co.)**
Purchased by	F Ltd. (Subsidiary Co.)	S Ltd. (Holding Co.)
Nature of transfer	Downstream Transfer	Upstream Transfer
Sale Price **Less:** Cost to Seller	₹ 4,20,000 ₹ 3,50,000	₹ 25,000 x 8 = ₹ 2,00,000 ₹ 97,500
A. Profit on Transfer	₹ 70,000	₹ 1,02,500
B. Rate of Depreciation	35,000/4,20,000 = 8.33%	30%
C. Depn. on profit element (A × B)	70,000 x 8.33% = ₹ 5,831	1,02,500 x 30% = ₹ 30,750
Unrealized Profit to be eliminated (A - C)	₹ **64,169**	₹ **71,750**
- Adjusted against Holding Co's Reserves	100% x ₹ 64,169 = ₹ **64,169**	Share of Holding Co. 70% x ₹ 71,750 = ₹ **50,225**
- Adjusted against Minority Interest	Unrealized profits on downstream transfer are adjusted fully against Group Reserves only	Share of Minority 30% x ₹ 71,750 = ₹ **21,525**
Consolidated Asset Balance (Holding Co. bal. + Subsidiary Co. bal. **Less** Unrealized Profit)	9,57,500 + 6,85,000 - 64,169 = ₹ **15,78,331**	2,50,000 + 5,00,000 - 71,750 = ₹ **6,78,250**

Illustration 10: Elimination of Mutual Owings

The following balances are extracted from the Balance Sheets of X Ltd. and Y Ltd. -

Particulars	**X Ltd. (₹)**	**Y Ltd. (₹)**
Bills Payable	7,50,000	4,50,000
Trade Creditors	5,00,000	7,00,000
Bills Receivable	3,50,000	5,00,000
Trade Debtors	8,00,000	7,00,000
Contingent Liability for Bills Discounted	2,00,000	1,50,000

Additional Information –

1. X Ltd. is wholly owned subsidiary of Y Ltd.
2. Creditors of X Ltd. include ₹ 2,50,000 due to Y Ltd. for goods supplied by it for ₹ 3,00,000. Debtors of Y Ltd. however shows a Debit balance of ₹ 3,00,000 due from X. X had remitted ₹ 50,000 by Demand Draft to Y which was not received by Y on the Balance Sheet date.
3. Bills payable of 'X' include ₹ 3,00,000 drawn in favour of Y Ltd. Y had discounted bills worth ₹ 1,20,000 with its bankers.

Determine how the above given balances will be disclosed in the Consolidated Balance Sheet of Y Ltd.

Solution:

Particulars		Bills Payable	Bills Receivable	Creditors	Debtors	Contingent Liabilities
Y Ltd.		7,50,000	3,50,000	5,00,000	8,00,000	2,00,000
X Ltd.		4,50,000	5,00,000	7,00,000	7,00,000	1,50,000
	Total before adj. Mutual Owings	**12,00,000**	**8,50,000**	**12,00,000**	**15,00,000**	**3,50,000**
Less:	Mutual Owings					
–	For goods supplied	–	–	(2,50,000)	(3,00,000)	–
–	Bills drawn in favour of Y (Only to the extent not discounted is reduced) (3,00,000-1,20,000)	(1,80,000)	(1,80,000)	–	–	–
–	Bills discounted (Only mutual bills discounted is reduced)	–	–	–	–	(1,20,000)
Balance for CBS		**10,20,000**	**6,70,000**	**9,50,000**	**12,00,000**	**2,30,000**

Note: *In addition to the above, in the Consolidated Balance Sheet, ₹ 50,000 will be shown as "Remittance-in Transit" under Current Assets after Trade Debtors and Bills Receivable.*

Illustration 11: Consolidated Balance Sheet – Line to Line Addition

From the Extract Balance Sheets and information given below, prepare Consolidated Balance Sheet of A Ltd. and K Ltd. as at 31st March, 2015 -

Liabilities	A (₹)	K (₹)	Assets		A (₹)	K (₹)
Equity Capital (₹ 10) General	30,000	20,000	Fixed Assets (Tangible)		20,000	15,000
Reserve	5,000	5,000	Investment in Shares of K Current		16,000	–
8% Debentures	10,000	5,000	Asset:	Stock in Trade	8,000	10,000
Creditors	5,000	5,000		Debtors	4,000	7,000
				Cash & Bank	2,000	3,000
Total	**50,000**	**35,000**	**Total**		**50,000**	**35,000**

A Ltd. holds 80% of Equity Shares in K since its incorporation. Prepare Consolidated Balance Sheet.

Solution:

1. Basic Information

Company Status		Dates		Holding Status	
Holding Co.	= A	**Acquisition:**	K's Incorporation	Holding Company	= 80%
Subsidiary	= K	**Consolidation:**	31st March	Minority Interest	= 20%

2. Analysis of General Reserves of K Ltd.

Balance as per Balance Sheet ₹ 5,000

Balance on date of acquisition	Acquisition to Consolidation
₹ NIL	(balancing figure) ₹ **5,000**
Capital Profit	**Revenue Reserve**

Note: Since A holds shares in K since its incorporation, the entire Reserve balance will be Revenue.

3. Analysis of Net Worth of K Ltd. **(₹ '000)**

	Particulars	Total	A 80%	Minority 20%
(a)	Equity Share Capital	20,000	16,000	4,000
(b)	Capital Profits	NIL	–	–
(c)	Revenue Reserve (General Reserve)	5,000	4,000	1,000
	Minority Interest			**5,000**

4. Cost of Control

	Particulars	₹
	Cost of Investment	16,000
Less:	Nominal Value of Equity Capital	(16,000)
Less:	Share of Capital Profits	NIL
	Goodwill / Capital Reserve	**NIL**

Note: If shares are purchased and held from the date of incorporation of subsidiary, there will not be any Goodwill or Capital Reserve.

5. Consolidation of Reserves

Particulars	₹
Balance as per Balance Sheet	5,000
Add: Share of Revenue Reserves	4,000
Consolidated Balance	**9,000**

Name of the Company: A Ltd. And its subsidiary K. Ltd.

Consolidated Balance Sheet as at 31st March, 2015

Ref No.		Particulars	Note No.	As at 31st March, 2015	As at 31st March, 2014
				₹	₹
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital @ ₹ 100 each		30,000.00	-
		(b) Reserves and surplus	1	9,000.00	-
				39,000.00	-
	2	**Minority Interest**		5,000.00	-
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**			
		(a) Long-term borrowings (8% Debenture)	2	15,000.00	-
				15,000.00	-
	5	**Current liabilities**			
		(a) Trade payables	3	10,000.00	-
				10,000.00	-
		TOTAL (1+2+3+4+5)		69,000.00	-
	B	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	4	35,000.00	-
				35,000.00	-
	2	**Current assets**			
		(a) Inventories	5	18,000.00	-
		(b) Trade receivables	6	11,000.00	-
		(c) Cash and cash equivalents	7	5,000.00	-
				34,000.00	-
		TOTAL (1+2)		69,000.00	-

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note 1. Reserve & Surplus (₹ '000)

	Current Year	Previous Year
General Reserve	9,000	-
	9,000	-

Note 2. Long term Borrowings :- (₹ '000)

	Current Year	Previous Year
8% Debentures		
- A Ltd	10,000.00	-
- K Ltd	5,000.00	-
	15,000.00	-

Note 3. Trade Payable :-

	Current Year	Previous Year
- A Ltd	5,000.00	-
- K Ltd	5,000.00	-
	10,000.00	-

Note 4. Tangible Assets:-

	Current Year	Previous Year
- A Ltd	20,000.00	-
- K Ltd	15,000.00	-
	35,000.00	-

Note 5. Inventories :-

	Current Year	Previous Year
- A Ltd	8,000.00	-
- K Ltd	10,000.00	-
	18,000.00	-

Note 6. Trade Receivable :-

	Current Year	Previous Year
- A Ltd	4,000.00	-
- K Ltd	7,000.00	-
	11,000.00	-

Note 7. Cash and cash Equivalent :-

	Current Year	Previous Year
- A Ltd	2,000.00	-
- K Ltd	3,000.00	-
	5,000.00	-

Illustration 12: Basic Problem

In Preparing the Consolidated Balance Sheet of A Ltd. as on 31.12.2014. You are required to show clearly what amount, if any, you would include in respect of B Ltd. with regard to:

(a) Cost of Control;

(b) Profit or Loss; and

(c) Minority Interest

Under each of the following assumptions:

1. 48,000 of the shares then in issue of B Ltd. were acquired at a cost of 75,000 on 1st March, 2012. A Ltd. participated in the proposed dividend of 8,000.

2. 48,000 of the shares then in issue of B Ltd., were acquired at a cost of 60,000 on 3rd Dec. 2012:

   A Ltd. participated in the bonus issue but not in the proposed dividend of 9,000.

3. 60,000 of the shares then in issue of B Ltd. were acquired at a cost of 80,000 on 1st July, 2014. A Ltd. did not participate in the proposed dividend of 6,000.

The Balance Sheet of B Ltd. as on 31st December, 2014 showed:

Particulars	Amount (₹)
(a) Share Capital, authorised and issued of 1 each	80,000
(b) Undistributed Profits	24,000
(C) 7% Debentures	40,000

The Profit and Loss appropriation, for the four years ending 31.12.2014 were as follows:

Particulars	2011 (₹)	2012 (₹)	2013 (₹)	2014 (₹)
(a) Balance at the beginning of the year	16,000	22,000	43,000	28000
(b) Bonus Issue of 1 share for every 4 shares: 1 Jan. 2013	Nil	Nil	(16,000)	Nil
(c) Profit for the year/(Loss)	14,000	30,000	7,000	(4,000)
(d) Profits available for appropriation	30,000	52,000	34,000	24,000
(e) Proposed Dividends	(8,000)	(9,000)	(6,000)	Nil
(f) Balance c/f	22,000	43,000	28,000	24,000

Solution:

Case: 1

A. Cost of Control:

Particulars	₹	₹
(a) Cost of Investment	75,000	67,875
1. Amount Invested	(7,125)	
2. Less: Pre-Acquisition Dividend (W. N.1)		
(b) Share of Net Asset represented by:	60,000	67,125
1. Share Capital (including bonus : 48,000 48,000 x 1/4)	7,125	
2. Capital Profit (W.N. 2)		
(c) Goodwill (a - b)		750

Working Notes:

1. Pre-Acquisition Dividend

1. Year 2009 = $\frac{48,000 \times 8,000}{64,000}$	₹ 6,000
2. Year 2010 = $\frac{48,000 \times 2 \times 9,000}{64,000 \times 12}$	₹ 1,125
Total	**₹ 7,125**

Share Capital before Bonus Issue = 80,000 × 4/5 = ₹ 64,000

(₹)

2.	Capital Profit	
	(a) Pre - Acquisition Profit upto 2011	22,000
	(b) Pre - Acquisition Profit of 2010 (30,000 - 9,000)x 2/12	3,500
	(c) Less: Bonus Issue	(16,000)
	(d) Remaining Capital Profits	9,500
	(e) A Ltd.'s share of above (48 / 64 x 9,500)	7,125

B	Consolidated Profit and Loss Account: (a) Closing Balance 24,000 (b) Minority Interest: 24,000 x 25% = ₹ 6,000 (c) Capital Profit Upto 2011 Upto 2012 (2 months)	 22,000 3,500
		25,500
	Less: Bonus Share Rem. CP	 16,000 9,500
	A Ltd.'s Share of Capital Profit = 7,125 (75%) A Ltd.'s Share of RP. For consolidation (bal. fig.) = 24,000 - 6,000 - 7,125 =10,875	

C. Minority Interest

Particulars	**Amount (₹)**
1. Share Capital (1/4 x₹ 80,000)	20,000
2. Share of Profit (as per B above)	6,000
Total	26,000

Case : 2

A. Cost of Control

Particulars	**(₹)**	**(₹)**
(a) Cost of Investment		
1. Amount Invested		60,000
(b) A Ltd. share of Net Assets of B Ltd. as on the date of acquisition represented by		
• Paid up share capital (including bonus) [48,000 + 48,000 x ¼]	60,000	
• Capital Profit (48,000/64,000 x (43,000 - 16,000)	20,250	80,250
(c) Capital Reserve		20,250

B. Consolidated Profit and Loss Account:

(a) Closing Balance = ₹ 24,000

(b) Minority interest $\left(\frac{20{,}000 \times 24{,}000}{80{,}000}\right) = ₹\ 6{,}000$

(c)	Pre - Acquisition Profit Closing Balance as on 31.12.2012 Less: Bonus Issue Balance A Ltd.'s Share of Capital Profit	 ₹43,000 ₹16,000 ₹27,000 ₹20,250
(d)	A Ltd.'s Share of RP for consolidation: (Bal. fig.)	
	= (24,000 - 6,000 - 20,250) = 2,250 (Dr.) (Bal. Fig.)	

C. Minority Interest

Particulars	Amount (₹)
(a) Share Capital (25% x 80,000)	20,000
(b) Share of Profit (as per B above)	6,000
Total	**26,000**

Case : 3

A. Cost of Control

	Particulars	Amount (₹)	Amount (₹)
(a)	(a) Cost of Investment		
	1. Amount Invested		80,000
(b)	Snare of Net Assets represented by		
	1. Share Capital	60,000	
	2. Pre- acquisition Profit		
	Upto Year 2013 - 60/80 x 28,000	21,000	
	Year 2014 - 60/80 x 4,000 x 6/12	(1,500)	79,500
(c)	Goodwill (a - b)		500

B. Consolidated Profit and Loss Account:

(a)	Closing Balance	₹24000
(b)	Minority interest $\left(\frac{20000 \times 24000}{80000}\right)$	₹6,000
(c)	Pre - Acquisition Profit	
	Closing Balance as on 31.12.2013	₹28,000
	Less: Loss for 2014 upto 30.6.2014	₹12,000
	Balance of A Ltd.'s Share of Capital Profit ₹ 19,500	
	A Ltd.'s Share of RP for consolidation (bal. fig.)	
	= ₹ (24,000 - 6,000 - 19,500)	
	= ₹ 1,500 (Dr.) (Bal. Fig.)	

C. Minority Interest

	Particulars	Amount (₹)
(a)	Share Capital (25% x 80,000)	20,000
(b)	Share of Profit (as per B above)	6,000
	Total	**26,000**

Illustration 13: Bonus issue - Before and After

On 31.03.2015, R Ltd. acquired 1,05,000 Shares of S Ltd. for ₹ 12,00,000. The Extract Balance Sheet of S Ltd. on that date was as under -

(₹ 000's)

Liabilities	₹	Assets	₹
1,50,000 Equity Shares of ₹ 10 each fully paid Pre- Incorporation Profits Profit & Loss Account Creditors	1,500 30 60 75	Fixed Assets (Tangible) Current Assets	1,050 615
Total	**1,665**	**Total**	**1,665**

On 31.03.2016, the Balance Sheets of the two Companies were as follows - (₹ 000's)

Liabilities	R	S	Assets	R	S
Equity Shares of ₹ 10 each fully paid (before Bonus Issue)	4,500	1,500	Fixed Assets (Tangible)	7,920	2,310
			1,05,000 Equity Shares in	1,200	–
Securities Premium	900	–	S Ltd. at Cost		
Pre-Incorporation Profits	–	30	Current Assets	4,410	1,755
General Reserve	6,000	1,905			
Profit and Loss Account	1,575	420			
Creditors	555	210			
Total	**13,530**	**4,065**	**Total**	**13,530**	**4,065**

Directors of S Ltd. made a bonus issue on 31.03.2016 in the ratio of one Equity Share of ₹ 10 each fully paid for every two Equity Shares held on that date.

Calculate as on 31.3.2016 (i) Cost of Control/Capital Reserve ; (ii) Minority Interest; (iii) Consolidated Profit and Loss Account in each of the following cases: (1) Before issue of Bonus Shares; (2) Immediately after the issue of Bonus Shares. It may be assumed that Bonus Shares were issued out of Post-Acquisition Profits by using General Reserve.

Prepare a Consolidated Balance Sheet after the Bonus Issue.

Solution:

1. Basic Information

Company Status		Dates		Holding Status	
Holding Company	= R Ltd.	Acquisition:	31.03.2015	Holding Company	= 70%
Subsidiary	= S Ltd.	Consolidation:	31.03.2016	Minority Interest	= 30%

2. Analysis of Reserves and Surplus of S Ltd.

(a) Pre-Incorporation Profits = ₹ 30,000 – **Capital Profit**

(b) General Reserve

Before Bonus Issue	
As on 31.3.2016	19,05,000
As on 01.04.15	Tfr between 01.04.15 & 31.3.2016
NIL **Capital**	**19,05,000** **Revenue**

After Bonus Issue		
As on 31.3.2016	19,05,000	
Less: Bonus Issue	7,50,000	(15 Lacs x 1/2)
Corrected Bal	11,55,000	
01.04.2015 **NIL** **Capital**	Tfr between 1.4.15 & 3 1.3.16 **11,55,000** **Revenue**	

(c) Profit & Loss Account

As on 31.03.2016 ₹ 4,20,000

As on 01.04.2005	60,000	Profits between 01.04.2015 & 31.03.2016	**3,60,000**
	Capital		**Revenue**

3. Analysis of Net Worth of S Ltd.

Particulars	Before Bonus Issue			After Bonus Issue		
	Total	**R**	**Minority**	**Total**	**R**	**Minority**
	100%	**70%**	**30%**	**100%**	**70%**	**30%**
(a) Share Capital	15,00,000			15,00,000		
Add: Bonus Issue	–			7,50,000		
	15,00,000	10,50,000	4,50,000	**22,50,000**	15,75,000	6,75,000
(b) Capital Profits						
Pre Incorporation Profits	30,000			30,000		
General Reserve	NIL			NIL		
Profit and Loss Account	60,000			60,000		
	90,000	63,000	27,000	**90,000**	63,000	27,000
(c) **Revenue Reserve:** Gen. Reserve	**19,05,000**	13,33,500	5,71,500	**11,55,000**	8,08,500	3,46,500
(d) **Revenue Profits:** P & L A/c	**3,60,000**	2,52,000	1,08,000	**3,60,000**	2,52,000	1,08,000
Minority Interest			**11,56,500**			**11,56,500**

4. Cost of Control

Particulars	Before Bonus Issue	After Bonus Issue
Cost of Investment	12,00,000	12,00,000
Less: (a) Nominal Value of Share Capital	(10,50,000)	(15,75,000)
(b) Share in Capital Profits	(63,000)	(63,000)
Goodwill / Capital Reserve on Consolidation	**87,000**	**(4,38,000)**

5. Consolidation of Reserves & Surplus

Particulars	Before Bonus Issue		After Bonus Issue	
	Gen. Res.	**P&L A/c**	**Gen. Res.**	**P&L A/c**
Balance as per Balance Sheet of R Ltd.	60,00,000	15,75,000	60,00,000	15,75,000
Add: Share of Revenue	13,33,500	2,52,000	8,08,500	2,52,000
Consolidated Balance	**73,33,500**	**18,27,000**	**68,08,500**	**18,27,000**

Name of the Company: R Ltd. And its subsidiary S Ltd.

Consolidated Balance Sheet as at 31st March 2016

Ref No.	Particulars		Note No.	As at 31st March, 2016	As at 31st March, 2015
				₹	₹
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital @ ₹ 10 each		45,00,000	-
		(b) Reserves and surplus	1	99,73,500	-
				1,44,73,500	-
	2	**Minority Interest**		11,56,500	-
	3	**Share application money pending allotment**		Nil	

Ref No.		Particulars	Note No.	As at 31st March, 2016	As at 31st March, 2015
				₹	₹
	4	**Non-current liabilities**		Nil	
	5	**Current liabilities**			
		(a) Other current liabilities	2	7,65,000	-
				7,65,000	-
		TOTAL (1+2+3+4+5)		1,63,95,000	-
	B	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	3	1,02,30,000	-
				1,02,30,000	-
	2	**Current assets**			
		(a) Other current assets	4	61,65,000	-
				61,65,000	-
		TOTAL (1+2)		1,63,95,000	-

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note 1. Reserve and Surplus :-

	Current Year	Previous Year
General Reserve	68,08,500	-
Profit and loss	18,27,000	-
Capital reserve on consolidation	4,38,000	-
Securities Premium	9,00,000	-
	99,73,500	-

Note 2. Current Liabilities :-

	Current Year	Previous Year
Bills Payable:-		
- R Ltd	5,55,000	-
- S Ltd	2,10,000	-
	7,65,000	-

Note 3. Tangible Assets:-

	Current Year	Previous Year
Fixed Assets		
- R Ltd	79,20,000	-
- S Ltd	23,10,000	-
	1,02,30,000	-

Note 4. Current Assets:-

	Current Year	Previous Year
Current Assets		
- R Ltd	44,10,000	-
- S Ltd	17,55,000	-
	61,65,000	-

Illustration 14: Bonus Issue, Reverse Working for Bonus Amount - Investment in Debentures

The summarised Balance Sheet of P Ltd. and Q Ltd. as at 31.03.2015 is given below (₹ in 000's)-

Liabilities	P	Q	Liabilities	P	Q
Equity Share Capital (₹ 10)	5,000	2,400	Goodwill	300	200
Securities Premium	200	140	Buildings	1,000	1,000
General Reserve	1,000	1,600	Machinery	4,000	2,440
Profit & Loss Account	900	600	Investment in Shares:		
8% Debentures	2,000	1,000	-1,92,000 Shares of Q Ltd.	1,500	
Trade Creditors	800	400	Investments in Debentures:		
Outstanding Expenses	270	180	- In Q Ltd. (Face Value ₹ 4,00,000)	450	
			- In P Ltd. (Face Value ₹ 2,00,000)		220
			Sundry Debtors	1,500	1,000
			Stock	1,000	1,000
			Cash and Bank	200	100
			Preliminary Expenses	100	50
			Outstanding Income	120	310
Total	**10,170**	**6,320**	**Total**	**10,170**	**6,320**

1. When the Shares were acquired, Q Ltd. had ₹ 2.2 Lakhs in General Reserve and ₹ 1,00,000 in Securities Premium, ₹ 3,00,000 (Dr.) in Profit and Loss Account.
2. Two years after the date of acquisition Bonus Shares at 1 to 1 were issued out of General Reserve.
3. One year after the Bonus issue, Rights Shares were issued at 10% Premium at 1 for 5 held and P Ltd. purchased all the shares offered to it.
4. P Ltd. received ₹ 1,92,000 dividend for the last year and ₹ 96,000 interim dividend in the current year, i.e. 3 years after the Rights Issue.
5. For the current year 15% dividend (including Interim Dividend) has been proposed by Q Ltd., 10% by P Ltd., but no effect has yet been given in the accounts.
6. On the same day referred to in (5) above, Bonus Dividend has been declared at 1 to 2, but no effect has yet been given.
7. 50% of the shares originally purchased in Q Ltd. were paid for to the shareholders of Q Ltd. by 50,000 shares of P Ltd. issued at 10% premium.
8. Debenture Interest of both the Companies falls due on 31st March, but payments are made a week later.

Prepare Consolidated Balance Sheet as at 31.03.2015.

Solution:

1. Basic Information

Company Status	Dates	Holding Status
Holding Company = P Ltd. Subsidiary = Q Ltd.	Consolidation: 31.03.2015	Holding Company = 80% Minority Interest = 20%

	Shares held as on 31.03.2015	1,92,000
Add:	Second Bonus Issue (1,92,000 x 1/2)	96,000
	Actual Shareholding	2,88,000

DOA - 1 (Original Acquisition)	First Bonus Issue (1 : 1 as at DOA-1)	DOA - 2 Rights Issue	Second Bonus Issue (1 :2 as at DOA-2)
80,000	**80,000**	**32,000**	**96,000**
(balancing figure)	[(1,92,000 - 32,000) ÷ 2]	[1,92,000 x 1 ÷ (5 + 1)]	

40,000	40,000
For Cash	For Shares of P Ltd.

2. Analysis of Reserves & Surplus of Q Ltd.

(a) Securities Premium

Balance on 31.03.2015 ₹ 1,40,000

DOA-1	₹ **1,00,000** **Capital Profit**	Proceeds from Rights Issue ₹ **40,000** **Capital**

(b) General Reserve

	Shares held as on 31.03.2015	16,00,000
Add:	Second Bonus Issue (24,00,000 x 1/2)	12,00,000
	Adjusted Balance	4,00,000

	DOA-1	₹ 22,00,000	Additions upto Consolidation
Less:	First Bonus	(₹ 10,00,000) (80,000 Shares/80% x ₹ 10)	(balancing figure) ₹ **4,00,000**
Less:	Second Bonus	(₹ 12,00,000)	**Revenue Reserve**
	Capital Profit	₹ **NIL**	

Note: In the absence of information in this regard, it is presumed that the second bonus issue has been made out of reserves as on the date of controlling acquisition.

(c) Profit & Loss Account

	Balance as on 31.03.2015	6,00,000	
Less:	Debenture Interest (10,00,000 x 8%)	(80,000)	
Add:	Debenture Interest from P (2,00,000 x 8%)	16,000	
Less:	Proposed Dividend (24,00,000 x 15% – Interim 1,20,000)	(2,40,000)	(See Note)
	Adjusted Balance	2,96,000	

DOA - 1	Additions to P&L A/c
(₹ 3,00,000) Debit balance given	₹ **5,96,000**
Capital Profit	**Revenue Profit**

Note: Interim Dividend received by Holding Company = ₹ 96,000 for 80% holding. Hence, Total Interim Dividend paid by Subsidiary = ₹ 96,000 ÷ 80% = ₹ 1,20,000

3. Analysis of Net Worth of Q Ltd.

Particulars			Total	P	Minority
			100%	**80%**	**20%**
(a)	**Equity Share Capital:**	(including Bonus ₹ 12,00,000)	**36,00,000**	28,80,000	7,20,000
(b)	**Capital Profits:**	Securities Premium Account	1,00,000		
		General Reserve	NIL		
		Profit & Loss Account	(3,00,000)		
		Preliminary Expenses	(50,000)		
			(2,50,000)	(2,00,000)	(50,000)
(c)	**Securities Premium** (after acquisition date)		**40,000**	32,000	8,000
(d)	**Revenue Reserves:**	General Reserve	**4,00,000**	3,20,000	80,000
(e)	**Revenue Profits:**	Profit & Loss A/c	**5,96,000**	4,76,800	1,19,200
(f)	**Proposed Equity Dividend**		**2,40,000**	1,92,000	48,000
Minority Interest					**9,25,200**

4. Cost of Control

	Particulars		₹
	Cost of Investment		15,00,000
Less:	(1) Nominal Value of Equity Capital	28,80,000	
	(2) Share in Capital Profit of Q Ltd.	(2,00,000)	(26,80,000)
	Capital Reserve on Consolidation		**(11,80,000)**

5. Gain / Loss on Consolidation of Debentures

	Particulars		₹
	Cost of Investment in Debentures:		
	Q Ltd. in P Ltd.	2,20,000	
	P Ltd. in Q Ltd.	4,50,000	6,70,000
Less:	Face Value of Debentures (₹ 20,000 + ₹ 40,000)		(6,00,000)
Loss on Consolidation of Debentures (Adjusted against Group Reserves)			**70,000**

6. Consolidation of Reserves & Surplus

	Particulars		Securities Premium	Gen. Res	P&L A/c
	Balance as per Balance Sheet of P Ltd.		2,00,000	10,00,000	9,00,000
Less:	Proposed Dividend	(₹ 50,00,000 x 10%)		–	(5,00,000)
Less:	Debenture Interest Due	(₹ 20,00,000 × 8%)	–	–	(1,60,000)
Add:	Share of Dividend from Q Ltd.	(₹ 2,40,000 x 80%)	–	–	1,92,000
Add:	Share of Debenture Int from Q	(₹ 4,00,000 x 8%)	–	–	32,000
	Adjusted Balance		**2,00,000**	**10,00,000**	**4,64,000**
Add:	Share of Reserves of Q Ltd.		32,000	3,20,000	4,76,800
Less:	Loss on Elimination of Debentures on Consolidation				(70,000)
	Consolidated Balance		**2,32,000**	**13,20,000**	**8,70,800**

Name of the Company: P Ltd. And its subsidiary Q Ltd.

Consolidated Balance Sheet as at 31st March, 2015

Ref No.		Particulars	Note No.	As at 31st March, 2015	As at 31st March, 2014
				₹	₹
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital @ ₹ 10 each	1	50,00,000	-
		(b) Reserves and surplus	2	36,02,800	-
				86,02,800	-
	2	**Minority Interest**		9,25,200	-
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**			
		(a) Long-term borrowings	3	25,92,000	-
				25,92,000	-
	5	**Current liabilities**			
		(b) Trade payables	4	12,00,000	-
		(c) Other current liabilities	5	4,50,000	-
		(d) Short-term provisions	6	5,00,000	-
				21,50,000	-
		TOTAL (1+2+3+4+5)		1,42,70,000	-

Ref No.	Particulars		Note No.	As at 31st March, 2015 ₹	As at 31st March, 2014 ₹
	B	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	7	84,40,000	-
		(ii) Intangible assets (goodwill)		5,00,000	-
				89,40,000	-
	2	**Current assets**			
		(a) Inventories	8	20,00,000	-
		(b) Trade receivables	9	25,00,000	-
		(c) Cash and cash equivalents	10	3,00,000	-
		(d) Other current assets	11	5,30,000	-
				53,30,000	-
		TOTAL (1+2)		1,42,70,000	-

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

ANNEXURE

Note 1. Share Capital

	Current Year	Previous Year
Authorised Capital	-	-
Issued and Paid Up	50,00,000	-
	-	-
	-	-
	50,00,000	-

Note 2. Reserve and Surplus :-

	Current Year	Previous Year
General Reserve	13,20,000	-
Profit and loss	8,70,800	-
Capital Reserve on Consolidation	11,80,000	-
Securities Premium	2,32,000	-
	36,02,800	-

Note 3. Long Term Borrowings

8% Debentures	Current Year	Previous Year
P	20,00,000	-
Q	10,00,000	-
	30,00,000	-
Less: Held by Q	2,00,000	-
	28,00,000	-
Less: Held by P	4,00,000	-
	24,00,000	-
Debenture int. accrued	1,92,000	-
	25,92,000	-

Note 4. Trade Payable

Sundry Creditors	Current Year	Previous Year
P	8,00,000	-
Q	4,00,000	-
	12,00,000	-

Note 5. Other Current Liabilities :-

	Current Year	Previous Year
Outstanding Expenses		
P	2,70,000	-
Q	1,80,000	-
	4,50,000	-

Note 6. Short Term Provisions

	Current Year	Previous Year
Proposed dividend	5,00,000	-
	5,00,000	-

Note 7. Tangible Assets :-

	Current Year	Previous Year
Land and Building (1000000+1000000)	20,00,000	
Plant and Machinery		
(4000000+2440000)	64,40,000	-
	84,40,000	-

Note 8. Inventories :-

	Current Year	Previous Year
Stock		
P Ltd	10,00,000	-
Q Ltd.	10,00,000	-
		-
	20,00,000	-

Note 9. Trade Receivable :-

	Current Year	Previous Year
Sundry Debtors		
P Ltd	15,00,000	-
Q Ltd.	10,00,000	-
	25,00,000	-

Note 10. Cash and cash equivqlent :-

	Current Year	Previous Year
Cash & Bank		
P Ltd	2,00,000	-
Q Ltd.	1,00,000	-
	3,00,000	-

Note 11. Other Current assets :-

	Current Year	Previous Year
Outstanding Income		
P Ltd	1,20,000	-
Q Ltd.	3,10,000	-
	4,30,000	-
Preliminary Expenditure	1,00,000	-
	5,30,000	-

Notes:

- It is presumed that the Companies have not accounted for the inter company owings in respect of Debenture interest and proposed dividends.
- Interest due on Debenture has been shown under Secured Loans together with Debentures in accordance with Schedule III to the Companies Act, 2013.

A. REVALUATION OF ASSETS

Illustration15: Asset Revaluation, Pre-acquisition Dividend

The Balance Sheets of A Ltd. and B Ltd. as on 31.03.2014 are as follows:

	A Ltd.		B. Ltd.	
	₹	₹	₹	₹
Equity and Liabilities				
Shareholders' Funds				
Share capital				
Equity Shares of ₹ 10 each, fully paid up	40,00,000		8,00,000	
14% Preference Shares of ₹ 100 each, fully paid up	—	40,00,000	5,00,000	13,00,000
Reserves and Surplus				
General reserve	18,00,000		50,000	
Profit and Loss A/c	17,00,000	35,00,000	6,50,000	7,00,000
Current Liabilities				
Trade payables		5,00,000		3,00,000
Total		80,00,000		23,00,000
Assets				
Non-current assets				
Tangible assets				
Plant and machinery	26,50,000		8,00,000	
Furniture and fixtures	8,00,000	34,50,000	5,40,000	13,40,000
Non-current investments				
Equity shares in B Ltd.	19,80,000			
Preference shares in B Ltd.	4,00,000	23,80,000		
Current Assets				
Inventories	8,70,000		4,60,000	
Trade receivables	7,50,000		3,70,000	
Cash and cash Equivalents	5,50,000	21,70,000	1,30,000	9,60,000
Total		80,00,000		23,00,000

A Ltd. acquired 80% of both classes of shares in B Ltd. on 01.04.2013. Additional information:

(i) The balance in Profit and Loss A/c of B Ltd. on 1.4.2013 was 2,50,000, out of which dividend of 15% p.a. on the Equity Capital of 8,00,000 was paid for the year 2012-2013.

(ii) General reserve balances of B Ltd. was the same as on 1.4.2013.

(iii) The dividend in respect of preference shares of B Ltd. for the year 2013-14 was still payable as on 31.3.2014.

(iv) A Ltd. credited its Profit and Loss A/c for the dividend received by it from B Ltd. for the year 2012-13.

(v) At the time of acquisition by A Ltd.; while determining the price to be paid for the shares in B Ltd. it was decided that the value of plant and machinery was to be increased by 20% and that of furniture and fixtures to be reduced by 30%. There was no transaction of purchase or sale of these assets during the year. The effect to these revaluations are to be given in the consolidated balance sheet.

(vi) Sundry creditors of A Ltd. included an amount of 2,20,000 for purchases from B Ltd., on which B Ltd. made a loss of 20,000.

(vii) 60% of the above goods were still with the closing stock of A Ltd. as at 31.03.2014.

Prepare the Consolidated Balance Sheet as at 31st March, 2014, assuming the rate of depreciation charged as 20% p.a. on plant and machinery and 10% p.a. on furniture and fixtures.

Solution:

Consolidated Balance Sheet of A Ltd. and its subsidiaries B Ltd. as 31st March, 2014.

	Particulars	Note No.	As at 31st March, 2014 (₹ in Lakhs)
I.	Equity and Liabilities		
	(a) Share Capital		40,00,000
	(b) Reserves and Surplus		38,12,000
	1. Minority Interest (W.N. 4)		4,02,000
	2. Current Liabilities		
	- Trade Payables	3	5,80,000
	Total (1 + 2 + 3)		87,94,000
II.	Assets		
	1. Non- current assets		
	(a) Fixed assets		
	(i) Tangible Assets	4	47,88,000
	(ii) Intangible Assets	5	10,84,000
	2. Current Assets		
	(a) Inventories	6	1 3,42000
	(b) Trade receivables	7	9,00,000
	(c) Cash and Cash equivalents	8	6,80,000
	Total (1 + 2)		87,94,000

Notes to the accounts

Note 1. Share Capital

	As at 31st March, 2014
Authorized, Issued, Subscribed and paid-up Share Capital:	
40,000 Equity share of ₹10 each	40,00,000
Total	40,00,000

Note 2. Reserve & Surplus

	As at 31st March, 2014
General Reserve	18,00,000
Profit and Loss A/c (W.N.6)	20,12,000
Total	38,12,000

Note 3. Trade Payables

	As at 31st March, 2014
Sundry Creditors - A Ltd.	5,00000
B Ltd.	3,00,000
	8,00,000
Less: Mutual Owing	2,20,000
Total	5,80,000

Note 4. Tangible Assets

		As at 31st March, 2014
Plant and Machinery - A Ltd.	26,50,000	
B Ltd.	9,60,00	36,10,000
Furniture and Fixture A Ltd.	8,00,000	
B Ltd.	3,78,000	11,78,000
Total		47,88,000

5. Intangible Assets

	As at 31st March, 2014
Goodwill	10,84,000
Total	10,84,000

Note 6. Inventories

	As at 31st March, 2014
Stock - A Ltd.	8,70,000
B Ltd.	4,60,000
Add: Unrealized Loss	12,000
Total	13,42,000

Note 7. Trade Receivables

	As at 31st March, 2014
Debtors - A Ltd.	7,50,000
B Ltd.	3,70,000
	11,20,000
Less: Mutual Owing	2,20,000
Total	9,00,000

Note 8. Cash and Cash equivalents

	As at 31st March, 2014
Cash and Bank Balance - A Ltd.	5,50,000
B. Ltd.	1,30,000
Total	**6,80,000**

Working Notes:

1. Calculation of Capital Profits (Pre - acquisition)

	Amount (₹)	Amount (₹)
General reserve balance as on 01.04.2013		50,000
Profit & Loss A/c Balance	2,50,000	
Less: Dividend at 15% p.a. on Equity Capital of 8,00,000 for the year 2012 - 13	1,20,000	1,30,000
		1,80,000
Add: Profit on revaluation of Plant & Machinery (W.N.7)		2,00,000
		3,80,000
Less: Loss on revaluation of Furniture & Fixtures (W.N.8)		1,80,000
		2,00,000
Share of A Ltd. (80%)		1,60,000
Share of Minority Interest (20%)		40,000

2. Calculation of Revenue Profits (Post Acquisition)

	Amount (₹)	Amount (₹)
Profits during the year 2013- 14 (6,50,000- 1,30,000)		5,20,000
Less: Preference dividend in 2012-13 @14% on ₹ 5,00,000		70,000
		4,50,000
Less: Under charging of depreciation on plant & machinery due to upward revaluation (2,00,000 x 20%)		40,000
		4,10,000
Add: Overcharging of depreciation on furniture & fixtures due to downward revaluation (1,80,000 x 10%)		18,000
		4,28,000
Share of A Ltd. (80%)		3,42,400
Share of Minority Interest (20%)		85,600

3. Calculation of dividend on preference share of B Ltd.

	₹
Dividend on preference shares (5,00,000 x14%)	70,000
Share of A Ltd. (80%)	56,000
Share of Minority Interest (20%)	14,000

4. Calculation of Minority Interest

	₹
Equity Share Capital (20%)	1,60,000
Preference Share Capital (20%)	1,00,000
Share of Capital Profit (W.N. 1)	40,000
Share of Revenue Profit (W.N. 2)	85,600
Share of Preference Dividend (W.N. 3)	14,000
Add: Unrealised Loss	2,400
	4,02,000

5. Calculation of Cost of Control - Goodwill

	Amount (₹)	Amount (₹)
Investment by A Ltd. in Equity shares of B	19,80,000	
Less: Dividend received for 2012-13 15% (8,00,000 × 80%)	96,000	18,84,000
Preference Shares		4,00,000
		22,84,000
Less: Paid up Value of Equity Shares (80%)	6,40,000	
Preference Shares (80%)	4,00,000	
Share in Capital Profit (W.N.1)	1,60,000	12,00,000
Goodwill		10,84,000

6. Calculation of Consolidated Profit & Loss A/c

	₹
Balance in Profit & Loss A/c	17,00,000
Add: Revenue Profit from B Ltd. (W.N.2)	3,42,400
Preference dividend of B Ltd. (W.N.3)	56,000
Share of Unrealised loss on stock (20,000 x 60% x 80%)	9,600
	21,10,400
Less: Dividend wrongly credited	96,000
	20,12,000

7. Value of Plant & Machinery of B Ltd.

	Amount (₹)	Amount (₹)
Value as on 01.04.2013 (8,00,000 x 100/80)		10,00,000
Add: Appreciation on revaluation (20%)		2,00,000
Revalued figure		12,00,000
Less: Depreciation		
Already charged (1 2,00,000 - 10,00,000)	2,00,000	2,40,000
Due to upward revaluation (2,00,000 x 20%)	40,000	9,60,000

8. Value of Furniture & Fixture of B Ltd.

	Amount (₹)	Amount (₹)
Value as on 01.04.2013 (5,40,000 x 100/90)		6,00,000
Less: Diminution on revaluation (30%)		(1,80,000)
Revalued figure		4,20,000
Less: Depreciation already charged (6,00,000 - 5,40,000)	60,000	
Less: Depreciation written back due to down		
word revaluation (1,80,000 x 10%)	18,000	(42,000)
		3,78,000

Illustration 16: Bonus Issue, Pre-acquisition Dividend, Preference Dividend

The following are the Extract Balance Sheets of Sky Ltd. and Star Ltd. as on 31.03.2015 -

Liabilities		Sky (₹)	Star (₹)	Assets		Sky (₹)	Star (₹)
Share Capital:				**Fixed Assets:**	Goodwill	60,000	40,000
Equity Shares of ₹ 10 each		5,00,000	2,00,000		Machinery	1,00,000	60,000
12% Pref. Shares of ₹ 100 each		1,00,000	50,000		Vehicles	1,80,000	70,000
Reserves:	General Reserve	1,00,000	60,000		Furniture	50,000	30,000
	Profit & Loss A/c	1,50,000	90,000	**Investment:** Shares of Star (Cost)		4,80,000	–
Current Liabilities & Provisions:				**Current Assets:** Stock		70,000	1,40,000
Creditors		1,60,000	70,000		Debtors	1,00,000	1,65,000
Income Tax		70,000	60,000		Bank Balance	40,000	25,000
Total		**10,80,000**	**5,30,000**	**Total**		**10,80,000**	**5,30,000**

The following further information is furnished:

1. Sky Ltd. acquired 12,000 Equity Shares and 400 Preference Shares on 01.04.2014 at a cost of ₹2,80,000 and ₹1,00,000 respectively.
2. The Profit & Loss Account of Star Ltd. had a credit balance of ₹ 30,000 as on 01.04.2014 and that of General Reserve on that date was ₹ 50,000.
3. On 01.07.2014, Star Ltd. declared dividend out of its pre-acquisition profit, 12% on its Share Capital; Sky Ltd. credited the receipt of dividend to its Profit & Loss Account.
4. On 01.10.2014 Star Ltd. issued one Equity Share for every three shares held, as Bonus Shares, at a face value of ₹ 100 per share out of its General Reserve. No entry has been made on the books of Sky Ltd. for the receipt of these bonus shares.
5. Star Ltd. owed Sky Ltd. ₹ 20,000 for purchase of goods from Sky Ltd. The entire stock of goods is held by Sea Ltd. on 31.03.2015. Ocean Ltd. made a profit of 25% on cost.

Prepare a Consolidated Balance Sheet as at 31.03.2015.

Solution:

1. Basic Information

Company Status		Dates		Holding Status	
Holding Company	= Sky Ltd.	Acquisition:	01.04.2014	Holding Company	= 80%
Subsidiary	= Star Ltd	Consolidation:	31.03.2015	Minority Interest	= 20%

Shareholding Status: Shares held on 31.03.2015 = 12,000+ 1/3 x 12,000 (Bonus) = 16,000 out of 20,000 = 80%.

Note: Share distribution pattern can be determined as under –

Date	Particulars	Held by Sky Ltd.	% of Holding	Total Shares
01.04.2014	Opening Balance	12,000	NIL	15,000 $(12,000 \times \frac{100}{80})$
01.10.2014	Bonus Shares (1 /3 x 12,000)	4,000	80% ←	5,000 $(4,000 \times \frac{100}{80})$
31.03.2015	Closing Balance	16,000	80% (16,000/20,000)	20,000 (From Balance Sheet Given)

2. Analysis of Reserves & Surplus of Star Ltd.

(a) General Reserve

Balance on 31.03.2015 ₹ 60,000

	Balance on 01.04.2014 (acquisition)	50,000	Transfer during 2014-15	60,000
Less:	Bonus Issue (1/3 x 15,000 Shares x ₹ 10)	50,000	(bal. fig)	Revenue Reserve
	Capital Profit	**Nil**		

(b) Profit & Loss Account

Balance on 31.03.2015 ₹ 90,000

	Balance on 01.04.2014 (acquisition)	30,000		Profit for 2014-15	₹ 84,000
Less:	Dividend on pre-acquisition profit		**Less:**	Preference Dividend	₹ 6,000
	(12% x 15,000 shares x ₹ 10 each)	(18,000)			**₹ 78,000**
Less:	Preference dividend (50,000 x 12%)	(6,000)			**Revenue Profit**
	Balance **Capital Profits**	₹ 6,000			

3. Analysis of Net Worth of Star Ltd.

Particulars		Total	Sky Ltd	Minority
		100%	**80%**	**20%**
(a) Share Capital:	Equity	**2,00,000**	1,60,000	40,000
	Preference	**50,000**	40,000	10,000
(b) Capital Profits:	General Reserve	Nil		
	Profit & Loss Account	6,000		
		6,000	4,800	1,200
(c) Revenue Reserve:		**60,000**	48,000	12,000
(d) Revenue Profit:	Profit & Loss Account	**78,000**	62,400	15,600
(e) Pref. Dividend:	of Star Ltd. for the year	**6,000**	4,800	1,200
Minority Interest				**80,000**

4. Cost of Control

	Particulars			₹
	Cost of Investment:	Equity Shares of Sea Ltd.		1,00,000
		Preference Shares of Sea Ltd.		3,80,000
	Total Cost of Investment			**4,80,000**
Less:	Dividend out of Pre-acquisition profits			
	Preference Shares	(400 Shares x ₹ 100 each x 12%)	4,800	
	In Equity Shares	(12,000 Shares x ₹ 10 each x 12%)	14,400	(19,200)
	Corrected Cost of Investment			**4,60,800**
Less:	(1) Nominal Value of Equity Share Capital		1,60,000	
	(2) Nominal Value of Preference Share Capital		40,000	
	(3) Share in Capital Profit of Star Ltd.		4,800	(2,04,800)
	Goodwill on Consolidation			**2,56,000**

5. Consolidation of Reserves & Surplus

	Particulars	Gen. Res	P&L A/c
	Balance as per Balance Sheet of Sky Ltd.	1,00,000	1,50,000
Add:	Share of Revenue Profits/ Reserves of Star Ltd.	48,000	62,400
Add:	Share of Preference Dividend from Star Ltd.	–	4,800
Less:	Dividend out of Pre-acquisition Profits (₹ 4,800 + ₹ 14,400)	–	(19,200)
Less:	Preference Dividend payable for the current year by Sky Ltd.	–	(12,000)
Less:	Stock Reserve on Closing Stock (20,000 x 25 /125)	–	(4,000)
	Adjusted Consolidated Balance	**1,48,000**	**1,82,000**

Name of the Company: Sky Ltd. And its subsidiary Star Ltd.

Consolidated Balance Sheet as at 31st March 2015

Ref No.		Particulars	Note No.	As at 31st March, 2015	As at 31st March, 2014
				₹	₹
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital @ ₹ 10 each	1	600,000	-
		(b) Reserves and surplus	2	330,000	-
				930,000	-
	2	**Minority Interest**		80,000	-
	3	**Share application money pendint allotment**		Nil	
	4	**Non-current liabilities**		Nil	
				-	-
	5	**Current liabilities**			
		(a) Trade payables	3	110,000	-
		(b) Short-term provisions	4	142,000	-
				252,000	-
		TOTAL (1+2+3+4+5)		1,262,000	-
	B	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	5	490,000	-
		(ii) Intangible assets (goodwill)	6	256,000	-
				746,000	-
	2	**Current assets**			
		(a) Inventories	7	206,000	-
		(b) Trade receivables	8	245,000	-
		(c) Cash and cash equivalents	9	65,000	-
				516,000	-
		TOTAL (1+2)		1,262,000	-

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note 1. Share Capital

	Current Year	Previous Year
Authorised Capital	-	-
Issued and Paid Up	-	
Equity Share capital @ ₹ 10	5,00,000	-
12% Preference Share	1,00,000	-
	6,00,000	-

Note 2. Reserve and Surplus :-

	Current Year	Previous Year
General Reserve	1,48,000	-
Profit and loss	1,82,000	-
	-	-
	3,30,000	-

Note 3. Trade Payable

	Current Year	Previous Year
Sundry Debtors		
Sky	60,000	-
Star	70,000	-
	1,30,000	-
Less: set off	20,000	-
	1,10,000	-

Note 4. Short Term Provisions

	Current Year	Previous Year
Prov. For taxations (70000+60000)	1,30,000	-
Proposed Pref Dividend payable Sky Ltd.	12,000	-
	1,42,000	-

Note 5. Tangible Assets :-

	Current Year	Previous Year
Fixed Assets		
Machinery (100000+60000)	1,60,000	-
Vehicles (180000+70000)	2,50,000	-
Furniture (50000+30000)	80,000	-
	-	-
	4,90,000	-

Note 6. Intangible Assets:-

	Current Year	Previous Year
Goodwill		
Sky	60,000	-
Star	40,000	-
	1,00,000	-
Goodwill on consolidation	1,56,000	-
	2,56,000	-

Note 7. Inventories :-

	Current Year	Previous Year
Stock		
Sky	70,000	-
Star	1,40,000	-
	2,10,000	-
Less: Stock Reserve	4,000	-
	2,06,000	-

Note 8. Trade Receivable :-

	Current Year	Previous Year
Sky	1,00,000	-
Star	1,65,000	-
	2,65,000	-
Less: Set off	20,000	-
	2,45,000	-

Note 9. Cash and cash equivqlent :-

	Current Year	Previous Year
Sky	40,000	-
Star	25,000	-
	65,000	-

Notes:

- Stock Reserve i.e. unrealized profits on Closing Stock have been eliminated in full against Holding Company's Profits, as it arose from downstream transaction (i.e. Holding to Subsidiary).
- Inter Company Owings have been eliminated in full.

Illustration 17: Bonus Issue

The following are the Balance Sheets of H Ltd. and S Ltd. As at 31st March, 2014

Liabilities	H Ltd.	S. Ltd.	Assets	H Ltd.	S. Ltd.
	(₹)	(₹)		(₹)	(₹)
Equity Shares of 10 each	1000,000	7,00,000	Land and Building	6,00,000	2,70,000
12% Preference Shares of 10 each	1,00,000	50,000	Plant and Machinery	2,00,000	2,70,000
			Shares in S Ltd. 900,	7,10,000	—
General Reserve	2,00,000	4,48,000	12% Debentures in S Ltd.	80,000	—
Profit & Loss A/c	3.60,000	1,77,000	Stock	1,00,000	3,00,000
12% Debentures	2,00,000	2,00,000	Debtors	4,00,000	10,10,000
Sundry Creditors	3,00,000	5,35,000	Cash at Bank	60,000	2,75,000
Bills Payable	1,40,000	1,40,000	Bills Receivable	1,00,000	1,00,000
			Preliminary Expenses	50,000	25,000
	23,00,000	22,50,000		23,00,000	22,50,000

Note : Contingent liability in respect of Bills discounted by H Ltd. ₹50,000. Contingent liability in respect of Bills discounted by S Ltd. ₹25,000 of which Bills of ₹5,000 were accepted by H Ltd.

Additional Information:

(a) H Ltd. acquired 40,000 Equity Shares of S Ltd. and 2,000. 12% Pref. Shares in S Ltd. on 1.7.2013 at a cost of ₹6,80,000 and ₹30,000 respectively. The credit balance of Profit and Loss Account of S Ltd. as on 1.4.2013 was ₹2,25,000 and that of General Reserve on that date was ₹6,00,000.

(b) On 30.9.2013, S Ltd. declared dividend @ 20% on equity shares for the yare 2012-2013. H Ltd. credited the receipt of dividend to its Profit and Loss Account.

(c) On 1.1.2014, S Ltd. issued 2 shares for every 5 shares held, as bonus shares. No entry has been made in the books of H Ltd. for the receipt of these bonus shares.

(d) H Ltd. purchased goods for 3 lakhs from S Ltd. which made at a profit of 20% on cost. 80% of these goods were sold by H Ltd. at a profit of 20% on cost till 31.03.2014.

(e) On 1.1.2014, H Ltd. sold to S Ltd. a Machine costing ₹2,40,000 at-a profit on 25% on selling price. Depreciation at 10% p.a. was provided by S Ltd. on this Machine.

(f) H Ltd. owed S Ltd. ₹2,90,000 but S Ltd. is owed ₹3,00,000 by H Ltd.

(g) The Land and Building of S Ltd. which stood at 3,00,000 on 1.4.2013, was considered as worth of 6,92,500 on 1.7.2013, for which necessary adjustments are yet to be made.

(h) All the Bills Payables of S Ltd. were drawn upon by H Ltd.

(i) The management of H Ltd. and S Ltd. wish to recommend a dividend of 15% p.a. and 10% p.a. respectively on equity shares for the year 2013- 2014.

Required: Calculate Minority Interest, Cost of Control and the Balance of Consolidated Profit and Loss Account to be shown in the Consolidated Balance Sheet of H Ltd. and its subsidiary, as at 31st March, 2014.

Answer:

Minority Interest

Particulars	(₹)
Paid up Value of Equity Shares (including Bonus Shares)	1,40,000
Paid up Value of Preference Shares presently held by Minority	30,000
Share of Minority in Capital Profits of S Ltd.	1,84,700
Share of Minority of Revenue Profits of S Ltd.	900
Share of Minority in Revenue Reserve of S Ltd.	7,200
Share of Minority in Proposed Preference Dividend of S. Ltd.	3,600
Total	3,66,400

Goodwill/ Capital Reserve of Consolidation

	Particulars	(₹)
A.	Corrected Net cost of Investment	
	(a) Net Cost of Equity Investment	6,80,000
	(b) Less: equity Dividend out of Pre- acquisition Profits	(80,000)
	(c) Cost of Investments in preference Shares	30,000
	(d) Less: Pref. Dividend receivable by Holding Co, out of Pre- acquisition. Profit [1,500 x 2,000/5,000]	(600)
		6,29,400
B.	Holding Co's share in Net Assets of Subsidiary Co.	
	(a) Paid .up Value of Equity Shares (including Bonus Shares)	6,89,400
	(b) Paid up Value of Preference Shares presently held by Holding Co.	5,60,000
	(c) Share of Holding Co. in Capital Profits of subsidiary Co.	20,000
		7,38,800
C.	Capital Reserve (B-A)	13,18,800

Consolidated Profit and Loss Account

	Particulars	(₹)
A.	Balance as given in the Balance Sheet of H Ltd.	3,60,000
B.	Add: (a) Holding Co's Share in Revenue Profit of S Ltd.	3600
	(b) Holding Co.'s Share in Proposed Pref. Dividend of S Ltd. [4,500 x 2,000/ 5,000]	1,800
	(c) Profit on Debentures held in S Ltd. [90,000 (face Value) — 80,000 (cost)]	10,000
C.	Less: (a) Dividend out of pre-acquisition profits wrongly credited to this account instead on Investment Account	(80,000)
	(b) Unrealized profit on Stock [(20% of 3,00,000) x 20/120]	(10,000)
	(c) Unrealized Profit on Machine [(2,40,000 x 1/3) — (80,000 x 10% x 3/12)]	(78,000)
	(d) Proposed Equity Dividend [10,00,000 x 15%]	(1,50,000)
	(e) Proposed pref. Dividend [1,00,000 x 12%]	(12,000)
D	Closing Balance to be taken to the Consolidate Balance Sheet (A+B-C)	45,400

Working Notes:

(i) General Reserve Account of S Ltd.

Dr. ***Cr.***

Particulars	(₹)	Particulars	(₹)
To Equity Shares Capital (Bonus)	2,00,000	By Balance b/d	6,00,000
To Balance c/d	4,48,000	By Profit and Loss A/c (b/f)	48,000
	6,48,000		6,48,000

(ii) Profit and Loss Account of S Ltd.

Dr. ***Cr.***

Particulars	(₹)	Particulars	(₹)
To Final Dividend for Previous year	1,00,000	By Balance c/d	2,25,000
To General Reserve	48,000	By Profit earned (b/f)	1,00,000
To Proposed Preference Dividend	6,000		
To Balance c/d [1,77,000- 6,000]	1,71,000		
	3,25,000		3,25,000

(iii) Calculation of Change in the Value of Fixed Assets and Provision of Depreciation

Particulars	₹
A. Book value as on operating date	3,00,000
B. Depreciation upto date of revaluation [₹3,00,000 x 10/100 x 3/12]	-7,500
C. Book value as on the date of revaluation (A - B)	2,92,500
D. Revalued figure as on the date of revaluation	6,92,500
E. Increase in Value (D - C)	4,00,000
F. Short Depreciation since the date of revaluation [4,00,000 x 10/100 x 9/12]	30,000

(iv) Analysis of Profits and Reserves of S Ltd.

Particulars	Capital Profits	Revenue Profits	Revenue Reserves
	(₹)	(₹)	(₹)
Opening Balance of General Reserve	6,00,000		
Less: Utilized for issue of Bonus Shares	(2,00,000)		
Reserve created	12,000		36,000
Opening Balance of Profits and Loss A/c	2,25,000		
Less: Final Dividend for the previous year.	(1,00,000)		
Less: Miscellaneous Expenditure	(25,000)	75,000	
Profits earned	25,000	(36,000)	
Less: Transfer to General Reserve	(12,000)	(4,500)	
Less: Proposed Preference Dividend	(1,500)		
Add: Increase in value of Fixed Assets	4,00,000		
Less: Short Provision of Depreciation		(30,000)	
Total	9,23,500	4,500	36,000
Share of Minority @ 20%	1,84,700	900	7,200
Share of Holding Company @ 80%	7,38,800	3,600	28,800

Illustration 18: Purchase in Lots - Before Controlling Acqn. - Loss of Stock post-acquisition

The following are the Extract Balance Sheets of L Ltd. and M Ltd. as at 31.03.2015 -

Liabilities	L Ltd. (₹)	M Ltd. (₹)	Assets	L Ltd. (₹)	M Ltd. (₹)
Equity Share Capital (₹10)	80,000	1,00,000	Shares in M Ltd	98,000	–
Profit & Loss Account Sundry	22,000	30,000	Cash	7,000	4,000
Creditors	3,000	8,000	Other Assets (Tangible)	–	1,34,000
Total	**1,05,000**	**1,38,000**	**Total**	**1,05,000**	**1,38,000**

1. Net Profit during 2014-15 included above were: L Ltd. ₹ 18,000; M Ltd. ₹ 12,000.
2. During 2014-15, M Ltd. credited ₹ 3,000 to its P & L Account in settlement of a claim of loss of stock (costing ₹ 5,400 - included in opening stock) by fire on 30.06.2014.
3. ₹ 300 p.m. expenses incurred by L Ltd. on behalf of M Ltd. has been debited to the Profit & Loss Account of L Ltd. and left unrecorded for in the books of M Ltd.
4. Both the Companies have proposed a dividend of 10% which is yet to be recorded.
5. On 01.04.2014, L Ltd., was formed and on the same day it acquired 4,000 Shares of M Ltd. at ₹ 55,000.
6. On 31.07.2014, 10% dividend was received from M Ltd. and also Bonus Share at 1:4 was received. The dividend was credited to Profit & Loss Account.
7. On 31.8.2014, L Ltd. purchased another 3,000 Shares of M Ltd. at ₹ 43,000.

   Draft a Consolidated Balance Sheet for the above Group.

Solution:

1. Basic Information

Company Status	Date of Acquisition	Holding Status
Holding Company = L Ltd. Subsidiary = M Ltd.	First Lot = 4,000 Shares = 01.04.2014 Bonus 1,000 Shares = 31.07.2014 Second Lot = 3,000 Shares = 31.08.2014	Holding Company = 80% Minority Interest = 20%

Date of Consolidation = 31.03.2015

Notes:

- As per M's B/Sheet, number of Shares = 10,000, which is after Bonus Issue of 1:4. Hence, Number of Shares prior to Bonus Issue = 10,000 Less 1/5th = 8,000 Shares.
- First Lot of 4,000 Shares do not constitute controlling acquisition. Hence, Date of Control = 31.08.2014. Shares held by L Ltd. = 8,000 Shares out of 10,000 = 80% Holding.

2. Analysis of Profit & Loss Account of M Ltd.

Note:

1. Normal Operating Profit of M for 2014-15 = 12,000 (given) + 2,400 (abnormal loss item) = ₹ **14,400.**
2. Presuming this to be earned uniformly, the Revenue Profits after date of controlling acquisition i.e. the period from 31.08.2014 to 31.03.2015 (i.e. 7 months) = ₹ 14,400 x 7/12 = ₹ **8,400.** Hence, amount relatable to pre-acquisition period = ₹ 14,400 - ₹ 8,400 = ₹ 6,000.

P & L balance on 31.03.2015 ₹ 30,000

Bal.in P&L last year	₹ **46,000**		Profit from 31.08.2014 to 31.03.2015	8,400
Less: Bonus Issue	20,000	(₹ 80,000 x 1 /4)	(See **Note 2** above)	
Less: Dividend	8,000	(₹ 80,000 x 10%)	**Less:** Expenses by L Ltd. (₹ 300 x 7)	(2,100)
Less: Stock Loss	2,400		**Less:** 2014-15 Dividend (1,00,000x10%)	(10,000)
	15,600	(30,000- 14,400)		**(₹ 3,700)**
2014-15 Pft **(Note 2)**	6,000	(₹ 14,400 x 5/12)	**Revenue Profit**	
Less: Exp. by L Ltd.	(1,500)	(₹ 300 x 5)		
	20,100	**Capital Profit**		

Note:

- The Opening Balance in P&L A/c ₹ 46,000 is derived by reverse working. From this balance, M Ltd. should have declared bonus shares, paid dividend and written off the stock losses.
- The net balance of Capital and Revenue Profits = ₹ 20,350 - ₹ 3,350 = ₹ **17,000.** This is confirmed with the corrected balance of M's P&L Account i.e. Balance as given = ₹ 30,000 **Less** Expenses incurred by L Ltd., now recorded = ₹ 3,000 **Less** Dividend for 2008-09 = ₹ 10,000; Net Balance = ₹ 17,000.

3. Analysis of Net Worth of M Ltd.

Particulars	Total 100%	L Ltd. (80%)	Minority 20%
(a) **Equity Share Capital**	1,00,000	80,000	20,000
(b) **Capital Profits:**	20,100	16,080	4,020
(c) **Revenue Profits:**	(3,700)	(2,960)	(740)
(d) **Proposed Dividend**	10,000	8,000	2,000
Minority Interest			**25,280**

4. Computation of Pre-acquisition Dividend of L Ltd.

Particulars	Total	1st Lot	2nd Lot
% of Holding on 31.03.2015	80%	50%	30%
Share of dividend	₹ 8,000	₹ 5,000	₹ 3,000
Period of holding during 2014-15	–	12 Months	7 Months
To be Credited to P&L A/c	₹ 6,750	₹ 5,000	₹ 1,750 (3,000x7/12)
To be Credited to Investment A/c (Pre-acquisition Dividend)	₹ 1,250	NIL	₹ 1,250 (3,000x5/12)

5. Cost of Control

	Particulars		₹
	Cost of Investment in M Ltd.		98,000
Less:	Dividend out of Pre-acquisition Profits (2013-14) of M Ltd. (₹ 8,000 x 50%)		(4,000)
Less:	Dividend out of Pre-acquisition Profits (2014-15) Working Note - 4 above		(1,250)
	Adjusted Cost of Investment		**92,750**
Less:	Nominal Value of Equity Capital	80,000	
	Share in Capital Profit of M Ltd.	16,080	96,080
	Capital Reserve on Consolidation		**(3,330)**

6. Consolidation of Profit and Loss Account

	Particulars		₹
	Balance as per Balance Sheet		22,000
Less:	Proposed Dividend	(₹ 80,000 x 10%)	(8,000)
Add:	Expenses incurred on behalf of M Ltd. by L Ltd.	(₹ 300 x 12 months)	3,600
Less:	Dividend out of Pre-acquisition Profits (2014-15)	(₹ 8,000 x 50%)	(4,000)
Add:	Share of Proposed Dividend for FY 2015-16	(WN4)	6,750
	Adjusted Balance		**20,350**
Less:	Share of Revenue Loss of M Ltd.		(2,960)
	Consolidated Balance		**17,390**

Name of the Company: L Ltd. And its subsidiary M Ltd.

Consolidated Balance Sheet as at 31st March 2015

Ref No.	Particulars		Note No.	As at 31st March, 2015	As at 31st March, 2014
				₹	₹
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital @ ₹ 10 each	1	80,000	-
		(b) Reserves and surplus	2	20,720	-
				1,00,720	-
	2	**Minority Interest**		25,280	-
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**		Nil	
				-	-
	5	**Current liabilities**			
		(a) Trade payables	3	11,000	-
		(b) Short-term provisions	4	8,000	-
				19,000	-
		TOTAL (1+2+3+4+5)		145,000	-
	B	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	5	134,000	-
				134,000	-
	2	**Current assets**			
		(a) Cash and cash equivalents	6	11,000	-
				11,000	-
		TOTAL (1+2)		145,000	-

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note 1. Share Capital

	Current Year	Previous Year
Authorised Capital	-	-
Issued and Paid Up	-	-
Equity Share capital @ ₹ 10	80,000	-
	-	-
	80,000	-

Note 2. Reserve and Surplus :-

	Current Year	Previous Year
General Reserve	17,390	-
Capital Reserve	3,330	-
	-	-
	20,720	-

Note 3. Trade Payable

	Current Year	Previous Year

Note 4. Short Term Provisions

	Current Year	Previous Year

Particulars	Amount (₹)	Amount (₹)
L	3,000	-
M	8,000	-
	11,000	-

Proposed Dividend -Shareholders of L. ltd.	8,000	-
	8,000	-

Note 5. Tangible Assets

	Current Year	Previous Year
Other Assets	1,34,000	-
	1,34,000	-

Note 6. Cash and cash equivqlent :-

	Current Year	Previous Year
Particulars	**Amount (₹)**	**Amount (₹)**
L	7,000	-
M	4,000	-
	11,000	-

Illustration 19:

A Ltd. acquired 80,000 shares of 100 each in B Ltd. on 30.09.2013. The summarized Balance Sheet of the 2 companies as on 31.03.2014 were as follows:

Liabilities	A. Ltd (₹)	B Ltd. (₹)	Assets	A. Ltd (₹)	B Ltd. (₹)
Share Capital: Shares of ₹ 100 each	3,00,00,000	1,00,00,000	Fixed Assets: Tangible	150,00,000	1,44,70,000
			Investment in B Ltd.	1,70,00,000	NIL
Capital reserve	NIL	55,00,000	Stock in hand	40,00,000	20,00,000
General Reserve	30,00,000	5,00,000	Loan to A Ltd.	NIL	2,00,000
Profit and Loss A/c	38,20,000	18,00,000	Debtors	25,00,000	18,00,000
Loan from B Ltd.	2,10,000	NIL	Bank	2,00,000	2,00,000
Creditors	17,90,000	7,00,000	Bills Receivable (including 50,000 from B. Ltd.)	1,20,000	NIL
Bills Payable (including 50,000 to A. Ltd.)	NIL	1,70,000			
Total	**3, 88.20,000**	**1,86.70,000**		**3, 88.20,000**	**1,86.70,000**

Contingent Liability (A Ltd.): Bills Discounted = 60,000

Additional Information:

(i) B Ltd. made a bonus issue on 31.03.2014 of one share for every two shares held, thereby reducing the Capital Reserve accordingly. The accounting effect has not been given in the above Balance Sheet.

(ii) Interest Receivable for the year (₹10,000) in respect of the loan due by A Ltd. to B Ltd. has not been credited in the accounts of B Ltd.

(iii) The credit balance in Profit and Loss A/c of B Ltd. on 01.04.2013 was ₹ 2,10,000.

(iv) The Directors decided on the date of the acquisition that the Fixed Assets of B Ltd. were over-valued and should be written down by ₹ 5,00,000. Consequential adjustments on depreciation are to be ignored.

(v) The balance in General Reserve of B Ltd. as on 01.04.2013 was ₹ 5,00,000.

Prepare the Consolidated Balance Sheet as at 31.03.2014 showing relevant workings.

Solution:

1. Analysis of Reserve & Surplus of B Ltd.

[a]	Capital reserve Balance as on date of consolidation Less: Bonus issue Corrected balance	 55,00,000 50,00,000 5,00,000	 (whole amount is Capital Profit)
[b]	Revaluation of Assets: Loss (5,00,000) = Capital Profit		
[c]	General Reserve	5,00,000	(whole amount is Capital Profit)
[d]	Profit & loss A/c Balance as on date of consolidation Add: Interest on loan Corrected balance	 18,00,000 10,000 18,10,000	
	Balance as on 01 .04.2013	2,10,000	(Capital Profit)
	Up to date of acquisition	16,00,000*6/ 12 = 8,00,000	(Capital Profit)
	Acquisition to Consolidation	16,00,000*6/ 12 = 8,00,000	(Revenue Profit)

Total Capital profit 2,10,000 + 8,00,000 = 10,10,000

2. Consolidation of Balances

Particulars	Total	Minority Interest	Pre-Acquisition	Post-Acquisition	
				Gen. Res.	P & L. A/c
Equity capital (1,00,00,000 + bonus 50,00,000)	 1,50,00,000	 30,00,000	 1,20,00,000		
General reserves	5,00,000	1,00,000	4,00,000		
Profit & loss A/c	18,10,000	3,62,000	8,08000		6,40,000
Capital reserve	5,00,000	1,00,000	4,00,000		
Loss on revaluation of assets	(5,00,000)	(1,00,000)	(4,00,000)		
Minority interest		34,62,000			
Total (Cr.)			1,32,08,000		
Cost of investment (Dr.)			(1,70,00,000)		
Parent's Balances				30,00,000	38,20,000
For consolidated balance sheet		34,62,000	(37,92,000)	30,00,000	44,60,000
			Good Will		

3. Consolidated Balance sheet balance sheet of A Ltd. and its subsidiary B Ltd. as 31.03.2014

	Particulars	Note	This Yr.	Prev. Yr.
I.	Equity And Liabilities			
	1. Shareholders Funds:			
	(a) Share Capital	1	3,00,00,000	
	(b) Reserves & Surplus	2	74,60,000	
	2. Minority Interest		34,62,000	
	3. Current Liabilities:			
	Trade payable	3	26,10,000	
	Total		4,35,32,000	
II.	Assets			
	1. Non-Current Assets			
	Fixed Assets			
	(i) Tangible Assets		2,89,70,000	
	(1,50,00,000+1,44,70,000- 5,00,000)			
	(ii) Intangible Assets — Goodwill		37,92,000	
	2. Current Assets			
	(i) Inventories		60,00,000	
	(ii) Trade Receivables	4	43,70,000	
	(iii) Cash,& Cash Equivalents		4,00,000	
	Total		4,35,32,000	

Contingent liability for bills discounted 60,000

Notes to the Balance Sheet

1.	Share capital Authorised		3,00,00,000
	Issued, Subscribed & paid up 3,00,000 Equity shares of 100 each		
2.	Reserves & Surplus Other Reserves		30,00,000
	Surplus		44,60,000
	Total		74,60,000
3.	Trade Payables		24,90,000
	Sundry Creditors		1.20,000
	Bills payables		
	Total		26,10,000
4.	Trade Receivables		43,00,000
	Sundry debtors		70,000
	Bills Receivables		
	Total		43,70,00

Note: fixed assets have been revalued for the purpose of consolidation and the depreciation on the revaluation loss has been ignored as it specially stated in the question.

Illustration 20:

The summarized Balance Sheets of Summer Ltd. and its Subsidiary Winter Ltd. is on 31st March, 2014 are as follows:

Liabilities	Summer Ltd.	Winter Ltd.	Assets	Summer Ltd.	Winter Ltd.
Equity shares of ₹10 each	9,600	4,000	Goodwill	900	600
10% Preference	1,400	760	Plant & Machinery	2,400	1,200
shares of ₹10 each			Motor Vehicles	1,900	1,500
General Reserve	1,100	840	Furniture & Fittings	1,300	600
Profit & Loss Account	2,000	1,200	Investments	5,200	900
Bank Overdraft	300	200	Stock	900	1,440
Sundry Creditors	800	900	Cash at Bank	400	420
Bills Payables	-	320	Debtors	1,910	1,560
			Bills receivables	290	-
Total	**15200**	**8220**	**Total**	**15200**	**8220**

Details of acquisition of shares by Summer Ltd. are as under:

Nature of shares	No. of shares acquisition	Date of acquisition	Cost of acquisition (₹)
Preference shares	28,500	01.04.2011	6,20,000
Equity shares	1,60,000	01.04.2012	19,00,000
Equity shares	1,40,000	01.04.2013	16,00,000

Other information:

(i) On 01.04.2013, profit and loss account and general reserve of Winter Ltd. has credit balances of ₹ 6,00,000 and ₹ 4,00,000 respectively.

(ii) Dividend @ 10% was paid by Winter Ltd. for the year 2012-13 out of its profit and loss account balance as on 01.04.2013. Summer Ltd. credited its share of dividend to its profit and loss account.

(iii) Winter Ltd. allotted bonus shares out of pre-acquisition general reserve at the rate of 1 share for every 10 shares held. Accounting thereof has not yet been done.

(iv) Bills receivables of Summer Ltd. were drawn upon Winter Ltd.

(v) During the year 2013-14, Summer Ltd. purchased goods from Winter Ltd. worth ₹ 2,00,000 at a sale pride of ₹2,40,000.40% of these goods remained unsold at close of the year.

(vi) On 01.04.2013, motor vehicles of Winter Ltd. were overvalued by 2,00,000, applicable depreciation rate is 20%.

(vii) Dividends recommended for the year 2013-14 by the holding and the subsidiary companies are 15% and 10% respectively.

Prepare Consolidated Balance Sheet as on 31st March, 2014.

Solution:

Basic Information at the beginning:

Company Details		
Holding Company	Summer Ltd.	3/4
Subsidiary Company	Winter Ltd.	1/4
Cost of control can be shown as follows:		

Cost of control can be shown as follows:

	₹	₹
Cost of investment in Winter Ltd.		41,20,000
[6,20,000 + 19,00,000 + 16,00,000]		
Less:		
Paid up value of equity shares including bonus		
shares = [1,60,000 + 1,40,000 + (10% of 3,00,000) × 10]	33,00,000	
Paid up value of preference share	2,85,000	
Pre-acquisition dividend	1,40,000	37,25,000
Control/Goodwill		3,95,000

Minority Interest

	₹
Equity share capital (10,00,000 + 1,00,000)	11,00,000
Preference Share Capital (7,60,000 - 2,85,000)	4,75,000
Share of revenue reserve (w.n.)	1,10,000
Share of revenue profit (w.n.)	2,41,000
	19,26,000

Proposed Preference Dividend to Minority = 47,500

Consolidated Balance Sheets (extracts) of Summer Ltd. and its subsidiary

Winter Ltd. As on 31st March 2014

	Particulars	Note No.	Amount (₹)
I.	**EQUITY AND LIABILITIES**		
	(1) Shareholders' Funds		
	(a) Share Capital	1	1,10,00,000
	(b) Reserves and Surplus	2	24,45,500
	(C) Minority Interest		19,26,000
	(2) Minority Interest (w.n.)		
	(3)Current Liabilities		
	(a) Short Term Borrowings	3	5,00,000
	(b) Trade Payables	4	17,30,000
	(c) Other current liabilities	5	15,80,000
	(d) Short term provision (w.n.)		47,500
	Total		**1,92,29,000**

II.	**ASSETS**		
	(1) Non Current Assets		
	(a) Fixed Assets	6	87,40,000
	(i) Tangible assets	7	18,95,000
	(ii) Intangible assets	8	19,80,000
	(b) Non-current investments		
	(c) Goodwill		
	(2) Current Assets		
	(a) Inventories	9	23,24,000
	(b) Trade Receivables	10	34,70,000
	(c) Cash and Cash equivalent	11	8,20,000
	Total		**1,92,29,000**

Notes to Accounts

(Amount In ₹)

1.	Share Capital			
	Authorised, Issued and paid up capital			
	9,60,000, equity shares of ₹ 10 each		96,00,000	
	1,40,000, 10% preference shares of ₹ 10 each		14,00,000	1,10,00,000
2.	Reserves and Surplus			
	General Reserve (W.N.)		14,30,000	
	Profit and Loss account (W.N.)		10,15,500	24,45,500
3.	Short term borrowings			
	Bank overdraft			
	Summer Ltd.		3,00,000	
	Winter Ltd.		2,00,000	5,00,000
4.	Trade payables		17,00,000	
	Sundry creditors			
	Summer Ltd.	8,00,000		
	Winter Ltd.	9,00,000		
	Bills payables			
	Winter Ltd.	3,20,000	.	
	Less: Mutual debt	2, 90,000	30,000	17,30,000
5.	Other current liabilities			
	Proposed Dividend			
	Equity Shares		14,40,000	
	Preference Shares		1,40,000	15,80,000

6.	Tangible assets			
	Plant and Machinery			
	Summer Ltd.	24,00,000		
	Winter Ltd.	12,00,000	36,00,000	
	Motor Vehicles			
	Summer Ltd.	19,00,000		
	Winter Ltd. (₹ 15,00,000 - 2,00,000 + 40,000)	13,40,000	32,40,000	
	Furniture & Fittings			
	Summer Ltd.	13,00,000		
	Winter Ltd.	6,00,000	19,00.000	87,40,000
7.	Intangible assets Goodwill		9,00,000	
	Summer Ltd.		6,00,000	
	Winter Ltd.		15,00,000	
	Add: Goodwill on consolidation (W.N.2)		3,95000	18,95,000
8.	Non-current investments			
	Investments		10,80,000	
	Summer Ltd. (52,00,000-41 .20,000) Winter Ltd.		9,00,000	19,80,000
9.	Inventories			
	Stock		9,00,000	
	Summer Ltd.		14,40,000	
	Winter Ltd.		23,40,000	
	Less: Unrealized profit		16,000	23,24,000
10.	Trade receivables			
	Debtors			
	Summer Ltd.	19,10,000		
	Winter Ltd.	15.60.000	34,70,000	
	Bills receivables	2,90,000	.	
	Summer Ltd. Less: Mutual Debt	2,90,000	Nil	34,70,000
11.	Cash and cash equivalents			
	Cash at hand			
	Summer Ltd.		4, 00,000	
	Winter Ltd.		4,20,000	8,20,000

Working notes:

	Particulars	₹	Capital profit (₹)	Revenue Reserve (₹)	Revenue Prof it (₹)
(a)	General Reserve as on 1.4.2013 Less: Bonus issue (1/10th of ₹ 40,00,000)	4,00,000 (4,00,000)			
(b)	Addition to general reserve during 201 3-14 (8,40,000-4,00,000)			4,40,000	
(c)	Profit and Loss Account balance as on 1.4.2013 Less: Dividend paid for the year 2012-13	6,00,000 4,00,000	2,00,000		
(d)	Profit for the year 2013-14 (12,00,000 2,00,000)				10,00,000
(e)	Adjustment for overvaluation of motor vehicles		(2,00,000)		
(f)	Adjustment of revenue profit due to overcharged depreciation (20% on 2,00,000)				40,000
(g)	Preference dividend for the year 2013-14 @10%				(76,000)
				4,40,000	9,64,000
	Summer Ltd.'s Share (3/4) Minority Interest (1/4)			3,30,000 1,10,000	7,23,000 2,41,000
				4,40,000	9,64,000

Profit and Loss Account - Summer Ltd.		19,73,500
Balance Share in profit of Winter Ltd. (W.N.1) Share in proposed preference dividend of Winter Ltd.		20,00,000 7,23,000 28,500
		27,51,500
Less: Pre-acquisition dividend credited to profit and loss a/c Unrealised profit on stock (40% of Z 40,000) Proposed equity dividend (96,00,000 * 15%) Proposed preference dividend (14,00,000 * 10%)	1 40,000 16,000 14,40,000 1,40,000	(17,36,000)
		10,15,500
General Reserve - Summer Ltd.		
Balance Add: Share in Winter Ltd. (W.N.1)		11,00,000 3,30,000
		14,30,000

A. CHAIN HOLDINIG

Illustration 21: ChainHolding

ANTEK Ltd., SINTEX Ltd. and ROLX Ltd. Are members of a group. ANTEK Ltd. bought 70% of the shares of SINTEX Ltd. on October 1, 2012 and 30% of the shares' of ROLEX Ltd. on January 1, 2014. SINTEX Ltd. bought 60% of the shares of ROLEX Ltd. on October 1, 2013.

The following information is available:

Extracts of Profit and Loss Account

Company Name	Balance April 1,2013	Profit / (Loss) for 2013-14	Balance March 31, 2014	Company formed on
	₹	₹	₹	
ANTEK Ltd.	2,75,000	1,25,000	4,00,000	April 1, 2011
S1NTEX Ltd.	1,00,000 (Dr.)	2,37,500	1,37,500	April 1, 2012
ROLEX Ltd.	-	1,20,000 (Loss)	1,20,000 (Dr.)	April 1, 2013

Assume, Profit/Loss for the year accrues evenly throughout the year.

Required:

State how the Profits/ (Losses) will be reflected in the Consolidated Balance Sheet of the group as on 31st March, 2014.

Solution:

(1) Basic Information

Company Details	
Holding Company	ANTEX Ltd.
Subsidiary Company	JSINTEX Ltd.
Sub-Subsidiary Company	ROLEX Ltd.

Acquisition Dates	
ANTEX Ltd. in SINTEX Ltd.	01.10.2012
ANTEX Ltd. in ROLEX Ltd.	01 .01.2014
SINTEX Ltd. in ROLEX Ltd.	01.10.2013

Holding Details		
Holding Company	SINTEX Ltd.	ROLEX Ltd.
ANTEX Ltd. in ROLEX Ltd.	70% (ANTEX Ltd.)	30% (ANTEX Ltd.)
SNTEX Ltd. in ROLEX Ltd.		60% (SINTEX Ltd.)
Minority Interest	30%	10%

(2) Analysis of Profit /(Loss) for Consolidation:

Particulars	Capital Profit (₹)	Revenue Profit (₹)
ROLEX LTD.		
Loss for the year(assumed accruing evenly)	60,000	60,000
Less: Due to Minority Interest	6,000	6,000
	54,000	54,000
Due to Sintex Ltd.(60%)	36,000	36,000
Share of Antex Ltd.(30%)	18,000	18,000
Revenue loss pertaining to further 3 months to be treated as Capital since share' are acquired on Jan 1, 2014	9,000	(9,000)
(Loss) / Profit	(27,000)	9,000
SINTEX LTD.		
Loss from Rolex Ltd.	(36,000)	(36,000)
Loss as on 1st April,2013	(50,000)	(50,000)
Profit during 201 3-14		2,37,500
	(86,000)	1,51,500
Due to outsiders(30%)	25,800	45,450
Due to Antex Ltd	(60,200)	1,06,050
ANTEX LTD.		
Loss from Rolex Ltd.	(27,000)	
Prof it/(Loss) from Sintex Ltd.	(60,200)	(9,000)
Own Profit		1,06,050
		4,00,000
	(87,200)	4,97,050

(3) Share of Minority Shareholders

(Amount in ₹)

Capital Loss in Rolex Ltd:	(6,000)
Revenue Loss in Rolex Ltd.	(6,000)
Capital Loss in Sintex Ltd.	(25,800)
Total Profit	(37,800)
Revenue Profit in Sintex Ltd.	45,450
Total share of Profits	7,650

Illustration 22: Chain Holding

M Ltd. is a holding company and N Ltd. and O Ltd. are subsidiaries of M Ltd. Their Balance Sheet as on 31.12.2013 are give below:

Amount in ₹)

Liabilities	M Ltd.	N Ltd.	O Ltd.	Assets	M Ltd.	N Ltd.	O Ltd.
Share Capital	6,00,000	6,00,000	3,60,000	Fixed Assets	1,20,000	3,60,000	2,58,000
Reserves	2,88,000	60,000	54,000	Investments:			
Profit and Loss	96,000	72,000	54,000	Shares in N Ltd	5,70,000		
Account				Shares in O Ltd.	78,000	3,18,000	
Sundry				Stock in Trade	72,000		
Creditors	42,000	30,000		Sundry Debtors	1,56,000	1,26,000	1,92,000
O Ltd. Balance	18,000			N Ltd. Balance	48,000		
M Ltd. Balance		42,000		M Ltd. Balance			18,000
Total	10,44,000	8,04,000	4,68,000	Total	10,44,000	8,04,000	4,68,000

The following particulars are given:

(i) The share capital of all companies is divided into shares of ₹ 10 each.

(ii) M Ltd. held 48,000 shares of N Ltd. and 6,000 shares of O Ltd.

(iii) N Ltd. held 24,000 shares of O Ltd.

(iv) All these investments were made on 30.06.2013.

(v) On 31.12.2012, the position was as shown below:

(Amount in ₹)

	N Ltd.	O Ltd.
Reserve	48,000	45,000
Profit & Loss Account	24,000	18,000
Sundry Creditors	30,000	6,000
Fixed Assets	3,60,000	2,58,000
Stock in trade	24,000	2,13,000
Sundry Debtors	2,88,000	1,98,000

(vi)	The whole of stock in trade of N Ltd. as on 30.06.2013 ₹ 24,000 was later sold to M Ltd. for ₹26,400 and remained unsold by M Ltd. as on 31.12.2013.
(vii)	Cash in transit from N Ltd. to M Ltd. was ₹ 6,000 as at the close of the year. You are required to prepare a Consolidated Balance Sheet of M Ltd. and its subsidiaries N Ltd. and 0 Ltd. as at 31.12.2013.

Solution:

Consolidated Balance Sheet of M Ltd. with subsidiaries N Ltd. And O Ltd. (As an 31st March, 2014)

	Particulars	Note No.	Amount (₹)
I.	**EQUITY AND LIABILITIES**		
	(1) Shareholders' Funds		
	(a) Share Capital	1	6,00,000
	(b) Reserves and Surplus	2	4,21,830
	(C) Minority Interest		2,26,920
	(2) Current Liabilities		
	(a) Sundry Creditor (42,000 + 30,000)		72,000
	(b) Inter Co. Debt 60,000		
	Contra (60,000)		
	Total		**13,20,750**
II.	**ASSETS**		
	(1) Non Current Assets		
	(a) Fixed Assets	3	7,38,000
	(b) Goodwill	4	33,150
	(2) Current Assets		
	(a) Stock (72,000-Unrealised Profit i.e. 2,400)		69,600
	(b) Sundry debtor		4,74,000
	(c) Cash in Transit		6,000
	Total		**13,20,750**

[Relevant Notes]

Note No: 1. Share Capital (₹)

Authorized, Issued, Subscribed and Paid-up Share Capital:-	
60,000 Equity Shares of ₹10 Each	6,00,000
Total	**6,00,000**

Note No: 2. Reserves and Surplus

Reserves	2,95,950
Profit & Loss A/c	1,25,880
Total	**4,21,830**

Note No: 3. Tangible Assets

Fixed Assets	7,38,000
Total	**7,38,000**

Note No: 4. Intangible Assets

Goodwill	33,150
Total	**33,150**

Working Notes:

(i) Position on 30.06.2013 (Amount in ₹)

	N Ltd.		**O Ltd.**	
	Reserves	P & L A/c	Reserves	P & L A/c
Balance as on 31.12.2013	60,000	72,000	54,000	54,000
Less: Balance as on 31.12. 2012	48,000	24,000	45,000	18,000
Increase during the year	12,000	48,000	9,000	36,000
Estimated increase for half year	6,000	24,000	4,500	18,000
Balance as on 30.06.2013	54,000	48,000	49,500	36,000

(ii) Analysis of Profit of O Ltd. (Amount in ₹)

	Capital Profit	Revenue Reserve	Revenue Profit
Reserve on 30.06.2013	49,500		
Profit and Loss A/c on 30.06.2013	36,000		
Increase in reserves		4,500	
Increase in profit			18,000
Total	85,500	4,500	18,000
Less: Minority Interest (1/6)	14,250	750	3,000
Balance	71,250	3,750	15,000
Shares of M Ltd. (1/6)	14,250	750	3,000
Shares of N Ltd. (4/6)	57,000	3,000	12,000

(iii) Analysis of Profit of N Ltd. (Amount in ₹)

	Capital Profit	Revenue Reserve	Revenue Profit
Reserve on 30.06.2013	54,000		
Profit and Loss A/c on 30.06.2013	48,000		
Increase in reserves		6,000	
Increase in profit			24,000
Share in O Ltd.		3,000	12,000
Total	1,02,000	9,000	36,000
Less: Minority Interest (1/5)	20,400	1,800	7,200
Shares of M Ltd. (4/5)	81,600	7,200	28,800

(iv) Cost of Control (Amount in ₹)

		₹
Investment in N Ltd.	5,70,000	
O Ltd.	3,96,000	9,66,000
Less: Paid up value of investment in		
N Ltd.	4,80,000	
O Ltd.	3,00,000	(7,80,000)
Less: Capital profits in		
N Ltd.	81,600	
O Ltd.	71,250	(1,52,850)
Goodwill		33,150

(v) Minority Interest (Amount in ₹)

		₹
Share Capital:		
N Ltd.	1,20,000	
O Ltd.	60,000	1,80,000
Share of profit and reserve (pre and post acquisition)		
N Ltd.	29,400	
O Ltd.	18,000	47,400
Less: Provision for unrealized profit (20% of 2,400)		(480)
		2,26,920

(vi) Reserves M Ltd.

	₹
Balance as on 31.12. 2013	2,88,000
Shares in - N Ltd.	7,200
O Ltd.	750
Total	**2,95,950**

(vii) Profit and Loss A/c M Ltd.

	₹
Balance as on 31.12. 2013	96,000
Share in — N Ltd.	28,800
O Ltd.	3,000
Total	**1,27,800**
Provision for Unrealized profit on stock: [80% of (26,400 - 24,000)]	1,920
Total	**1,25,880**

Illustration 23:

The following is an abstract of the Balance Sheets of H Ltd., S Ltd. and D Ltd. as on March 31,2012:

Particulars	**H Ltd.**	**S Ltd.**	**D Ltd.**
	(₹)	**(₹)**	**(₹)**
Liabilities:			
Share Capital:			
Equity Shares of ₹10 each fully paid	20,00,000	10,00,000	6,00,000
Reserves and Surplus:			
Reserves	1,80,000	2,00,000	1,44,000
Profit & Loss A/c	2,00,000	40,000	1,02,000
Current Liabilities & Provisions:			
Creditors	60,000	60,000	20,000
	24,40,000	13,00,000	8,66,000
Assets:			
Fixed Assets	11,00,000	6,00,000	8,00,000
Investments:			
75,000 shares in S Ltd.	10,00,000	—	—
15,000 shares in D Ltd.	2,00,000	—	—
40,000 shares in D Ltd.	—	5,60,000	—
Current Assets, Loans & Advances:			
Stock	1,20,000	1,00,000	56,000
Cash at Bank	20,000	40,000	10,000
	24,40,000	13,00,000	8,66,000

H Ltd. purchased the shares in S Ltd. and in D Ltd. on September 30,2011, and S Ltd. also purchased the shares in D Ltd. on the same day. The following are the balances at the beginning of the year (1.4.2011):

	S Ltd. (₹)	**D Ltd. (₹)**
Reserves	1,80,000	1,20,000
Profit & Loss A/c	20,000	16,800

You are to assume that profits accrue uniformly every month.

Required:

Prepare a Consolidated Balance Sheet of H Ltd: and its Subsidiaries as at March 31,2012.

Solution:

Consolidated Balance Sheet As at 31st March, 2012

	Particulars	Note No.	Amount (₹)
I.	Equity and Liabilities		
	1. Shareholders' Funds		
	(a) Share Capital	1	20,00,000
	(b) Reserves & Surplus	2	4,35,950
	(c) Minority Interest		3,89,600
	2. Current Liabilities(60,000+60,000+20,000)		1,40,000
	Total		29,65,550
II.	Assets		
	1. Non Current Assets		
	Fixed Assets		
	(a) Tangible Assets	3	25,00,000
	(b) Intangible Assets – Goodwill		1,19,550
	2. Current Assets		
	(a) Stock (1,20,000 + 1,00,000 + 56,000)		2,76,000
	(b) Cash at Bank (20,000 + 40,000 +10,000)		70,000
	Total		29,65,550

Notes to Accounts:

Note -1: Share Capital

	As on 31st March, 2012 (₹)
(a) Authorised Share Capital:	
(b) Issued, Subscribed & fully paid-up (2,00,000 shares of ₹10 each)	20,00,000
Total	20,00,000

Note - 2: Reserves & Surplus

	As on 31st March, 2012 (₹)
General Reserve	1,96,500
Surplus	2,39,450
Total	4,35,950

Note -3: Tangible Asset

	As on 31st March, 2012 (₹)
Fixed Assets of H Ltd.	11,00,000
Fixed Assets of S Ltd.	6,00,000
Fixed Assets of D Ltd.	8,00,000
Total	25,00,000

Working Notes:

(1) Analysis

Particulars	Capital Profits (₹)	Revenue Profits (₹)	Revenue Reserves (₹)
(i) D Ltd.:			
Reserve as on 1.4.2011	1,20,000		—
Profit & Loss as on 1.4.2011	16,800	—	—
Increase in Reserve during the year	12,000	12,000	
Increase in P &L during the year	42,600	—	42,600
	1,91,400	12,000	42,600
Less: Share of H Ltd. (1/4)	47,850	3,000	10,650
	1,43,550	9,000	31,950
Less Minority interest (1/12)	15,950	1,000	3,550
Shares of S Ltd.	1,27,600	8,000	28,400
(ii) S Ltd.:			
Reserve as on 1.4.2011	1,80,000		
Profit & Loss A/c	20,000		
Balance as on 1.4.2011	10,000	10,000	
Increase in Reserve during the year 2011-12	10,000		10,000
Increase in profit & Loss A/c during the year 2011-12			
From D Ltd.	2,20,000	8,000	28,400
Total	55,000	18,000	38,400
Less: Minority Interest (1/4)	1,65,000	4,500	9,600
		13,500	28,800

(2)

Cost of Control	Amount (₹)	Amount (₹)
Cost of Investment in S Ltd.		10,00,000
Cost of Investment in D Ltd.		7,60,000
		17,60,000
Paid up Value of Shares in S Ltd.	7,50,000	
Paid up Value of Shares in D Ltd.	5,50,000	
Capital Profit in S Ltd.	1,65,000	
Capital Profit in D Ltd.	1,75,450	16,40,450
Goodwill		1,19,550

(3)

Minority Interest	S. Ltd. (₹)	C Ltd. (₹)
Shares Capital	2,50,000	50,000
capital Profits	55,000	15,950
Revenue Reserve	4,500	1,000
Revenue Profit	9,600	3,550
	3,19,100	70,500

(4)

	Reserves (₹)	Profit & Loss (₹)
H. Ltd. Balance	1,80,000	2,00,000
Shares in S Ltd.	13,500	28,800
Shares in D. Ltd.	3,000	10,650
	1,96,500	2,39,450

Illustration 24:

The following is an abstract of the Balance Sheet as on 31st March, 2013 of H LTD. and its two Subsidiaries (B LTD. and C LTD).

Particulars	H Ltd.	B Ltd.	C Ltd.
	(₹)	(₹)	(₹)
Liabilities:			
Share Capital:			
Authorised and Issued Equity Shares of ₹100 each fully paid	50,00,000	25,00,000	10,00,000
Reserves and Surplus:			
Capital Reserve	5,00,000	1,50,000	1,00,000
Revenue Reserve	10,00,000	7,50,000	6,00,000
Current liabilities & Provisions:			
Creditors	90,00,000	47,50,000	23,00,000
Income Tax	20,00,000	10,00,000	3,00,000
	5,00,000	3,50,000	3,00,000
Assets:			
Fixed Assets (at cost less depreciation)	32,00,000	16,00,000	3,00,000
Investments:			
Shares in B Ltd. at cost	45,00,000		
Shares in C Ltd. at cost	5,00,000	10,00,000	—
Stock	2,00,000	9,00,000	7,00,000
Debtors	4,00,000	10,50,000	11,50,000
Bank Balance	2,00,000	2,00,000	1,50,000
	90,00,000	47,50,000	23,00,000

Additional Information:

(a) B Ltd. acquired 6000 shares in C Ltd. on 01.4.2011 when the balance on Capital Reserve had been ₹1,00,000 and Revenue Reserve ₹3,50,000.

(b) H Ltd. purchased 20000 shares in B Ltd. on 01.4.2012 when the latter's balance on Consolidated Revenue Reserve had been ₹5,50,000. The Balance of Capital Reserve in B Ltd. at that time was ₹1,50,000.

(c) H Ltd. also acquired 3000 shares in C Ltd. on 01.4.2012 when the balance on Capital Reserve had been ₹1,00,000 and Revenue Reserve ₹3,50,000.

Required:

Prepare a Consolidated Balance Sheet of H Ltd. and its subsidiaries as on March 31, 2013 together with consolidation schedules.

Solution:

H Ltd. and its subsidiaries B Ltd. and C Ltd.

Consolidated Balance Sheet As on 31st March, 2013

	Particulars	Note No.	Amount (₹)
I.	Equity and Liabilities		
	1. Shareholders' Funds		
	(a) Share Capital	1	50,00,000
	(b) Reserve & Surplus	2	19,51,000
	(c) Minority Interest		9,04,000
	2. Current Liabilities		
	(a) Creditor		33,00,000
	(b) Income Tax		11,50,000
	Total		1,23,05,000
II.	Assets		
	1. Non Current Assets		
	Fixed Assets		
	- Tangible Fixed Assets		51,00,000
	- Intangible Fixed Assets		22,55,000
	2. Current Assets		
	(a) Stock		18,00,000
	(b) Debtors		26,00,000
	(c) Bank Balance		5,50,000
	Total		1,23,05,000

Notes to Accounts:

Note -1: Share Capital

	As on 31st March, 2013 (₹)
((a) Authorised Share Capital: 50,000 Equity Shares @ ₹100 each	50.00,000
(b) Issued, Subscribed & Paid-up Capital:	
(50,000 Equity Shares @ ₹100 each)	50,00,000
Total	50,00,000

Note -2: Reserve & Surplus

	As on 31st March, 2013 (₹)
Capital Reserve	5,00,000
Revenue Reserve	14,51,000
Total	19,51,000

Working Notes:

1. Analysis of Profit of C Ltd:

(a)	From the view point of H Ltd:	**Capital Profit (₹)**	**Revenue Profit (₹)**
	Capital Reserve as on 01.04.2012: Revenue Reserve as on 01 .04.201 2: Increase in Revenue Reserve	1,00,000 3,50,000 —	 2,50,000
		4,50,000	2,50,000
	Share of H Ltd. (3/10)	1,35,000	75,000
(b)	Minority Interest in C Ltd. Capital Reserve (1/10): Revenue Reserve (1/10):		 10,000 60,000
			70,000
(c)	From the view point of B Ltd.		
	Capital Reserve as on 01.04.2011: Revenue Reserve as on 01.04.2011: Increase in Revenue Reserve	1,00,000 1,50,000 —	 4,50,000
		2,50,000	4,50,000
	Share of B Ltd. (3/5)	1,50,000	2,70,000

Share of Capital Profit of B in C will be taken to cost of control. However, share of Revenue Profit of B Ltd. in C Ltd. will be divided between Capital and Revenue from the point of view of H Ltd. as follows:

Increase in Capital Reserves of C Ltd. from 01.04.2011 to 01.04.2012 (3,50,000 — 1,50,000)	2,00,000
Increase in Capital I Revenue Reserves of C Ltd. from 01.04.2012 to 31.03.2013 (6,00,000 — 3,50,000)	2,50,000

The derived Revenue profits of 270000 of B Ltd. from C Ltd. will therefore be divided between Capital and Revenue in the ratio of 20 : 25 i.e., 4 : 5

Capital Profit : 2,70,000 x 4/9 = ₹ 1,20,000

Revenue Profit : 2,70,000 x 5/9 = ₹ 1,50,000

2. Analysis of profit of B Ltd. from the view point of H Ltd.

Particulars	**Capital Profit (₹)**	**Revenue Profit (₹)**
Consolidated Reserve on 01.04.2012: (including 1,20,000 from C Ltd., its own being only ₹ 4,30,000). Capital Reserve 01.04.2012 Increase in Revenue Reserved since 01 .04.2012 i.e. (7,50,000 - 4,30,000) Derived Revenue Profit from C Ltd:	5,50,000 1,50,000	— 3,20,000 1.50,000
	7,00,000	4,70,000
Less: Minority Interest (1/5):	1,40,000	94,000
H Share of H Ltd.	5,60,000	3,76,000

3. Cost of Control: (₹)

Amount Paid for Shares by H Ltd.: In B Ltd.		4,50,000
Amount Paid for Shares by H Ltd.: In C Ltd.		
Amount Paid for Shares by B Ltd. :		5,00,000
In C Ltd.		10,00,000
Less: Paid up Value of Shares		60,00,000
6,00,000+20,00,000+3,00,000:	29,00,000	
Capital Profit in C Ltd.		
Share of H Ltd.:	1,35,000	
Share of BLtd.:	1,50,000	
Share of H Ltd. in Capital Profit of B Ltd.:	5,60,000	37,45,000
Goodwill:		22,55,000

4. Consolidated Revenue Reserve

Particulars	(₹)
Revenue Reserve of H Ltd.:	10,00,000
Share of H Ltd. in C Ltd.:	75,000
Share of H Ltd. in B Ltd.:	3,76,000
	14,51,000

5. Minority Interest

Particulars	(₹)
Paid up value of Shares	
In B Ltd.	5,00,000
In C Ltd	1,00,000
Share of Capital Profits	1,10,000
In B Ltd	1,40,000
In C Ltd.	10,000
Share of Revenue Profits	
In B Ltd.	94,000
In C Ltd.	60,000

Illustration 25:

AIR LTD., SEA LTD. and RAIL LTD. are members of a group. AIR LTD bought 70% of the shares of SEA LTD. on October 1,2008 and 30% of the shares of RAIL LTD. on January, 2010. SEA LTD. Bought 60% of the shares of RAIL LTD. on October 1, 2009.

Profit and Loss Account

	Balance as on 1.4.2014	Profit/(Loss) for 2014-15	Balance as on 31.3.2015	Company Formed
	(₹)	(₹)	(₹)	(₹)
AIR LTD.	55,000	25,000	80,000	April 1, 2012
SEA LTD.	20,000 (Dr.)	47,500	27,500	April 1, 2013
RAIL LTD.	—	24,000 (Dr.)	24,000 (Dr.)	April 1, 2014

State how the Profit/ (loss) will be reflected in the consolidated Balance Sheet.

Solution:

	Capital Profit (₹)	Revenue Profit (₹)
Rail ltd.		
Loss for the year (assumed accruing evenly)	12,000	12,000
Less: Due to minority interest 10%	1,200	1,200
	10,800	10,800
Due to Sea Ltd. (60%)	7,200	7,200
Share of Air Ltd. (30%)	3,600	3,600
Revenue Loss Pertaining to further 3 months to be treated as Capita Since Shares are acquired on Jan 1.2010	1,800	(1,800)
Loss	5,400	1,800
Sea Ltd:		
Profit form Rail ltd.	(7,200)	(7,200)
Profit as on Aprill,2014	(10,000)	(10,000)
Profit during 2014-15	-	47.503
	17,200	(50,300)
Due to Outsider, 30%	5,160	9,090
	12,040	21,210
Air Ltd.		
Profit from Rail Ltd.	(5,400)	(1,800)
Profit from Sea Ltd.	(12,040)	21,210
Own Profit	-	80.000
	(17,440)	99,410
Share of Minority Shareholders:		
Capital Loss in Rail Ltd.		(1,200)
Revenue Loss in Rail Ltd.		(1,200)
Capital Loss in Sea Ltd.		(5,160)
Total Profit Loss		(7,560)
Revenue Profit in Sea Ltd.		9,090
Share of Outsiders		1,530

Illustration 26: Purchase in Lots - Before Controlling Acqn. - Ex-Dividend & Ex-Bonus

The Summarised Balance Sheets of G Ltd. and M Ltd. as on 31.03.2015 are as follows - (₹)

Liabilities	G	M	Assets	G	M
Share Capital (₹ 100 Shares)	1,60,000	2,00,000	Investment: Shares in M	–	–
Profit & Loss Account Creditors	50,000	60,000	Debtors	1,96,000	1,20,000
		16,000	Stock in Trade		80,000
			Cash at Bank		70,000
			Cash in Hand	14,000	6,000
Total	**2,10,000**	**2,76,000**	**Total**	**2,10,000**	**2,76,000**

Particulars of G Ltd. -

1. This Company was formed on 01.04.2014.
2. It acquired the shares of M Ltd. as under –

Date of Acquisition	No. of Shares	Cost ₹
01.04.2014	800	1,10,000
31.07.2014	600	86,000

3. The shares purchased on 31.07.2014 are ex-dividend and ex-bonus from existing holders.
4. On 31.07.2014 dividend at 10% was received from M and was credited to Profit & Loss Account.
5. On 31.07.2014 it received Bonus Shares from M in the ratio of One Share on every Four Shares held.
6. G incurred an expenditure of ₹ 500 per month on behalf of M Ltd. and this was debited to the Profit and Loss Account of G Ltd, but nothing has been done in the books of M Ltd.
7. The balance in Profit & Loss A/c as on 31.03.2015 included ₹ 36,000 being the net profit made during the year.
8. Dividend proposed for 2014-15 at 10% was not provided for yet.

Particulars of Maurya Ltd. -

1. The balance in the Profit & Loss A/c as on 31.03.2015 is after the issue of Bonus Shares made on 31.07.2014.
2. The Net Profit made during the year is ₹ 24,000 including ₹ 6,000 received from Insurance Company in settlement of the claim towards loss of stock by fire on 30.06.2014 (Cost ₹ 10,800 included in Opening Stock)
3. Dividend proposed for 2014-15 at 10% was not provided for in the accounts.

Prepare the Consolidated Balance Sheet as at 31.03.2015.

Solution: **1. Basic Information**

Company Status	Dates of Acquisition	Holding Status
Holding Company = G	Lot 1 800 Shares 01.04.2014	Holding Company = 80%
Subsidiary = M	Lot 2 600 Shares 31.07.2014	Minority Interest = 20%

Consolidation: 31.03.2015

Shareholding Status: 800 (Lot 1 on 01.04.2014) + 600 (Lot 2 on 31.07.2014) + 200 (Bonus Issue 1/4th x 800 shares) = 1,600 Shares out of Total 2,000 Shares = 80%

2. Analysis of Profit & Loss Account of M Ltd.

Balance on 31.03.2015 ₹ 60,000

Balance on 01.04.2014	36,000		Profit for 2014-15 (Upto consolidation) (bal fig.)		24,000
(60,000 - 24,000)		**Less:**	Expenses incurred by G Ltd. (₹ 500 x 12)		(6,000)
Less: Dividend adjusted	(2,000)	**Add:**	Abnormal Item - Loss of Stock	₹ 10,800	
(20,000 Less 18,000)			Insurance Claim	₹ 6,000	4,800
Balance Capital Profit	**34,000**		Profit for the year before Dividend		22,800

	01.04.2014 to 31.07.2014 (upto acquisition)		01.07.2014 to 31.03.2015 (upto consolidation)	
	₹ 22,800x4/12=	7,600	₹ 22,800 x 8/12 =	15,200
Less:	Abnormal Item	4,800	**Less:** Dividend 10% x 2,00,000	(15,200)
	Profit after stock loss	2,800	restricted to profits available	
Less:	Balance Dvd ₹ 4,800		Revenue Profit	NIL
	(20,000 - 15,200) adj.	(2,800)		
	to the extent of Profit			
	Balance Capital Profit	NIL		

3. Analysis of Net Worth of M Ltd.

Particulars		Total 100%	G Ltd. 80%	Minority 20%
(a)	Equity Share Capital	2,00,000	1,60,000	40,000
(b)	Capital Profits: Profit & Loss Account	34,000	27,200	6,800
(c)	Revenue Profits: Profit & Loss Account	NIL	–	–
(d)	Proposed Dividend	20,000	16,000	4,000
Minority Interest				**50,800**

4. Cost of Control

	Particulars	₹
	Cost of Investment in M Ltd.	1,96,000
Less:	Dividend out of Pre-acquisition profits (2013-14) (800 Shares x ₹ 10 x 10%)	(8,000)
	FY 2013-14 ₹ 2,000 x 80% x 1,000 Shares/1,600 Shares	(1,000)
	Adjusted Cost of Investment	**1,87,000**
Less:	(1) Nominal Value of Equity Capital	(1,60,000)
	(2) Share in Capital Profit of M Ltd.	(27,200)
	Capital Reserve on Consolidation	**(200)**

Note: Out of the Dividend for the year declared, ₹ 2,000 is from Profits prior to the date of acquisition. Holding Company's share of pre-acquisition dividend ₹ 800 (₹ 2,000 x 80% x 800 Shares ÷ 1,600 Shares) (to the extent of 1,000 Shares including bonus of 200 Shares only) should be adjusted against Investment Account. The balance dividend should be credited to Profit and Loss Account only because –

- For the first lot of 800 Shares, dividends for the preceding year 2013-14 alone should be reduced from Investment Account.
- Second Lot of 600 Shares were purchased ex-dividend and ex-bonus and therefore the entire dividend received on them should be credited to Profit and Loss Account.

5. Consolidation of Profit and Loss Account

	Particulars	₹
	Balance as per Balance Sheet of G Ltd.	50,000
Less:	Proposed Dividend (₹ 1,60,000 x 10%)	(16,000)
Add:	Expenses incurred by M Ltd., (₹ 500 x 12)	6,000
Less:	Dividend out of Pre-acquisition Profits (FY 2013-14 8,000 + FY 14-15 1,000)	(9,000)
Add:	Share of Proposed Dividend for FY 2014-15 (1,600 Shares x ₹ 10 x 10%)	16,000
	Adjusted Balance as at 31.3.2015	**47,000**
Add:	Share of Revenue Profits of M Ltd.	–
	Consolidated Balance	**47,000**

Name of the Company: G Ltd. And its subsidiary M Ltd.

Consolidated Balance Sheet as at 31st, March 2015

Ref No.	Particulars		Note No.	As at 31st March, 2015	As at 31st March, 2014
				₹	₹
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital @ ₹ 10 each	1	160,000	-
		(b) Reserves and surplus	2	47,200	-
				207,200	-
	2	**Minority Interest**		50,800	-
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**		Nil	
				-	-
	5	**Current liabilities**			
		(a) Trade payables	3	16,000	-
		(b) Short-term provisions	4	16,000	-
				32,000	-
		TOTAL (1+2+3+4+5)		290,000	-
	B	**ASSETS**			
	1	**Non-current assets**		Nil	
				-	-
	2	**Current assets**			
		(a) Inventories	5	80,000	-
		(b) Trade receivables	6	120,000	-
		(c) Cash and cash equivalents	7	90,000	-
				2,90,000	-
		TOTAL (1+2)		2,90,000	-

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note 1. Share Capital

	Current Year	Previous Year
Authorised Capital	-	-
Issued and Paid Up	-	-
Equity Share capital @ ₹ 10 each	160,000	-
	160,000	-

Note 2. Reserve and Surplus :-

	Current Year	Previous Year
Capital Reserve on consolidation	200	-
Profit and loss	47,000	-
	-	-
	47,200	-

Note 3. Trade Payable

	Current Year	Previous Year
Creditors (M)	16,000	-
	16,000	-

Note 4. Short Term Provisions

	Current Year	Previous Year
Proposed Dividend	16,000	-
	16,000	-

Note 5. Inventories

	Current Year	Previous Year
Stock in Trade	80,000	-
	80,000	-

Note 6. Trade Receivable

	Current Year	Previous Year
Debtors	1,20,000	-
	1,20,000	-

Note 7. Cash and cash equivqlent :-

Particulars	**Current Year Amount (₹)**	**Previous Year Amount (₹)**
Cash in Hand	-	
G	14,000	-
M	6,000	-
	20,000	-
Add: Cash at Bank	70,000	-
	90,000	-

Illustration 27: Triangle Holding - Trfr of Shares by Holding Company to its Subsidiary

K Ltd. acquired 15,000 Equity Shares out of 20,000 Equity Shares of ₹ 10 each of G Ltd. on 01.04.2014 for ₹2,40,000. As on 01.07.2014, it transferred 5,000 Shares to its Subsidiary M Ltd. for ₹ 90,000. The summarised Balance Sheets of K Ltd., M Ltd., and G Ltd. as on 31.03.2015 were as follows - (₹ 000's)

(₹)

Liabilities	K Ltd.	M Ltd.	G Ltd.	Assets	K Ltd.	M Ltd.	G Ltd.
Share Capital (₹ 10 each)	1,000	500	200	Fixed Assets (Tangible)	1,000	500	300
General Reserve	500	200	40	Investments			
Profit & Loss A/c	100	40	20	- In M Ltd.	250	–	–
14% Loans	50	100	100	- In G Ltd.	160	90	–
Sundry Creditors	50	80	40	- Others	100	50	20
Proposed Dividends	200	100	40	Inventories	100	50	50
				Debtors	100	200	40
				Loan to M Ltd.	100	-	-
				Loan to G Ltd.	50	50	-
				Cash & Bank	40	80	30
Total	**1,900**	**1,020**	**440**	**Total**	**1,900**	**1,020**	**440**

K Ltd. acquired 60% shares of M Ltd. on 01.04.2014. As on that date, balances in M Ltd.'s General Reserve and P & L were ₹ 1,00,000 and ₹ 10,000 respectively.

As on 01.04.2014, G Ltd.'s books showed General Reserve ₹ 10,000 and Profit and Loss Account ₹ 2,000. Interest on Inter-Corporate Loans within the group has not been accounted for.

Prepare Consolidated Balance Sheet of K Ltd. and its Subsidiary M Ltd. and G Ltd. as on 31.03.2015.

Solution:

1. Basic Information

Company Status		Dates		Holding Status		
Holding Company	= K Ltd.	Acquisitions	1.04.2014		**M Ltd.**	**G Ltd.**
Subsidiary	= M Ltd.	Consolidation:	31.03.2015	a. Holding Co.	(K Ltd.) 60%	(K Ltd.) 50%
Sub-Subsidiary	= G Ltd.				–	(M Ltd.) 25%
				b. Minority Int.	40%	25%

Note: *Shareholding Pattern is as under–*

Company	Held by K Ltd.	Held by M Ltd.	Total Holdings	Minority Interest	Total number of shares
M Ltd.	30,000 (60%)	–	30,000 (60%)	20,000 (40%)	50,000
G Ltd.	10,000 (50%)	5,000 (25%)	15,000 (75%)	5,000 (25%)	20,000

3. Analysis of Reserves and Surplus of G Ltd.

(a) General Reserve

Balance on 31.3.2015 ₹ 40,000

Balance on 1.4.2014 (Acquisition date)	**10,000** **Capital Profit**	Transfer during 2014-15 (bal. fig)	**₹ 30,000** **Revenue Reserve**

(b) Profit & Loss Account

	Balance on 31.03.2015	₹ 20,000
Less:	Loan Interest (₹ 1,00,000 x 14%)	₹ 14,000
	Corrected Balance	₹ **6,000**

Balance on 1.4.2014 (Acquisition date)	**₹ 2,000** **Capital Profits**	Profit for 2014-15 (balancing figure)	**₹ 4,000** **Revenue Profits**

4. Analysis of Reserves & Surplus of M Ltd.

(a) General Reserve

Balance on 31.3.2015 ₹ 2,00,000

Balance on 1.4.2014 (Acquisition date)	**1,00,000** **Capital Profit**	Transfer during 2014-15 (bal. fig)	**1,00,000** **Revenue Reserve**

(b) Profit & Loss Account

	Balance on 31.03.2015	₹ 20,000
Add:	Dividend from G Ltd. (40,000 x 25% x 9/12)	₹ 7,500
Add:	Loan Interest receiced from G Ltd. (50,000 x 14%)	₹ 7,000
Less:	Loan Interest (₹ 1,00,000 x 14%)	₹ 14,000
	Adjusted Balance	**₹ 40,500**

Balance on 1.4.2014 (Given Acqn Date)	**₹ 10,000** **Capital Profit**	Profit for 2014-15 (balancing figure)	**₹ 30,500** **Revenue Profit**

Total Capital Profits: ₹ 10,000; Total Revenue Profits: ₹ 30,500

Note: Proposed Dividend from G Ltd. is considered only to the extent of period of holding by M Ltd. The balance dividend for 3 months will be reduced from Cost of Investments as it relates to pre-acquisition period.

5. Computation of Minority Interest

Particulars		K Ltd. 60% M Ltd.	K Ltd. 50% G Ltd. (M Ltd. 25%)	Minority Interest M Ltd. 40%	Minority Interest G Ltd. 25%
(a) Share Capital		5,00,000	2,00,000		
Less: Minority Interest		(2,00,000)	(50,000)	2,00,000	50,000
		3,00,000	**1,50,000**		
(b) Capital Profits	General Reserve	1,00,000	10,000		
	Profit & Loss A/c	10,000	2,000		
		1,10,000	**12,000**		
Transfer of M's Share in G (12000 x 25% x 9/12)		2,250	(2,250)		
		1,12,250	**9,750**		
Less: Minority Interest		(44,900)	(3,000)	44,900	3,000
		67,350	**6,750**		
(c) Revenue Reserve:		**1,00,000**	**30,000**		
Transfer of M's Share in G (30,000 x 25% x 9/12)		5,625	(5,625)		
		1,05,625	24,375		
Less: Minority Interest		(42,250)	(7,500)	42,250	7,500
		63,375	**16,875**		
(d) Revenue Profits:		**30,500**	**4,000**		
Transfer of M's Share in G (4,000 x 25% x 9/12)		750	(750)		
		31,250	**3,250**		
Less: Minority Interest		(12,500)	(1,000)	12,500	1,000
		18,750	**2,250**		10,000
(e) Proposed Dividend:		1,00,000	40,000		
Less: Minority Interest		(40,000)	(10,000)	40,000	
		60,000	**30,000**		
Total Minority Interest				**3,39,650**	**71,500**

For G Ltd.: Capital Reserve, Revenue Reserve & Revenue Profits are to be considered only from the period of holding of M Ltd.

6. Cost of Control

	Particulars			₹
	Cost of Investment in Equity Shares	K Ltd. in M Ltd.		2,50,000
		K Ltd. in G Ltd.		1,60,000
		M Ltd. in G Ltd.		90,000
	Total Cost of Investment			**5,00,000**
Less:	Dividend out of Pre-acquisition profits in M Ltd. (40,000 x 25% x 3/12)		2,500	
Less:	Unrealized Profit on sale of Investment by K to M [90,000 - (240000 / 5,000 / 15,000)		10,000	12,500
	Adjusted Cost of Investment			**4,87,500**
Less:	Nominal Value of Equity Capital:	M Ltd.	3,00,000	
		G Ltd.	1,50,000	
	Share in Capital Profit:	M Ltd.	67,350	
		G Ltd.	6,750	(5,24,100)
	Capital Reserve on Consolidation			**36,600**

7. Consolidation of Reserves and Surplus

	Particulars		Gen. Res.	P&L A/c
	Balance as per Balance Sheet of K Ltd.		5,00,000	1,00,000
Add:	Proposed Dividends	From G Ltd. (₹ 40,000 x 50/100)		20,000
		From M Ltd. (₹ 1,00,000 x 60/100)		60,000
Add:	Interest on Loans [₹ 1,00,000 to M + ₹ 50,000 to G) x 14%]			21,000
Add:	Share of Revenue Profits / Reserves:	M Ltd.	63,375	18,750
		G Ltd.	16,875	2,250
Less:	Unrealized Profit on Sale of Investment to M			(10,000)
	Consolidated Balance		**5,80,250**	**2,12,000**

Name of the Company: K Ltd. And its subsidiary M & G Ltd.

Consolidated Balance Sheet as at 31st, March 2015

Ref No.		Particulars	Note No.	As at 31st March, 2015 ₹	As at 31st March, 2014 ₹
	A	**EQUITY AND LIABILITIES**			
	1	**Shareholders' funds**			
		(a) Share capital	1	1,000,000	-
		(b) Reserves and surplus	2	8,28,850	-
				18,28,850	-
	2	**Minority Interest (339650 + 71500)**		411,150	-
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**			
		(a) Long-term borrowings	3	50,000	-
				-	-
	5	**Current liabilities**			
		(a) Trade payables	4	170,000	-
		(b) Short-term provisions	5	200,000	-
				370,000	-
		TOTAL (1+2+3+4+5)		26,60,000	-
	B	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	6	1,800,000	-
		(b) Non-current investments	7	170,000	-
				19,70,000	-
	2	**Current assets**			
		(a) Inventories	8	200,000	-
		(b) Trade receivables	9	340,000	-
		(c) Cash and cash equivalents	10	150,000	-
				690,000	-
		TOTAL (1+2)		26,60,000	-

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Note 1. Share Capital

	Current Year	Previous Year
Authorised Capital	-	-
Issued and Paid Up	-	
Equity Share capital	1,000,000	
	-	
	1,000,000	-

Note 2. Reserve and Surplus :-

	Current Year	Previous Year
General Reserve	580,250	
Profit & Loss A/c	212,000	
Capitla Reserve	36,600	
on consolidation		
	8,28,850	

Note 3. Long Term Borrowings

	Current Year	Previous Year
K	50,000	
M	100,000	
G	100,000	
	250,000	
Less: Loan to M & G	150,000	
	100,000	
Less: Loan to M by G	50,000	
	50,000	

Note 4. Trade Payable

	Current Year	Previous Year
Sundary Creditors		
K	50,000	
M	80,000	
G	40,000	
	170,000	
	-	
	170,000	

Note 5. Short Term Provision

	Current Year	Previous Year
Proposed Dividend	200,000	
	200,000	

Note 6. Tangible Assets :-

	Current Year	Previous Year
K	1,000,000	
M	500,000	
G	300,000	
	-	
	1,800,000	

Note 7. Non Current Investment

	Current Year	Previous Year
K	100,000	
M	50,000	
G	20,000	
	170,000	-

Note 8. Inventories

	Current Year	Previous Year
Stock in Trade		
K	100,000	
M	50,000	
G	50,000	
	200,000	

Note 9. Trade Receivable

	Current Year	Previous Year
Sundary Debtors		
K	100,000	
M	200,000	
G	40,000	
	340,000	

Note 10. Cash and cash equivqlent

	Current Year	Previous Year
Cash and Bank		
K	40,000	
M	80,000	
G	30,000	
	150,000	

Illustration 28.

The Balance Sheet of Big Ltd., Small Ltd. and Little Ltd. as at 1st March, 2013 are given below:

	Big Ltd.	Small Ltd.	Little Ltd.
Equity and Liabilities			
Shareholders' Funds			
Share Capital			
Equity Shares of ₹ 10 each, fully paid up	2,00,000	1,00,000	60,000
Reserves and Surplus			
General Reserve	60,000	50,000	40,000
Profit and Loss A/c	50,000	40,000	30,000
Current Liabilities			
Trade Payables	35,000	30,000	40,000
Big Ltd.		15,000	5,000
Total	3,45,000	2,35,000	1,75,000
Assets			
Non-current Assets			
Tangible Assets			
Plant and machinery	80,000	1,10,000	1,15,000
Non-current investments (at cost)			
Equity shares in Small Ltd.	90,000		
Equity shares in Little Ltd.	40,000	60,000	
Current Assets			
Inventories	60,000	35,000	35,000
Trade receivables	35,000	20,000	15,000
Small Ltd:	18,000		
Little Ltd.	7,000		
Cash and cash equivalents	15,000	10,000	10,000
Total	3,45,000	2,35,000	1,75,000

(i) Big Ltd. held 8000 shares of Small Ltd. and 1800 shares of Little Ltd.

(ii) Small Ltd. held 3600 shares of Little Ltd.

(iii) All investments were made on July 2012

(iv) The following balances were there on July 2012:

	Small Limited	Little Limited
Reserves	25,000	15,000
Profit and Loss A/c	30,000	25,000

(v) Small Ltd. invoiced goods to Big Ltd. at cost + 25% in December 2012. The closing stock of Big Ltd. includes goods with invoice value ₹6,000.

(vi) Little Ltd. sold to Small Ltd. an equipment costing 24,000 at a profit of 25% on selling price on January 2013. Depreciation at 10% p.a. was provided by Small Ltd. on this equipment.

(vii) Big Ltd. proposes dividend at 10%.

Prepare the Consolidated Balance Sheet of the group as at 31 March 2013 by the direct approach. Workings should form part of the answer.

Solution:

(a) Consolidated Balance Sheet of Big Ltd. and its subsidiaries Small Ltd. and Little Ltd. as at 31st March, 2013

	Particulars	Note No.	Amount (₹in Lakhs)
I.	**Equity and Liabilities**		
	(a) Share Capital	1	2,00,000
	(b) Reserves and Surplus	2	1,57,420
	1. Minority Interest (W.N. 4)		53,580
	2. Current Liabilities		
	(a) Trade payables	3	1,05,000
	(b) Short- term provisions	4	20,000
	Total (1 + 2 + 3)		5,36,000
II.	**Assets**		
	1. Non- Current Assets		
	Fixed Assets		
	- Tangible Assets	5	2,97,200
	2. Current Assets		
	(a) Inventories	6	1,28,800
	(b) Trade receivables	7	70,000
	(c) Cash and cash equivalents	8	35,000
	(d) Other current assets	9	5,000
	Total (1 + 2)		5,36,000

Notes to Accounts:

Note -1: Share Capital

	As on 31st March, 2013 (₹)
Authorized, Issued, Subscribed and paid-up Share capital: 20,000 Equity Shares of ₹10 each	2,00,000
Total	**2,00,000**

Reconciliation of Share Capital

For Enquiry Share

	As at 31st March, 2013	
	Nos.	**Amount (₹)**
Opening Balance as on 01 .04.12	20,000	2,00,000
Add: Fresh Issue (Including Bonus shares, right shares, split shares, share issued other than cash)		
Less: Buy Back of Share		
Total	20,000	2,00,000

Note 2. Reserve & Surplus

	As on 31st March, 2013 (₹)
Capital Reserve (W.N. 3)	24,000
Revenue Reserve (W.N. 7)	99,500
Profit and Loss A/c (W.N. 6)	33,920
Total	1,57,420

Note 3. Trade Payables

	As on 31st March, 2013 (₹)
Sundry Creditors (35,000 + 30,000 + 40,000)	1,05,000
Total	**1,05,000**

Note 4. Short -term provisions

	As on 31st March, 2013 (₹)
Proposed dividend	20,000
Total	20,000

Note 5. Tangible Assets

	As at 31st March, 2013 (₹)	
Fixed Assets less depreciation — Big Ltd.	80,000	
Small Ltd.	1,10,000	
Little Ltd.	1,15,000	3,05,000
Less: Unrealised Profit (W.N. 5)		7,800
Total		2,97,200

Note 6. Inventories

	As on 31st March, 2013 (₹)
Stock (60,000 + 35,000 + 35,000)	1,200
Less: Unrealised Profit	1,28,800
Total	1,30,000

Note 7. Trade Receivables

	As on 31st March, 2013 (₹)
Debtors (more than six months considered good)- (35,000+ 20,000+ 15,000)	70,000
Total	70,000

Note 8. Cash and Cash equivalents

	As on 31st March, 2013 (₹)
Cash and Bank Balance (15,000 + 10,000 + 10,000)	35,000
Total	35,000

Note 9. Other Current Assets

	As on 31st March, 2013 (₹)
Bills receivables — (18,000 + 7,000)	25,000
Less.: Mutual debts (15,000 + 5,000)	20,000
Total	55,000

Working Notes:

1. Analysis of Profit of Little Ltd.

Particulars	Capital Profits	Revenue Reserves	Revenue Profits
	(₹)	(₹)	(₹)
Reserve on 01.07.2012	15,000		
Prof it and Loss A/c on 01.07.2012	25,000		
Increase in Reserves		25,000	
Increase in Profit			5,000
	40,000	25,000	5,000
Less: Minority Interest (10%)	(4,000)	(2,500)	(500)
	36,000	22,500	4,500
Share of Big Ltd. (30%)	12,000	7,500	1,500
Share of Small Ltd. (60%)	24,000	15,000	3,000

2. Analysis of Profit of Small Ltd. (by direct approach)

Particulars	Capital Profits	Revenue Reserves	Revenue Profits
	(₹)	(₹)	(₹)
Reserve on 01.07.2012	25,000		
Profit and Loss A/c on 01.07.2012	30,000		
Increase in Reserves		25,000	
Increase in Profit		-	10,000
	55,000	25,000	10,000
Share in Little Ltd.		15,000	3,000
	55,000	40,000	13,000
Less: Minority Interest (20%)	(11,000)	(8,000)	(2,600)
Share of Big Ltd. (80%)	44,000	32,000	10,400

3. Cost of Control:

Particulars	Amount (₹)	Amount (₹)	Amount (₹)
Invest in Small Ltd. Invest in Little Ltd.			90,000 1,00,000
			1,90,000
Less: Paid up value of Investment In Small Ltd. In Little Ltd.	 80,000 54,000	 1,34,000	
Capital Profit In Small Ltd. In Little Ltd.	 44,000 36,000	 80,000	 2,14,000
Capital Reserve			24,000

4. Minority Interest

Particulars	Small Ltd. (₹)	Little Ltd. (₹)
Share Capital Capital Profit Revenue Reserves Revenue Profit	20,000 11,000 8,000 2,600	6,000 4,000 2,500 500
	41,600	13,000
Less: Unrealized profit on stock (20%of ₹6,000 x 25/125) Unrealized profit on equipment (10% of ₹7,800)	240	 780
	41,360	12,220

5. Unrealized Profit on equipment sold

Particulars	(₹)
Selling Price (24,000 x 100/75) Less: Cost Profit Unrealized Profit = ₹ (8,000-8,000 x 10/100 x 3/12) = ₹7,800	32,000 (24,000) 8,000

6. Profit and Loss Account - Big Ltd.

Particulars	(₹)
Balance Less: Proposed dividend	50,000 (20,000)
	30,000
Add: Share in Small Ltd. Share in Little Ltd.	10,400 1,500
	41,900
Less: Unrealized profit on equipment (90% of ₹7,800)	(7,020)
	34,880
Less: Unrealized profit on stock (₹6,000 x 25/1 25 x 80%)	(960)
	33,920

7. Revenue Reserves - Big Ltd.

Particulars	(₹)
Balance Share in Small Ltd. Share in Little Ltd.	60,000 32,000 7,500
	99,500

Illustration 29:

The following are the summarised Balance Sheets of Arun Ltd., Brown Ltd. and Crown Ltd. as at 31.03.2015:

Liabilities:	Arun Ltd.	Brown Ltd.	Crown Ltd.
	₹	₹	₹
Share Capital (Shares of ₹ 100 each)	10,80,000	7,20,000	4,32,000
Reserves	1,44,000	72,000	54,000
Profit and Loss Account	3,60,000	2,16,000	1,80,000
Sundry Creditors	1,44,000	1,80,000	1,08,000
Arun Ltd.	--	72,000	57,600
Total	17,28,000	12,60,000	8,31,600

Assets:

Goodwill	1,44,000	1,08,000	72,000
Fixed Assets	5,04,000	3,60,000	4,32,000
Shares in:			
Brown Ltd. (5,400 Shares)	6,48,000	--	--
Crown Ltd. (720 Shares)	1,08,000	--	--
Crown Ltd. (2,520 Shares)	--	3,74,000	--
Due from: Brown Ltd.	86,400	--	--
Crown Ltd.	57,600	--	--
Current Assets	1,80,000	4,17,600	3,27,000
Total	17,28,000	12,60,000	8,31,000

(i) All shares were acquired on 1.10.2014.

(ii) On 1.4.2012 the balances to the various accounts were as under:

Particulars	Arun Ltd. ₹	Brown Ltd. ₹	Crown Ltd. ₹
Reserves	72,000	72,000	36,000
Profit and Loss account	36,000	(Dr.) 36,000	21,600

(iii) During 2014-15, Profits accrued evenly.

(iv) In November, 2014, each company paid interim dividend of 10%. Arun Ltd. and Brown Ltd. have credited their profit and loss account with the dividends received.

(v) During 2014-15, Crown Ltd. sold an equipment costing ₹ 72,000 to Brown Ltd. for ₹ 86,400 and Brown Ltd. in turn sold the same to Arun Ltd. for ₹ 93,600.

Prepare the consolidated Balance Sheet as at 31.03.2015 of Arun Ltd. and its subsidiaries.

solution:

Consolidated Balance Sheet of Arun Ltd. and its subsidiaries as on 31.03.2015 (₹)

Ref No.	Particulars		Note No.	As at 31st March, 2015	As at 31st March, 2014
	I	**EQUITY AND LIABILITIES**			
	1	**Shareholder's Fund**			
		(a) Share capital	1	10,80,000	
		(b) Reserves and surplus	2	6,07,088	
	2	**Minority Interest (W.N.4)**		4,02,712	
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**		Nil	
	5	**Current Liabilities**			
		(a) Trade payables	3	4,32,000	
		Total (1+2+3+4+5)		**25,39,800**	
	II	**ASSETS**			
	1	Non-current assets			
		(a) Fixed assets			
		(i) Tangible assets	4	12,74,400	
		(ii) Intangible assets	5	3,25,800	
	2	**Current assets**			
		(d) Cash and cash equivalents	6	9,39,600	
		Total (1+2)		**25,39,800**	

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Notes of the Accounts

(₹)

Note 1. Share Capital	**As at 31st March, 2015**	**As at 31st March, 2014**
Authorized, Issued, Subscribed and paid-up Share capital:-		
10,800 Equity share of ₹100 each	10,80,000	
Total	10,80,000	

RECONCILIATION OF SHARE CAPITAL

FOR EQUITY SHARE	**As at 31st March, 2015**		**As at 31st March, 2014**	
	Nos.	Amount (₹)	Nos.	Amount (₹)
Opening Balance as on 01.04.14	10,800	10,80,000		
Add: Fresh Issue (Including Bonus shares, right shares, split shares, share issued other than cash)				
	10,800	10,80,000		
Less: Buy Back of share				
Total	10,800	10,80,000		

Note 2. Reserve & Surplus	As at 31st March, 2015	As at 31st March, 2014
Reserve (wn.8)	1,49,438	
Profit and Loss (WN.8)	4,57,650	
Total	6,07,088	

Note 3. Trade Payables	As at 31st March, 2015	As at 31st March, 2014
Sundry Creditors (1,44,000+1,80,000+1,08,000)	4,32,000	
Total	4,32,000	

Note 4. Tangible Assets	As at 31st March, 2015	As at 31st March, 2014
Fixed Assets	12,74,400	
Total	12,74,400	

Note 5. Intangible assets	As at 31st March, 2015	As at 31st March, 2014
Goodwill (WN.5)	3,25,800	
Total	3,25,800	

Note 6. Cash and cash equivalents	As at 31st March, 2015	As at 31st March, 2014
Cash at Bank other than cash in transit	9,25,200	
Cash in transit	14,400	
Total	9,39,600	

Note 10.Other current assets	As at 31st March, 2015	As at 31st March, 2014
Bills receivables- (55+110)	165	
Less: mutual debts	11	
Total	154	

Working Notes:

1. Shareholding Pattern

In Brown Ltd.:	Number of Shares	%age of Holding
Arun Ltd.	5,400	75%
Minority Interest	1,800	25%
In Crown Ltd.:		
Arun Ltd.	720	16.667%
Brown Ltd.	2,520	58.333%
Minority Interest	1,080	25%

2. Analysis of apportionment of profit in Crown Ltd.

(a) Calculation of Unrealized Profit in Equipment

Crown Ltd sold equipment to Brown Ltd. at a profit of ₹ 14,400 and this would be apportioned to

	₹
Arun Ltd.	2,399
Brown Ltd.	8,401
Minority Interest	3,600
	14,400

Brown Ltd sold the equipment to Arun Ltd. at a profit of ₹ 7,200. This would be apportioned to:

	₹
Arun Ltd.	5,400
Minority Interest	1,800
	7,200

The above amounts are to be deducted from the respective share of profits.

(b) Reserves

	₹	
Closing balance	54,000	
Opening balance	36,000	Capital Profit
Current year Appropriation	18,000	
Apportionment of Profit from 1.4.2014 to 30.9.2014	9,000	Capital Profit
Apportionment of Profit from 1.10.2014 to 31.03.2015	9,000	Revenue Reserve

(c) Profit and Loss Account

Closing balance	1,80,000	
Opening balance	21,600	Capital Profit
Current year profits before interim dividend	2,01,600	
Apportionment of Profit from 1.4.2014 to 30.9.2014	1,00,800	
Less: Interim Dividend	43,200	
	57,600	Capital Profit
From 1.10.2014 to 31.03.2015	1,00,800	Revenue Profit

(d) Apportionment of profits of Crown Ltd.

	Pre-Acquisition	Post Acquisition	
	Capital Profit ₹	Revenue Reserve ₹	Revenue Profit ₹
Reserves	45,000	9,000	--
Profit & Loss Account	79,200	--	1,00,800
	1,24,200	9,000	1,00,800
Arun Ltd [16.667%]	20,700	1,499	16,799
Brown Ltd. [58.333%]	72,450	5,251	58,801
Minority Interest [25%]	31,050	2,250	25,200

3. **Analysis of Profit of Brown Ltd**

(a) **Reserves**

	₹	
Closing balance	72,000	
Opening balance	72,000	(Capital Profit)
Current year Appropriation	Nil	

(b) **Profit and Loss Account**

	₹
Closing balance	2,16,000
Opening balance (Dr.)	36,000
Current year Appropriation after interim dividend	2,52,000
Interim Dividend	72,000
Profit before Interim Dividend	3,24,000
Less: Dividend from Crown Ltd.	25,200
	2,98,800
Apportionment of Profit from 1.4.2014 to 30.9.2014	1,49,400
Less: Interim Dividend	72,000
Capital profit	77,400
Apportionment of Profit from 1.10.2014 to 31.03.2015 (Revenue profit)	1,49,400

(c) **Apportionment of Profit of Brown Ltd.**

	Pre-Acquisition	Post-Acquisition	
	Capital Profit ₹	Revenue Reserve ₹	Revenue Profit ₹
Reserves	72,000	--	--
Profit & Loss Account (Opening balance (-) 36,000 + 77,400)	41,400		1,49,400
Less: Unrealised Profit of Equipment from Crown Ltd.			(8,401)
Share of Post-Acquisition Profit of Crown Ltd.	--	5,251	58,801
	1,13,400	5,251	1,99,800
Arun Ltd. 75%	85,050	3,938	1,49,850
Minority Interest 25%	28,350	1,312	49,950

4. **Minority Interest**

	Brown Ltd. ₹	Crown Ltd. ₹
Share Capital	1,80,000	1,08,000
Capital Profit	28,350	31,050
Revenue: Reserves	1,312	2,250
Profit & Loss Account	49,950	25,200
Unrealised Profit on Equipment	(1,800)	(3,600)
	2,57,812	1,62,900
Total Minority Interest: ₹ 2,57,812+ ₹ 1,62,900 = ₹ 4,20,712		

5. Cost of Control

	Arun Ltd. in Brown Ltd. ₹	**Arun Ltd. in Crown Ltd.** ₹	**Brown Ltd in Crown Ltd.** ₹
Amount Invested	6,48,000	1,08,000	3,74,400
Less: Pre-acquisition dividend[4*]	54,000	7,200	25,200
Adjusted Cost of Investment (A)	5,94,000	1,00,800	3,49,200
Share capital	5,40,000	72,000	2,52,000
Capital Profit	85,050	20,700	72,450
(B)	6,25,050	92,700	3,24,450
Capital Reserve/Goodwill (A)-(B)	(31,050)	8,100	24,750
Net Goodwill	₹ 1,800		
Goodwill on Consolidation ₹ (1,44,000+ 1,08,000 + 72,000 + 1,800) = ₹ 3,25,800			

6. Dividend declared

	Brown Ltd. ₹	Crown Ltd. ₹
Dividend declared	72,000	43,200
Share of: Arun Ltd.	54,000	7,200
Brown Ltd.		25,200
Minority	18,000	10,800

7. Inter-Company Transactions

(a) Owings

	Dr.	Cr.	Cr.
	Arun Ltd. ₹	Brown Ltd. ₹	Crown Ltd. ₹
Balance in books	1,44,000	72,000	57,600
Less: Inter- co. owings	1,29,600	72,000	57,600
Cash-in-transit	14,400	NIL	NIL

(b) Fixed Assets

	₹
Total Fixed Assets	12,96,000
Less: Unrealised Profit on sale of equipment	21,600
Amount to be taken to consolidated Balance Sheet	12,74,400

8. Reserves and Profit and Loss Account balances in the Consolidated Balance Sheet

	Reserves ₹	Profit and Loss A/c ₹
Balance in Books	1,44,000	3,60,000
Add: Shares of Post Acquisition Profits:		
From Brown Ltd.	3,938	1,49,850
From Crown Ltd	1,499	16,799
Less: Pre-Acquisition dividend:		
From Brown Ltd.		(54,000)
From Crown Ltd		(7,200)
Less: Unrealised Profit on Equipment:		
From Brown Ltd.		(5,400)
From Crown Ltd.		(2,399)
	1,49,437	4,57,650

Illustration 30.

The draft Balance Sheets of 3 Companies as at 31st March, 2015 are as below:

			(In ₹ 000's)
Liabilities	**Morning Ltd.**	**Evening Ltd.**	**Night Ltd.**
Share Capital – shares of ₹ 100 each	1,00,000	50,000	25,000
Reserves	4,500	2,500	2,250
P/L A/c (1.4.13)	3,750	5,000	2,000
Profit for 2013-14	17,500	9,500	4,500
Loan from Morning Ltd.	-	12,500	--
Creditors	6,250	2,500	3,500
	1,32,000	82,000	37,250
Assets			
Investments:			
4,00,000 shares in Evening	45,000	-	-
1,87,000 shares in Night	20,000	-	-
Loan to Evening Ltd.	12,500	-	-
Sundry assets	54,500	82,000	37,250
	1,32,000	82,000	37,250

Following additional information is also available:

(a) Dividend is proposed by each company at 10%.

(b) Stock transferred by Night Ltd. to Evening Ltd. fully paid for was ₹ 20 lacs on which the former made a Profit of ₹ 7.5 lacs. On 31st March, 2015, this was in the inventory of the latter.

(c) Loan referred to is against 8% interest. Neither Morning Ltd. nor Evening Ltd. has considered the interest.

(d) Reserves as on 1.4.2014 of Evening Ltd. and Night Ltd. were ₹ 20,00,000 and ₹ 18,75,000 respectively.

(e) Cash-in-transit from Evening Ltd. to Morning Ltd. was ₹ 2,50,000 as on 31.3.2015.

(f) The shares of the subsidiaries were all acquired by Morning Ltd. on 1st April, 2014.

Prepare consolidated Balance Sheet as on 31st March, 2015. Workings should be part of the answer.

Solution:

Consolidated Balance Sheet of Morning Ltd. with its subsidiaries Evening Ltd. and Night Ltd.
As on 31st March, 2015

(₹ in thousand)

Ref No.	Particulars		Note No.	As at 31st March, 2015	As at 31st March, 2014
	I	**EQUITY AND LIABILITIES**			
	1	**Shareholder's Fund**			
		(a) Share capital	1	1,00,000.00	
		(b) Reserves and surplus	2	29,112.50.00	
	2	**Minority Interest** (12,200+7812.5)		20,012.50	
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**		Nil	
	5	**Current Liabilities**			
		(a) Trade payables	3	12,250.00	
		(b) Short-term provisions	4	11,625.00	
		Total (1+2+3+4+5)		**1,73,000.00**	
	II	**ASSETS**			
	1	**Non-current assets**			
	2	**Current assets**			
		(a) inventories	5	86,125.00	
		(b) Cash and cash equivalents	6	86,875.00	
		Total (1+2)		**1,73,000.00**	

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Notes on the Accounts

(₹ In '000)

Note 1. Share Capital	**As at 31st March, 2015**	**As at 31st March, 2014**
Authorized, Issued, Subscribed and paid-up Share capital:-		
1,000 Equity share of ₹100 each	1,00,000	
Total	1,00,000	

RECONCILIATION OF SHARE CAPITAL

FOR EQUITY SHARE	**As at 31st March, 2015**		**As at 31st March, 2014**	
	Nos.	Amount (₹)	Nos.	Amount (₹)
Opening Balance as on 01.04.14	1,000	1,00,000		
Add: Fresh Issue (Including Bonus shares, right shares, split shares, share issued other than cash)				
	1,000	1,00,000		
Less: Buy Back of share	–	–		
Total	1,000	1,00,000		

Note 2. Reserve & Surplus		As at 31st March, 2015	As at 31st March, 2014
Capital Reserve (wn.5)		2,256.00	
General reserve- Morning Ltd	4,500		
Evening Ltd	400		
Night Ltd	281.25	5,181.25	
Profit & Loss A/c			
Balance as on 1.04.14	3,750		
Profit during the year	17,500		
Add: Interest on loan	1,000		
Less: Proposed dividend	(10,000)	12,250.00	
Profit & Loss of Evening Ltd		6,800.00	
Profit & Loss of Night Ltd		2625.00	
Total		29,112.50	

Note 3. Trade Payables	As at 31st March, 2015	As at 31st March, 2014
Sundry Creditors- Morning Ltd	6,250	
Evening Ltd	2,500	
Night Ltd	3,500	
Total	12,250	
Note 4. Short-term provisions	**As at 31st March, 2015**	**As at 31st March, 2014**
Proposed dividend- Morning Ltd	10,000	
Evening Ltd- (Minority)	1,000	
Night Ltd- (Minority)	625	
	11,625	

Note 5. Inventories		As at 31st March, 2015	As at 31st March, 2014
Stock in trade- Morning Ltd		27,250	
Evening Ltd	41,000		
Less: Unrealised Profit	750	40,250	
Night Ltd		18,625	
Total		86,125	

Note 6. Cash and cash equivalents	As at 31st March, 2015	As at 31st March, 2014
Cash at Bank- Morning Ltd	27,250	
Evening Ltd	41,000	
Night Ltd	18,625	
Total	86,875	

Workings Notes:

A. Morning Ltd.'s holding in Evening Ltd. is 4,00,000 shares out of 5,00,000 shares, i.e., 4/5th or 80%; Minority holding 1/5th or 20%.

B. Morning Ltd.'s holding in Night Ltd. is 1,87,500 shares out of 2,00,000 shares, i.e., 3/4th or 75%; Minority holding 1/4th or 25%.

Analysis of Reserves and Profits of Subsidiary Companies

		Evening Ltd. (₹'000)	Night Ltd ₹('000)	Minority interest in Evening Ltd. (1/5) ₹('000)	Minority interest in Night Ltd. (1/4) ₹('000)
1.	**Capital Reserve (pre-acquisition reserves and profits)**				
	Reserves on 1.04.2014	2,000	1,875		
	Profit on 1.04.2014	5,000	2,000		
		7,000	3,875		
	Less: Minority interest	1,400	968.75	1,400	968.75
		5,600	2,906.25		
2.	**General Reserve**				
	Reserves as per Balance Sheet	2,500	2,500		
	Less: Capital Reserve [See Note A]	2,000	1,875		
		500	625		
	Less: Minority interest	100	156.25	100	37.5
		160	468.75		
3.	**Profit and Loss Account**				
	Profit for the year as per Balance Sheet	9,500	4,500		
	Less: Interest on Loan (12,500 × 8%)	1,000			
		8,500			
	Less: Minority Interest	1,700	1,125	1,750	1,125
		6,800	3,375		
	Less: Unrealised profit on stock transfer	____	750[6*]		
		6,800	2,625		
4.	**Share Capital**				
	As per Balance sheet	50,000	25,000		
	Less: Minority interest	10,000	6,250	10,000	6,250
	Transferred for computation of Goodwill/Capital Reserve	40,000	18,750	13,200	8,437.50
	Less: Proposed dividend shown separately			1,000	625
	Transferred to Consolidated Balance Sheet			12,200	7,812.50

5. Computation of Cost of Control i.e. Goodwill / Capital Reserve on consolidation

(₹ in thousand)

	Evening Ltd.	Night Ltd.
Cost of Investments	45,000	20,000
Less: Paid up value of shares [Refer Note 4]	40,000	18,750
	5,000	1,250
Less: Capital Reserve [Refer Note 1]	5,600	2,906.25
	(600)	(1,656.25)
Total Capital Reserve (₹ 600 + ₹ 1,656.25)	2,256.25	

Illustration 31.

X Ltd. purchases its raw materials from Y Ltd. and sells goods to Z Ltd. In order to ensure regular supply of raw materials and patronage for finished goods, X Ltd. through its wholly owned subsidiary, X Investments Ltd. acquires on 31st March, 2015, 51% of equity capital of Y Ltd. for ₹ 150 crores and 76% of equity capital of Z Ltd. for ₹ 300 crores. X Investments Ltd. was floated by X Ltd. in 2008-09 from which date it was wholly owned by X Ltd.

The following are the Balance Sheets of the four companies as on 31st March, 2015:

(₹ in crores)

	X Ltd.		X Investments Ltd.		Y Ltd.		Z Ltd.	
(₹ in crores)	₹		₹		₹		₹	
Share Capital:								
Equity (Fully paid) ₹ 10 each	250		50		100		150	
Reserves and Surplus	750	1,000	200	250	150	250	200	350
Loan Funds:								
Secured	150		-		50		200	
Unsecured	100	250	500	500	100	150	150	350
Total Sources		**1250**		**750**		**400**		**700**
Fixed Assets:								
Cost	600		-		150		300	
Less: Depreciation	350	250	-	-	70	80	170	130
Investments at cost in Equity Shares, fully paid								
X Investments Ltd.		50		-		-		-
Y Ltd.		-		150		-		-
Z Ltd.		-		300		-		-
Other Companies								
(Market Value ₹ 1160 Cr.)		-		290		-		-
Net Current Assets:								
Current Assets	1050		10		960		2000	
Current Liabilities	100	950	-	10	640	320	1430	570
		1250		**750**		**400**		**700**

There are no intercompany transactions outstanding between the companies.

You are asked to prepare consolidated balance sheet as at 31st March, 2015 in vertical form.

Solution:

Consolidated Balance Sheet of X Ltd. and its subsidiaries X Investments Ltd., Y Ltd. and Z Ltd. as at 31st March, 2015

(₹ in crores)

Ref No.	Particulars		Note No.	As at 31st March, 2015	As at 31st March, 2014
	I	**EQUITY AND LIABILITIES**			
	1	**Shareholder's Fund**			
		(a) Share capital	1	250	
		(b) Reserves and surplus	2	950	

	2	**Minority Interest (W.N.3)**		206.50	
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**		Nil	
		(a) Long-term borrowings	3	1,250	
	5	**Current Liabilities**			
		(b) Trade payables	4	2,170	
		Total (1+2+3+4+5)		**4,826.50**	
	II	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	5	460	
		(ii) Intangible assets	6	56.50	
		(b) Non-current investments	7	290	
	2	**Current assets**			
		(a) Cash and cash equivalents	8	4020	
		Total (1+2)		**4,826.50**	

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Notes on the Accounts

(₹ in crores)

Note 1. Share Capital	**As at 31st March, 2015**	**As at 31st March, 2014**
Authorized, Issued, Subscribed and paid-up Share capital -		
25 crores Equity share of ₹ 10 each	250	
Total	250	

Note 2. Reserve & Surplus	**As at 31st March, 2015**	**As at 31st March, 2014**
General reserve (750+200)	950	
Total	950	

Note 3. Long-Term Borrowings	**As at 31st March, 2015**	**As at 31st March, 2014**
Loan fund- Secured (150+50+200)	400	
Unsecured (100+500+100+150)	850	
Total	1,250	

Note 4. Trade Payables	**As at 31st March, 2015**	**As at 31st March, 2014**
Sundry Creditors- (100+640+1,430)	2,170	
Total	2,170	

Note No. 5 Tangible Assets	As at 31st March, 2015	As at 31st March, 2014
Fixed assets- Gross block	1,050	
Less: Depreciation	590	
Total	460	

Note 6. Intangible Assets	As at 31st March, 2015	As at 31st March, 2014
Goodwill on consolidation- Y Ltd.	22.50	
Z Ltd.	34.00	
Total	56.50	

Note 7.Non-current Investments	As at 31st March, 2015	As at 31st March, 2014
Investment at cost	290	
(Equity share of other companies- Market value ₹116 crores) Winter Ltd.		
Total	290	

Note 8. Cash and cash equivalents	As at 31st March, 2015	As at 31st March, 2014
Cash at bank – (1,050+10+960+2,000)	4,020	
Total	4,020	

Working Notes:

(A) X Investments Ltd.

(₹ in crores)

(1)	**Analysis of Profits and Share Capital:**				
			Capital Profit	**Revenue Profit**	**Share Capital**
	(i)	Y Ltd.	150.00	-	100.00
		Minority Interest (49%)	73.50	-	49.00
		Share of X Investments Ltd.	76.50	-	51.00
	(ii)	Z Ltd.	200.00	-	150.00
		Minority Interest (24%)	48.00	-	36.00
		Share of X Investments Ltd.	152.00	-	114.00
(2)	**Cost of Control:**		**Y Ltd.**		**Z Ltd.**
	Cost of investments		150.00		300.00
	Less: Paid up value of shares 51.00			114.00	
	Capital profits 76.50			152.00	
			127.50		266.60
	Goodwill on consolidation		22.50		34.00
(3)	**Minority interest**		**Y Ltd.**		**Z Ltd.**
	Share Capital		49.00		36.00
	Capital Profits		73.50		48.00
	Revenue Profits		-		-
			122.50		**84.00**

Name Of the Company: X Investments Ltd.

Consolidated balance Sheet of X Investments Ltd. and its subsidiaries Y Ltd. and Z Ltd. as at 31st Mach, 2015.

(₹ in crores)

Ref No.	Particulars		Note No.	As at 31st March, 2015	As at 31st March, 2014
	I	**EQUITY AND LIABILITIES**			
	1	**Shareholder's Fund**			
		(a) Share capital	1	50.00	
		(b) Reserves and surplus	2	200.00	
	2	**Minority Interest (W.N.3)**		206.50	
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**			
		(a) Long-term borrowings	3	1,000.00	
	5	**Current Liabilities**			
		(a) Trade payables	4	2,070.00	
		Total		3,526.50	
	II	**ASSETS**			
	1	Non-current assets			
		(a) Fixed assets			
		(i) Tangible assets	5	210.00	
		(ii) Intangible assets	6	56.50	
		(b) Non-current investments	7	290.00	
	2	**Current assets**			
		(a) Cash and cash equivalents	8	2,970.00	
		Total		3,526.50	

Note - Relevant items of Assets/ Liabilities are reflected in Balance Sheet and Schedule III. Hence sub-item not having any value for the given illustration is not shown/ represented in Balance Sheet.

Notes to the Accounts (₹ in crores)

Note 1. Share Capital	As at 31st March, 2015	As at 31st March, 2014
Authorized, Issued, Subscribed and paid-up Share capital:-		
5 crores Equity share of ₹10 each	50	
Total	50	

RECONCILIATION OF SHARE CAPITAL

FOR EQUITY SHARE	As at 31st March, 2015		As at 31st March, 2014	
	Nos.	Amount (₹)	Nos.	Amount (₹)
Opening Balance as on 01.04.14 (crores)	5	50		
Add: Fresh Issue (Including Bonus shares, right shares, split shares, share issued other than cash)				
	5	50		
Less: Buy Back of share				
Total	5	50		

Note 2. Reserve & Surplus	As at 31st March, 2015	As at 31st March, 2014
General reserve	200	
Total	200	

Note 3. Long-Term Borrowings	As at 31st March, 2015	As at 31st March, 2014
Loan fund- Secured(50+200)	250	
Unsecured (500+100+150)	750	
Total	1,000	

Note 4. Trade Payables	As at 31st March, 2015	As at 31st March, 2014
Sundry Creditors- (640+1,430)	2 ,070	
Total	2,070	

Note No. 5 Tangible Assets	As at 31st March, 2015	As at 31st March, 2014
Fixed assets- Gross block	450	
Less: Depreciation	240	
Total	210	

Note 6. Intangible Assets	As at 31st March, 2015	As at 31st March, 2014
Goodwill on consolidation- Y Ltd.	22.50	
Z Ltd.	34.00	
Total	56.50	

Note 7.Non-current Investments	As at 31st March, 2015	As at 31st March, 2014
Investment at cost	290	
(Equity share of other companies- Market value ₹116 crores) Winter Ltd.		
Total	290	

Note 8. Cash and cash equivalents	As at 31st March, 2015	As at 31st March, 2014
Cash at bank – (10+960+2,000)	2,970	
Total	2,970	

X Ltd.

(i) Analysis of Profits of X Investments Ltd.:

		Capital Profit	Revenue Profit
	Reserves and Surplus		200
	Minority Interest (X Investments Ltd. being wholly owned subsidiary of X Ltd.)		
(ii)	Minority Interest in X Investments Ltd.		
(iii)	Cost of Control:		
	Cost of investments in X Investments Ltd.		50
	Less: Paid-up value of shares held in X Investments Ltd. by X Ltd.	50	
	Capital Profit		50
	Cost of Control		

DISPOSAL OF SHARES

Illustration 32.

Sale of share Cum – Dividend

The summarized balance sheets of Soubhagya Ltd. and Tirtha Ltd as at 31.03.2015 are as follows-

Liabilities	Soubhagya Ltd. ₹	Tirtha Ltd. ₹	Assets	Soubhagya Ltd. ₹	Tirtha Ltd. ₹
Equity Share Capital (₹10)	1,75,000	50,000	Fixed assets	2,00,000	80,000
Reserves	20,000	5,000	Current Assets	32,000	8,000
Profit & Loss Account – as at	30,000	10,000	Investments at cost:		
01.04.2014			3,000 Shares in Tharini Ltd.	35,000	-
Add: Profit for the year	8,000	8,000			
Add: Dividends from Tharini Ltd	4,000	-			
Less: Dividends paid	-	(5,000)			
Creditors	30,000	20,000			
Total	**2,67,000**	**88,000**	**Total**	**2,67,000**	**88,000**

Soubhagya Ltd acquired 4,000 shares in Tirtha Ltd at ₹20 each on 01.04.2014 and sold 1,000 of them at the same price on 01.01.2015. The sale cum- dividend. An interim dividend of 10% was paid by Tirtha Ltd on 01.10.2014.

Prepare the consolidated Balance Sheet as at 31.03.2015.

Solution:

1. Basic Information

Company Status	Dates	Holding Status
Holding company = Soubhagya Ltd.	Acquisition: 01.04.14	Holding Co: = 60%
Subsidiary = Tirtha Ltd.	Consolidation: 31.03.15	Minority Interest: = 40%

2. Analysis of Reserves and surplus of Tirtha Ltd

(a) **General Reserve**

Balance as on 31.03.2015 ₹5,000

Balance on 01.04.2014 (date of acquisition) ₹ 5,000 **(Capital Profit)**

Transfer during 2014-15 (upto consolidation) (balancing figure) ₹ **NIL** **(Revenue Reserve)**

(b) **Profit and Loss Account**

Balance as on 31.03.2015 ₹13,000

Balance on 01.04.2014 (date of acquisition) ₹13,000 **(Capital Profit)**

Profit for 2014-15 (upto consolidation)	8,000
Less: Interim Dividend	5,000
Revenue Profit	3,000

3. Computation of Cost of Control & Minority Interest

Particulars	Total	Minority Interest	Pre-Acquisition.	Post Acquisition.	
Tirtha Ltd (Holding 60%, minority 40%)				**Gen. Res.**	**P&L A/c**
Equity Capital	50,000	20,000	30,000		
General Reserves	5,000	2,000	3,000		
Profit and Loss A/c	13,000	5,200	6,000		1,800
Minority interest		**27,200**			
Total [Cr.]			**39,000**		
Cost of Investment [Dr.] (Note 1)			**(35,000)**	20,000	42,000
Parent's Balance (Note 1)					
For consolidated balance sheet			**(4,000) (Capital Reserve)**	**20,000**	**43,800**

Note: adjustment for dividend is required since the shares are sold on cum – dividend basis i.e. including dividend. The dividend when declared will be received by the buyer of the shares.

Name of the Company: Soubhagys Ltd. and its subsidiary Tirtha Ltd.

Balance Sheet as at : 31.03.2015

Ref No.	Particulars		Note No.	As at 31.03.15	As at 31.03.14
				(₹)	(₹)
	I	**EQUITY AND LIABILITIES**			
	1	**Shareholders' fund**			
		(a) Share capital	1	1,75,000	
		(b) Reserves and surplus	2	67,800	
	2	**Minority Interest (W.N)**		27,200	
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**		Nil	
	5	**Current Liabilities**			
		(a) Other current liabilities	3	50,000	
		Total		**3,20,000**	
	II	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	4	2,80,000	
	2	**Current assets**			
		(a) Other current assets	5	40,000	
		Total		**3,20,000**	

Workings: (₹)

1. Share capital	**31.03.15**	**31.03.14**
Equity Share Capital	1,75,000	
Total	**1,75,000**	

2. Reserve and Surplus	31.03.15	31.03.14
General Reserve	20,000	
Profit & Loss A/c Capital Reserve	43,800	
Total	**67,800**	

3. Other current liabilities	31.03.15	31.03.14
Current Liabilities (30,000 + 20,000)	50,000	
Total	**50,000**	

4. Tangible Assets	31.03.15	31.03.14
Other Fixed Assets (2,00,000+80,000)	2,80,000	
Total	**2,80,000**	

5. Other Current Assets	31.03.15	31.03.14
Current Assets (32,000 + 8,000)	40,000	
Total	**40,000**	

Sale & Subsequent Purchase of shares in subsidiary company

Acquisition and Disposal of Shares in subsidiary

Illustration 33.

Abhi Ltd acquired 60% of Bob Ltd on 01.04.2013 for ₹80,000 (Nominal Value ₹60,000) and 90% of Chand Ltd on 01.04.2012 for ₹55,000 (Nominal Value ₹45,000).

On 30.09.2014, 15% of Chand Ltd was sold for ₹8,000 and 15% of Bob Ltd was further acquired for ₹17,000.

The following were the profit & Loss Account balance on different dates –

Company / Dates	01.04.2012	01.04.2013	01.04.2014	31.03.2015
Bob Ltd	12,000	15,000	40,000	90,000
Chand Ltd	8,000	20,000	30,000	(10,000)

Assuming that there was no other balance in Reserves, find out:

1. Goodwill / Capital reserve on Consolidation.
2. Current Profit on the different relevant dates for the consolidated Balance Sheet as at 31.03.2013, 31.03.2014 and 31.03.2015
3. Minority interest on these dates.

Solution:

A. **FOR CONSOLIDATION ON 31.03.2013**

1. **Basic Information**

Company	Share of Abhi	Minority Interest	Date of Acquisition
Bob Ltd	(No Acquisition on 31.03.2013)		N .A
Chand Ltd	90%	10%	01.04.2012

2. **Analysis of Profit & Loss Account of Subsidiaries – Chand Ltd**

Balance on 31.03.2013 ₹20,000

As on 01.04.2012 ₹8,000 (Date of Acquisition) **Capital Profits**

Profit for 2012-13 ₹12,000 (balancing figure) **Revenue Profit**

3. **Consolidation of Balances**

Particulars	Total	Minority Interest	Pre-Acquisition	Post Acqn P&L A/c-
Chand Ltd (Holding 90%, Minority 10%)				
Equity Capital	50,000	5,000	45,000	
Profit and Loss A/c	20,000	2,000	7,200	10,800
Minority Interest		**7,000**		
Total [Cr]			**52,200**	**10,800**
Cost of Investment [Dr.]			**(55,000)**	
For Consolidated Balance sheet			**2,800 (Goodwill)**	

B. **FOR CONSOLIDATION ON 31.03.2014**

1. **Basic Information**

Company	Share of Abhishek	Minority Interest	Date of Acquisition
Bob Ltd	60%	40%	01.04.2013
Chand Ltd	90%	10%	01.04.2012

2. **Analysis of Profit & Loss Account of subsidiaries**

Bob Ltd.,

As on 31.03.2014 ₹40,000

01.04.13 ₹**15,000** (DOA) **Capital**

Profit for ₹25,000 2013 – 14 Revenue

Chand Ltd.

As on 31.03.2014 ₹30,000

01.04.12 ₹ **8,000** (DOA) **Capital**

Profit for ₹ **22,000** 12 – 13 & 2013 – 14 **Revenue**

3. **Consolidation of Balances**

Particulars	Total	Minority Interest	Pre-Acquisition	Post Acqn P&L A/c-
Bob Ltd (Holding 60%, Minority 40%)				
Equity Capital	1,00,000	40,000	**60,000**	
Profit and Loss A/c	40,000	16,000	**9,000**	15,000
Minority Interest		**56,000**	**69,000**	**15,000**
Chand Ltd (Holding 90%, Minority 10%)				
Equity Capital	50,000	5,000	45,000	19,800
Profit and Loss A/c	30,000	3,000	7,200	
Minority Interest		**8,000**	**52,200**	**19,800**
Total [Cr]			**1,21,200**	**34,800**
Cost of Investment [Dr.] (₹80,000 + ₹55,000)			(1,35,000)	
For Consolidated Balance sheet			**13,800 (Goodwill)**	

C. FOR CONSOLIDATION ON 31.03.2015

1. Basic Information

Company	Share of Abhi Ltd	Minority Interest	Date of Acquisition
Bob Ltd	60% + 15% (Acquired on 30.09.14) = 75%	25%	01.04.2013
Chand Ltd	90% - 15% (Sold on 30.09.14) = 75%	25%	01.04.2012

2. Analysis of Profit & Loss account of subsidiaries

(a) **Chand Ltd**

As on 31.03.2015 (₹10,000)

01.04.12 (DOA) ₹ **8,000 Capital** — Profit for 12 – 13, 13 – 14 and 14- 15 **(₹18,000) Revenue**

(b) **Bob Ltd**

As on 31.03.2015 (₹90,000)

01.04.13 (DOA) ₹**15,000** Capital — Profit for 13 – 14, 14 – 15 **(₹ 75,000)**

- 2013 -14 **25,000**: for 60% Revenue; for 15% Capital
- 2014 – 15 **50,000**
  - 01.04.14 to 30.09.14 **25,000**: for 60% Revenue; for 15% Capital
  - 01.10.14 to 31.03.15 **25,000**: Revenue; Capital

					Total
Minority Int.(25%)	3,750	6,250	6,250	6,250	22,500
Group Interest (75%)					
Pre	75% = 11,250	15% = 3,750	15% = 3,750	-	18,750
Post	-	60% = 15,000	60% = 15,000	75%= 25,000	55,000

3. Consolidation of Balances

Particulars	Total	Minority Interest	Pre-Acquisition	Post Acqn P&L A/c-
Bob Ltd (Holding 75%, Minority 25%)				
Equity capital	1,00,000	25,000	75,000	
Profit and Loss A/c	90,000	22,500	18,750	55,000
Minority Interest		**47,500**	**93,750**	**55,000**
Chand Ltd (Holding 75%, Minority 25%)				
Equity Capital	50,000	12,500	37,500	
Profit and Loss A/c	(10,000)	(2,500)	6,000	(13,500)
Minority Interest		**10,000**	**43,500**	**(13,500)**
Total [Cr.]			**1,37,250**	
Cost of Investment [Dr.] (₹97,000 + ₹48,000)			**(1,45,000)**	
For Consolidated Balance Sheet			**7,750 (Goodwill)**	

Note:

1. Adjusted Cost of Investment

Particulars	**Bob**	**Chand**
Cost of Investment (as at 31.03.2013)	80,000	55,000
Add: Acquisition of 15% Share Capital of Bobby	17,000	-
Less: Sale of 15% Share Capital of Chand (₹42,000 x 15% / 90%)	-	(7,000)
Adjusted cost of Investment (as at 31.03.2015)	**97,000**	**48,000**

DISPOSAL OF SHARES IN SUBSIDIARY – GAIN / LOSS

Illustration 34.

Rupmati Ltd owns 80% of voting power of Srimathy Ltd, its only investment, acquired on 01.04.2014 for ₹70,000. The net assets of Srimathy Ltd on 01.04.2014 was ₹1,00,000. On 01.10.2015, the investment in Srimathy Ltd was sold for ₹ 1,80,000. The Net Assets of Srimathy Ltd on 31.03.2015 and 30.09.2015 were ₹1,50,000 and ₹1,80,000, respectively the difference representing the profit for the period. Compute the gain/ Loss on disposal of the subsidiary. Determine the gain or loss if the sale consideration was ₹1,10,000 and the shares were sold on 31.03.2015.

Solution:

1. Cost of Control

Particulars	₹
Share in Net Assets as on date of acquisition (₹1,00,000 x 80%) Less: Cost of Investment	80,000 (70,000)
Capital Reserve	**10,000**

2. Gain / Loss on disposal of investment in Subsidiary

Particulars	**01.10.2015**	**31.03.2015**
Sale Consideration Less: Share in Net Assets as on date of sale (1,80,000 x 80%) / (1,50,000 x 80%)	1,80,000 (1,44,000)	1,10,000 (1,20,000)
Transfer to Profit and Loss Account	36,000	10,000
	Gain	Loss

FOREIGN SUBSIDIARY – INTEGRAL VS NON – INTEGRAL OPERATIONS

Illustration 35.

The draft balance Sheets of A Ltd. and its American subsidiary B Inc. as at 31.03.2015 are as under –

Liabilities	A Ltd	B Inc.	Assets	A Ltd	B Inc.
	₹	US $		₹	US $
Share Capital in Equity shares	30,00,000	30,000	Fixed assets	18,00,000	20,000
Profit & Loss Account	20,00,000	40,000	Investments in B	17,00,000	-
Loan Funds	13,00,000	20,000	Stocks	12,00,000	30,000
Trade Creditors	6,00,000	10,000	Debtors	24,00,000	60,000
Provision for Taxation	10,00,000	20,000	Cash and Bank	8,00,000	10,000
Total	79,00,000	1,20,000	Total	79,00,000	1,20,000

1. A Ltd. acquired 80% of shares in B Inc. on 01.04.2011, when the P & L A/c showed a balance of $20,000.
2. Exchange rates per $ prevalent dates were: 01.04.2011: ₹30, 01.04.2014 = ₹ 36 : 31.03.2015: ₹42.
3. A Ltd decided to amortise goodwill, if any, over a period of eight years.
4. Prepare the consolidated Balance shaeet of A Ltd and its subsidiary at 31.03.2015.

Solution:

1. Basic information

Company Status	Dates	Holding Status
Holding Company = A Ltd.	Acquisition: 01.04.2011	Holding Company = 80%
Subsidiary = B Inc.	Consolidation: 31.03.2015	Minority Interest = 20%

1. **Analysis of Profit and Loss Account of B Inc. (for Translation Purposes)**

Balance on 31.03.2015 $40,000

01.04.2011 (Acquisition) **$20,000** Addition between 01.04.11 to 31.03.15 **$20,000**

Capital (balancing figure) **Revenue**

Translation into ₹

Particulars	Pre Acquisition reserve	Post Acquisition Reserve	Total
In American Dollar Conversion rate Per $ In Indian ₹	20,000 30 (date of Acqn.) 6,00,000	20,000 (30 + 42)/2 = 36 (Average rate) 7,20,000	40,000 13,20,000

2. **Translation of B Inc's Balance sheet into Indian Rupees**

Particulars			Integral Operations			Non – Integral Operations		
	Debit ($)	**Credit ($)**	**₹ per $**	**Debit (₹)**	**Credit (₹)**	**₹ per $**	**Debit (₹)**	**Credit (₹)**
Share Capital		30,000	30		9,00,000	30		9,00,000
Reserves		40,000	WN 2		13,20,000	WN 2		13,20,000
Loan Funds		20,000	42		8,40,000	42		8,40,000
Creditors		10,000	42		4,20,000	42		4,20,000
Taxation		20,000	42		8,40,000	42		8,40,000
Fixed Assets	20,000		30	6,00,000		42	8,40,000	
Stock in Trade	30,000		42	12,60,000		42	12,60,000	
Debtors	60,000		42	25,20,000		42	25,20,000	
Cash in Bank	10,000		42	4,20,000		42	4,20,000	
Total	**1,20,000**	**1,20,000**		**48,00,000**	**43,20,000**		**50,40,000**	**43,20,000**
Exch. Rate Gain					**4,80,000**			**-**
Translation reserve					**-**			**7,20,000**
Total				**48,00,000**	**48,00,000**		**50,40,000**	**50,40,000**

3. **Analysis of Reserves & Surplus on B Inc. (for Consolidation Purposes)**

(a) **Profit & Loss Account:** Balance on 31.03.2015 ₹13,20,000

As on date of Acquisition — 01.04.2011 ₹**6,00,000** — **Capital Profits**

Acquisition to consolidation — Profit between 01.04.11 to 31.03.15 ₹ **7,20,000** (balancing figure) **Revenue**

(b) **Exchange Gain (Only for Integral Operation) = ₹4,80,000 = Revenue Profit**

4. **Consolidation of Balances**

Particulars	Integral Operations				Non Integral Operations				
	Total	**Minority Interest**	**Pre. Acqn.**	**Post. Acqn. P& L A/c**	**Total**	**Minority Interest**	**Pre. Acqn**	**Post. Acqn.**	
								P& L A/c	**Trams. Res.**
Equity Capital	9,00,000	1,80,000	7,20,000		9,00,000	1,80,000	7,20,000		
Profit & Loss A/c	13,20,000	2,64,000	4,80,000	5,76,000	13,20,000	2,64,000	4,80,000	5,76,000	5,76,000
Exchange. Rate Gain	4,80,000	96,000		3,84,000	-	-			
Trans. Reserve					7,20,000	1,44,000			
Sub Total		5,40,000	12,00,000	9,60,000		5,88,000	12,00,000		
Cost of Investment Part's balances			(17,00,000)	20,00,000			(17,00,000)	20,00,000	
Consolidated Balance		5,40,000	(5,00,000) (Goodwill)	29,60,000 (2,00,000)		5,88,000	(5,00,000) (Goodwill)	25,76,000 (2,00,000)	5,76,000
Goodwill Already Amortized			2,00,000				2,00,000		
For CBS		5,40,000	(3,00,000)	27,60,000		5,88,000	(3,00,000)	23,76,000	5,76,000

Name of the Company: A Ltd. and its subsidiary B Ltd.

Balance Sheet as at : 31.03.2015

				Integral		Non Integral	
Ref No.	**Particulars**		**Note No.**	**As at 31.03.15**	**As at 31.03.14**	**As at 31.03.15**	**As at 31.03.14**
				(₹)	(₹)	(₹)	(₹)
	I	**EQUITY AND LIABILITIES**					
	1	**Shareholders' fund**					
		(a) Share capital	1	30,00,000		30,00,000	
		(b) Reserves and surplus	2	27,60,000		33,36,000	
	2	**Minority Interest (W.N 4)**		5,40,000		5,88,000	
	3	**Share application money pending allotment**		Nil		Nil	
	4	**Non-current liabilities**		Nil		Nil	
	5	**Current Liabilities**					
		(a) Short-term borrowings	3	21,40,000		21,40,000	
		(b) Trade payables	4	10,20,000		10,20,000	
		(c) Short-term provisions	5	18,40,000		18,40,000	
		Total		**1,12,20,000**		**1,12,20,000**	
	II	**ASSETS**					
	1	**Non-current assets**					
		(a) Fixed assets					
		(i) Tangible assets	6	24,00,000		24,00,000	
		(ii) Intangible assets	7	3,00,000		3,00,000	
	2	**Current assets**					
		(a) Inventories	8	24,60,000		24,60,000	
		(b) Trade receivables	9	49,20,000		49,20,000	
		(c) Cash and cash equivalents	10	12,20,000		12,20,000	
		Total		**1,12,20,000**		**1,12,20,000**	

Workings:

	Integral		Non Integral	
1. Share capital	**31.03.15**	**31.03.14**	**31.03.15**	**31.03.14**
Equity Share Capital	30,00,000		30,00,000	
Total	30,00,000		30,00,000	

	Integral		Non Integral	
2. Reserve and Surplus	**31.03.15**	**31.03.14**	**31.03.15**	**31.03.14**
Profit & Loss A/c	27,60,000		27,60,000	
Foreign Exchange Translation Reserve	-		5,76,000	
Total	**27,60,000**		**33,36,000**	

	Integral		Non Integral	
3. Short Term Borrowings	**31.03.15**	**31.03.14**	**31.03.15**	**31.03.14**
Loan Fund (13,00,000 + 8,40,000)	21,40,000		21,40,000	
Total	21,40,000		21,40,000	

	Integral		Non Integral	
4. Trade Payables	**31.03.15**	**31.03.14**	**31.03.15**	**31.03.14**
Creditors	10,20,000		10,20,000	
Total	**10,20,000**		**10,20,000**	

	Integral		Non Integral	
5. Short Term Provisions	**31.03.15**	**31.03.14**	**31.03.15**	**31.03.14**
Taxation	18,40,000		18,40,000	
Total	**18,40,000**		**18,40,000**	

	Integral		Non Integral	
6. Tangible Assets	**31.03.15**	**31.03.14**	**31.03.15**	**31.03.14**
Tangible Assets	24,00,000		24,00,000	
Total	**24,00,000**		**24,60,000**	

	Integral		Non Integral	
7. Intangible Assets	**31.03.15**	**31.03.14**	**31.03.15**	**31.03.14**
Goodwill	3,00,000		3,00,000	
Total	**3,00,000**		**3,00,000**	

	Integral		Non Integral	
8. Inventories	**31.03.15**	**31.03.14**	**31.03.15**	**31.03.14**
Stock	24,60,000		24,60,000	
Total	**24,60,000**		**24,60,000**	

	Integral		Non Integral	
9. Trade receivables	**31.03.15**	**31.03.14**	**31.03.15**	**31.03.14**
Debtors	49,20,000		49,20,000	
Total	**49,20,000**		**49,20,000**	

	Integral		Non Integral	
10. Cash and cash equivalents	**31.03.15**	**31.03.14**	**31.03.15**	**31.03.14**
Cash	12,20,000		12,20,000	
Total	**12,20,000**		**12,20,000**	

FOREIGN SUBSIDIARY – INTEGRAL OPERATIONS

Illustration 36.

The following summarized Balance Sheets as on 31.03.2015 are given – (₹ in '000s)

Liabilities	AA Ltd	BB Ltd	CC Ltd	Assets	AA Ltd	BB Ltd	CC Ltd
	₹	₹	Ts.		₹	₹	₹
Share Capital (100)	2,000.00	500.00	500.00	Fixed Assets	1600.00	500.00	600.00
Reserves & surplus	600.00	250.00	350.00	Investment In BB	472.50	-	-
Loan from BB (incl. Interest)	225.00	-	-	Investment in CC	525.00	-	-
				Loan – AA	-	200.00	-
Bank Overdraft	-	140.00	-	Loan – others	45.00	-	30.00
Sundry Creditors	240.00	210.00	160.00	Cash at Bank	120.00	16.00	60.00
				Other Current assets	302.50	384.00	320.00
Total	3065.00	1100.00	1010.00	Total	3065.00	1100.00	1010.00

Additional Information:

1. CC Ltd. is a Tanzanian Company, and the amount expressed above is in Tanzanian Shilling.
2. The reserves of the various companies as on 01.04.2015 are: AA Ltd- ₹4,30,000; BB Ltd - ₹2,00,000; CC Ltd – Ts.1,70,000.
3. BB Ltd had advanced the loan to AA Ltd on 01.04.2015.
4. On 01.10.2015, BB Ltd had issued fully paid Bonus Shares at the rate of one Share for every Four held. On the same date, a dividend of 10% was paid for the year 2014-15
5. AA Ltd had purchased 4,375 Shares in BB Ltd on 01.07.2015, but had disposed of 375 shares on 31.01.2016 at ₹140, the sale proceeds being credited to the concerned investment Account which so far has only this entry in addition to that made on the acquisition of shares.
6. 3,500 shares were acquired in CC Ltd on 30.09.2015 at ₹150 per share.
7. Stock of CC Ltd include goods costing ₹10,000 sent by A Ltd at the invoice value of ₹12,500 which were recorded in the books of CC Ltd at Ts. 11,625.
8. There has been no movement in the Fixed Assets or Share Capital of CC Ltd during the year.
9. CC Ltd paid in January 2016 an interim dividend at 6% p.a. for six months. CC Ltd remitted the amount due to AA Ltd when ₹100 was equal to Ts. 94.
10. The exchange rates between India and Tanzania during 2015-16 were as follows- 01.04.2015 - ₹100 = Ts. 92; 30.09.2015 - ₹100 = Ts. 90; 31.03.2016 - ₹100 = Ts. 93. Average ₹100 = Ts. 91.

Prepare the consolidated balance Sheet of the Group.

Solution:

1. **Basic Information**

Company Status	Date of Acquisition		Holding Status	
Holding company = AA Ltd	01.07.15 Purchase	4,375 shares	Held by AA	Minority
Subsidiary 1 = BB Ltd	31.03.16 Sales	(375) shares	80%	20%
Subsidiary 2 = CC Ltd	31.03.16 Balance	4,000 shares	70%	30%
	30.09.2015	3,500 shares		

Date of consolidation = 31.03.2016

Shareholding in BB Ltd. Lot 1 Purchase 3,500 shares + Bonus at 1 for 4 held (3,500 x ¼) 875 Shares – Sale 375 Shares = 3,500 shares.

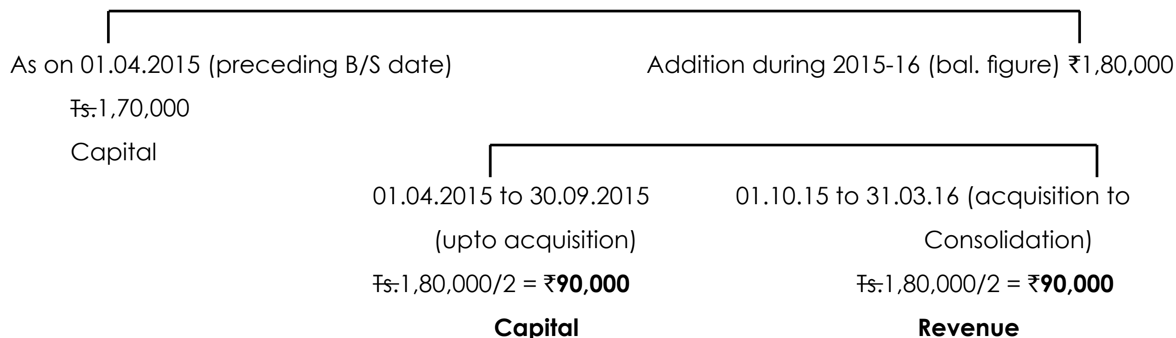
2. **Translation of CC Ltd's Balance sheet in to Indian Rupees**

Particulars	**Debit (Ts.)**	**Credit (Ts.)**	**(Ts.) per ₹100**	**Debit (Ts.)**	**Credit (Ts.)**
Share Capital		5,00,000	90		5,55,555
Reserves & Surplus		3,50,000	WN		3,87,790
Creditors		1,60,000	93		1,72,043
Fixed Assets	6,00,000		90	6,66,667	
Investment	30,000		90	33,333	
Cash in Bank	60,000		93	64,516	
Stock in Trade supplied by A	11,625		93	12,500	
Other Current Assets (Total 3,20,000 – Stock from A 11,625)	3,08,375			3,31,586	
Total	**10,10,000**	**10,10,000**		**11,08,602**	**11,15,388**
Loss on Exch. Rate difference				**6,786**	
Total				**11,15,388**	**11,15,388**

Working Note:

Translation and Analysis of Reserves

Balance as per Balance Sheet ₹3,50,000



Total Pre Acquisition reserves = 1,70,000 + 90,000 = Ts.2,60,000; Total acquisition Reserve = ₹90,000

Conversion into ₹

Particulars	**Pre Acquisition Reserve**	**Post Acquisition Reserve**	**Total**
In Tanzanian Shilling	2,60,000	90,000	3,50,000
Conversion Rate per ₹100	90 (Date of Acqn.)	91 (Average Rate)	N. A.
In Indian ₹	2,88,889	98,901	3,87,790

3. **Analysis of reserves and Surplus of Subsidiaries**

CC Ltd.

Balance on 31.03.2016 ₹3,87,790

Capital Profit	Revenue Reserve
₹2,88,889	₹98,901
(from 2 above)	(from, 2 above)

BB Ltd

Balance on 31.03.2016	₹ 2,50,000
Add: Interest	₹ 25,000
Corrected Balance	₹ 2,75,000

01.04.15 (Prev. b/s) 2,00,000

Bonus (1,00,000)

Dividend (40,000)

Capital 60,000

Profit for 2015-16 (b/f) 2,15,000

01.04.15 – 30.06.15	01.07.15 - 31.03.16
(upto acqn.)	(acqn. To cons.)
(2,15,000 x 3/12)	(2,15,000 x 9/12)
₹53,750	**₹1,61,250**
Capital	**Revenue**

Total capital Profit = 60,000 + 53,750 = ₹1,13,750;

Revenue Profit = ₹1,61,250

Note: Bonus for BB Ltd: ₹5,00,000 x 1/5 = ₹1,00,000; Dividend: 10% of (₹5,00,000 - ₹1,00,000) = ₹40,000; Interest: Balance as per AA Ltd ₹2,25,000 Less Balance as per BB Ltd's books ₹2,00,000 = ₹25,000

4. **Consolidation of Balances**

Particulars	**Total**	**Minority Interest**	**Pre- Acqn.**	**Post Acqn. Reserves**
BB Ltd (Holding 80%, Minority 20%)				
Equity Capital	5,00,000	1,00,000	4,00,000	
Reserves and surplus	2,75,000	55,000	91,000	1,29,000
Minority interest		**1,55,000**		
CC Ltd (holding 70%, Minority 30%)				
Equity Capital	5,55,555	1,66,666	3,88,889	69,231
Reserves and surplus	3,87,790	1,16,337	2,02,222	(4,750)
Exchange Rate Loss	(6,786)	(2,036)		
Minority Interest		**2,80,967**		
Total [Cr]		**4,35,967**	**10,82,111**	**1,93,481**
Cost of Investment [Dr.] (Note)			(9,61,830)	5,64,330
Parent's Balance (Note 1)				(2,500)
Stock Reserve (₹12,500 - ₹10,000) (Note 2)				
For consolidated Balance sheet		**4,37,967**	**1,20,281 (Cap. Res.)**	**7,55,311**

Note:

1. **Parent's P & L A/c balance and Cost of Investment**

Particulars	Investment		P & L A/c
	BB Ltd	CC Ltd	
Balance as per balance sheet	4,72,500	5,25,000	6,00,000
Add: Sale proceeds wrongly credited in full (375 shares x ₹140)	52,500	-	52,500
Less: Pre acquisition dividend for 2014-15 (BB Ltd 3500Sh. × ₹100 x 10%)	(35,000)	-	(35,000)
Less: Pre acquisition dividend for 01.01.15 to 30.09.15 – CC Ltd: 3500 shares x ~~Rs.~~100 per Share x 6% x 6/12 months x ₹100 / ~~Rs.~~94		(11,170)	(11,170)
Adjusted Cost of Investment	**4,90,000**	**5,13,830**	
Less: Cost of BB Ltd shares Sold [375/4375 (incl. Bonus)] x ₹4,90,000	(42,000)	**-**	(42,000)
For Consolidation of Balance	**4,48,000**	**5,13,830**	**5,64,330**

Total cost of Investment = ₹4,48,000 + ₹5,13,830 = 9,61,830

2. Stock Reserve: Stock Reserve i.e. unrealized profits on closing Stock have been eliminated in full from group reserve as it relates to downstream transaction.

   Name of the Company: AA Ltd. and its two subsidiaries BB Ltd. and CC Ltd.

   Balance Sheet as at : 31.03.2016

(₹ in thousands)

Ref No.		Particulars	Note No.	As at 31.03.16	As at 31.03.15
				(₹)	(₹)
	I	**EQUITY AND LIABILITIES**			
	1	**Shareholders' fund**			
		(a) Share capital	1	20,00,000	
		(b) Reserves and surplus	2	8,75,592	
	2	**Minority Interest (W.N 4)**		4,37,967	
	3	**Share application money pending allotment**		Nil	
	4	**Non-current liabilities**		Nil	
	5	**Current Liabilities**			
		(a) Trade payables	3	7,62,043	
		Total		**40,73,602**	
	II	**ASSETS**			
	1	**Non-current assets**			
		(a) Fixed assets			
		(i) Tangible assets	4	27,66,667	
	2	**Current assets**			
		(a) Cash and cash equivalents	5	2,00,516	
		(b) Short-term loans and advances	6	78,333	
		(c) Other current assets	7	10,28,086	
		Total		**40,73,602**	

Workings:

1. Share capital	**31.03.16**	**31.03.15**
Equity Share Capital	20,00,000	
Total	**20,00,000**	

2. Reserve and Surplus	**31.03.16**	**31.03.15**
Capital Reserve	1,20,281	
Profit & Loss A/c	7,55,311	
Total	**8,75,592**	

3. Trade Payables	**31.03.16**	**31.03.15**
Creditors (2,40,000+2,10,000+1,72,043)	6,22,043	
Bank Overdraft	1,40,000	
Total	**7,62,043**	

4. Tangible Assets	**31.03.16**	**31.03.15**
Tangible Fixed Assets (16,00,000+5,00,000+6,66,667)	27,66,667	
Total	**27,66,667**	

5. Cash and Cash Equivalent	**31.03.16**	**31.03.15**
Bank (1,20,000+16,000+64,516)	2,00,516	
Total	**2,00,516**	

6. Short-term loans and advances	**31.03.16**	**31.03.15**
Loans Receivable (45,000+33,333)	78,333	
Total	**78,333**	

7. Other Current Assets	**31.03.16**	**31.03.15**
Other Current Assets (3,03,5000+3,84,000+3,44,086-2,500) Stock Reserve	10,28,086	
Total	**10,28,086**	

3.4 TREATMENT OF INVESTMENT IN ASSOCIATE IN CONSOLIDATED FINANCIAL STATEMENT (AS-23)

1. **Associate:** An Associate is an enterprise in which the Investor has **significant influence** and which is neither a subsidiary nor a joint Venture of the Investor.
2. **Investor:** An Investor is an enterprise or person who has a significant influence over the Associate.
3. **Equity** is the **Residual Interest** in the assets of an enterprise after deducting all its liabilities**.**
4. **Equity Method** is a method of accounting with the following features-

   (a) **Acquisition:** Investment is initially recorded at **cost**, identifying any goodwill / Capital Reserve arising at the time of acquisition.

   (b) **Post Acquisition Profits:** The carrying amount of the Investment is **adjusted** to recognise the **investor's Share** of Profits or Losses of the investee (i.e. the Associate) after the date of acquisition.

(c) **Consolidated P & L Account**: The consolidated Statement of profit and Loss reflects the Investor's Share of the results of operations of the investee (i.e. the Associate).

(d) **Distributions:** Distributions received from an Investee **reduce** the carrying amount of the investment.

The major principles used in application of the Equity Method:

I. **Principles of AS – 21[para 10]:** The application of the Equity Method is similar to the consolidation procedures set out in AS – 21. The broad concepts underlying the consolidation procedures used in the acquisition of a subsidiary are adopted on the acquisition of an investment in an Associate.

II. **Relevant Date [para 11]:** An Investment in an Associate is accounted for under the Equity Method from the date on which it falls within the definition of an Associate.

III. **Goodwill / Capital Reserve [para 12]:**

(a) When cost of Acquisition > Share of the Equity; it is treated as Goodwill

(b) When cost of Acquisition < Share of the Equity, it is treated as Capital Reserve

(c) Such Goodwill / Capital Reserve arising on the acquisition of an Associate is included in the carrying Amount of Investment in the Associate and **disclosed separately**.

IV. **Elimination of Unrealised profits/Losses [para 13]:** Unrealised profits and Losses resulting from transactions between the investor (or its consolidated Subsidiaries) and the associate are **eliminated** to the extent of the investor's interest in the Associate. However, Unrealised Losses should not be eliminated if and to the extent, the cost of the transferred asset cannot be recovered.

V. **Arrears of Fixed Cumulative Dividend to be provided [para 17]:** If an Associate has outstanding cumulative preference Shares held outside the Group, the Investor should compute its Share of profits or Losses after adjusting for preference Dividends, whether or not the dividends have been declared.

VI. **Provision for Proposed Dividend [ASI – 16]:** Carrying amount of investment is reduced by the distributions (dividends received) from Associates. However, when the Associate has made a provision for proposed Dividend in its Financial Statements, the investor's Share from the Associate should be computed **without** taking into consideration the proposed Dividend.

VII. **Changes in share of Equity without routing through P & L [para 6 and ASI – 17]:** Where adjustments are required for items which are reflected in the Associate's P & L, the same should be reflected in the carrying amount of investment, without routing it through the Investor's consolidated P & L Account.

VIII. **Excessive Losses = Nil value of Investment [para 17]:** If an investor's share of Losses of an Associate **equals or exceeds the carrying amount** of the investment, the Investor ordinarily **discontinues** recognising its share of further losses and the investment is reported at **Nil Value.**

IX. **Additional Losses due to Investor's obligations [para 18]:** Additional losses are provided for to the extent that the Investor has incurred obligations or made payments on behalf of the Associate to satisfy obligations of the Associate that the Investor has guaranteed or to which the Investor is otherwise committed.

X. **Subsequent profits & Prudence principle [para 18]:** If the Associate subsequently reports profits, the Investor resumes including its share of those profits only after its share of the profits equals the share of net losses that have not been recognised. See point VI above.

XI. **Subsidiary's CFS to be used [para 19]:** Where an Associate presents Consolidated Financial statements, the Results and Net Assets to be taken into account are those reported in that Associate's CFS.

XII. **Permanent Decline in value [para 20]:** The Carrying Amount of investment in an Associate should be reduced to **recognise a decline, other than temporary**, in the value of the Investment, such reduction being determined and made for each Investment **individually**.

XIII. **Dates of Reporting [para 14 – 15]:** Generally, the Associate uses the same reporting date as that of the Investor, so that consolidation procedures/ equity method application is made simple.

XIV. **Uniform Accounting Policies [para 16]:** when an associate uses different accounting policies (from that of the investors), appropriate adjustments are made to its (the Associate's) Financial statements. If it is not practicable to do so, that fact is disclosed along with a brief description of the difference between the accounting policies.

3.5 TREATMENT OF INVESTMENT IN JOINT VENTURES IN CONSOLIDATED FINANCIAL STATEMENT (AS-27)

A. Jointly controlled Operations (JCO)

a. **Meaning: JCO** is an arrangement where two or more Ventures combine their operations, resources and expertise, to manufacture, market and distribute, a product **Jointly.**

b. **Example(s):** Different parts of the manufacturing process of a product (say Aircraft) are carried out by each of the venturers, each venture bearing its own costs and sharing the revenue from the sale of the aircraft, such share being determined in accordance with the contractual arrangement.

c. **Legal Entity:** Not a separate entity.

d. **Creation and Ownership of Assets:** Venturer creates and fully owns the assets.

e. **Books of Account:** Not maintained separately.

f. **Financial Statements:** Not prepared separately.

g. **Recognition Principle in Venture's books:**

In both SFS and CFS –

- Asset it controls and the Liability it incurs
- Expenses incurred by it and its share of Income from the JCO

B. Jointly controlled Assets (JCA)

a. **Meaning: JCA** exists when there is (a) joint control and (b) joint Ownership by the ventures, of one or more assets, which are contributed to/ acquired for and dedicated to the purposed of the JV.

b. **Example(s):**

(i) Oil pipelines jointly controlled and operated by a number of oil production companies, each company uses the pipeline to transport its own products and bears an agreed proportion of the operating expenses;

(ii) Two enterprises jointly control a property, each taking a share of the rents received and bearing a share of the expenses.

c. **Legal Entity:** Not a separate entity.

d. **Creation and Ownership of Assets:** Venture does not fully own the assets, but owns them jointly or there is a common control over the assets.

e. **Books of Account:** Not maintained separately.

f. **Financial Statements:** Not prepared separately.

g. **Recognition Principle in Venture's books: In both SFS and CFS –**

- Share in JCA classified according to the nature of the Asset.
- Direct Liabilities incurred by the Venture
- Share in Joint Liabilities, if any, incurred
- Share of Income & Exps

C. Jointly controlled Entities (JCE)

a. **Meaning: JCE** is a separate entity, whose economic activity is jointly controlled by two or more jointly Ventures as a result of a contractual arrangement**.**

b. Example(s):

(i) When two enterprise combine their activities in a particular line of business by transferring the relevant assets and liabilities in to a JCE;

(ii) When an enterprise establishes a JCE abroad, in conjunction with the Government or other Agency in that country, the JCE jointly controlled by the enterprise & the Government / other Agency.

c. Legal Entity: Separate Legal Entity.

d. Creation and Ownership of Assets: Venture does not own the asset, but owns the interest in the JCE jointly with others leading to common control.

e. Books of Account: Maintained separately.

f. Financial Statements: Prepared separately for applying proportionate consolidation Method.

g. Recognition Principle in Venture's books: In both SFS and CFS –

- **In SFS:** Interest in JCE will be accounted as per AS – 13.
- **In CFS:** Proportionate Consolidation Method will be used. Income, Expenses, Assets or Liabilities will be reflected as **separate line items**.

<table>
<tr><th>Particulars</th><th>Jointly controlled Operations (JCO)</th><th>Jointly controlled Assets (JCA)</th><th>Jointly controlled Entities (JCE)</th></tr>
<tr><td>Contribution/ sale of asset by Venturer to JV</td><td colspan="2">1. Recognize the share of profit or Loss attributable to other Venturers.
2. Recognize fully Loss if there is reduction in NRV of current Asset or Impairment Loss</td><td>In SFS: Fully gain / Loss should be recognised.
In CFS: Principles 1 and 2 given here will apply.</td></tr>
<tr><td>Purchase of asset by venture from JV</td><td colspan="2">1. Recognize the share of profit or Loss when it resells the asset to an independent party.
2. Recognize fully Loss if there is reduction in NRV of current Asset or Impairment Loss.</td><td>In SFS: Fully gain / Loss should be recognised.
In CFS: Principles 1 and 2 given here will apply.</td></tr>
<tr><td>Disclosure Requirements</td><td colspan="3">In SFS as well as CFS:
• List of all Joint Ventures and description of interest in significant Joint ventures
• Proportion of ownership interest, name and country of incorporation or residence in respect of JCE's
• Aggregate amount of the following Contingent Liabilities (unless the probability of loss is remote) disclosed separately – (a) Any contingent Liabilities that the venture has incurred in relation to its interests in JV and its share in each of the contingent Liabilities which have been incurred jointly with other ventures, (b) Its share of the Contingent Liabilities of the JV's themselves for which it is contingently liable; and (c) Those contingent Liabilities that arise because the venturer is contingently liable for the liabilities of the other venturers of a Joint venture.
• Aggregate amount of the following commitments disclosed separately – (a) Any capital commitments of the venturer in relation to its interests in JV's and its share in the capital commitments that have been incurred jointly with other venturers; and (b) Its share of the capital commitments of the joint ventures themselves.
In SFS only: Aggregate amounts of each of the Assets, Liabilities, income and Expenses related to its interests in the JCE's.</td></tr>
</table>

Illustration on Investment in Associates & Joint Ventures

Investment in Associate – Disclosure in Consolidated Balance Sheet

Illustration 37.

Amrit Ltd acquired 25% of shares in Balu Ltd as on 31.03.2014 for ₹6 Lakhs. The Extract Balance Sheet of Balu Ltd as on 31.03.2014 is given below-

Liabilities	₹	Assets	₹
Share Capital	10,00,000	Fixed Assets	10,00,000
Reserves and Surplus	10,00,000	Investments	4,00,000
		Current Assets	6,00,000
Total	**20,00,000**	**Total**	**20,00,000**

Following additional information are available for the year ended 3103.2015 –

1. Amrit Ltd received dividend from Balu Ltd for the year ended 31.03.2014 at 40% from the Reserves.
2. Balu Ltd made a profit After Tax of ₹14 Lakhs for the year ended 31.03.2015.
3. Balu Ltd declared a dividend @ 50% for the year ended 31.03.2012 on 30.04.2015.

Amrit Ltd is preparing consolidated Financial Statements in accordance with AS – 21 for its various subsidiaries.

1. Calculate Goodwill if any on acquisition of Balu Ltd.'s shares.
2. How Amrit Ltd will reflect the value of investment in Balu Ltd in the consolidated Financial Statements?
3. How the dividend received from Balu Ltd will be shown in the consolidated Financial Statements?

Solution:

1. Basic Information

Amrit's stake in Balu Ltd	Nature of Investment in Balu	Date of Consolidation
25% Shares	Associate in terms of AS 23	31.03.2015

2. Calculation of Goodwill

Particulars	₹ Lakhs
Amrit's share in the Equity of Balu Ltd (as at the date of investment) [25% of ₹10 lakhs (Equity Capital ₹5 Lakhs + Reserves ₹5 Lakhs)] **Less:** Cost of Investment	5.00 (6.00)
Goodwill	**(1.00)**

3. Extract of Consolidate Profit and Loss Account of Amrit Ltd for the year ended 31.03.2015

Expenditure	₹ Lakhs	Income		₹ Lakhs
		By Share of Profits from Balu (25% x Profits of ₹14 lakhs)		3.50
		By Dividend from Balu (10 lakhs x 25% invst x 40%)	1.00	
		Less: Transfer to Investment in Balu A/c	(1.00)	Nil

4. **Extract of Consolidated Balance Sheet of Amrit Ltd as at 31.03.2015**

Liabilities	₹ Lakhs	Assets		₹ Lakhs
		Fixed Assets Goodwill		1.00
		Investments		
		Investment in Balu (Cost)	6.00	
		Less: Goodwill on Consolidation	(1.00)	
		Less: Dividend Received	(1.00)	
		Add: Share of Profit for FY 2013-14	3.50	7.50

Note: Dividend declared on 30.04.2016 will not be recognized in consolidated Financial Statements.

Illustration 38:

A Ltd. owned 80% of B Ltd. 35% of C Ltd. and 30% of D Ltd. C Ltd. is jointly controlled entity and D Ltd. is an associate. Balance Sheet of all four companies as on 31.03.2014 are:

(₹ in lakhs)

Particulars	A Ltd.	B Ltd.	C Ltd.	D Ltd.
Liabilities				
Equity Share of ₹1each fully paid-up	1,500	600	1,200	1,200
Retained Earnings	6,000	5,100	5,400	5,400
Creditors	300	450	380	375
Total	7800	6150	6980	6975
Assets				
Fixed Assets	1,500	1,200	2,100	1,500
Investment in B Ltd.	1,200			
Investment in C Ltd.	900			
Investment in D Ltd.	900			
Current Assets	3,300	4,950	4,880	5,475
Total	7800	6150	6980	6975

A Ltd. acquired shares in

(i) B Ltd. many years ago, when the company had retained earnings of ₹780 lakhs.

(ii) C Ltd. at the beginning of the year, when the, company had retained earnings of ₹ 600 lakhs.

(iii) D Ltd. on 01 .04.2013, when the company had. retained earnings of ₹ 600 lakhs.

The balance of goodwill relating to B Ltd. had been written off three years ago. The value of goodwill in C Ltd. remains unchanged.

Prepare the Consolidated Balance Sheet of A Ltd. as on 31.03.2014 as per AS-21, AS-23 and AS-27.

Solution:

Consolidated Balance Sheet of A Ltd. as 31st March, 2014

(₹in lakhs)

	Particulars	Note No.	Amount
I.	**EQUITY AND LIABILITIES**		
	1. Shareholders' Funds		
	(a) Share Capital	1	1,500
	(b) Reserves and Surplus	2	12,480
	2. Share Application money pending allotment		
	3. Minority interest		11,40
	4. Non-current Liabilities		
	5. Current Liabilities		
	(a) Trade Payables	3	883
	Total		16,003
II.	ASSETS		
	1. Non-current Assets		
	(a) Fixed Assets	4	3,435
	(i) Tangible Assets	5	270
	(ii) Intangible Assets	6	2,340
	(b) Non-current Investments		
	2. Current Assets		
	(a) Other current assets	7	9,958
	Total		16,003

[Relevant notes]

Note No: 1. Share Capital

(₹ in lakhs)

Share capital in equity shares	1,500
Total	1,500

Note No: 2. Reserves and Surplus

Retained Earnings (W.N. 2)	12,480
Total	12,480

Note No: 3. Trade Payables

Creditors [300 + 450 + 133 (35% of 380)]	883
Total	883

Note No: 4. Tangible Assets

Fixed Assets [1,500 + 1,200 + (35% of 2,100)]	3,435
Total	3,435

Note No: 5. Intangible Assets

Goodwill (W.N.2)	270
Total	270

Note No: 6. Non-current Investments

Investments in Associates (W.N.4)	2,340
Total	2,340

Note No: 7. Other current assets

Other current assets [3,300 + 4,950 + 1,708 (35% of 4,880)]	9,958
Total	9,958

Working Notes:

1. Computation of Goodwill

B Ltd. (subsidiary)		
Cost of investment		1,200
Less: Paid up value of shares acquired	480	
Share in pre-acquisition profits of B Ltd. (780 x 80%)	624	1,104
Goodwill		96
C Ltd. (Jointly Controlled Entity)		
Cost of Investment		900
Less: Paid up value of shares acquired (35% of 1,200)	420	
Share in pre-acquisition profits of C Ltd. (35% of 600)	210	630
Good Will		270
Note: Jointly controlled entity C Ltd. to be consolidated on proportionate basis i.e. 35% as per AS-27.		

D Ltd. (Associate as per AS-23)		
Cost of Investment		900
Less: Paid up value of shares acquired (30% of 1,200)	360	
Share in pre-acquisition profits of C Ltd. (30% of 600)	180	540
Goodwill		360
Goodwill to be shown in the consolidated B/S		
Goodwill of C Ltd.		270
Goodwill of B Ltd.		96
Less: Goodwill written off of B Ltd.		96
Goodwill		270

2. Consolidated Retained Earnings:

(₹ in lakhs)

A Ltd.	6,000
Share in post acquisition profits of B Ltd: 8C% (5,100 -780)	3,456
Share in post acquisition profits of C Ltd: 35% (5,400 - 600)	1,680
Share in post acquisition profits of D Ltd: 30% (5,400 - 600)	1,440
Less: Goodwill written off	(96)
Total	**12,480**

3. Minority Interest B Ltd:

(₹ in lakhs)

Share Capital (20% of 600)	120
Share in Retained Earnings	1020
Total	**1140**

4. Investment in Associates:

(₹ in lakhs)

Cost of Investments (including goodwill i.e. 360 lakhs)	900
Share of post acquisition profits	1,440
Carrying amount of investment (including good will 360 lakhs)	2,340

Illustration 39:

X has 60% interest in a joint venture with Y, X sold a plant with w. d. v. ₹ 60 lacs for ₹ 80 lacs. Calculate how much profit X should recognize in its books as per AS-27 in case the joint venture is

(i) jointly controlled operation

(ii) jointly controlled asset

(iii) jointly controlled entity

Solution:

According to AS 27, in the case of Jointly Controlled Operations (JCO) and Jointly Controlled Assets (JCA), there are no separate financial statements for the Joint Venture. The venturer may prepare accounts for internal reporting purposes. In JCO, venturers' assets are used. In JCA, the assets are dedicated to the venture. In the case of Jointly Controlled Entity (JCE), there is a separate legal entity for the venture and it operates like any other enterprise.

When X sells the plant to the venture at a profit of ₹20 lacs, the following is the treatment according to AS 27- transactions of the venture with the venture.

	JCO / JCA (₹)	JCE (₹)
X should consider in its Separate Financial Statements (SFS): The extent of profit attributable to the other venturers, i.e. 40% of ₹ 20 lacs	8	
X should consider the full amount of profit in its SFS		20
In the Consolidated Financial Statements (CFS) of X, its share should be eliminated and hence, only the other venturer's profit is considered.	8	8

If the candidate assumes that X sells the plant to a third party, then,

(i) In the case of a JCO, X would have used its own asset for X's own business and that of the venture's. Since it is X's own asset, all the profit of ₹ 20 lacs would be considered in the SFS of X as well as in the CFS of X.

(ii) In the case of JCA, the asset would have been dedicated to the venture. Hence X will recognize its share viz. 60% of ₹ 20 lacs = ₹12 lacs in both the SFS and the CFS.

(iii) In the case of a JCE, the venture considers its interest in the JCE. Hence ₹12 lace will be considered as 'income from investment', since the interest in a JCE is reported as an investment rather than a line item of the individual asset.

3.6 PREPARATION OF GROUP CASH FLOW STATEMENT

The actual cash paid for the subsidiary is shown under the heading 'Acquisitions and Disposals'. It is possible that the purchase consideration will include other forms of payments such as the issue of shares or loan stock and there is no cash flow effect in these cases.

In exchange for the purchase consideration, the group acquires the individual net assets of the subsidiary and goodwill is recognized on acquisition.

The net assets in the closing consolidated Balance Sheet will include those of the newly acquired subsidiary. The preparation of the group cash flow statement must recognize that the movement from opening to closing positions is increased in party by the net assets of the new subsidiary and the amounts relating to that subsidiary are therefore excluded from the cash flow statement.

For example, additions to fixed assets are represented by purchases during the year plus fixed assets of the acquired subsidiary. This is broken down as follows:

Opening + cash purchases + fixed assets of – disposals- depreciation=closing

NBV for additions acquired subsidiary NBV

Only cash purchase for additions are included in the cash flow statement under 'inventive activities'.

Statement of Cash Flows

"The information provided in a statement of cash flows, if used with related disclosures and information in the other financial statements, should help investors, creditors, and others to (a) assess the enterprise's ability to generate positive future net cash flows; (b) assess the enterprise's ability to meet its obligations, its ability to pay dividends, and its needs for external financing; (c) assess the reasons for differences between net income and associated cash receipts and payments; and (d) assess the effects on an enterprise's financial position of both its cash and non-cash investing and financing transactions during the period." - SFAS 95 Statement of Cash Flows, Financial Accounting Standards Board, US.

LEARNING OBJECTIVES

After learning this Chapter, you will be able to understand that—

- When a company earns profit that may not be available in cash. Cash profit and accounting profit are different.
- What is the meaning of 'cash and cash equivalent'?
- How to classify cash flow from operational activities, financing activities and investment activities?
- How to reconcile cash balance of a company?

Importance of Cash flows

Cash flows are crucial to business decisions. Cash is invested in the business and the rationality of such investment is evaluated taking into account the future cash flows it is expected to generate. Economic value of an asset is derived on the basis of its ability to generate future cash flows. Economic value of an asset is given by the present value of future cash flows expected to be derived from the asset.

Profit is an accounting concept. Profit is derived on accrual assumption. Profit and cash flows from operational activities are not the same. Dividend decision is taken on the basis of profit, although it is to be paid in cash. Similarly, debt servicing capacity of a company is determined on the basis of cash flows from operations before interest. Ploughing back of profit is a much talked about source of financing modernisation, expansion and diversification. Unless retained profit is supported by cash, ploughing back is not possible. Thus cash flows analysis is an important basis for making several management decisions.

Meaning of Cash and Cash Equivalent

A cash flow statement explains the reasons for change in the cash and cash equivalent between two financial statement dates. Before we introduce the technique of cash flow analysis, let us learn the meaning of the term 'cash and cash equivalent'.

Cash means cash in hand and balance of foreign currency. Cash equivalent implies bank balance and other risk-free short term investments, and advances which are readily encashable. Cash equivalent means short term

highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value. An investment of short maturity, say three months or less from the date of acquisition is generally considered as cash equivalent. Equity investments are not considered as cash equivalent because of high market risk. Investments in call money market, money market mutual funds, repo transactions, badla transactions, etc., are usually classified as cash equivalents.

Types of Cash flow

Cash Flow Statement explains cash movements under three different heads, namely

- Cash flow from operating activities;
- Cash flow from investing activities;
- Cash flow from financing activities.

Sum of these three types of cash flow reflects net increase or decrease of cash and cash equivalents.

Operating activities are the principal revenue - producing activities of the enterprise and other activities that are not investing and financing. Operating activities include all transactions that are not defined as investing or financing. Operating activities generally involve producing and delivering goods and providing services.

Investment activities are the acquisition and disposal of long term assets and other investments not included in cash equivalents.

Financing activities are activities that result in changes in the size and composition of the owners' capital (including preference share capital in the case of a company) and borrowings of the enterprise.

Elements of operating cash flow

Given below are elements of operating cash flow:

Description of elements of operating cash flow
• Cash receipts from sale of goods and rendering services.
• Cash receipts from royalty, fees, commissions and other revenue.
• Cash payments to suppliers for goods and services.
• Cash payments to and on behalf of employees.
• Cash receipts and cash payments by an insurance enterprise for premiums and claims, annuities and other policy benefits.
• Cash payments and refunds of income taxes unless these are specifically identified as cash flow from financing or investment.
• Cash receipts and payments relating to contracts held for dealing or trading purposes.
• Cash flow arising from dealing in securities when an enterprise holds securities for such purpose.
• Cash advances and loans made by financial institutions including all contracts held for trading purposes which may range from sale licence, export-import quota, any other operating contract. This may not necessarily be a contract relating to derivative instruments.

Elements of cash flow from investment activities

Given below are eight elements of investment cash flow:

Elements of cash flow from investment activities:	
1.	Cash payments for acquisition of fixed assets including intangibles.
2.	Cash receipts from disposal of fixed assets.
3.	Cash payments to acquire shares, warrants or debt instruments of other enterprises and interests in joint venture.
	This does not include an item covered in cash equivalents and items held for dealing or trading purposes.
4.	Cash receipts from disposal of shares, warrants or debt instruments of other enterprises and interests in joint venture.
	This does not include an item covered in cash equivalents and items held for dealing or trading purposes.
5.	Cash advances and loans made to third parties.
	This does not include loans and advances made by financial institutions as these fall under operating cash flow.

6.	Cash receipts from repayments of advances and loans made to third parties. This does not include loans and advances made by financial institutions as these fall under operating cash flow.
7.	Cash payments for future, forward, option and swap contracts.
	This does not include contracts held for dealing or trading purposes or contracts which are classified as financing activities.
8.	Cash receipts from future, forward, option and swap contracts.
	This does not include contracts held for dealing or trading purposes or contracts which are classified as financing activities.

Classification of derivative transactions –

Derivative Transactions which are for Heading	Speculative contracts
• Of Operating transactions like oil future, currency forward relating to sale or purchase of goods or services, commodity futures or options that relates to raw materials and finished goods: Should be classified as operating cash flow. • Of investment transactions like stock index futures to protect value investment in shares, T- bill futures or options to protect value of in vestment debt instruments Should be classified as investment cash flow. • Of financing activities like swaps against foreign currency loans and floating rate interest: Should be classified as financing cash flow.	• Of dealers - Operating activities. • Of others - Investment activities.

Elements of cash flow from financing activities

Given below are five elements illustrated cash flow from financing activities:

Elements of cash flow from financing activities	
1.	Cash proceeds from issuing shares or other equity instruments.
2.	Cash payments to owners to acquire or redeem the enterprise's shares.
3.	Cash proceeds from issuing debentures, loans, notes, bonds, mortgages, and other short term and long term borrowings.
4.	Cash repayments of amounts borrowed.
5.	Cash payments by a lease for the reduction of the outstanding liability relating to a finance lease.

Cash Flow from Operating Activities

Operating cash flows can be derived either in pursuance of a direct method or indirect method. Under direct approach major classes of cash receipts and payments are disclosed. Whereas under indirect approach net profit or loss adjusted to derive operating cash flow. Although direct method is not appropriate, the SEBI requires computation of cash flow from operating activities using indirect method.

Direct Method

Cash flow from operating activities is computed taking into account the following items:

Cash Receipts	Cash Payments
• Cash sales and cash collection = Sales + Opening Balance of Receivables — Closing Balance of Receivables.	• Cash purchase of raw materials and spares for manufacturing activities = [Raw material consumed + Closing stock - Opening Stock] + [Opening creditors - Closing creditors] • Cash purchase of finished goods for trading [Goods sold + Closing stock - Opening Stock] + [Opening creditors - Closing creditors]. • Payment to and on behalf of employees Wages & Salaries + Closing outstanding balance -Opening outstanding balance. • Payment of expenses = Expenses incurred + Opening balance of outstanding - Closing balance of outstanding.

Notes:

(1) Figures of cash sales may be directly available from cash book. Then Cash collection can be derived taking Credit sales + Opening balance of debtors - closing balance of debtors.

(2) Similarly figures of cash purchases can also be obtained from cash books.

(3) Interest and dividend are investment cash inflow and, therefore, to be excluded.

(4) Interest expense is financing cash outflow.

(5) Tax provision is not cash expense, advance tax paid should be treated as tax cash outflow.

Indirect Method

Under this method operating cash flow is derived indirectly by making adjustments for non-cash items, cash flow of different types included in the profit and working capital adjustments. Starting from profit before tax adjustments can be made to arrive at operating cash flow.

Profit Before Tax Add: Depreciation and Amortisation being non-cash item Interest - being financing cash outflow Lease rental of finance lease - being financing cash outflow
Less : Interest and dividend received - being investment cash inflow Lease rental received of finance lease - being investment cash inflow Advance tax paid to the extent relates to operating cash flow (Tax paid for financing cash flow and investment cash flow should be separated)
Add/Less : Working Capital Adjustments Increase in current assets like receivables, inventories (-) Decrease in current assets like receivables, inventories (+) Increase in current liabilities (+) Decrease in current liabilities (-)

Illustrations on Cash Flow Statement

Given below is Profit and Loss Account of ABC Ltd. and relevant Balance Sheet information :

Example:

Profit and Loss Account of ABC Ltd. for the year ended 31-03-2015	
	(₹ in Lakhs)
Revenue	
Sales	4150
Interest and dividend	100
Stock adjustment	20
Total	**4270**
Expenditure	
Purchases	2400
Wages and salaries	800
Other expenses	200
Interest	60
Depreciation	100
Total	**3560**
Profit before tax	710
Tax Provision	200
Profit after tax	**510**
Balance of Profit & Loss Account	50

Profit available for distribution	560
Appropriation	
Transfer to General Reserve	200
Proposed dividend	300
Distribution tax	30
Total	**530**
Balance	30

Relevant Balance Sheet information	**31-03-2015** (₹ in Lakhs)	**31-03-2014** (₹ in Lakhs)
Debtors	400	250
Inventories	200	180
Creditors	250	230
Outstanding wages	50	40
Outstanding expenses	20	10
Advance tax	195	180
Tax provision	200	180
Assessed tax liability		180

Let us now study the technique of direct method of calculating operating cash flow:

Computation of cash flow from Operating		
Activities		
Direct Method		
Cash Receipts		
Cash sales & Collection from debtors		
Sales+Opening Debtors - Closing Debtors	(4150+250-400)	4000
Cash Payments		
Cash purchases & Payment to creditors		
Purchases+ Opening Creditors - Closing creditors	(2400+230-250)	2380
Wages & salaries paid	(800+40-50)	790
Cash Expenses	(200+10-20)	190
Taxes paid - Advance tax		195
		3555
Cash Flow from Operating Activities		**445**
Indirect Method		
Profit before tax		710
Add : Non-cash items : Depreciation		100
Add : Interest : Financing cash outflow		60
Less : Interest and Dividend : Investment		
Cash inflow		-100
Less : Tax paid		-195
Working Capital Adjustments		
Debtors	(250-400)	-150
Inventories	(180-200)	-20
Creditors	(250-230)	20
Outstanding wages	(50-40)	10
Outstanding expenses	(20-10)	10
Cash Flow from Operating Activities		**445**

Illustration 40.

Deepak Chemicals presents the following Balance Sheets as at 31-03-15 and 31-03-14. You are required to prepare cash flow statement.

(₹ in thousand)

Balance Sheet		**31-03-15**		**31-03-14**
Equity share capital	8,500		7,000	
General Reserve	3,800		4,000	
Profit & Loss Account	0		250	
Share Premium Account	1,500		750	
Shareholders' Funds		13,800		12,000
Secured Loans	4,800		500	
Unsecured Loans	5,350		4,000	
Loan Funds		10,150		9,000
Sources		23,950		21,000
Fixed Assets				
Gross Block	22,400		21,000	
Accumulated Depreciation	3,450		3,200	
Net Block		18,950		17,800
Capital Work-in-progress		1,860		0
Investments		1,650		2,320
Current Assets, Loans & Advances				
Inventories	2,150			
Debtors	1,090			
Cash & Bank Balances	120			
Loans	1,700			
Advance Tax	0			
Creditors	1,050		1,200	
Outstanding expenses	30		0	
Tax Provision	0		500	
Proposed Dividend	3,400		2,800	
	4,480		4,500	
Net Current Assets		940		280
Miscellaneous Expenditure		550		600
Applications		23,950		21,000

Other Information:

(1) Fixed assets costing ₹ 4,00,000, accumulated depreciation ₹ 3,00,000 were sold for ₹ 1,50,000.

(2) Actual tax liability for 2013-14 was ₹ 5,00,000.

(3) Loans represent long term loans given to group companies.

(4) Interest on loan funds for 2013-14 was ₹ 14,21,000 and interest and dividend income were ₹ 4,02,000.

(5) Investments costing ₹ 20,00,000 were sold for ₹ 25,00,000.

Solution: (₹ in thousand)

Cash flow from operating activities		
Change in general reserve	-200	
Change in profit and loss account	-250	
Proposed dividend	3400	
Provision for tax	0	
Profit Before tax		2950
Add : Depreciation	550	
Add : Misc.Expn.	50	
Add/(Less) Loss (profit) on sale of fixed assets	-50	
Add/(Less) Loss (profit) on sale of Investments	-500	
Funds flow from operations		3000
Add: Interest paid		1421
Less Interest and Dividend Received		-402
Add/Less Working Capital Adjustment		
Inventories	90	
Debtors	110	
Creditors	-150	
Outstanding expenses	30	80
Cash Flow from Operating Activities (Before tax)		4099
Less Advance tax for 2014-15		0
Cash flow from Operating Activities (After Tax)		4099
Cash flow Financing Activities		
Issue of shares		
Face value	1500	
Premium	750	2250
Repayment of Secured Loans	-200	
Raising of Unsecured Loans	1350	
Net loan		1150
Interest payment		-1421
Dividend payment for 2013-14		-2800
		-821
Cash flow from Investment Activities		
Purchase of Fixed Assets	-1800	
Sale of Fixed Assets	150	
Capital WIP	-1860	
Fixed Assets (Net)		-3510
Purchase of Investments	-1330	
Sale Proceeds of Investments	2500	
Investments (Net)		1170
Loans		-1500
Interest & Dividend Income		402
		-3438
Cash Flow Statement		
Cash flow from Operating Activities (After Tax)		4099
Cash flow from Financing Activities		-821
Cash flow from Investment Activities		-3438
Increase/decrease in Cash & Bank Balance		-160

Illustration 41.

Given below are summarised Balance Sheets of Harsh Chemicals Ltd. as at 31-03-14 and 31-03-15. The company issued one bonus share for every 4 shares held. The company also acquired machinery amounting to ₹ 30,00,000 from Levenz of France on deferred credit basis. You are required to prepare the cash flow statement.

(₹ in thousand)

Balance Sheet		31-03-15		31-03-14
Equity share capital	8,500		4,000	
General Reserve	7,000		7,600	
Profit & Loss Account	1,200		1,000	
Share Premium Account	1,500		750	
Shareholders' Funds		18,200		13,350
Secured Loans	4,800		5,400	
Unsecured Loans	5,350		4,000	
Deferred Credit	3,000		0	
Loan Funds		13,150		9,400
Sources		31,350		22,750
Fixed Assets				
Gross Block	22,400		17,000	
Accumulated Depreciation	3,450		3,200	
Net Block		18,950		13,800
Capital Work-in-progress		8,200		3,000
Investments		1,650		2,320
Current Assets, Loans & Advances				
Inventories	4,000		3,200	
Debtors	1,090		2,200	
Cash & Bank Balances	540		750	
Loans	1,700		200	
Advance Tax	1,600		1,400	
	8,930		7,750	
Creditors	1,050		1,600	
Outstanding expenses	880		120	
Tax Provision	1,600		1,400	
Proposed Dividend	3,400		1,600	
	6,930		4,720	
Net Current Assets		2,000		3,030
Miscellaneous Expenditure		550		600
Applications		31350		22750

Other Information:

(1) Fixed assets costing ₹ 4,00,000, accumulated depreciation ₹ 3,00,000 were sold for ₹ 1,50,000.

(2) Actual tax liability for 2013-14 was ₹ 14,00,000.

(3) Loans represent long term loans given to group companies.

(4) Interest on loan funds for 2014-15 was ₹ 18,41,000 and interest and dividend income were ₹ 4,02,000.

(5) Investments costing ₹ 20,00,000 were sold for ₹ 25,00,000.

Solution: (₹ in thousand)

Cash flow from operating activities		
Change in general reserve	400	
Change in profit and loss account	200	
Proposed dividend	3,400	
Provision for tax	1,600	
Profit before tax		5,600
Add : Depreciation	550	
Add : Misc. Expenses	50	
Add/(Less) Loss (profit) on sale of fixed assets	(50)	
Add/(Less) Loss (profit) on sale of Investments	(500)	
Funds flow from operations		5,650
Add : Interest paid		1,841
Less : Interest and Dividend Received		-402
Add/Less Working Capital Adjustment		
Inventories	(800)	
Debtors	1,110	
Creditors	(550)	
Outstanding expenses	760	520
Cash Flow from Operating Activities (Before tax)		7,609
Less : Advance tax for 2014-15		1,600
Cash flow from Operating Activities (After Tax)		6,009
Cash flow Financing Activities		
Issue of shares		
Face value	3,500	
Premium	750	4,250
Repayment of Secured Loans	(600)	
Raising of Unsecured Loans	1350	
Net loan		750
Interest payment		-1,841
Dividend payment for 2013-14		-1,600
		1,559
Cash flow from Investment Activities		
Purchase of Fixed Assets	(5,800)	
Sale of Fixed Assets	150	
Capital WIP	(2,200)	
Fixed Assets (Net)		(7,850)
Purchase of Investments	(1,330)	
Sale Proceeds of Investments	2,500	
Investments (Net)		1,170
Loans		(1,500)
Interest & Dividend Income		402
		(7,778)
Cash Flow Statement		
Cash flow from Operating Activities (After Tax)		6,009
Cash flow from Financing Activities		1,559
Cash flow from Investment Activities		(7,778)
Increase/decrease in Cash & Bank Balance		(210)

Illustration 42.

From the following Summary Cash Account of X Ltd. prepare Cash Flow Statement for the year ended 31st March, 2015 in accordance with AS 3 (Revised) using the direct method. The company does not have any cash equivalents.

Summary Cash Account for the year ended 31.03.2015

Particulars	₹ '000	Particulars	₹ '000
Balance on 1.4.2014	50	Payment to Suppliers	2,000
Issue of Equity Shares	300	Purchase of Fixed Assets	200
Receipts from Customers	2,800	Overhead expense	200
Sale of Fixed Assets	100	Wages and Salaries	100
		Taxation	250
		Dividend	50
		Repayment of Bank Loan	300
		Balance on 31.3.2015	150
	3,250		3,250

Solution:

X Ltd.
Cash Flow Statement for the year ended 31st March, 2015
(Using the direct method)

	₹ '000	₹ '000
Cash flows from operating activities		
Cash receipts from customers	2,800	
Cash payment to suppliers	(2,000)	
Cash paid to employees	(100)	
Cash payments for overheads	(200)	
Cash generated from operations	500	
Income tax paid	(250)	
Net cash from operating activities		250
Cash flows from investing activities		
Payment for purchase of fixed assets	(200)	
Proceeds from sale of fixed assets	100	
Net cash used in investing activities		(100)
Cash flows from financing activities		
Proceeds from issuance of equity shares	300	
Bank loan repaid	(300)	
Dividend paid	(50)	
Net cash used in financing activities		(50)
Net increase in cash		100
Cash at beginning of the period		50
Cash at end of the period		150

Illustration 43.

(a) Arrange and redraft the following Cash Flow Statement in proper order keeping in mind the requirements of AS 3:

		₹ in Lakhs	₹ in Lakhs
Net Profit			60,000
Add:	Sale of Investments		70,000
	Depreciation on Assets		11,000
	Issue of Preference Shares		9,000
	Loan raised		4,500
	Decrease in Stock		12,000
			1,66,500
Less:	Purchase of Fixed Assets	65,000	
	Decrease in Creditors	6,000	
	Increase in Debtors	8,000	
	Exchange gain	8,000	
	Profit on sale of investments	12,000	
	Redemption of Debenture	5,700	
	Dividend paid	1,400	
	Interest paid	945	1,07,045
			59,455
Add:	Opening cash and cash equivalent		12,341
Closing cash and cash equivalent			71,796

Solution:

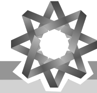
(a) **Cash Flow Statement**

Cash flows from operating activities		(₹ in Lakhs)
Net profit		60,000
Less: Exchange gain		(8,000)
Less: Profit on sale of investments		(12,000)
		40,000
Add: Depreciation on assets		11,000
Change in current assets and current liabilities		51,000
(-) Increase in debtors	(8,000)	
(+) Decrease in stock	12,000	
(-) Decrease in creditors	(6,000)	(2,000)

Net cash from operating activities		49,000
Cash flows from investing activities		
Sale of investments	70,000	
Purchase of fixed assets	(65,000)	
Net cash from Investing activities		5,000
Cash flows from financing activities		
Issue of preference shares	9,000	
Loan raised	4,500	
Redemption of Debentures	(5,700)	
Interest paid	(945)	
Dividend paid	(1,400)	
Net cash from financing activities		5,455
Net increase in cash & cash equivalents		59,455
Add: Opening cash and cash equivalents		12,341
Closing cash and cash equivalents		71,796

Study Note - 4

RECENT TRENDS IN FINANCIAL REPORTING



This Study Note includes

4.1 Sustainability Reporting
4.2 Concept of Triple Bottom Line (TBL)
4.3 Concept of Triple Bottom Line Reporting
4.4 Benefits of Triple Bottom Line Reporting
4.5 Implementation of Triple Bottom Line Reporting
4.6 Forms of TBL Reporting
4.7 Users of TBL Reporting
4.8 Financial Reporting vis- à-vis Triple Bottom Line Reporting
4.9 Challenges of Triple Bottom Line Reporting Framework

4.1 SUSTAINABILITY REPORTING

In the modern era, sustainability has often been considered as a goal of every kind of organisation, be it business, non-profit organisation or government. Sustainability is a balancing act where business decisions take into account the impact they may have on the various aspects of sustainability including the economic viability of the business. Sustainability usually makes us think about carbon footprints, greenhouse gases and ecosystems. This is the environmental aspect of sustainability. Moreover, two additional aspects are generally recognised as contributing to sustainability: economic factors and social factors. Together these three pillars of sustainability are often referred to as '***People – Planet – Profit***'. In this scenario, the three forms of sustainability that are considered by the organisations are:

- **Social sustainability** activities focus on maintaining mutually beneficial relationships with employees, customers and the community. These activities often have benefits in terms of positive profile and customer and community support.
- **Environmental sustainability** activities focus on the impact of resource usage, hazardous substances, waste and emissions on the physical environment. These activities may have a direct benefit for a business by reducing costs.
- **Economic sustainability** activities focus on business efficiency, productivity and profit.

With the shift in societal focus toward environmental longevity, businesses are encouraged to look at the big picture and see their impact on the world around them. Sustainable development was identified by the Brundtland Commission of the United Nations in 1987. The need was felt by the various entities to incorporate the concept of sustainability, in their financial reporting framework.

In 1981, Freer Spreckley first articulated this theme in a publication called 'Social Audit - A Management Tool for Co-operative Working' in which, he stated that enterprises should measure and report on social, environmental and financial performance.

The growth of this broader "world sustainability" viewpoint can be seen in the number of companies that have begun reporting on more than just financial operations. Large corporations such as Weyerhaeuser Company, The Boeing Company, PricewaterhouseCoopers, The Procter & Gamble Company, Sony Corporation, and Toyota Motor Corporation, have joined with many others to create the World Business Council for Sustainable Development (WBCSD).

4.2 CONCEPT OF TRIPLE BOTTOM LINE (TBL)

The phrase "triple bottom line" was first coined in 1994 by John Elkington, the founder of a British consultancy called 'Sustain Ability'. He further articulated the concept in his 1997 book '*Cannibals with Forks: The Triple Bottom Line of 21st Century Business*'.

The concept of 'Triple bottom line 'incorporates two technical terminologies – 'Triple' and 'Bottom Line'. We first understand these two for better understanding of the concept of Triple bottom line reporting.

- **Bottom Line:** In traditional accounting and common parlance, the "bottom line" refers to either the "operating result", which is usually recorded at the very last line (or, bottom) of the income statement. Over the last few decades, environmentalists and advocates of social justice have been challenged to introduce a broader concept of 'bottom line' into public consciousness by introducing full cost accounting.

- **Triple:** The Triple bottom line concept requires an organisation to measure and report on three dimensions viz. social, environmental and economic/ financial performance of the organisation.

For example, a leather tanning firm may report a financial profit, but their output may cause adverse health effect, and pollute the nearby water reserves; and the government may end up spending the taxpayer money on health care and environmental clean-up. Now the question that arises in the mind of the proponents of full-cost accounting is 'How do we perform a full societal cost benefit analysis?' in this respect, the triple bottom line adds two more "bottom lines", namely, social and environmental (ecological) concerns.

Thus, the concept of 'triple bottom line' consists of three dimensions, namely 'social equity', 'economic', and 'environmental factors'. In other words, the triple bottom line (TBL) consists of three Ps: profit, people and planet. It aims to measure the financial, social and environmental performance of the corporation over a period of time. At it's core, triple bottom line thinking ties the social and environmental impact of an organization's activities to its economic performance. Thus, it is also referred to as "TBL," "3BL," "People, Planet, Profit" and "The Three Pillars."

However, it is to be noted that TBL does not mean that companies are required to maximise returns across three dimensions of performance - in terms of corporate performance, it is recognized that financial performance is the primary consideration in assessing its business success.

4.3 CONCEPT OF TRIPLE BOTTOM LINE REPORTING

Triple bottom line reporting (TBLR) expands the traditional reporting framework to take into account social and environmental performance in addition to financial performance. The concept of Triple bottom line reporting states that reporting should incorporate the social, environmental and financial performance of an organization.

TBL reporting refers to the publication of economic, environmental and social information in an integrated manner that reflects activities and outcomes across these three dimensions of a company's performance. Triple Bottom Line Reporting requires that organisations should be reporting on three different 'bottom lines' that are quite distinct, but related from one another. They are discussed hereunder:

- The first bottom line happens to be the bottom line of the "income statement" (which is the traditional measure of operating result).

- The second bottom line is that of anorganisation's "people account" (a measure in some shape or form of how socially responsible an organisation has been throughout its operations); and

- The third bottom line is that of the organisation's "planet account" (which measures how environmentally responsible the company has been).

Thus, only a company that produces a TBL reports is taking account of the full cost involved in doing business.

4.4 BENEFITS OF TRIPLE BOTTOM LINE REPORTING

The benefits emerging from triple bottom line reporting are discussed hereunder:

- **Enhancement of reputation and brand:** Corporate reputation is a function of the way in which a company is perceived by its stakeholders. Effective communication with stakeholders on one or more of the environmental, social, and economic dimensions can play an important role in managing stakeholder perceptions and, in doing so, protect and enhance corporate reputation.
- **Securing a social license to operate:** A 'license to operate' is not a piece of paper, but informal community and stakeholder support for an organisation's operations. Business is increasingly recognising the link between ongoing business success and its 'license to operate', especially in the resources sector. Communication with stakeholders is often critical to securing and maintaining a 'license to operate'. Communities and stakeholders generally, are likely to be more supportive of companies that communicate openly and honestly about their management and performance in relation to environmental, social and economic factors.
- **Attraction and retention of high calibre employees:** Existing and prospective employees have expectations about corporate environmental, social and economic behaviour, and include such factors in their decisions regarding working for an organisation.. The publication of TBL-related information can play a role in positioning an employer as an 'employer of choice' which can enhance employee loyalty, reduce staff turnover and increase a company's ability to attract high quality employees.
- **Improved access to investor market:** A growing number of investors are including environmental and social factors within their decision-making processes. The growth in socially responsible investment and shareholder activism is evidence of this. Responding to investor requirements through the publication of TBL-related information is a way of ensuring that the company is aligning its communication with this stakeholder group, and therefore enhancing its attractiveness to this segment of the investment market.
- **Establish position as a preferred supplier:** Obtaining a differentiated position in the market place is one way to establish the status of preferred supplier. Effectively communicating with stakeholder groups on environmental, social and economic issues is central to obtaining a differentiated position in the market place.
- **Reduced risk profile:** There is an expanding body of evidence to suggest that performance in respect of economic, social and environmental factors has the capacity to affect the views of market participants about a company's exposure to, and management of risk. TBL reporting enables a company to demonstrate its commitment to effectively managing such factors and to communicate its performance in these areas. A communication policy that addresses these issues can play an important role in the company's overall risk management strategy.
- **Identification of potential cost savings:** TBL reporting often involves the collection, collation and analysis of data on resource and materials usage, and the assessment of business processes. For example, this can enable a company to better identify opportunities for cost savings through more efficient use of resources and materials.
- **Increased scope for innovation:** The development of innovative products and services can be facilitated through the alignment of R&D activity with the expectations of stakeholders. The process of publishing TBL reporting provides a medium by which companies can engage with stakeholders and understand their priorities and concerns.
- **Aligning stakeholder needs with management focus:** External reporting of information focuses management attention on not only the integrity of the data but also the continuous improvement of the indicator being reported.
- **Creation of sound basis for stakeholder dialogue:** Publication of TBL reporting provides a powerful platform for engaging in dialogue with stakeholders. Understanding stakeholder requirements and alignment of business performance with such requirements is fundamental to business success. TBL reporting demonstrates to stakeholders the company's commitment to managing all of its impacts, and, in doing so, establishes a sound basis for stakeholder dialogue to take place.

In addition to the benefits obtained through superior relationships with key stakeholder groups, the decision to be publicly accountable for environmental and social performance is often recognised as a powerful driver of internal behavioural change. The availability of relevant information on economic, environmental and social performance that previously may not have been collected and evaluated in a readily understood manner may enable executives to identify and focus attention on specific aspects of corporate performance where improvement is required.

4.5 IMPLEMENTATION OF TRIPLE BOTTOM LINE REPORTING

Prerequisites of implementation of TBL Reporting

TBL reporting would be of little relevance to the reporting company or its stakeholders if it is not **aligned to the company's overall business strategy**. A decision to move to full TBL reporting should not be taken lightly. It must have **senior management endorsement and commitment**, as it may have major resource implications, and a half-hearted approach is likely to be worse than not adopting it all.

Strategy for implementation

Critical issues for consideration in the development and implementation of TBL reporting include:

- clear definition of the role of TBL reporting in driving strategic business objectives;
- establishment of the resource and cost requirements;
- awareness of associated legal implications; and
- understanding the risks involved in publishing TBL information.

Key Challenges for Implementation

The key challenges for implementation of TBL reporting framework are:

- Awareness of relevant issues associated with TBL reporting;
- Understanding stakeholder requirements;
- Aligning TBL reporting with objectives and risks; and
- Determining and measuring performance indicators.

4.6 FORMS OF TBL LINE REPORTING

A number of options, ranging from the inclusion of minimal TBL-related information within statutory reporting through to the publication of a full TBL report, are available to companies considering TBL reporting.

In choosing an appropriate path forward, companies are likely to take into account various factors including:

- the overall strategic objectives;
- current capacity to report;
- prioritization of stakeholder requirements; and
- the reporting activities within the industry sector.

4.7 USERS OF TBL REPORTING

All types of entities viz. Businesses, non-profits organisations and government entities alike can all use the TBL.

Businesses: The TBL and its core value of sustainability have become compelling in the business world due to accumulating anecdotal evidence of greater long-term profitability. For example, reducing waste from packaging can also reduce costs. Among the firms that have been exemplars of these approaches are General Electric, Unilever, Proctor and Gamble, 3M among others.

Non-profit Organisations: Many non-profit organizations have adopted the TBL and some have partnered with private firms to address broad sustainability issues that affect mutual stakeholders. Companies recognize that aligning with nonprofit organizations makes good business sense, particularly those nonprofits with goals of economic prosperity, social well-being and environmental protection.

Government: State, regional and local governments are increasingly adopting the TBL and analogous sustainability assessment frameworks as decision-making and performance-monitoring tools.

4.8 FINANCIAL REPORTING VIS-À-VIS TRIPLE BOTTOM LINE REPORTING

Origin: The origination of financial reporting precedes that of Triple bottom line reporting, the latter being just a few decades old.

Nature: It is mandatory for corporates to prepare and present their financial reports; while preparation of full TBL reports including social and environmental dimension is voluntary in nature.

Scope: Triple bottom line reporting is broader in scope than financial reporting, as the former includes the reporting of social and environmental performances in addition to the financial performance of an organisation.

Contents: The information contained within a TBL report is of a different nature to that included in a financial report. Thus, TBL reporting enables environmental and social risks that have the capacity to materially affect long-term financial performance to be identified and, therefore, taken into consideration when preparing financial reports.

4.9 CHALLENGES OF TRIPLE BOTTOM LINE REPORTING FRAMEWORK

The primary challenge in TBL Reporting is the calculation of the TBL**.** The 3Ps under TBL reporting framework are not measured using any common unit. Profits are expressed in monetary amounts. But is it possible to measure social capital in it? What about environmental or ecological health? Finding a common unit of measurement is one challenge.

Some proponents of TBL concept suggest monetizing all the dimensions of the TBL, including social welfare or environmental damage. While that would have the benefit of having a common monetary unit, it would be a big challenge. The challenge lies in identifying the proper method of finding the right price for lost environment and social value creation.

Solution to the Challenge

The solution advocated by some experts of the field has been to calculate the TBL in terms of an index. In this way, it would be possible to eliminate the incompatible units issue and, as long as there is a universally accepted accounting method, it would allow for comparisons between entities, e.g., comparing performance between companies, cities, development projects or some other benchmark.

An example of an index that compares a county versus the nation's performance for a variety of components is the Indiana Business Research Center's Innovation Index. However, there remains some subjectivity even when using an index regarding:

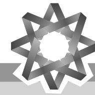
- How are the index components weighted?
- Would each "P" get equal weighting?
- What about the sub-components within each "P"?
- Do they each get equal weighting?
- Is the 'People' category more important than the 'Planet'?
- Who would take decision in these respect?

Another option would do away with measuring sustainability in monetary terms or using an index. It suggests each sustainability measure would stand alone. For example, "Acres of wetlands" would be a measure, and progress would be expressed based on wetland creation, destruction or status quo over time. The downside to this approach is the proliferation of metrics that may be pertinent to measuring sustainability. The TBL user may get 'metric fatigue'.

Having discussed the difficulties with calculating the TBL, we turn our attention to potential metrics for inclusion in a TBL calculation. Following that, we will discuss how businesses and other entities have applied the TBL framework.

Study Note - 5

VALUATION, ACCOUNTING AND REPORTING OF FINANCIAL INSTRUMENTS AND OTHERS



This Study Note includes

5.1 Recognition & Valuation of Financial Instruments

5.2 Accounting for CENVAT & State – Level VAT

5.3 NBFC - Provisioning Norms and Accounting

5.4 Valuation of Shares

5.5 Valuation of Goodwill

5.1 RECOGNITION & VALUATION OF FINANCIAL INSTRUMENTS

INTRODUCTION

Financial instruments are legal agreements that require one party to pay money or something else of value or to promise to pay under stipulated conditions to counter-party in exchange for the payment of interest, for the acquisition of rights, for premiums, or for indemnification against risk. In exchange for the payment of the money, the counterparty hopes to generate profit by receiving interest, capital gains, premiums, or indemnification for a loss event.

In simple terms, accounting for financial instruments refers that how we account for investments in shares, investments in bonds and receivables (financial assets), how we account for trade payables and long-term loans (financial liabilities) and how we account for equity share capital (equity instruments) and derivatives. There are various issues around classification, initial measurement and subsequent measurement and valuation in considering the rules related to the accounting for financial instruments.

Important Terminology:
Financial Instruments: Financial Instrument is a contract that gives rise to a **Financial Asset** for one enterprise and a **Financial Liability** or **Equity** for another enterprise. E.g. Investments, Debtors, Deposits etc.
Financial Assets: A Financial asset is an asset that is: • Cash • Equity instruments of other enterprise, Eg: Investment in ordinary shares. • A contractual right to receive cash, or to exchange financial assets or liabilities with other enterprise under conditions that are potentially favourable to the enterprise.
Financial Liability: Financial Liability is a contractual obligation to deliver cash or to exchange financial assets or financial liabilities with another enterprise under conditions which are potentially unfavourable to the enterprise. It also includes contracts which may be settled in the enterprise's equity shares. Eg: Convertible Debenture, Convertible Preference share.
Concept Note:
Fixed assets, stock, pre-paid expenses are not financial assets. Deferred incomes and warranty obligation are not financial liabilities.

CLASSIFICATION OF FINANCIAL ASSETS:

Financial asset has been classified as under:

- **Held for trading:** Financial assets at fair value through Profit & Loss. They are held for trading or they are designated as such. It includes derivatives also.
- **Held to maturity:** Assets with fixed maturity and the entity has a positive intention and ability to hold till maturity.
- **Loans & receivables:** Assets with fixed payments (determinable and which are not quoted in the market.
- **Available for sale:** These are those assets which are not classified under any of the above categories. (residual)

CLASSIFICATION OF FINANCIAL LIABILITIES:

A financial liability has been classified as under:

- Financial liability at fair value through profit & loss (Held for trading liabilities.)
- Other liabilities

RECOGNITION AND MEASUREMENT OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

Financial instruments are initially recognised when an entity becomes a party to the contractual provisions of the instrument, and are classified into various categories depending upon the type of instrument, which then determines the subsequent measurement of the instrument (typically amortised cost or fair value).

Initial Measurement

When a financial asset or financial liability is recognised initially, an entity shall measure it at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

Subsequent Measurement of Financial Assets

After initial recognition, an entity shall measure financial assets, including derivatives that are assets, at their fair values, without any deduction for transaction costs it may incur on sale or other disposal, except for the following financial assets: (a) loans and receivables, which shall be measured at amortised cost using the effective interest method; (b) held-to-maturity investments, which shall be measured at amortised cost using the effective interest method; and (c) investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments, which shall be measured at cost.

Financial assets that are designated as hedged items are subject to measurement under the hedge accounting requirements

Subsequent Measurement of Financial Liabilities

After initial recognition, an entity shall measure all financial liabilities at amortised cost using the effective interest method, except for:

(a) Financial liabilities at fair value through profit or loss. Such liabilities, including derivatives that are liabilities, shall be measured at fair value except for a derivative liability that is linked to and must be settled by delivery of an unquoted equity instrument whose fair value cannot be reliably measured, which shall be measured at cost.

(b) Financial liabilities that arise when a transfer of a financial asset does not qualify for derecognition or when the continuing involvement approach applies.

(c) Financial guarantee contracts as defined in paragraph 9. After initial recognition, an issuer of such a contract shall (unless paragraph 47(a) or (b) applies) measure it at the higher of: (i) the amount determined in accordance with Ind AS 37; and (ii) the amount initially recognised (see paragraph 43) less, when appropriate, cumulative amortisation recognised in accordance with Ind AS 18.

(d) Commitments to provide a loan at a below-market interest rate. After initial recognition, an issuer of such a commitment shall (unless paragraph 47(a) applies) measure it at the higher of:

 (i) the amount determined in accordance with Ind AS 37; and

 (ii) the amount initially recognised *Less* when appropriate, cumulative amortisation recognised in accordance with Ind AS 18. Financial liabilities that are designated as hedged items are subject to the hedge accounting requirements

Illustration 1. 28.03.2015 – Purchase 100 share of ₹ 600 each

31.03.2015 – Fair value ₹ 632 each

04.04.2015 – Settlement date – Fair value ₹ 624

22.04.2015 – Sold ₹ 690/ share (settled on the same date.)

Journalise the transactions

(a) Using trade date accounting; and

(b) Using settlement date accounting.

Solution:

(a) Using trade date accounting

Journal

Date	Particulars		Debit (₹)	Credit (₹)
28.03.2015	Investment A/c To, Liabilities A/c	Dr.	60,000	 60,000
31.03.2015	Investment A/c To, P/L A/c	Dr.	3,200	 3,200
04.04.2015	P/L A/c To, Investment A/c	Dr.	800	 800
	Liabilities A/c To, Bank A/c	Dr.	60,000	 60,000
22.04.2015	Bank A/c To, Investment A/c To, P/L A/c	Dr.	69,000	 62,400 6,600

(b) Using settlement date accounting

Journal

Date	Particulars		Debit (₹)	Credit (₹)
31.03.2015	Fair value adjustment A/c To P/L A/c	Dr.	3,200	 3,200
04.04.2015	Investment A/c P/LA/c To Bank A/c To Fair value adjustment A/c	Dr. Dr.	62,400 800	 60,000 3,200
22.04.2015	Bank A/c To Investment A/c To P/L A/c	Dr.	69,000	 62,400 6,600

DERECOGNITION OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES:

Derecognition refers to the removal of an asset or liability (or a portion thereof) from an entity's balance sheet. Derecognition questions can arise with respect to all types of assets and liabilities.

Derecognition of a financial asset

The basic premise for the derecognition model is to determine whether the asset under consideration for derecognition is:

- an asset in its entirety, or
- specifically identified cash flows from an asset, or
- a fully proportionate share of the cash flows from an asset, or
- a fully proportionate share of specifically identified cash flows from a financial asset.

Once the asset under consideration for derecognition has been determined, an assessment is made as to whether the asset has been transferred, and if so, whether the transfer of that asset is subsequently eligible for derecognition.

An asset is transferred if either the entity has transferred the contractual rights to receive the cash flows, or the entity has retained the contractual rights to receive the cash flows from the asset, but has assumed a contractual obligation to pass those cash flows on under an arrangement that meets the following three conditions:

- the entity has no obligation to pay amounts to the eventual recipient unless it collects equivalent amounts on the original asset
- the entity is prohibited from selling or pledging the original asset (other than as security to the eventual recipient),
- the entity has an obligation to remit those cash flows without material delay.

Once an entity has determined that the asset has been transferred, it then determines whether or not it has transferred substantially all of the risks and rewards of ownership of the asset. If substantially all the risks and rewards have been transferred, the asset is derecognised. If substantially all the risks and rewards have been retained, derecognition of the asset is precluded.

If the entity has neither retained nor transferred substantially all of the risks and rewards of the asset, then the entity must assess whether it has relinquished control of the asset or not. If the entity does not control the asset then derecognition is appropriate; however if the entity has retained control of the asset, then the entity continues to recognise the asset to the extent to which it has a continuing involvement in the asset.

Derecognition of a financial liability

An entity shall remove a financial liability (or a part of a financial liability) from its balance sheet when, and only when, it is extinguished—i.e. when the obligation specified in the contract is discharged or cancelled or expires.

An exchange between an existing borrower and lender of debt instruments with substantially different terms shall be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. Similarly, a substantial modification of the terms of an existing financial liability or a part of it (whether or not attributable to the financial difficulty of the debtor) shall be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.

The difference between the carrying amount of a financial liability (or part of a financial liability) extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, shall be recognised in profit or loss.

HEDGE ACCOUNTING

- **Hedging**: It is an action designated to reduce uncertainty of value of assets, value of liabilities, cash flows, firm commitments.
- Some of the examples of most hedged items are portfolios of equity, foreign currency receivables, foreign currency payables, inventories etc. Instruments used for hedging are forward, futures, option, swaps.

- **Hedging relationships**: Hedging relationships are of three types:
  - (a) **Fair Value Hedge**: A hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect profit or loss.
  - (b) **Cash Flow Hedge**: a hedge of the exposure to variability in cash flows that (i) is attributable to a particular risk associated with a recognised asset or liability (such as all or some future interest payments on variable rate debt) or a highly probable forecast transaction and (ii) could affect profit or loss.
  - (c) **Hedge of a net investment in a foreign operation**
- **Hedge accounting** recognises the off-setting effects on profit or loss of changes in the fair values of the hedging instrument and the hedged item.
- **Conditions for applying Hedge Accounting**

A hedging relationship qualifies for hedge accounting if, and only if, all of the following conditions are met:

(a) At the inception of the hedge there is formal designation and documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge. That documentation shall include identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk.

(b) The hedge is expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk, consistently with the originally documented risk management strategy for that particular hedging relationship.

(c) For cash flow hedges, a forecast transaction that is the subject of the hedge must be highly probable and must present an exposure to variations in cash flows that could ultimately affect profit or loss.

(d) The effectiveness of the hedge can be reliably measured, ie the fair value or cash flows of the hedged item that are attributable to the hedged risk and the fair value of the hedging instrument can be reliably measured.

(e) The hedge is assessed on an ongoing basis and determined actually to have been highly effective throughout the financial reporting periods for which the hedge was designated.

Discontinuance of Hedge Accounting

An entity shall discontinue prospectively the hedge accounting in the following cases:

(a) the hedging instrument expires or is sold, terminated or exercised (for this purpose, the replacement or rollover of a hedging instrument into another hedging instrument is not an expiration or termination if such replacement or rollover is part of the entity's documented hedging strategy);

(b) the hedge no longer meets the criteria for hedge accounting in paragraph 88; or

(c) the entity revokes the designation.

Illustration 2.

An enterprise has 100 kgs of tea valued at ₹6,00,000. It entered into a sale – future contract of ₹6,00,000 of tea - future. The date was 01.03.2015. On 31.03.2015 the market price of tea & tea future is ₹6,30,000. Pass the journal entries.

Solution:

Date	Particular		Debit ₹	Credit ₹
01.0. 2015	No Entry			
31.03.2015	P & L A/c	Dr.	30,000	
	To, Liabilities (future)			30,000

Re-measuring the inventory

Date	Particular		Debit ₹	Credit ₹
31.03.2015	Inventory A/c To, P/L A/c	Dr.	30,000	 30,000

Example:

A foreign currency debtor is hedged through a sale – forward contract. Exchange rate falls down. The loss in foreign currency debtors is ₹1,00,000 where as the profit in forward contract is ₹120,000 so the ineffective portion is ₹20,000. The accounting will be as follows:-

Date	Particular		Debit ₹	Credit ₹
31.03.2015	Forward assets A/c To, Hedging Reserve A/c To, P/L A/c	Dr.	1,20,000	 1,00,000 20,000
	Hedging Reserve A/c To, Debtors A/c	Dr.	1,00,000	 1,00,000

COMPOUND INSTRUMENTS:

Definition:

A compound instrument is a non-derivative financial instrument that contains both a financial liability component and an equity component. The equity component grants an option to the holder of the instrument to convert the instrument into an equity instrument of the issuer.

E.g.: Convertible Bond, Readable Preference share etc.

ACCOUNTING FOR COMPOUND FINANCIAL INSTRUMENTS:

Accounting treatment in the books of issuer:

Issuer is someone who creates the compound financial instrument. They are also known as "borrower" because they raises money by issuing compound financial instrument.

The "**split accounting**" method is to be followed for compound financial instruments in the books of issuer. The steps are as under:

1. **Identify the various components of the compound financial instrument:** The instrument is to be bifurcated into 'liability' element and 'equity' element.
2. **Determination of the fair value of the compound financial instrument as a whole:** Asthe transaction happens under market conditions, then the fair value of the instrument as a whole equals to cash received in return for the instrument.
3. **Determination of the fair value of the liability component:** The fair value of the liability component can be determined at fair value of a similar liability that does NOT have any associated equity conversion feature.

   E.g. The fair value of the liability component of the convertible bond equals to fair value of the bond with the same parameters (maturity, coupon rate, etc.) but without the option to convert into issuer's shares.
4. **Determine the fair value of the equity component.**

   The equity component is determined simply as the fair value of the compound financial instrument as a whole (step 2) less the fair value of the liability component (step 3).

Journal entry:

Bank A/c Dr.	XX	
To Convertible Instrument A/c [Liability]		XX
To Convertible Instrument A/c [Equity]		XX

Accounting treatment in holder's financial statements:

Holder is someone who acquires compound financial instrument and they also referred as "lender".

When holder buys a compound financial instrument, it also has two components:

1. **A derivative financial asset:** which is the call option for issuer's share in this example, and
2. **A receivable towards issuer:** which is the loan provided to issuer by acquiring his bond.

Worked out Illustration

Illustration 3.

Mayank buys the following Equity Index option and the seller/writer of this option is Shiva:

(i)	Date of buy	28th March, 2010
(ii)	Type of option	S&P CNX NIFTY - call
(iii)	Expiry date	31st May, 2010
(iv)	Premium per unit	₹ 21
(v)	Contract Multiplier (No. of units)	2,500
(vi)	Margin per unit	₹ 180
(vii)	Strike price	₹ 920

Margin calculated by SPAN on 29.3.2010 is ₹5,60,000; on 30.3.2010 is ₹3,80,000; and on 31.3.2010 is ₹ 4,10,000.

The prevailing premium rate for the above option on 31.3.2010 is ₹ 16 per unit.

You are required to give the journal entries in the books of both the parties. Also, show the Balance Sheet (as on 31.3.2010) extract containing the appropriate disclosure of balance in margin account.

Solution:

(i) **Books of Mayank**
Journal

Date	Particulars		Dr. (₹)	Cr. (₹)
28.3.10	Equity Stock Option Premium A/c	Dr.	52,500	
	To Bank A/c			52,500
	(Being Premium Paid @ ₹ 21 Per Unit for 2,500 Units)			
31.3.10	Profit and Loss A/c	Dr.	12,500	
	To Provision for Loss on Equity Stock Option A/c			12,500
	(Being Provision made for Loss on Equity Stock Option A/c to the extent of ₹ 5 per Unit for 2,500 Units)			

Balance Sheet of Mayank as on 31st March, 2010 (includes)

Current Assets:	₹	₹
Equity index Option Premium	52,500	
Less: Provision for Loss	12,500	40,000

Books of Shiva (Seller/Writer)

Journal

Date	Particulars		Dr. (₹)	Cr. (₹)
27.3.10	Bank A/c	Dr.	52,500	
	To Equity Stock Option Premium A/c			52,500
	(Being premium received ₹21 on 2500 units on Sale of Stock option)			
	Equity Index Option Margin A/c	Dr.	4,50,000	
	To Bank A/c			4,50,000
	(Being Initial margin paid on option contract at ₹ 180 per Unit for 2500 Units)			
29.3.10	Equity Index Option Margin A/c	Dr.	1,10,000	
	To Bank A/c			1,10,000
	(Being further margin collected by the Stock Exchange as per SPAN)			
30.3.10	Bank A/c	Dr.	1,80,000	
	To Equity Index Option Margin A/c			1,80,000
	(Being excess margin received as per SPAN)			
31.3.10	Equity index Option Margin A/c	Dr.	30,000	
	To Bank A/c			30,000
	(Being further margin collection by the Stock Exchange as per SPAN)			

(ii) Balance Sheet of Shiva as on 31st March, 2010 (includes)

<u>Equity & Liabilities:</u>		₹
Current Liabilities:		
Equity Stock Option Premium		52,500
<u>Assets:</u>		
<u>Current Assets:</u>		
Equity Index Option Margin		4,10,000

Illustration 4.

Mr. RAJA enters into certain equity derivative instruments contracts on March 27, 2010. The initial margin on these contracts, calculated as per SPAN, is ₹ 35,000. The margin for the subsequent days, calculated as per span is as follows:

On 29th March, 2010 — ₹ 40,000

On 30th March, 2010 — ₹ 30,000

On 31s' March, 2010 — ₹ 32,000

Show the journal entries for the Payment/Receipt of the initial margin and disclosure requirement in the Balance Sheet.

Solution:

Journal

Date	Particulars		Dr. (₹)	Cr. (₹)
27.03.10	Initial Margin- Equity Derivative Instruments A/c	Dr.	35,000	
	To Bank A/c			35,000
	(Being initial margin paid on Equity Derivative Instruments)			
29.03.10	Initial Margin - Equity Derivative Instruments A/c	Dr.	5,000	
	To Bank A/c			5,000
	(Being further Margin paid to the Exchange)			
30.03.10	Bank A/c	Dr.	10,000	
	To Initial Margin- Equity Derivative Instruments A/c			10,000
	(Being refund of Margin from the exchange)			
30. 03.10	Initial Margin- Equity Derivative Instruments A/c	Dr.	2,000	
	To Bank A/c			2,000
	(Being further Margin paid to the exchange)			

The initial Margin paid on equity derivative instruments will be disclosed in the Balance Sheet as follows:

1. Extracts from the balance sheet Current Assets

   Initial Margins- Equity Derivative Instruments A/c ₹ 32,000

2. In respect of initial margin, the following disclosure may be made in the notes to accounts:

   'Initial Margin on Equity Derivative instruments contracts has been paid in cash only'.

Illustration 5.

Difficult Ltd. has given a 12.50% fixed rate loan to its subsidiary Easy Ltd. Difficult Ltd. measures this loan at an amortized cost of ₹2,50,000. Difficult Ltd. has plans to hive off the receivable at a later stage and as a measure to safeguard against fall in value of its dues enters into a pay-fixed, receive floating interest rate swap to convert the fixed interest receipts into floating interest receipts. Difficult Ltd. designates the swap as a Hedging instrument in a fair value hedge of the Loan Asset. Over the following months, market interest rates increase and Difficult Ltd. earns interest income of ₹ 25,000 on the loan and ₹ 1,000 as net interest payments on the swap. The fair value of the Loan Asset decreases by ₹ 5,000 while that of the interest rate swap increases by ₹ 5,000. You are informed that all conditions required for the Hedge Accounting are satisfied.

You are required to pass-Journal Entries, with suitable narrations in the books of Difficult Ltd. to record the above transactions.

Solution:

Books of Difficult Ltd.

Journal

Particulars		Dr. Amount (₹)	Cr. Amount (₹)
Cash A/c	Dr.	25,000	
To Interest A/c			25,000
(Being the receipt of interest income on the loan asset)			
Derivative A/c	Dr.	5,000	
To Hedging gain A/c			5,000
(Being increase in the fair value of the interest rate swap)			
Hedging loss A/c	Dr.	5,000	
To Loan to Easy Ltd. A/c			5,000
(Being decrease in the fair value of loan to Easy Ltd. attributable to the hedged risk recorded)			
Cash A/c	Dr.	1,000	
To Interest A/c			1,000
(Being the entry to record the interest settlement of the swap)			

Illustration 6.

MS. AINDRILA, an investor buys a stock option of ANISHA LTD. in July, 2012 with a strike price on 30th July, 2012 ₹ 300, to be expired on 30th August, 2012. The premium is ₹ 25 per unit and the market lot is 100. The margin to be paid is ₹130 per unit.

Required:

Show the accounting treatment (Journal Entries) in the Books of MS. ANDRILA, when

(i) The option is settled by delivery of the asset;

(ii) The option is settled in cash and the index price is ₹ 310 per unit.

Solution:

(i) When the option is settled by delivery of the Assets

Date	Particulars	Dr. Amount (₹)	Cr. Amount (₹)
30.7.2012	Equity Stock Option Premium (Anisha Ltd.) A/c Dr.	2,500	
	To Bank A/c		2,500
	(Being Premium paid on Stock Option of Anisha Ltd. purchased at ₹ 25 per unit for 100 units constituting one lot.)		
30.8.2012	Equity Shares of Anisha Ltd. A/c Dr.	30,000	
	To Bank A/c		30,000
	(Being Call option exercised and shared acquired)		
30.8.2012	Profit & Loss A/c Dr.	2,500	
	To Equity Stock Option Premium (Anisha) A/c		2,500
	(Being Premium on option written off on exercise of option)		

Note: No entries have been passed in respect of Margin Payments. This is because; the buyer of the option contract is not required to pay any margin.

(ii) When the option in settled in cash and the index price ₹ 310 per unit:

Journal Entries

Date	Particulars	Dr. Amount (₹)	Cr. Amount (₹)
30.7.2012	Equity Stock Option Premium (ANISHA Ltd.) A/c Dr.	2,500	
	To Bank A/c		2,500
	(Being Premium paid on Stock Option of Anisha Ltd. purchased at ₹25 per unit for100 units constituting one lot)		
30.8.2012	Bank A/c Dr.	1,000	
	To Profit & Loss A/c		1,000
	(Being the profit on exercise of option received)		
30.8.2012	Profit & Loss A/c Dr.	2,500	
	To Equity Stock Option Premium (Anisha) A/c		2,500
	(Being Premium on option written off on exercise of option).		

Illustration 7.

A Ltd. issued convertible 10% Debenture of ₹10,00,000 on 01.04.2013. Interest is payable annually and the debentures are to be converted on 31.03.2016. Similarly, Debenture without conversion carry 15% p.a. rate of interest. Calculate the value of Equity instrument and financial liability. Show the journal entry at time of issue of debenture and the Debenture (Liability) A/c for the three years.

Solution:

Statement showing computation of Liability & Equity Components

Year	Cash flow (₹)	DF @ 15%	Amount (₹)
2013-14	1,00,000	0.869	86,900
2014-15	1,00,000	0.756	75,600
2015-16	1,00,000	0.658	65,800
		Liability component	2,28,300
		Equity component [B/Fig.]	7,71,700
			10,00,000

Journal entry

Particulars		Dr. (₹)	Cr. (₹)
Bank A/c	Dr.	10,00,000	
To Convertible Debentures A/c [Liability]			2,28,300
To Convertible Debentures A/c [Equity]			7,71,700

Convertible Debentures Account [Liability]

Dr. **Cr.**

Date	Particulars	₹	Date	Particulars	₹
2013-14	To Bank A/c	1,00,000	2013-14	By Bank A/c	2,28,300
	To Balance c/d	1,62,545		By Interest A/c	34,245
				[2,28,300 x 15%]	
		2,62,545			2,62,545
2014-15	To Bank A/c	1,00,000	2014-15	By Balance b/d	1,62,545
	To Balance c/d	86,927		By Interest A/c	24,382
				[1,62,545 x 15%]	
		1,86,927			1,86,927
2015-16	To Bank A/c	1,00,000	2015-16	By Balance b/d	86,927
				By Interest A/c [B/Fig.]	13,073
		1,00,000			1,00,000

Illustration 8.

A Ltd. issued convertible 12% Debenture of ₹10,00,000 on 01.04.13.Interest is payable annually and the debentures are to be converted on 31.03.17. Similarly, Debenture without conversion carry 14% p.a. rate of interest. Calculate the value of Equity instrument and financial liability and the Debenture(Liability) A/c.

Solution:

Statement showing computation of Liability & Equity Components

Year	Cash flow (₹)	DF @ 14%	Amount (₹)
2013-14	1,20,000	0.8772	1,05,264
2014-15	1,20,000	0.7695	92,340
2015-16	1,20,000	0.6750	81,000
2016-17	1,20,000	0.5921	71,052
		2.9137	
∴ Value of Liability [₹ 1,20,000 x PVIFA (14%, 4)]		1,20,000 × 2.9137	3,49,656
∴ Value of Equity [B/Fig.]			6,50,355
			10,00,000

Journal entry:

Particulars		Dr. (₹)	Cr. (₹)
Bank A/c	Dr.	10,00,000	
To Convertible Debentures A/c [Liability]			3,49,645
To Convertible Debentures A/c [Equity]			6,50,355

Convertible Debentures Account [Liability]

Dr. **Cr.**

Date	Particulars	₹	Date	Particulars	₹
2013-14	To Bank A/c	1,20,000	2013-14	By Bank A/c	3,49,645
	To Balance c/d	2,78,595		By Interest A/c	48,950
				[3,49,645 x 14%]	
		3,98,595			3,98,595
2014-15	To Bank A/c	1,20,000	2014-15	By Balance b/d	2,78,595
	To Balance c/d	1,97,598		By Interest A/c	39,003
				[2,78,595 x 14%]	
		3,17,598			3,17,598
2015-16	To Bank A/c	1,20,000	2015-16	By Balance b/d	1,97,598
	To Balance c/d	1,05,262		By Interest A/c	27,664
				[1,97,598 x 14%]	
		2,25,262			2,25,262
2016-17	To Bank A/c	1,20,000	2016-17	By Balance b/d	1,05,262
				By Interest A/c [B/Fig.]	14,738
		1,20,000			1,20,000

Illustration 9.

On 1 April, 2012 Delta Ltd. issued ₹ 30,00,000, 6% convertible debentures of face value of ₹ 100 per debenture at par. The debentures are redeemable at a premium of 10% on 31.03.2016 or these may be converted into ordinary share at the option of the holder the interest rate for equivalent debentures without conversion rights would have been 10%.

Being compound financial instrument, you are required to separate equity and debt portion as on 1.4.2012.

The present value of ₹ 1 receivable at the end of each year based on discount rates of 6% and 10% can be taken as:

	6%	10%
End of year 1	0.94	0.91
End of year 2	0.89	0.83
End of year 3	0.84	0.75
End of year 4	0.79	0.68

Compute value of embedded derivative.

Solution:

Statement showing computation of Liability & Equity Components

Year	Cash flow (₹)	DF @ 10%	Amount (₹)
2013-14	1,80,000	0.91	1,63,800
2014-15	1,80,000	0.83	1,49,400
2015-16	1,80,000	0.75	1,35,000
2016-17	34,80,000	0.68	23,66,400
∴ Value of Liability			28,14,600
∴ Value of Equity [B/Fig.]			1,85,400
			30,00,000

Journal entry:

Particulars		Dr.	Cr.
Bank A/c	Dr.	₹30,00,000	
To Convertible Debentures A/c [Liability]			₹28,14,600
To Convertible Debentures A/c [Equity]			₹1,85,400

Convertible Debentures Account [Liability]

Dr. **Cr.**

Date	Particulars	₹	Date	Particulars	₹
2013-14	To Bank A/c	1,80,000	2013-14	By Bank A/c	28,14,600
	To Balance c/d	29,16,060		By Interest A/c	2,81,460
		30,96,060			30,96,060
2014-15	To Bank A/c	1,80,000	2014-15	By Balance b/d	29,16,060
	To Balance c/d	30,27,666		By Interest A/c	2,91,606
		32,07,666			32,07,666
2015-16	To Bank A/c	1,80,000	2015-16	By Balance b/d	30,27,666
	To Balance c/d	31,50,433		By Interest A/c	3,02,767
		33,30,433			33,30,433
2016-17	To Bank A/c	1,80,000	2016-17	By Balance b/d	31,50,433
	To Bank/ Equity A/c	32,85,476		By Interest A/c [B/Fig.]	3,15,043
		34,65,476			34,65,476

5.2 ACCOUNTING FOR CENVAT & STATE-LEVEL VAT

ACCOUNTING FOR CENVAT

- The Government of India levies various indirect taxes over different activities of the value chain which include, production, manufacture, rendering of services, purchase/ sale etc. accordingly, taxes on manufacture and production, and on purchase/ sale hold important place in the indirect tax arena.
- The duty levied in the event of production/ manufacture of goods in India is Excise Duty. This excise duty has been renamed as Central Value Added Tax (CENVAT).
- No sale or further utilization of excisable goods can take place, unless the duty is paid. Hence, Excise Duty is a necessary expense to be incurred if the goods are to be put in the location and condition in which they can be sold or further used in the manufacturing process.

ACCOUNTING TREATMENT

For the purpose of accounting of CENVAT, the following points with regard to CENVAT i.e. excise duty are to be noted:

- It is a product cost, and **cannot** be treated as a Period Cost.
- It should be considered as a manufacturing expense;
- It has to be considered as an element of cost for Inventory Valuation.
- Where Excise Duty is paid on excisable goods (inputs) and such goods are subsequently utilized in the manufacturing process, the duty paid on such goods (inputs), if the same is not **recoverable from taxing authorities,** becomes a manufacturing cost, and must be **included in the valuation of WIP** or **Finished Goods** arising from the subsequent processing of such goods;
- Where the liability for excise duty has been incurred but its collection is deferred, Provision for the Unpaid Liability should be made.

CENVAT SCHEME

- Central Valued Added Tax (CENVAT) scheme has been applicable w.e.f.01.04.2000.
- The Scheme allows instant credit of duties paid on inputs (Raw Materials) and specified Capital Goods, used in relation to manufacture of specified final excisable goods, to be utilized for payment of excise duties in respect of such goods. Hence, the **CENVAT Credit** taken (on inputs) is in the nature of set-off against the payment of duty on the final products.
- In respect of Capital Goods received in a factory at any point of time in a given financial year, credit can be taken only for an amount not exceeding 50% of the duty paid on such capital goods in such financial year. The balance credit can be taken in any subsequent financial year, provided the Capital Goods are still in the possession and use of the manufacture of final products, in such subsequent year(s).
- The journal entries regarding **CENVAT Credit on Inputs** used in manufacture of final products are as under:

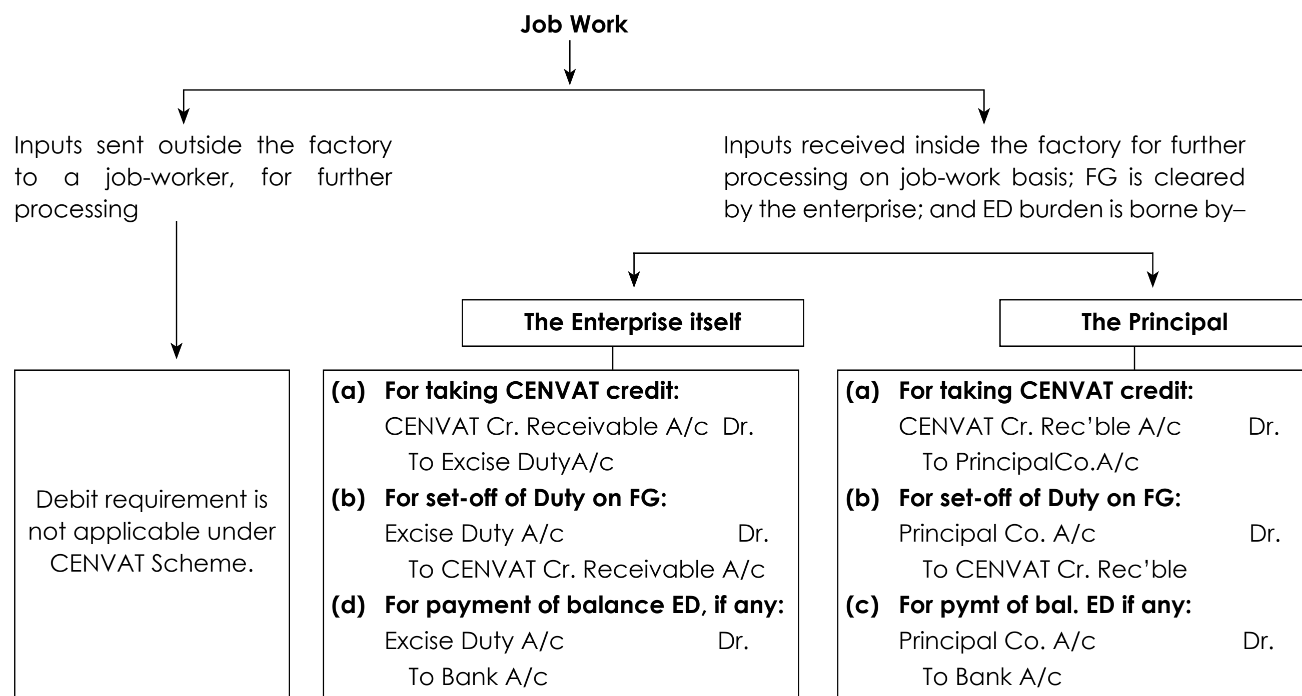
Particulars		Debit (₹)	Credit (₹)
Purchase of Inputs (with Excise Duty there on)			
Purchases A/c	Dr.	Pure Price net of ED	Pure Price incl. ED
CENVAT Credit Receivable (Inputs) A/c	Dr.	ED on Purchases	
To Suppliers / Sundry Creditors / Bank A/c			

Entry		
Sale of dutiable goods Bank/Sundry Debtors A/c Dr. To Sales A/c	FG Price incl. ED on Sales	FG Price incl. ED on Sales
Set-off of CENVAT Credit Excise Duty A/c Dr. To CENVAT Credit Receivable (Inputs)A/c	Credit available or ED payable, Whichever is less	
Payment of balance ED (if credit receivable is less) Excise Duty A/c Dr. To Bank A/c	To the extent of ED actually paid in cash i.e. when Credit Receivable < ED Payable on Sales	

ED = Excise Duty

- **Disclosure in Balance Sheet:** Debit balance in CENVAT Credit Receivable (Inputs)i.e. balance Credit Available for use in subsequent periods, will be shown under the Assets Head of the Balance Sheet under the sub-head **"Other Current Assets".**

ACCOUNTING TREATMENT IN CASE OF JOB WORK



CENVAT CREDIT ON CAPITAL GOODS USED IN MANUFACTURE OF SPECIFIED GOODS

(a) CENVAT credit in respect of Capital Goods should be recognized in the books of account only if – (i)the enterprise is entitled to CENVAT Credit as per Rules; and(ii)there is a reasonable certainty that the CENVAT Credit would be utilized.

(b) The Journal Entries are given below:

Particulars		Debit (₹)	Credit (₹)
Purchase of Capital Goods (with Duty there on)			
Fixed Assets A/c	Dr.	Pure Price net of ED	
CENVAT Credit Receivable (Capital Goods) A/c	Dr.	Credit taken during the year	
CENVAT Credit Deferred(Capital Goods)A/c	Dr.	Balance cr. to be availed in subsequent years	
To Asset Vendor / Bank A/c			Pure Price incl. ED
Set-off of CENVAT Credit during the year			
Excise Duty A/c	Dr.	Credit available during the year or ED payable, whichever is less	
To CENVAT Credit Receivable (Capital Goods) A/c			
Transfer of balance Credit available in subsequent years			
CENVAT Credit Rec'ble (Capital Goods) A/c Dr.		Balance Credit Available for set-off in subsequent financial years.	
To CENVAT Credit Deferred(Capital Goods) A/c			

Note:

- Debit balance in CENVAT Credit Receivable (Capital Goods) A/c and CENVAT Credit Deferred (Capital Goods) A/c i.e. balance Credit Available for use in subsequent periods, will be shown under the Assets Head of the Balance Sheet under the sub-head **"Other Current Assets".**
- Journal Entries for Sale, payment of balance Excise Duty are as in Point 2 above.

CENVAT CREDIT WHERE CAPITAL GOODS ARE ACQUIRED ON LEASE /HIREPURCHASE:

(a) **Accounting in Lessor's Books:** Lessor should account for the price of asset acquired from the Supplier, **net of excise duty only.** When the financing arrangement also covers ED portion, ED recoverable from the lessee should be debited to a separate a/c (and not included in Minimum Lease Payments) and recovered from the lessee. When the financing arrangement does not cover ED portion, the lessee would pay the ED directly to the Supplier and hence need not be recorded in the books of the Lessor.

(b) **Accounting in Lessee's Books:** CENVAT Credit Receivable on Capital Goods acquired on lease should be treated in the same manner as in the case of outright purchase of asset.

(c) **Review of balances in CENVAT Receivable Accounts:**

(i) **Write-off:** Balances in CENVAT Credit Receivable Accounts (Inputs and Capital Goods), should be reviewed at the end of every year. If it is found that the balances of the CENVAT are not likely to be used in the normal course of business, then, notwithstanding the right to carry forward such amount sunder Excise Rules, the **non usable excess credit** should be adjusted in the accounts, asunder -

CENVAT Credit relating to	Treatment
(i) Inputs	• Debit the specific Raw Material or Purchase A/c, so as to increase the cost of consumption, & valuation of closing stocks. • Apportion the excess credit pro-rata to all purchases/ components, if the specific Raw Material cannot be identified.
(ii) Capital Goods /FA purchased	• Debit the cost of Specific Fixed Asset. • Charge depreciation on the revised unamortized depreciable amount, over the balance useful life, prospectively. • If the specific Fixed Asset no longer exists, write off the excess unutilisable credit to P&L Account.
(iii) Capital Goods on Lease / HP	Write off on pro-rata basis to P&L A/c, along with Lease Rentals.

(ii) Reconciliation: A reconciliation statement between the CENVAT Credit Receivable (Dr.) as per financial accounts and the credit available as per Excise Registers, should be prepared.

(iii) Non compliance with conditions: Where conditions for availing credit have not been complied with, or are not being capable of compliance, e.g. where inputs are destroyed or fixed assets cannot be used for manufacture of the final products, the appropriate adjustments should be made as per point (i) above.

(v) Payment of Duty Demands by set-off i.e. Debit to CENVAT Credit Receivable Account:

Situation	Treatment	RM Valuation
(a) Duty relating to Finished Goods	Excise Duty A/c Dr. To CENVAT Credit Receivable A/c	No change
(b) Disallowance of CENVAT Credit on purchases during the period	Purchases / Raw Material A/c Dr. To CENVAT Credit Receivable A/c	RM Inputs Cost to be Increased to include ED
(c) Disallowance of CENVAT Credit on purchases of previous periods	If such inputs are consumed during the year: Same entry in (a) above. If such inputs are still in stock at the End of year: Same entry in(b)above.	**Not Applicable** RM Inputs Cost to be Increased to include ED

(vii) Inventory Valuation Principles: The principles of inventory valuation are summarized here under:

Item valued	Inventory Valuation Principle
Inputs where CENVAT Credit Availed	Purchase Price net of Input Duty. (See ***Note*** below)
Inputs if CENVAT Credit is not availed	Total Purchase Price, including Input Duty. e.g. purchases without requisite documents for availing CENVAT Credit;-purchases from Small Scale Supplier's who are Exempted from duty; purchases from dealers who are not eligible to issue CENVAT Invoice as per Excise Rules etc.
Final Products	Value of Inputs should be net of duty on inputs i.e. Purchase Price, net of Input Duty. However, provision should be made/ added for Excise Duty Liability on Final Products.
Capital Goods	Purchase Price net of Input Duty.

Note:

If any input is used in the production of more than one final product, some of which are excisable while others are not excisable or charged to Nil rate of duty,the valuation of RM input will be as under-

- **If separate Raw Material (RM) inventory records are not maintained**: All RM Inventory should be valued net of input duty.
- **If separate Raw Material (RM) inventory records are maintained**: In such cases, valuation will differ and will be done as under:
- **RM Inventory used for production of excisable final products** should be valued net of input duty;
- **RM Inventory used for production of non-excisable goods or Nil duty goods** should be valued at actual cost, inclusive of input duty.

Illustration 10: Excise Duty Treatment

Ram Ltd. is manufacturing goods for local sale and exports. As on 31st March, it has the following finished stocks in the factory warehouse:

(a) Goods meant for local sale ₹ 100 Lakhs (Cost ₹75 Lakhs).

(b) Goods meant for exports ₹ 50 Lakhs (Cost ₹ 20 Lakhs).

Excise duty is payable at the rate of 16%. The Company's Managing Director says that Excise Duty is payable only on clearance of goods and hence is not a cost. Advise the Company on the proper treatment of Excise Duty.

Solution:

- Excise Duty is an indirect tax, arising as a consequence of manufacture of excisable goods irrespective of the manner of use/disposal of goods there after i.e. sale, destruction or captive consumption.
- **Regarding Managing Director's contention**: Levy of excise duty is and remains upon the manufacture or production alone. Only collection part of it is shifted to the stage of removal. Hence, the Managing Director's contention that "Excise Duty is payable only on clearance of goods and hence is not a cost" is **incorrect.** As per the Guidance Note on Accounting Treatment for Excise Duty, Excise Duty should be considered as a manufacturing expense and like other manufacturing expenses be considered as an element of cost for inventory valuation. The Guidance Note also requires that where the liability for excise duty has been incurred but its collection is deferred, Provision for the Unpaid Liability should be made.
- **Duty on goods meant for local sale**: CENVAT i.e. Excise duty on the goods meant for local sales should be provided for at the rate of 16% on the Selling Price i.e. 16% of ₹ 100 Lakhs = ₹ 16 Lakhs for valuation of stock.
- **Duty on goods meant for exports**: Excise Duty need not be provided for the goods meant for exports, even though the manufacture there of is completed, presuming that all the necessary conditions specified in the Central Excise Rules, regarding export of excisable goods without payment of duty have been fulfilled by the Company.

Illustration 11: Inventory Valuation principles

A Factory started activities on 1stApril. From the following data, obtain the Value of Closing Stock on 30th April.

- Raw Materials purchased during April = 80,000 kg at ₹12 (out of which Excise Duty = ₹2 per kg). Stock on hand as on 30thApril = 5,000 kg.
- Production during April = 14,000 units (of which 10,000 units were sold). In addition to the production, 1,000 units were lying as WIP on 30th April (100% complete as to Materials and 60% complete as to conversion).
- Wages and Production Overheads = ₹30 per completed unit.
- Selling Price = ₹110 per unit(of which Excise Duty is ₹10 per unit)

Solution:

Particulars	Computation	₹
1. Raw Material Valuation (net of Input Excise Duty)	5,000 kg x ₹10 per kg.	50,000
2. WIP Valuation (net of RM input duty)	(₹50 + 60% of ₹30) x 1,000 units	68,000
3. Finished Goods Valuation (including ED on SP)	(RM 50 + Lab & OH 30 + ED 10) = ₹90 × (14,000 units - 10,000 units)	3,60,000
Total		**4,78,000**

Computation of Cost per unit of production:

- Raw Materials: (80,000 - 5,000) = 75,000 kg for 15,000 units total = 5 kg x ₹10 (net of ED) = ₹50
- Wages and Production Overhead =₹30 per completed unit (given)

Illustration 12: CENVAT Credit Accounting

A Factory went into commercial production on 1stApril, it uses two raw materials M and N, on which excise duty of ₹30 per Kg and ₹20 per Kg respectively is paid. On 31st March it had stock of 2,000 Kg of M and 1,500 Kg of N which it had purchased at an all inclusive price of ₹150 per Kg for M and ₹120 per Kg for N. The Suppliers of the materials are to receive payment on 15th May.

During the month of April, the Factory manufactured 4,000 units of the end product for which the consumption of Materials M and N were 6,000 Kg and 4,500 Kg respectively. The Excise Duty on the end product is 60 per unit. 30,000 units of the end product were despatched, 800 units were kept in bonded warehouse and balance 200 units were kept in finished goods godown.

During the month the Factory purchased 5,000 Kg of M at ₹145 per kg (inclusive of Excise Duty ₹30 per Kg) on credit of 60 days and 5,000 Kg of N at ₹110 per Kg (inclusive of Excise Duty ₹20 per Kg) on credit of 45 days.

The cost of "converting" the raw materials into finished product amounts to ₹150 per unit of end product of which ₹100 is "cash cost" paid immediately and ₹50 represents non-cash charge for depreciation. There is no Work-in-Process.

Sales are made at ₹750 per unit in respect of credit transactions and at ₹700 per unit in respect of cash transactions. 20% of despatches were in respect of cash transactions while the balance 80% were in respect of credit transactions (1 month credit).

(i) Calculate CENVAT Credit Available, CENVAT Credit Availed of and balance in CENVAT Credit as on 30th April.

(ii) Show the necessary ledger accounts in respect of CENVAT.

(iii) Value the inventory of - (a) Raw Material; (b) Finished Goods in Bonded Warehouse and(c)Finished Goods in Finished Goods Godown on "First-In-First-Out" principle.

(iv) Show the Ledger Accounts of Customers, Suppliers and Bank, assuming that the necessary bank Balance is available at the start of the month to meet "cash" expenses of that month.

(v) Calculate the profit earned for the month.

(vi) Calculate the Working Capital as on 30th April. State the impact of 'CENVAT' on Working Capital Requirement of the Factory as on 30thApril.

Solution:

1. CENVAT Credit Available, Availed of and Balance Credit at the end of April

Material	M			N			Total Amount
	Kgs.	**ED Rate**	**Amount**	**Kgs.**	**ED Rate**	**Amount**	₹
Opening Stock for April	2,000	30	60,000	1,500	20	30,000	90,000
Purchases during April	5,000	30	1,50,000	5,000	20	1,00,000	2,50,000
Total Credit Available			**2,10,000**			**1,30,000**	**3,40,000**
Less: CENVAT Credit availed on Production of 40,000 units at ₹60 p.u. **(See Note)**							2,40,000
Balance in CENVAT Credit at the end of April							**1,00,000**

Note:

- Guidance Note on Accounting Treatment for Excise Duty, requires that a provision for liability in respect of unpaid excise duty should be made in the accounts in respect of stocks lying in the factory or bonded ware house since the liability for excise duty arises when the manufacture of the goods is completed.
- CENVAT Rules permit storage of goods in bonded warehouses, without payment of duty. In the absence of information, Excise Duty has been considered on 800 units also which were kept in bonded warehouse.

Note: Valuation of Finished Goods is based on FIFO principle. Hence, Closing Stock of Finished Goods would consist of goods produced by consuming materials out of current period purchase. Hence, entire raw materials consumption has been taken at current period net purchase price of ₹115 and ₹90 per kg respectively.

2. Customers, Suppliers and BankAccounts

(a) Customers Account

Dr. **Cr.**

Date	Particulars	₹	Date	Particulars	₹
April 1,	To Sales 3,000 × 80% x ₹750	18,00,000	April 30	By Balance c/d (closing balance)	18,00,000

(b) Suppliers Account

Dr. **Cr.**

Date	Particulars	₹	Date	Particulars	₹
April 30	To Balance c/d	17,55,000	April 1	By Balance b/d (opening balance) M: 2,000 kg × ₹150 = 3,00,000 N: 1,500 kg × ₹120 = 1,80,000	4,80,000
				By Purchases A/c (value net of ED)	10,25,000
			April	By CENVAT Credit Receivable M: 5,000 kg × ₹30 = 1,50,000 N : 5,000 kg × ₹20 = 1,00,000	2,50,000
		17,55,000			**17,55,000**

(c) Bank Account

Dr. **Cr.**

Date	Particulars	₹	Date	Particulars	₹
April 1	To Balance b/d (See Note)	4,00,000	April	By Expenses A/c (4,000 × ₹100)	4,00,000
April	To Sales A/c (3,000 × 20% × ₹700)	4,20,000	Apr30	By Balance c/d (closing balance)	4,20,000
		8,20,000			**8,20,000**

Note: It is assumed that the Factory has adequate cash balance equivalent to meet cash expenses for the month.

3. (a) Profit and Loss Account for the month of April

Dr. **Cr.**

Particulars	₹	Particulars	₹
To Opening Stock of Materials:		By Sales: Cash: 3,000 × 20% × 700	4,20,000
M (150-30) × 2,000 kgs	2,40,000	Credit: 3,000 × 80% × 750	18,00,000
N (120-20) ×1,500 kgs	1,50,000	By Closing Stocks:	
To Purchases(as per PurchA/c above)	10,25,000	- Material M (as per valuation above)	1,15,000
To Excise Duty (CENVAT availed)	2,40,000	- Material N (as per valuation above)	1,80,000
To Conversion Costs (4,000 × 150)	6,00,000	- Finished Goods (as per vain above)	4,83,750
To Gross Profit c/d	7,43,750		
	29,98,750		**29,98,750**

Note: It is assumed that Sale Prices of ₹700 and ₹750 are inclusive of the Duty of ₹60 per unit on FG.

3. (b) Reconciliation of Profits

Particulars	₹
Profits for Output Sold: Cash Sales: 3,000 x 20% × (700- 483.75)	1,29,750
Credit Sales: 3,000 x 80% x (750 - 483.75)	6,39,000
Total Profit based on Quantity Sold	7,68,750
Less: Excess Cost of Opening Stock of Materials not considered in FG Valuation:	
M:2,000 kgs × (₹120 - ₹115)(all prices net of ED)	10,000
N:1,500 kgs ×(₹100 - ₹90)(all prices net of ED)	15,000
Profit as per above P&L Account	**7,43,750**

4. Computation of Working Capital as on 30th April

Particulars		₹
Current Assets:		
A. Raw Materials Stock		
Material M	1,15,000	
Material N	1,80,000	2,95,000
Finished Goods Stock Bonded Warehouse	3,87,000	
Finished Goods Godown	96,750	4,83,750
Debtors/Customers		18,00,000
Bank Balance		4,20,000
CENVAT Credit Receivable		1,00,000
Total Current Assets		**30,98,750**
A. Current Liabilities: Suppliers/Sundry Creditors		17,55,000
B. Net Working Capital (A-B)		13,43,750

Impact of CENVAT on Working Capital Requirements:

- 3,000 units of Finished Goods have been dispatched by way of sale without payment of a single rupee in cash. Cash out lay so saved at ₹60 per unit is ₹2,40,000. (i.e. to the extent of CENVAT Credit Availed).
- Creation of a Current Asset worth ₹1,00,000 in CENVAT Credit Receivable Account, reduces the Pressure on Working Capital.

Illustration 13: CENVAT on Capital Goods

A Company purchased a plant for ₹50 Lakhs during the financial year and installed it immediately. The price charged by the Vendor included Excise Duty (CENVAT Credit Available) of ₹5 Lakhs. During this year, the Company also produced excisable goods on which Excise Duty chargeable is ₹4.50 Lakhs. Show the Journal Entries describing CENVAT Credit treatment. At what amount should the Plant be capitalized?

Solution:

Journal

Particulars		Dr. (₹)	Cr. (₹)
Fixed Assets A/c	Dr.	45,00,000	
CENVAT Credit Receivable (Capital Goods)A/c	Dr.	2,50,000	
CENVAT Credit Deferred (Capital Goods)A/c	Dr.	2,50,000	
To Asset Vendor / Bank A/c			50,00,000
(Being Plant purchased recorded, including immediate CENVAT Credit available of 50%, balance 50% (assumed) credit available in subsequent year)			
Excise Duty A/c	Dr.	2,50,000	
To CENVAT Credit Receivable A/c (Capital Goods)			2,50,000
(Being set off of CENVAT Credit during the year)			
Excise Duty A/c	Dr.	2,00,000	
To Bank A/c			2,00,000
(Being balance Excise Duty payable ₹4,50,000 ,₹2,50,000 set-off, now justify settled)			
Subsequent Financial Year			
CENVAT Credit Receivable (Capital Goods)A/c	Dr.	2,50,000	
To CENVAT Credit Deferred (Capital Goods)A/c			2,50,000
(Being transfer of balance CENVAT Credit available on Capital Goods)			

Assets	₹
Non-current Assets	
Fixed Assets:	
Tangible – Plant at Cost	45,00,000
Other Non-current Assets:	2,50,000

ACCOUNTING FOR STATE LEVEL VALUE ADDED TAX

Over the years the Indian sales tax structure was devoid of the VAT system. However, during the first decade of the 21st century, the state-level statutes were for first time brought under VAT.

Features of Sales Tax under VAT structure:

(a) **VAT Credit:** A registered dealer(trader/manufacturer)is entitled to an input tax credit(called as VAT Credit), in respect of taxes paid on purchases made during the period, where the purchases arise in the course of his activities as a dealer.

(b) **Set Off Facility:** VAT Credit is followed for purchase of inputs/supplies meant for sale, or for utilization in the process of production for such sale, irrespective of when these are utilized/sold, and reduces the immediate tax liability of the dealer.

(c) **Purchase within State:** VAT Credit is available for all for purchase of inputs /supplies in a State, meant for sales within the State or sale into the States. Even for Stock Transfer/Consignment Sales of goods out of the State, input tax paid in excess of a certain percentage is eligible for VAT Credit. VAT Credit is not allowable for taxes paid on purchases from other States.

(d) **Refund of Excess VAT Credit:** Where VAT Credit exceeds the tax payable on sales in a month, the excess credit is carried over to the future month(s). Any excess unadjusted VAT Credit at the end of the specified period, is eligible for refund.

(e) **VAT Goods, Exempt and Zero Rate Goods:** VAT legislation of each State will specify the goods which are covered under VAT, and the relevant VAT rates. In case of "exempt" goods, the dealer is not eligible to claim VAT Credit for tax paid on the purchase of inputs. However, in case of "Zero Rate" Goods, the dealer is eligible to claim VAT Credit for tax paid on the purchase of inputs. Also, Goods not covered by VAT are taxed under the Sales Tax Actor other Act.

(f) **Export Sales:** Export Sales are "Zero Rate" Sales under VAT. Hence, VAT need not be charged and paid on Sales made. However, the Exporter is entitled to VAT Credit in respect of tax paid with in a State on the purchase of inputs. This VAT Credit is not restricted only to those goods which are meant or used in the manufacture of exports. If in any tax period, the VAT Credit exceeds the output tax, and the dealer has declared international exports in the same tax period, he can claim refund of excess VAT credit. The units located in SEZ / EOU's are either exempted from payment of input tax, or eligible for refund of input tax paid, within a specified period.

(g) **Deferral Scheme:** In some State VAT laws, industrial units may be granted deferral facility for payment of tax, net of VAT Credit, i.e. output tax is collected from customers at the time of making sale; but the payment (after setting off VAT Credit on inputs) is deferred to a future point of time.

(h) **Capital Goods–36 months spread over:** VAT Credit is also available on capital goods (except a few items included in the negative list of respective State laws). This may be adjusted over a maximum of 36 equal monthly instalments. However, some States may reduce the number of instalments or may grant full credit in the month of purchase of Capital Goods.

(i) **Small Dealrs – Composition Scheme:** Small dealers with annual gross turnover not exceeding specified limits, who are otherwise liable to pay VAT, however, have the option to pay tax under the Composition Scheme. Such dealers may pay tax at a prescribed small percentage of the Gross Turnover, and are not entitled to any VAT Credit.

(j) Works Contracts: Dealers executing Works Contracts may have the following options-(a) pay tax on the value of goods at the time of incorporation of goods in the works executed, at the rates applicable to those goods; or (b) pay tax under composition scheme, at a prescribed rate on the total consideration received. In the second case, such dealers may not been titled to any VAT Credit or may be eligible for partial VAT Credit.

VAT CREDIT IN CASE OF INPUTS OR SUPPLIES:

The Accounting treatment illustrated here under is required only where VAT Credit is available.

Accounting Treatment:

Particulars		Debit (₹)	Credit (₹)
Purchase of Inputs (with VAT thereon)			
Purchases A/c	Dr.	Purchase Price net of VAT	
VAT Credit Receivable (Inputs)A/c	Dr.	VAT Paid on Purchases	
To Suppliers / Sundry Creditors / Bank A/c			Purchase Priceincl.VAT
Sale of goods			
Bank/Sundry Debtors A/c	Dr.	Price incl.VAT on sales	
To Sales A/c			Price excl.VAT
To VAT Payable A/c			VAT on Sales
Set-off of VAT Credit			
VAT Payable A/c	Dr.	VAT Credit available or VAT payable,	
To VAT Credit Receivable(Inputs)A/c		Whichever is less	
Payment of balance VAT			
(if credit receivable is less)		To the extent of VAT actually paid in cash, i.e. when Credit Receivable < VAT Payable on Sales	
VAT Payable A/c	Dr.		
To BankA/c			

Note:

Disclosure in Balance Sheet:

(a) Debit balance in VAT Credit Receivable (Inputs), if any, will be shown on the Assets Side of the Balance Sheet under the sub-head **"Other Current Assets".**

(b) Alternatively, credit balance in VAT Payable A/c, if any, will be shown under **"Current Liabilities".** Where the dealer enjoys deferral benefits of VAT Payable, the credit balance will be shown as **'Other Non-current Liabilities'.**

NB: The above treatment is not required in the following situations:

- Dealers not registered under VAT;
- Dealers having turnover below the specified limits and opting for Composition Scheme;
- Dealers engaged in Works Contracts and opting for tax by way of composition; and
- Purchase of goods from Unregistered Dealers (not eligible for VAT Credit).

VAT CREDIT IN CASE OF COMMON INPUTS

Where common inputs are used for making taxable sales as well as exempt sales the under-mentioned principles should be followed:

- The dealer should, on the date of purchase, estimate the inputs expected to be used for making the taxable sales and for making exempt sales.
- VAT Credit should be recognized only in respect of inputs which are expected to be used in making taxable sales.
- No VAT Credit should be recognized on inputs which are expected to be used in making exempt sales.
- Where the actual use is different from the estimated use, an adjustment entry should be passed.

VAT CREDIT IN CASE OF STOCK TRANSFER/CONSIGNMENT SALES

In case of Stock Transfer / Consignment Sale of goods outside the State where VAT Credit is available only to an extent of input tax paid, the dealer should estimate the expected Stock Transfers/Consignment Sales and account for accordingly.

VAT CREDIT IN CASE OF ELIGIBLE CAPITAL GOODS

Particulars		Debit (₹)	Credit (₹)
Purchase of Capital Goods (with VAT thereon)			
Fixed Assets A/c	Dr.	Purchase Price net of VAT	
VAT Credit Deferred (Capital Goods) A/c	Dr.	VAT paid on Purchases	
To Asset Vendor / Bank A/c			Purchase Price incl. VAT
Transfer of VAT Credit Receivable during the year			
VAT Credit Receivable(Capital Goods) A/c	Dr.	Credit available during the year as per the relevant State VAT Law	
To VAT Credit Deferred (Capital Goods) A/c			

Note:

- Debit balance in VAT Credit Receivable (Capital Goods) A/c (after utilization for set-off for payment during the period) and Debit balance in VAT Credit Deferred (Capital Goods) A/c i.e. balance Credit Available for use in subsequent periods, will be shown on the Assets Side of the Balance Sheet under the head **"Loans and Advances"**.
- Depreciation on Machinery will be charged on the Purchase Price net of VAT.

(i) Adjustment (i.e. Debit) to VAT Credit Receivable A/c -

Situation	Treatment		Other Points
(a) Set-off of VAT Payable on Sales	VAT Payable A/c	Dr.	No change in Input Stock Valuation.
	To VAT Credit Receivable A/c		
(b) Disallowance of VAT Credit on purchases during the period	Purchases / Raw Material A/c	Dr.	RM Inputs Cost to be increased to include VAT
	To VAT Credit Receivable A/c		
(a) Disallowance of VAT Credit on purchases of previous periods	<u>If such inputs are used/sold during the year;</u> (prior period item)		RM Inputs Cost to be increased to include VAT
	Profit and Loss A/c	Dr.	
	To VAT Credit Receivable A/c		
	<u>If such inputs are still in stock at the end of year:</u> Same entry in (b)above.		
(b) Disallowance of VAT Credit on Capital Goods(See Note below)	<u>If asset is still in use:</u>		Deprn to be charged on revised amt, incl. VAT
	Relevant Asset A/c	Dr.	
	To VAT Credit Receivable A/c		Appropriate disclosure to be made in A/cs.
	<u>If asset no longer exists:</u>		
	Profit and Loss A/c	Dr.	
	To VAT Credit Receivable A/c		

Note: Insituation (d) above, where the VAT Credit disallowed on Capital Goods is VAT Credit Deferred (Capital Goods) Account and has not be transferred to VAT the former account shall be credited while passing the Journal Entries.

(ii) Inventory Valuation Principles: The principles of inventory valuation are summarized below-

Item Valued	Inventory Valuation Principle
Inputs where VAT Credit Availed	Purchase Price net of Input VAT.
Inputs if VAT Credit Not Availed	Total Purchase Price, including Input VAT. e.g. purchases without requisite documents for availing VAT Credit, purchases from small dealers who are exempted from VAT; purchases from unregistered dealers who are not eligible to issue VAT Invoice etc.
Final Products	Value of Inputs should be net of VAT on inputs i.e. Purchase Price, Net of Input VAT.
Capital Goods, Components etc.	Purchase Price net of Input Duty

(iii) Income Accounting: Sales should be reported net of VAT. Hence, VAT Collection and VAT Payment should **not** be treated as Income and Expense respectively. VAT charged and collected by a dealer on Sales made by him should be credited separately to"VAT Payable Account". When a dealer has not charged VAT separately, but has made a composite charge, he should segregate the portion of Sale Price and VAT Collection at periodic intervals and credit the VAT Collection to "VAT Payable Account".

(iv) VAT Refund Accounting: Input tax which cannot be adjusted against VAT payable over the specified period of time and input tax paid on purchases made for exports, are eligible for refund. Refund of such VAT is recorded by the following entry –

Bank A/c	Dr.	

(v) VAT Credit on Inputs lying in Stock at the beginning of the Scheme: VAT Credit is also available on tax-paid goods lying in stock at the inception of the VAT Scheme, if required documents are available with the dealer. The suggested accounting treatment is -

Particulars		Debit (₹)	Credit (₹)
VAT Credit available on Opening Stock			
VAT Credit Receivable (Inputs)A/c	Dr.	If Credit is available	
VAT Credit Deferred (Opening Stock) A/c	Dr.	immediately	
To VAT Credit Available on Opening Stock A/c		If Credit is available in future	Credit Available

Note:

- A Transfer Entry will be made from VAT Credit Deferred (Opening Stock) A/c to VAT Credit Receivable (Inputs) A/c, as and when VAT Credit on Opening Stock becomes available.
- VAT Credit Available on Opening Stock A/c (Credit Balance) will be shown as a deduction from "Opening Stock" in the Profit and Loss Account.

Illustration 14: VAT Accounting – Inputs / Supplies

The details of purchases made by a Registered Dealer during March are –

Particulars	Total Purchase Value	Input Tax Paid	Net Balance Amount
4% VAT Goods	₹20,80,000	₹80,000	₹20,00,000
12.5% VAT Goods	₹18,00,000	₹2,00,000	₹16,00,000
VAT Exempt Goods	₹4,00,000	–	₹4,00,000
Total	**₹42,80,000**	**₹2,80,000**	**₹40,00,000**

The above input tax paid is fully eligible for VAT Credit. The details of Sales during this month are -

Particulars	Total Sale Value	Output Tax Collected	Net Sales Consideration
4% VAT Goods	₹22,88,000	₹88,000	₹22,00,000
12.5% VAT Goods	₹20,25,000	₹2,25,000	₹18,00,000
VAT Exempt Goods	₹5,00,000		₹5,00,000
Total	**₹48,13,000**	**₹3,13,000**	**₹45,00,000**

Suggest the accounting treatment for the above.

Solution:

Particulars		Debit (₹)	Credit (₹)
4% VAT Goods Purchase A/c	Dr.	20,00,000	
12.5% VAT Goods Purchase A/c	Dr.	16,00,000	
VAT Exempt Goods Purchase A/c	Dr.	4,00,000	
VAT Credit Receivable (Inputs)A/c	Dr.	2,80,000	
To Bank/ Suppliers/Sundry Creditors A/c			42,80,000
(Being purchases of various goods and input tax thereon paid)			
Bank/Customers/Sundry DebtorsA/c	Dr.	48,13,000	
To 4% VAT Goods Sales A/c			22,00,000
To 12.5% VAT Goods Sales A/c			18,00,000
To VAT Exempt Sales A/c			5,00,000
To VAT Payable A/c			3,13,000
(Being sale of various goods and VAT collection thereon)			
VAT Payable A/c	Dr.	2,80,000	
To VAT Credit Receivable(Inputs)A/c			2,80,000
(Being set-off of VAT Credit against liability for VAT payment)			
• At the end of this month, the balance in VAT Payable A/c ₹33,000 will be displayed in the B/Sheet under the head **"Current Liabilities".**			
• The dealer may include the following disclosures in the Notes: (a)Cost of Inventoriesis net of VAT Credit; (b) Sales are exclusive of VAT.			

For payment of VAT in the subsequent month			
VAT Payable A/c	Dr.	33,000	
To Bank A/c			33,000
(Being liability for VAT of previous month, now settled)			

Illustration 15: VAT Accounting – Capital Goods

On 1st June, a Registered Dealer purchased a Machinery for ₹93,60,000 which includes State VAT of ₹3,60,000. As per the State VAT Laws, the input VAT on Capital Goods is adjustable in 36 equal monthly installments beginning from 1st July of the year. During the financial year, the dealer has set-off a sum of ₹25,000 from the VAT Credit Receivable on Capital Goods, against VAT payable on the sales made by him. The dealer charges 10% p.a. depreciation on Machinery. Suggest the accounting treatment for the above.

Solution:

Particulars		Debit (₹)	Credit (₹)
Machinery A/c	Dr.	90,00,000	
VAT Credit Deferred (Capital Goods) A/c	Dr.	3,60,000	
To Bank/Asset Vendor A/c			93,60,000
(Being machinery purchased and input tax thereon paid)			
VAT Credit Receivable (Capital Goods) A/c	Dr.	90,000	
To VAT Credit Deferred (Capital Goods) A/c			90,000
(Being VAT Credit available on Capital Goods for the current period i.e. 1st July to 31st March = ₹3,60,000 x 9/36 = ₹90,000)			
VAT Payable A/c	Dr.	25,000	
To VAT Credit Receivable (Capital Goods) A/c			25,000
(Being set-off of VAT Credit against liability for VAT payment)			
Depreciation A/c	Dr.	7,50,000	
To Machinery A/c			7,50,000
[Being Depreciation on Machinery = (₹90,00,000 x 10% x 10/12)]			

Balance Sheet as on 31st March end of financial year (includes)

Assets		₹
Non-current Assets		
Fixed Assets:		
Tangible – Machinery	90,00,000	
Less: Depreciation	7,50,000	82,50,000
Other Non-current Assets:		
VAT Credit Deferred (Capital Goods)		2,70,000
VAT Credit Receivable(Capital Goods)		65,000

5.3 NON-BANKING FINANCIAL COMPANY (NBF) – PROVISIONING NORMS & ACCOUNTING

INTRODUCTION

The financial sector in any economy consists of several intermediaries, which include the banks, investment intermediaries (viz. mutual funds, hedge funds, pension funds etc.), risk transfer entities (i.e. the insurance companies), information and analysis providers (viz. rating agencies, financial advisers, etc), investment banks, portfolio managers. All the above mentioned financial intermediaries, other than the banks, are broadly referred to as Non-Banking Financial Institutions.

Non-Banking Financial Companies (NBFCs), forms an integral part of Indian financial system, providing various financial services. In recent times, activities of NBFCs have undergone variety of changes through financial innovation. NBFC initially gets incorporated under Indian Companies Act, 2013 and later on obtains Certificate of Incorporation from RBI.

NON-BANKING FINANCIAL COMPANY (NBFC) – CONCEPT

- Non-Banking Finance Company (NBFC) is a financial institution which does not meet the legal definition of bank but carries the similar activities to that of bank like lending and making investments i.e. such an institution does not hold a banking license.
- As per Sec. 45I(f) of RBI Act, 1934, a non-banking financial company'' means:
  (i) a financial institution which is a company;
  (ii) a non-banking institution which is a company and which has as its principal business the receiving of deposits, under any scheme or arrangement or in any other manner, or lending in any manner;
  (iii) such other non-banking institution or class of such institutions, as the Bank may, with the previous approval of the Central Government and by notification in the Official Gazette, specify.
- A Non-Banking Financial Company (NBFC) is a company registered under the Companies Act, 2013 which is engaged in the business of:
  ✓ loans and advances,
  ✓ acquisition of shares/stocks/bonds/debentures/securities issued by Government or local authority or other marketable securities of a like nature,
  ✓ leasing,
  ✓ hire-purchase,
  ✓ insurance business,
  ✓ chit business.

  However, such a company but does not include any institution whose principal business is that of:
  ✓ agriculture activity,
  ✓ industrial activity,
  ✓ purchase or sale of any goods (other than securities), or providing any services, and
  ✓ sale/ purchase/ construction of immovable property.
- Moreover, a non-banking institution which is a company and has principal business of receiving deposits, under any scheme or arrangement, in one lump sum or in installments, by way of contributions or in any other manner, is also a non-banking financial company (called a **Residuary non-banking company**).

CLASSIFICATION OF NON- BANKING FIANNCIAL COMPANIES (NBFCs)

NBFCs can be classified on the following bases:

[A] On the basis of Liability Structure

On the basis of liability structure, the NBFCs can be divided into two categories: NBFCs accepting public deposits (referred to as NBFCs-D), and NBFCs not raising public deposits (referred to as NBFCs-ND).

1. **Deposit taking NBFCs (referred to as NBFCs-D):** These NBFCs are subject to the requirements of Capital adequacy norms, Liquid assets maintenance norms, Exposure norms (including restrictions on exposure to investments in land, building and unquoted shares), Asset Liability Management (ALM) discipline and reporting requirements.
2. **Non-Deposit taking NBFCs (referred to as NBFCs-ND):** Till 2006 NBFCs-ND were subject to minimal regulations. However, since 2007, NBFCs-ND with assets of ₹ 100 crores and above are being classified as **Systemically Important Non-Deposit taking NBFCs (NBFCs-ND-SI).**

Presently, in the light of the overall increase in the growth of the NBFC sector, the threshold for defining systemic significance for NBFCs-ND (non-deposit taking NBFCs) has been revised. Accordingly, the NBFCs-ND-SI will henceforth be those NBFCs-ND which have asset size of ₹500 crore and above as per the last audited balance sheet.

Thus, now the NBFCs-ND shall be categorized into two broad categories in accordance with the revised threshold limit for systemic significance:

- NBFCs-ND (those with assets of less than ₹ 500 crore) and
- NBFCs-ND-SI (those with assets of ₹ 500 crore and above).

The prudential regulations, such as capital adequacy requirements and exposure norms along with reporting requirements, have been made applicable to the NBFCs-ND-SIs. The ALM reporting and disclosure norms have also been made applicable to them at different points of time.

NB: NBFCs that are part of a corporate group or are floated by a common set of promoters will not be viewed on a standalone basis. The total assets of NBFCs in a group including deposit taking NBFCs, if any, will be aggregated to determine if such consolidation falls within the asset sizes of the above two categories i.e. NBFCs-ND and NBFCs-ND-SI. For this purpose, Statutory Auditors would be required to certify the asset size of all the NBFCs in the Group.

[B] On the basis of nature of primary activities performed

On this basis, the NBFCs can be classified into the following categories:

1. **Asset Finance company** is a company which carries on as its principal business the financing of physical assets supporting productive/economic and general purpose assets.
2. **Leasing company** is a company which carries on as its principal business, the business of leasing of equipments or the financing of such activity.
3. **Investment company** means any company which carries on as its principle business the acquisition of securities.
4. **Loan company** means any company which is a financial institution carrying on as its principal business the providing of finance whether by making loans or advances or otherwise for any activity other than its own but does not include an Asset Finance Company.
5. **Infrastructure finance company** is a company which carries on as its principle business, the financing of the acquisition or construction of infrastructure facilities of various kinds.
6. **Infrastructure Debt Fund** is a company registered as NBFC to facilitate the flow of long term debt into infrastructure projects.
7. **Venture capital company** means any company which carries on as its principle business the providing of start-up capital to new business ventures.
8. **NBFC-Factor** is a non-deposit taking NBFC engaged in the principal business of factoring.
9. **NBFC- Non-Operative Financial Holding Company (NOFHC)** is financial institution through which promoter / promoter groups will be permitted to set up a new bank .It's a wholly-owned Non-Operative Financial Holding Company (NOFHC) which will hold the bank as well as all other financial services companies regulated by RBI or other financial sector regulators, to the extent permissible under the applicable regulatory prescriptions.

REGULATORY APPROACH FOR NBFCs

- **NBFCs-ND Regulatory Approach (Asset size < ₹ 500 Crore):**

The regulatory approach in respect of NBFCs-ND with an asset size of less than ₹ 500 crore will be as under:

(i) **No Regulations for No Deposits and No Customer Interface:** They shall not be subjected to any regulation either prudential or conduct of business regulations if they have not accessed any public funds and do not have a customer interface.

(ii) Conduct of business regulations if have Customer Interface: Those having customer interface will be subjected only to conduct of business regulations if they are not accessing public funds.

(iii) Prudential Regulations for Public Deposits: Those accepting public funds will be subjected to only limited prudential regulations if they have no customer interface.

(iv) Both Regulations for Deposits and Customer Interface: Where both public funds are accepted and customer interface exist, such companies will be subjected both to limited prudential regulations and conduct of business regulations.

(v) Compulsory Compliance of Sec. 45-IA: Irrespective of whichever category the NBFC falls in, registration under Section 45 IA of the RBI Act will be mandatory.

- **NBFCs-ND Regulatory Approach (Asset size > ₹ 500 Crores):**

All NBFCs-ND with assets of ₹ 500 crores and above shall have to comply with prudential regulations as applicable to NBFCs-ND-SI even if they have not accessed public funds.

However, the NBFCs-ND having assets size of ₹500 crores and more shall comply with conduct of business regulations only if customer interface exists.

MANDATORY REQUIREMENTS OF MINIUM NET OWNED FUND BY NBFC:

- In terms of Section 45 IA of the RBI Act, 1934, no NBFC can commence or carry on business of a non-banking financial institution without having a Net Owned Funds (NOF) of ₹ 25 lakhs.
- Thereafter, the requirement of NOF has been increased to ₹200 lakhs for all new companies w.e.f. April 21. 1999 vide RBI Notification No. DNBS.132 CGM (VSNM) - 99 dated April 21, 1999.
- But now all NBFCs are compulsorily required to attain a minimum Net Owned Fund of ₹ 2 crore by the end of March 2017 as per the milestones given below:
  - ✓ ₹ 1 crore by the end of March 2016
  - ✓ ₹ 2 crore by the end of March 2017
- Consequently, the companies that were already in existence even before April 21. 1999 have to attain the above minimum NOF in addition to the new companies applying for grant of COR to commence business of an NBFC on and after November 10, 2014.
- In other words, it shall be mandatory for all NBFCs to attain a minimum NOF of NOF of ₹ 100 lakh by the end of March 2016 and ₹ 200 lakh by the end of March 2017.

NB: All NBFCs, the NOF of which currently falls below ₹ 200 lakh shall submit a statutory auditor's certificate certifying compliance to the revised levels at the end of each of the two financial years as given above.

If any NBFC fails to achieve the prescribed ceiling within the stipulated time period, the Bank will initiate the process for cancellation of COR against such NBFCs.

GETTING RATING TO ACCEPT OR RENEW PUBLIC DEPOSITS FOR NBFC:

In accordance with the revised regulatory framework for NBFCs, all unrated Asset Finance Company (AFC) had to get an investment grade by March 31, 2016 otherwise they would not be allowed to renew existing or accept fresh deposits thereafter. Moreover, the limit for acceptance of deposits for rated AFCs has also been reduced from 4 times to 1.5 times of NOF.

Meanwhile i.e. till March 31, 2016, the unrated AFCs or those with a sub-investment grade rating can only renew existing deposits on maturity but not allowed to accept fresh deposits till they obtain an investment grade rating.

Earlier to this amendment, the unrated AFC having NOF of ₹ 25 lakh or more and maintaining capital adequacy ratio of not less than 15% were allowed to accept or renew public deposits 1.5 times of its NOF subject to ₹10 crore as per extant NBFCs Acceptance of Public Deposit (Reserve Bank) Directions, 1998.

PRUDENTIAL NORMS FOR NBFCs

The Reserve Bank of India has issued detailed directions on prudential norms, vide

✓ Non-Banking Financial (Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2007,

✓ Non-Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015 and

✓ Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015. Applicable regulations vary based on the deposit acceptance or systemic importance of the NBFC.

The directions inter alia, prescribe guidelines on income recognition, asset classification and provisioning requirements applicable to NBFCs, exposure norms, disclosures in the balance sheet, requirement of capital adequacy, restrictions on investments in land and building and unquoted shares, loan to value (LTV) ratio for NBFCs predominantly engaged in business of lending against gold jewellery, besides others. Deposit accepting NBFCs have also to comply with the statutory liquidity requirements.

Enhanced prudential regulations shall be made applicable to NBFCs wherever public funds are accepted and conduct of business regulations will be made applicable wherever customer interface is involved.

The term 'Public Funds' includes:

(a) Funds raised directly or indirectly through public deposits;

(b) Commercial papers;

(c) Debentures;

(d) Inter-corporate deposits; and

(e) Bank finance.

However, the term Public Funds does not includes funds raised by issue of instruments compulsorily convertible into equity shares within a period not exceeding 5 years from the date of issue.

APPLICATION OF PRUDENTIAL REGULATION FOR NBFCs

- **Prudential Regulations for NBFCs-ND (Assets size < ₹ 500 crores):**

  The NBFCs-ND with asset size of less than ₹ 500 crores shall be:

  (A) Exempted from the requirement of maintaining CRAR;

  (B) Exempted from complying with Credit Concentration Norms: and

  (C) Maintain a leverage ratio (Total Outside Liabilities Owned Funds) of 7 to link Asset Growth with the Capital.

- **Prudential Regulations for NBFCs-ND-SI (Asset size > ₹ 500 Crore) and all NBFCs-D:**

Tier 1 Capital:

All NBFCs-ND which have an asset size of ₹ 500 crore and above and all NBFCs-D shall maintain minimum Tier 1 Capital of 10%. The compliance to the revised Tier 1 capital will be phased in as follows:

✓ 8.5% by end of March 2016.

✓ 10% by end of March 2017.

ASSET CLASSIFICATION FOR NBFCs

Every non-banking financial company shall, after taking into account the degree of well defined credit weaknesses and extent of dependence on collateral security for realisation, classify its lease/hire purchase assets, loans and advances and any other forms of credit into the following classes, namely:

(i) Standard assets;

(ii) Sub-standard assets;

(iii) Doubtful assets; and

(iv) Loss assets.

Standard Asset:

Standard Asset means the asset in respect of which, no default in repayment of principal or payment of interest is perceived and which does not disclose any problem nor carry more than normal risk attached to the business.

Sub-standard Asset:

- As per the "Non-Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015, a Sub-standard asset means:

  (a) an asset which has been classified as non-performing asset for a period not exceeding 18 months;

  (b) an asset where the terms of the agreement regarding interest and/ or principal have been renegotiated or rescheduled or restructured after commencement of operations, until the expiry of one year of satisfactory performance under the renegotiated or rescheduled or restructured terms: Provided that the classification of infrastructure loan as a sub-standard asset shall be in accordance with the provisions of paragraph 27 of these Directions.

  NB: The class of assets referred to above shall not be upgraded merely as a result of rescheduling, unless it satisfies the conditions required for the upgradation.

- As per the "Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015", a Sub-standard asset means:

  (a) an asset which has been classified as non-performing asset for a period not exceeding 18 months;

  Provided that the period 'not exceeding 18 months' stipulated in this sub-clause shall be 'not exceeding 16 months' for the financial year ending March 31, 2016; 'not exceeding 14 months' for the financial year ending March 31, 2017; and 'not exceeding 12 months' for the financial year ending March 31, 2018 and thereafter.

  (b) an asset where the terms of the agreement regarding interest and / or principal have been renegotiated or rescheduled or restructured after commencement of operations, until the expiry of one year of satisfactory performance under the renegotiated or rescheduled or restructured terms: Provided that the classification of infrastructure loan as a sub-standard asset shall be in accordance with the provisions of paragraph 27 of these Directions.

Doubtful Asset:

- As per the "Non-systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015", a Doubtful asset means:

  (a) a term loan, or (b) a lease asset, or (c) a hire purchase asset, or (d) any other asset, which remains a sub-standard asset for a period exceeding 18 months.

- As per the "Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015", a Doubtful asset means:

  (a) a term loan, or (b) a lease asset, or (c) a hire purchase asset, or (d) any other asset, which remains a sub-standard asset for a period 'exceeding 18 months' for the financial year ended March 31, 2015; 'exceeding 16 months' for the financial year ended March 31, 2016; 'exceeding 14 months' for the financial year ending March 31, 2017 and 'exceeding 12 months' for the financial year ending March 31, 2018 and thereafter.

Loss Asset:

- As per the "Non-systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015", a Loss asset means:
  - (a) an asset which has been identified as loss asset by the non-banking financial company or its internal or external auditor or by the Reserve Bank of India during the inspection of the non-banking financial company, to the extent it is not written off by the non-banking financial company; and
  - (b) an asset which is adversely affected by a potential threat of non-recoverability due to either erosion in the value of security or non-availability of security or due to any fraudulent act or omission on the part of the borrower.
- As per the "Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015", a Loss asset means:
  - (a) an asset which has been identified as loss asset by the non-banking financial company or its internal or external auditor or by the Reserve Bank of India during the inspection of the non-banking financial company, to the extent it is not written off by the non-banking financial company; and
  - (b) an asset which is adversely affected by a potential threat of non-recoverability due to either erosion in the value of security or non availability of security or due to any fraudulent act or omission on the part of the borrower.

Non-performing Asset:

- As per the "Non-systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015", a non-performing asset (NPA) means:
  - (a) an asset, in respect of which, interest has remained overdue for a period of six months or more;
  - (b) a term loan inclusive of unpaid interest, when the instalment is overdue for a period of six months or more or on which interest amount remained overdue for a period of six months or more;
  - (c) a demand or call loan, which remained overdue for a period of six months or more from the date of demand or call or on which interest amount remained overdue for a period of six months or more;
  - (d) a bill which remains overdue for a period of six months or more;
  - (e) the interest in respect of a debt or the income on receivables under the head 'other current assets' in the nature of short term loans/ advances, which facility remained overdue for a period of six months or more;
  - (f) any dues on account of sale of assets or services rendered or reimbursement of expenses incurred, which remained overdue for a period of six months or more;
  - (g) the lease rental and hire purchase instalment, which has become overdue for a period of twelve months or more;
  - (h) in respect of loans, advances and other credit facilities (including bills purchased and discounted), the balance outstanding under the credit facilities (including accrued interest) made available to the same borrower/ beneficiary when any of the above credit facilities becomes non-performing asset:

Provided that in the case of lease and hire purchase transactions, a non-banking financial company may classify each such account on the basis of its record of recovery.

- As per the "Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015", a non-performing asset (NPA) means:
  - (i) an asset, in respect of which, interest has remained overdue for a period of six months or more;
  - (ii) a term loan inclusive of unpaid interest, when the instalment is overdue for a period of six months or more or on which interest amount remained overdue for a period of six months or more;
  - (iii) a demand or call loan, which remained overdue for a period of six months or more from the date of demand or call or on which interest amount remained overdue for a period of six months or more;

(iv) a bill which remains overdue for a period of six months or more;

(v) the interest in respect of a debt or the income on receivables under the head 'other current assets' in the nature of short term loans/advances, which facility remained overdue for a period of six months or more;

(vi) any dues on account of sale of assets or services rendered or reimbursement of expenses incurred, which remained overdue for a period of six months or more; Provided that the period of 'six months or more' stipulated in sub-clauses (a) to (f) shall be 'five months or more' for the financial year ending March 31, 2016; 'four months or more' for the financial year ending March 31, 2017 and 'three months or more', for the financial year ending March 31, 2018 and thereafter.

(vii) the lease rental and hire purchase instalment, which has become overdue for a period of twelve months or more;

Provided that the period of 'twelve months or more' stipulated in this sub-clause shall be 'nine months or more' for the financial year ending March 31, 2016; 'six months or more' for the financial year ending March 31, 2017; and 'three months or more' for the financial year ending March 31, 2018 and thereafter.

(viii) in respect of loans, advances and other credit facilities (including bills purchased and discounted), the balance outstanding under the credit facilities (including accrued interest) made available to the same borrower/beneficiary when any of the above credit facilities becomes non-performing asset:

Provided that in the case of lease and hire purchase transactions, a non-banking financial company may classify each such account on the basis of its record of recovery.

HORMONISATION OF ASSET CLASSIFICATION FOR NBFCs

In the interest of harmonisation, the asset classification norms for NBFCs-ND-SI and NBFCs-D are being brought in line with that of banks, in a phased manner, as provided below:

(1) Non-Performing Asset (NPA):

(A) Lease Rental and Hire-Purchase Assets:

(i) Overdue for 9 Months as on 31st March 2016: Lease Rental and Hire-Purchase Assets shall become NPA if they become overdue for 9 months (currently 12 months) for the financial year ending March 31,2016;

(ii) Overdue for 6 Months as on 31st March 2017: Lease Rental and Hire-Purchase Assets shall become NPA if overdue for 6 months for the financial year ending March 31. 2017; and

(iii) Overdue for 3 Months as on 31st March 2018 and Onwards:

Lease Rental and Hire-Purchase Assets shall become NPA if overdue for 3 months for the financial year ending March 31, 2018 and thereafter.

(B) Assets other than 'Lease Rental and Hire-Purchase Assets':

(i) Overdue for 5 Months as on 31st March 2016: Assets other than Lease Rental and Hire-Purchase Assets shall become NPA if they become overdue for 5 months for the financial year ending March 31, 2016;

(ii) Overdue for 4 Months as on 31st March 2017: Assets other than Lease Rental and Hire-Purchase Assets shall become NPA if overdue for 4 months for the financial year ending March 31. 2017; and

(iii) Overdue for 3 Months as on 31st March 2018 and Onwards: Assets other than Lease Rental and Hire-Purchase Assets shall become NPA if overdue for 3 months for the financial year ending March 31. 2018 and thereafter.

(2) Sub-Standard Assets:

For all loan and hire-purchase and lease assets, sub-standard asset would mean:

(i) NPA upto 16 Months on 31/03/2016: An asset that has been classified as NPA for a period not exceeding 16 months (currently 18 months) for the financial year ending March 31. 2016;

(ii) **NPA upto 14 Months on 31/03/2017:** An asset that has been classified as NPA for a period not exceeding 14 months for the financial year ending March 31, 2017; and

(iii) **NPA upto 12 Months on 31/03/2018:** An asset that has been classified as NPA for a period not exceeding 12 months for the financial year ending March 31, 2018 and thereafter.

(3) Doubtful Asset

For all loan and hire-purchase and lease assets, doubtful asset would mean:

(i) **Sub-Standard Asset for 16 Months on March 31, 2016:** An asset that has remained sub-standard for a period exceeding 16 months (currently 18 months) for the financial year ending March 31, 2016

(ii) **Sub-Standard Asset for 14 Months on March 31, 2017:** An asset that has remained sub-standard for a period exceeding 14 months for the financial year ending March 31, 2017; and

(iii) **Sub-Standard Asset for 12 Months on March 31, 201S and thereafter:** An asset that has remained sub-standard for a period exceeding 12 months for the financial year ending March 31, 2018 and thereafter.

ACCOUNTING GUIDELINES FOR NBFCs

The issues related to accounting include Income Recognition criteria, Accounting of Investments, asset classification and provisioning requirements. These hav been provided in details in the RBI Directions, namely "Non-Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015" and "Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015".

RBI has prescribed that Income recognition should be based on recognised accounting principles, however Accounting Standards and Guidance Notes issued by the Institute of Chartered Accountants of India (referred to in these Directions as "ICAI" shall be followed in so far as they are not inconsistent with any of these Directions.

Income Recognition

- The income recognition of NBFCs, irrespective of their categorisation, shall be based on recognised accounting principles.
- Income including interest/ discount/ hire charges/ lease rentals or any other charges on NPA shall be recognised only when it is actually realised. Any such income recognised before the asset became non-performing and remaining unrealised shall be reversed.
- Income like interest /discount /any other charges on NPAs shall be recognised only when actually realised, RBI also requires that income recognised before asset becoming NPA should be reversed in the financial year in which such asset becomes NPA.
- The NBFCs are required to recognise income from dividends on shares of corporate bodies and units of mutual funds on cash basis, unless the company has declared the dividend in AGM and right of the company to receive the same has been established, in such cases, it can be recognized on accrual basis.
- Income from bonds and debentures of corporate bodies and from government securities/bonds may be taken into account on accrual basis provided it is paid regularly and is not in arrears.
- Income on securities of corporate bodies or public sector undertakings may be taken into account on accrual basis provided the payment of interest and repayment of the security has been guaranteed by Central Government.

Principles for accounting of Investments

- Investing is one of the core activities of NBFCs, hence RBI requires the Board of Directors to Frame investment policy of the company and implement the same.
- The investments in securities shall be classified into current and long term, at the time of making each investment;

- The Board of the company should include in the investment policy the criteria for classification of investments into current and long-term.
- The investments need to be classified into current or long term at the time of making each investment.
- There can be no inter-class transfer of investments on ad hoc basis later on. Inter class transfer, if warranted, should be done at the beginning of half year, on April 1 or October 1, and with the approval of the Board.
- The investments shall be transferred scrip-wise, from current to long-term or vice-versa, at book value or market value, whichever is lower;
- The depreciation, if any, in each scrip shall be fully provided for and appreciation, if any, shall be ignored. Moreover, the depreciation in one scrip shall not be set off against appreciation in another scrip, at the time of such inter-class transfer, even in respect of the scrips of the same category.

Valuation of Investments

- The directions also specifies various valuation guidelines in respect of Quoted and Unquoted current investments leaving the Long term Investments to be valued as per ICAI Accounting Standards.

  It requires **Quoted current investments** to be grouped into specified categories, viz. (i) equity shares, (ii) preference shares, (iii) debentures and bonds, (iv) Government securities including treasury bills, (v) units of mutual fund, and (vi) others.
- The valuation of each specified category is to be done at aggregate cost or aggregate market value whichever is lower. For this purpose, the investments in each category shall be considered scrip-wise and the cost and market value aggregated for all investments in each category. If the aggregate market value for the category is less than the aggregate cost for that category, the net depreciation shall be provided for or charged to the profit and loss account. If the aggregate market value for the category exceeds the aggregate cost for the category, the net appreciation shall be ignored. Depreciation in one category of investments shall not be set off against appreciation in another category.
- **Unquoted equity shares in the nature of current investments** shall be valued at cost or break-up value, whichever is lower. However, the RBI Directions has prescribed that fair value for the break-up value of the shares may be replaced, if considered necessary. "Breakup value" means the equity capital and reserves as reduced by intangible assets and revaluation reserves, divided by the number of equity shares of the investee company. Where the balance sheet of the investee company is not available for two years, such shares shall be valued at one rupee only.
- **Unquoted preference shares in the nature of current investments** shall be valued at cost or face value, whichever is lower.
- **Investments in unquoted Government securities or Government guaranteed bonds** shall be valued at carrying cost.
- **Unquoted investments in the units of mutual funds in the nature of current investments** shall be valued at the net asset value declared by the mutual fund in respect of each particular scheme.
- **Commercial papers** shall be valued at carrying cost.
- **A long term investment** shall be valued in accordance with the Accounting Standard issued by ICAI.
- Explanation: **Unquoted debentures** shall be treated as term loans or other type of credit facilities depending upon the tenure of such debentures for the purpose of income recognition and asset classification.

Transactions in Government Securities

Every non-banking financial company shall undertake transactions in Government securities through its CSGL account or its demat account: Provided that no non-banking financial company shall undertake any transaction in government security in physical form through any broker.

Preparation of Balance Sheet and Profit and Loss Account

- Every non-banking financial company shall prepare its balance sheet and profit and loss account as on March 31 every year. Whenever a non-banking financial company intends to extend the date of its balance sheet as per provisions of the Companies Act, it should take prior approval of the Reserve Bank of India before approaching the Registrar of Companies for this purpose.
- Further, even in cases where the Bank and the Registrar of Companies grant extension of time, the non-banking financial company shall furnish to the Bank a proforma balance sheet (unaudited) as on March 31 of the year and the statutory returns due on the said date. Every non-banking financial company shall finalise its balance sheet within a period of 3 months from the date to which it pertains.
- Every non-banking financial company shall append to its balance sheet prescribed under the Companies Act, 2013, the particulars in the schedule as set out in Annex I.

Disclosures in the Balance Sheet

- The directions specify certain disclosure requirements in the balance sheet.
- Disclosure of provisions created without netting them from the income or against the value of assets. The provisions shall be distinctly indicated under separate heads of account as (i) Provisions for bad and doubtful debts; and (ii) Provisions for depreciation in investments.
- Provisions shall not be appropriated from the general provisions and loss reserves held. Provisions shall be debited to the profit and loss account.
- The excess of provisions, if any, held under the heads general provisions and loss reserves may be written back without making adjustment against the provisions.
- Every non-banking financial company shall append to its balance sheet prescribed under the Companies Act, 2013, the particulars in the schedule as set out in Annex I.
- The following disclosure requirements are applicable only to systemically important (Asset Size more than Rs. 500 crores) non-deposit taking non-banking financial company:
  - ➢ Capital to Risk Assets Ratio (CRAR);
    - ✓ Exposure to real estate sector, both direct and indirect; and
    - ✓ Maturity pattern of assets and liabilities."

The formats for the above disclosures are also specified by RBI.

PROVISION REQUIREMENTS FOR NBFCs

[A] Provision against sub-standard assets, doubtful assets and loss assets

Every NBFC shall, after taking into account the time lag between an account becoming non-performing, its recognition as such, the realisation of the security and the erosion over time in the value of security charged, make provision against sub-standard assets, doubtful assets and loss assets as provided hereunder:

1. On loans, advances and other credit facilities including bills purchased and discounted

Loss Assets	The entire asset shall be written off. If the assets are permitted to remain in the books for any reason, 100% of the outstanding should be provided for;
Doubtful Assets	(a) 100% provision to the extent to which the advance is not covered by the realisable value of the security to which the non-banking financial company has a valid recourse shall be made. The realisable value is to be estimated on a realistic basis;

	(b) In addition to item (a) above, depending upon the period for which the asset has remained doubtful, provision to the extent of 20% to 50% of the secured portion (i.e. Estimated realisable value of the outstanding) shall be made on the following basis:	
	Period for which the asset has been considered as doubtful:	Per cent of provision
	- Up to one year	20
	- One to three years	30
	- More than three years	50
Sub-standard assets	A general provision of 10 per cent of total outstanding shall be made	

2. On Lease and Hire Purchase assets

As per the RBI Directions, the provisioning requirements in respect of hire purchase and leased assets shall be as under:

- In respect of hire purchase assets, the total dues (overdue and future instalments taken together) as reduced by: (a) the finance charges not credited to the profit and loss account and carried forward as unmatured finance charges; and (b) the depreciated value of the underlying asset, shall be provided for.

  Explanation: For the purpose of this paragraph, (1) the depreciated value of the asset shall be notionally computed as the original cost of the asset to be reduced by depreciation at the rate of twenty per cent per annum on a straight line method; and (2) in the case of second hand asset, the original cost shall be the actual cost incurred for acquisition of such second hand asset.

- **Additional provision for hire purchase and leased assets**: In respect of such assets, additional provision shall be made as under:

(a) Where hire charges or lease rentals are overdue upto 12 months	Nil
(b) Where hire charges or lease rentals are overdue for more than 12 months but upto 24 months	10 per cent of the net book value
(c) Where hire charges or lease rentals are overdue for more than 24 months but upto 36 months	40 per cent of the net book value
(d) Where hire charges or lease rentals are overdue for more than 36 months but upto 48 months	70 per cent of the net book value
(e) Where hire charges or lease rentals are overdue for more than 48 months	100 per cent of the net book value

  - On expiry of a period of 12 months after the due date of the last instalment of hire purchase/ leased asset, the entire net book value shall be fully provided for.

Notes:

1. The amount of caution money/ margin money or security deposits kept by the borrower with the non-banking financial company in pursuance of the hire purchase agreement may be deducted against the provisions stipulated under clause (i) above, if not already taken into account while arriving at the equated monthly instalments under the agreement. The value of any other security available in pursuance to the hire purchase agreement may be deducted only against the provisions stipulated under clause (ii) above.
2. The amount of security deposits kept by the borrower with the non-banking financial company in pursuance to the lease agreement together with the value of any other security available in pursuance to the lease agreement may be deducted only against the provisions stipulated under clause (ii) above.
3. It is clarified that income recognition on and provisioning against NPAs are two different aspects of prudential norms and provisions as per the norms are required to be made on NPAs on total outstanding balances including the depreciated book value of the leased asset under reference after adjusting the balance, if any, in the lease adjustment account. The fact that income on an NPA has not been recognised cannot be taken as reason for not making provision.

4. An asset which has been renegotiated or rescheduled as referred to in paragraph (2) (1) (xxv) (b) of these Directions shall be a sub-standard asset or continue to remain in the same category in which it was prior to its renegotiation or reschedulement as a doubtful asset or a loss asset as the case may be. Necessary provision is required to be made as applicable to such asset till it is upgraded.

5. The balance sheet to be prepared by the NBFC may be in accordance with the provisions contained in sub-paragraph (2) of paragraph 11.

6. All financial leases written on or after April 1, 2001 attract the provisioning requirements as applicable to hire purchase assets.

7. In case of NBFC-MFIs, if the advance covered by Credit Risk Guarantee Fund Trust for Low Income Housing (CRGFTLIH) guarantee becomes non-performing, no provision need be made towards the guaranteed portion. The amount outstanding in excess of the guaranteed portion should be provided for as per the extant guidelines on provisioning for non-performing advances.

[B] Provision against Standard Assets

- As per the "Non-systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015", every Non-Banking Financial Company shall make provision for standard assets at 0.25 percent of the outstanding, which shall not be reckoned for arriving at net NPAs.

- As per the "Systemically Important Non-Banking Financial (Non-Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2015", every Non-Banking Financial Company shall make provisions for standard assets at 0.25 per cent by the end of March 2015; 0.30 per cent by the end of March 2016; 0.35 per cent by the end of March 2017 and 0.40 per cent by the end of March 2018 and thereafter, of the outstanding, which shall not be reckoned for arriving at net NPAs. Thus, the provision for standard assets for NBFCs-ND-SI and for all NBFCs-D has now been increased to 0.40% (at present 0.25%). The compliance to the revised norm will be phased in as given below:

  ✓ 0.30% by the end of March 2016

  ✓ 0.35% by the end of March 2017

  ✓ 0.40% by the end of March 2018

- The provision towards standard assets need not be netted from gross advances but shall be shown separately as 'Contingent Provisions against Standard Assets' in the balance sheet.

Illustration 16:

While closing its books of accounts on 31stMarch, a NBFC has its advances classified as follows –

Particulars	**₹ Lakhs**	**Particulars**	**₹ Lakhs**
Standard Assets	8,400	Unsecured Portion of Doubtful Debts	87
Sub-Standard Assets	910	Loss Assets	24
Secured Portions of Doubtful Debts:			
- Up to one year	160		
- One year to three years	70		
- more than three years	20		

Calculate the amount of provision which must be made against the advances.

Solution:

Particulars	**Loan (₹ Lakhs)**	**Provision (%)**	**Provision (₹ Lakhs)**
Standard Assets	8,400	Nil	Nil
Sub- Standard Assets	910	10%	91
Secured Portions of Doubtful Debts:			
- Up to one year	160	20%	32
- 1 year to 2 years	70	30%	21
- more than three years	20	50%	10
Unsecured Portions of Doubtful Assets	87	100%	87
Loss Assets	24	100%	24
Total			265

Illustration 17:

While closing its books of account on March 31st of a financial year, a Non-banking Finance company has its advances classified as follows:

Particulars	₹ Lakhs
Standard Assets	16,800
Sub- Standard Assets	1,340
Secured Positions of Doubtful Debts:	
- Up to one year	320
- one year to three years	90
- more than three years	30
Unsecured Portions of Doubtful debts	97
Loss Assets	48

Calculate the amount of provision which must be made against the advances.

Solution:

Particulars	**Loan (₹ Lakhs)**	**Provision (%)**	**Provision (₹ Lakhs)**
Standard Assets	16,800	Nil	Nil
Sub- Standard Assets	1,340	10%	134
Secured Portion of Doubtful Debts:			
- Up to one year	320	20%	64
- 1 year to 2 years	90	30%	27
- more than 3 years	30	50%	15
Unsecured Portion of Doubtful debts	97	100%	97
Loss Assets	48	100%	48
Total			385

Illustration 18:

While closing its books of accounts on 31st March, a NBFC has its advances classified as follows:

Particulars	₹ Lakhs
Standard Assets	10,000
Sub- Standard Assets	1,000
Secured Positions of Doubtful Debts:	
- Up to one year	160
- one year to three years	70
- more than three years	20
Unsecured Portions of Doubtful debts	90
Loss Assets	30

Calculate the amount of provision which must be made against the advances.

Solution:

Particulars	**Loan (₹ Lakhs)**	**Provision (%)**	**Provision (₹Lakhs)**
Standard Assets	10,000	Nil	Nil
Sub- Standard Assets	1,000	10%	100
Secured Portions of Doubtful Debts:			
- Up to one year	160	20%	32
- 1 year to 2 years	70	30%	21
- more than three years	20	50%	10
Unsecured Portions of Doubtful Assets	90	100%	90
Loss Assets	30	100%	30
Total			283

Illustration 19:

Samvedan Ltd. is a non-banking finance company. It accepts public deposit and also deals in the hire purchase business. It provides you with the following information regarding major hire purchase deals as on 31.3.14. few machines were sold on hire-purchase basis. The hp price was set as ₹100 lakhs as against cash price of ₹ 80 lakhs. The amount was payable as ₹ 80 lakhs down payment and balance in 5 equal installments. The Hire-vendor collected first installment as on 31.3.15, but could not collect the second installment which was due on 31.3.16. the company was finalizing accounts for the year ending 31.3.16. till 15.5.16, the date on which the Board of Directors signed the accounts, the second installment was not collected. Presume IRR to be 10.42%.

Required:

(a) What should be the principal outstanding on 1.4.15? Should the company recognise finance charge for the year 2015-16 as income?

(ii) What should be the net book value of assets as on 31.3.16 so far Samvedan Ltd. is concerned as per NBFC prudential norms requirement for provisioning?

(iii) What should be the amount of provision to be made as per prudential norms for NBFC laid down by RBI?

Solution:

(i) Since, the hire-purchaser paid the first installment due of 31.3.15, the notional principal outstanding on 01.04.2015 was ₹ 50.25 lakhs. [WN: 1]

(ii) In the year ended 31.3.16, the installment due of ₹ 16 lakhs has not been received. However, it was due on 31.3.16 i.e. on the Balance Sheet date, and therefore, it will be classified as Standard Asset. Samvedan Ltd. will recognise ₹ 5.24 lakhs as interest income included in that due installment as this should be treated as finance charge.

(iii) The net book value of the assets as on 31.3.2015

Particulars	₹ Lakhs
Overdue installment	16
Installments not due (₹ 16 lakhs x 3)	48
	64
Less: Finance charge not matured and not credited to P/L A/c [4.11+2.88+1.52]	(8.51)
	55.49
Less: Provision as per NBFC prudential norms	7.49
∴ Net Book Value of assets for Samvedan Ltd.	48.00

(iii) Amount of Provision

Particulars	₹ Lakhs
Overdue installment	16
Installments not due (₹ 16 lakhs x 3)	48
	64
Less: Finance charge not matured and not credited to P/L A/c [4.11+2.88+1.52]	(8.51)
	55.49
Less: Depreciated value (Cash Price Less Depreciation for 2 years on SLM @ 20%)	48
Provision as per NBFC prudential norms	7.49

Since, the installment of ₹ 16 lakhs not paid, was due on 31.03.2016 only, the asset is classified as standard asset. Therefore, no additional provision has been made for it.

Workings:

It is necessary to segregate the installments into principal outstanding and interest components by using IRR @10.42%

Time	Opening outstanding amount (a)	Cash flow (b)	Interest @ 10.42% (c) = (a) × 10.42%	Principal repayment (d) = (b) – (c)	Closing outstanding (e) = (a) – (d)
31.3.14	—	60	—	—	60
31.3.15	60	16	6.25	9.75	50.25
31.3.16	50.25	16	5.24	10.76	39.49
31.3.17	39.49	16	4.11	11.89	27.6
31.3.18	27.6	16	2.88	13.12	14.48
31.3.19	14.48	16	1.52	14.48	0

5.4 VALUATION OF SHARES

INTRODUCTION

A share is the smallest unit of ownership of a company. It happens to be one of the sources by which a company raises funds from the market. The value of a share does not remain static over its life-time. Rather it changes over the period due to various circumstances. Thus, knowing the value of share at a particular point of time is of great importance.

PURPOSE OF SHARE VALUATION

The shares of a company are required to valued for various purposes. Some of the most important purposes include the following:

1. For selling shares of a shareholder to a purchaser (which are not quoted in the stock exchange)
2. For acquiring a block of shares which may or may not give the holder thereof a controlling interest in the company.
3. To shares by employees of the company where the retention of such shares is limited to the period of their employment.
4. To formulate schemes of merger and acquisition.
5. To acquire interest of dissenting shareholders under a scheme of reconstruction.
6. For granting loans on the basis of security of shares
7. To compensate shareholders on the acquisition of their shares by the government under a scheme of nationalization.
8. For conversion of securities, say preference shares into equity shares.
9. To advance a loan on the security of shares.
10. To resolve a deadlock in the management of a company on the basis of the controlling block of shares given to either of the parties.

FACTORS AFFECTING VALUATION OF SHARES

The different factors that affect the valuation of shares are:

1. Nature of the industry to which the company belongs
2. The companies past performance
3. Economic conditions of the country
4. Other political and economic factors (e.g., possibility of nationalization, excise duty on goods produced, etc.)
5. Demand and supply of shares
6. Income yielding capacity of the company
7. The availability of sufficient assets over liabilities
8. Proportion of liabilities and capital
9. Rate of proposed dividend and past profit of the company
10. Yield of other related shares of the Stock Exchange.

METHODS OF SHARE VALUATION

There are three basic methods of valuing shares. They are as follows :

1. Asset-backing or Intrinsic Value Method.
2. Yield-basis or Earning Capacity Method.
3. Fair Value Method or Dual Method.

A. Asset-Backing Method:

Since the valuation is made on the basis of the assets of the company, it is known as Asset-Basis or Asset- Backing Method. At the same time, the shares are valued on the basis of real internal value of the assets of the company and that is why the method is also termed Intrinsic Value Method or Real Value Basis Method.

This method may be made either:

(i) On a going concern basis; or(ii) On Break-up value basis.

In case of the former, the utility of the assets is to be considered for the purpose of arriving at the value of the assets, but, in the case of the latter, the realizable value of the assets is to be taken. Under this method, value of the net assets of the company is to be determined first. Thereafter, the net assets are to be divided by the number of shares in order to find out the value of each share. At the same time, value of goodwill (at its market value), investment (non-trading assets) are to be added to net assets. Similarly, if there are any preference shares, those are also to be deducted with their arrear dividends from the net assets.

Net Assets or the Funds Available for Equity Shareholders are ascertained as under:

(a) Ascertain the total market value of fixed assets and current assets;

(b) Compute the value of goodwill (as per the required method);

(c) Ascertain the total market value of non-trading assets (like investment) which are to be added;

(d) All fictitious assets (viz, Preliminary Expenses, Discount on issue of Shares/Debentures, Debit-Balance of P&L A/c etc.) must be excluded;

(e) Deduct the total amount of Current Liabilities, Amount of Debentures with arrear interest," if any, Preference Share Capital with arrear dividend, if any.

(f) The balance left is called the Net Assets or Funds Available for Equity Shareholders.

The following chart will make the above principle clear:

Computation of Net Assets		
Particulars	₹	₹
Net Assets		
Fixed Assets (Market Value)		XXX
Investments (Market Vaslue)		XXX
Current Assets (Market Value)		XXX
Goodwill if any (Market Value)		XXX
		XXXX
Less:		
Current Liabilities	XXX	
Debentures	XXX	
Preference Share Capital (with arrear dividend)	XXX	XXXX
Net Assets/Funds Available for Equity Shareholders		XXXX
		XXXX

$$\therefore \text{ Intrinsic Value of each Share} = \frac{\text{Funds Available for Equity Shareholder's}}{\text{Number of Equity Shares}}$$

Alternatively:

Net Assets = Share Capital + Reserves and Surplus Revaluation – Loss on Revaluation

Applicability of the Method:

(i) The permanent investors determine the value of shares under this method at the time of purchasing the shares;

(ii) The method is particularly applicable when the shares are valued at the time of Amalgamation, Absorption and Liquidation of companies; and

(iii) This method is also applicable when shares are acquired for control motives.

B. Yield-Basis Method:

Yield is the effective rate of return on investments which is invested by the investors. It is always expressed in terms of percentage. Since the valuation of shares is made on the basis of Yield, it is called Yield-Basis Method.

Under Yield-Basis method, valuation of shares is made on either of the following basis:

(i) Profit Basis; or (ii) Dividend Basis.

(i) **Under Profit Basis:** Under this method, at first, profit should be ascertained on the basis of past average profit; thereafter, capitalized value of profit is to be determined on the basis of normal rate of return, and, the same (capitalized value of profit) is divided by the number of shares in order to find out the value of each share.

The following steps are followed for the purpose of valuation:

$$\therefore \text{ Capitalised Value of Profit} = \frac{\text{Profit}^1}{\text{Normal rate of Return}} \times 100$$

$$\text{Value of each Equity Share} = \frac{\text{Capitalised Value of Profit}}{\text{Number of Shares}}$$

$$\text{Or, Value of each Equity Share} = \frac{\text{Profit}}{\text{Normal rate of Return} \times \text{Number of Equity Shares}} \times 100$$

(ii) Under Dividend Basis: Valuation of shares may be made either (a) on the basis of total amount of dividend, or (b) on the basis of percentage or rate of dividend:

(a) on the basis of Total Value of Dividend :

$$\text{Capitalised Value of Profit} = \frac{\text{Dividend Profit, i.e. Total amount of Dividend}}{\text{Normal Rate of Return, i.e. Yield}} \times 100$$

$$\therefore \text{ Value of each Equity Share} = \frac{\text{Capitalised Value of Profit}}{\text{Number of Equity Shares}}$$

$$\text{Or, Value of each Equity Shate} = \frac{\text{Divisible Profit} \times 100}{\text{Normal Rate of Return} \times \text{No. of Equity Shares}}$$

(b) On the basis of percentage or Rate of Dividend:

$$\text{Value of each Equity Share} = \frac{\text{Rate of Dividend}}{\text{Normal Rate of Return}} \times \text{Paid-up Value of each Equity Share}$$

When the Rate of Dividend is not given

$$\text{Rate of Dividend} = \frac{\text{Profit}}{\text{Equity Share Capital (Paid-up)}} \times 100$$

Whether Profit Basis or Dividend Basis method is to be followed for ascertaining the value of shares depends on the shares that are held by the respective shareholders. In other words, the shareholders holding minimum number of shares (i.e., minority holding) may determine the value of shares on dividend basis in order satisfy the rate of dividend which is recommended by the Board of Directors, i.esuch shareholders have no such power to control the affairs of the company.

On the contrary, the shareholders holding maximum number of shares (i.e., majority holding) have got more controlling rights over the affairs of the company including the recommendation for the rate of dividend among others. Under the circumstances, valuation of shares should be made on profit basis. In short, Profit Basis should be followed in the case of Majority Holding, and Dividend Basis should be followed in the case of Minority Holding.

C. Fair Value Method:

There are some valuers who do not accept either the Intrinsic Value or the Yield Value for ascertaining the value of shares. They prescribe the Fair Value Method which happens to be the arithmetic mean of Intrinsic Value Method and Yield Value Method. The same provides a better indication about the value of shares than the earlier two methods.

$$\therefore \text{ Fair Value} = \frac{\text{Intrinsic Value} + \text{Yield Value}}{2}$$

WORKED OUT PROBLEMS

Illustration 20:

The following abridged Balance Sheet as on 31st March, 2016 pertains to S Ltd.

Liabilities	₹ in lakhs	Assets	₹ in lakhs
Share Capital :		Goodwill, at cost	420
180 lakh Equity shares of ₹ 10 each, fully paid up	1,800	Other Fixed Assets	11,166
90 lakh Equity shares of ₹10 each, ₹8 paid up	720	Current Assets	2,910
150 lakh Equity shares of ₹5 each, fully paid-up	750	Loans and Advances	933
Reserves and Surplus	5,628	Miscellaneous Expenditure	171
Secured Loans	4,500		
Current Liabilities	1,242		
Provisions	960		
	15,600		15,600

You are required to calculate the following for each one of three categories of equity shares appearing in the above mentioned Balance Sheet:

(i) Intrinsic value on the basis of book values of Assets and Liabilities including goodwill;

(ii) Value per share on the basis of dividend yield.

Normal rate of dividend in the concerned industry is 15%, whereas Glorious Ltd. has been paying 20% dividend for the last four years and is expected to maintain it in the next few years; and

(iii) Value per share on the basis of EPS.

For the year ended 31st March, 2016 the company has earned ₹1,371 lakh as profit after tax, which can be considered to be normal for the company. Average EPS for a fully paid share of ₹10 of a Company in the same industry is ₹2.

Solution:

(A) Calculation of Intrinsic value [Based on book value]

	₹
Goodwill	420
Fixed Assets	11,166
Current Assets	2,910
Loan Advances	933
Total	15,429
Less: Provision	960
Current liabilities	1,242
Secured loans	4,500
Net Assets available for Equity share holder	8,727
Add: Notional calls [90x2]	180
Total Assets	8,907
÷ Equity share capital [1,800 + 900 + 750)	3,450
Intrinsic value per Rupee	2.58
Paid up value ₹10 x 2.58 =	25.8
Paid up value ₹8 x 2.58 =	20.64
Paid up value ₹5 x 2.58 =	12.90

(B) Dividend Yield = $\frac{\text{Dividend Rate}}{\text{Normal rate of Return}} \times \text{Paid up Share Capital}$

Paid up value 10 = $\frac{20\%}{15\%} \times 10 =$ ₹ 13.33

Paid up value 8 = $\frac{20\%}{15\%} \times 8 =$ ₹ 10.67

Paid up value 5 = $\frac{20\%}{15\%} \times 5 =$ ₹ 6.67

(C) Earning per Rupee of Share Capital = $\frac{\text{Earning after tax}}{\text{Paid up Share Capital}}$

$$= \frac{1{,}371}{3{,}270} = 0.419$$

Earning per fully paid shares of ₹10 = 0.419

Earning per share of ₹10 each, ₹ 8 paid-up = ₹0.419×8 = ₹3.35

Earnng per share of ₹5, fully paid-up = ₹0.419 × 5= ₹2.10

Value of fully paid share of ₹10 = ₹ $\frac{4.19}{2} \times 10$ = ₹ 20.95

Value of share of ₹10, ₹8 paid-up = ₹ $\frac{4.19}{2} \times 10$ = ₹ 16.75

Value of fully paid-up share of ₹5 = ₹ $\frac{4.19}{2} \times 10$ = ₹ 10.50.

Illustration 21:

The following is. the Balance Sheet (as on 31st December, 2015) of N Ltd.:

Liabilities	₹ in Lakh	Assets	₹ in Lakh
Share Capital:		**Fixed Assets:**	
80,000 Equity shares of ₹10 each fully paid up	8,00,000	Goodwill	1,00,000
50,000 Equity shares of ₹10 each 8 paid up	4,00,000	Plant and Machinery	8,00,000
36,000 Equity shares of ₹5 each fully paid up	1,80,000	Land and Building	10,00,000
30,000 Equity shares of ₹5 each 4 paid-up	1,20,000	Furniture and Fixtures	1,00,000
3,000 10% Preference shares of ₹100 each fully paid	3,00,000	Vehicles	2,00,000
Reserves and Surplus:		Investments	3,00,000
General reserve	1,40,000	**Current Assets:**	
Profit and Loss account	2,10,000	Stock	2,10,000
Secured Loan: 12% debentures	2,00,000	Debtors	1,95,000
Unsecured loan: 15% Term Loan	1,50,000	Prepaid Expenses	40,000
Deposits	1,00,000	Advances	45,000
Current Liabilities:		Cash and Bank balance	2,00,000
Bank Loan	50,000	Preliminary Expenses	10,000
Creditors	1,50,000		
Outstanding expenses	20,000		
Provision for tax	2,00,000		
Proposed Dividend:			
Equity	1,50,000		
Preference	30,000		
	32,00,000		**32,00,000**

Additional Information:

(1) In 2013 a new machinery costing ₹50,000 was purchased, but wrongly charged to revenue (no rectification has yet been made for the same).

(2) Stock is overvalued by ₹10,000 in 2014. Debtors are to be reduced by ₹5,000 in 2015, some old furniture (Book value ₹10,000) was disposed of fort ₹6,000.

(3) Fixed assets are worth 5 per cent more than their actual book value. Depreciation on appreciated value of Fixed assets except machinery is not to be considered for valuation of goodwill.

(4) Of the investment 20 per cent is trading and the balance is non-trading. All trade investments are to be valued at 20 per cent below cost. Trade investment were purchased on 1st January, 2015. 50 per cent of the non-trade investments were acquired on 1st January, 2014 and the rest on January, 2013. A uniform rate of dividend of 10 percent is earned on all investments.

(5) Expected increase in expenditure without commensurate increase in selling price ₹20,000.

(6) Research and Development expenses anticipated in future ₹30,000 per annum.

(7) In a similar business a normal return on capital employed is 10%.

(8) Profit (after tax) are as follows:

In 2013 — ₹2,10,000, in 2014 — ₹1,90,000 and in 2015 — ₹2,00,000.

(9) Current income tax rate is 50%, expected income tax rate will be 40%. From the above, ascertain the ex-dividend and cum-dividend intrinsic value for different categories of Equity shares. For this purpose goodwill may be taken as 3 years purchase of super profits. Depreciation is charged on machinery @ 10% on reducing system.

Solution:

Computation of Value of Shares:

		₹
Value of Net Assets (As computed for Goodwill)		21,02,073
Value of Goodwill [Refer W.N.3]		11,406
Non-trade investments		2,40,000
		23,53,479
Less :		
Preference Share Capital	3,00,000	
Proposed Dividend of Preference shares	30,000	
Proposed Dividend of Equity shares	1,50,000	4,80,000
Net Assets available for Equity Shareholders		18,73,479

Computation of Number of Equivalent Equity Shares:

Equity shares	No. of Equivalent Shares
80,000 shares + 50,000 shares = 1,30,000 shares of ₹10 each 1,30,000 x $\frac{10}{10}$	1,30,000
36,000 shares + 30,000 shares = 66,000 shares of ₹5 each 66,000 x $\frac{5}{10}$	33,000
Total Equivalent Equity Shares of ₹10 each	1,63.000

Calculation of Ex-Dividend intrinsic value of different categories of Equity Shares of N Ltd.

= Net Assets available to deemed fully paid-up Equity Shareholders

= Net Assets as computed above + Notional Cash from partly paid-up shares

= ₹18,73,479 + (50,000 × 2 + 30,000 × 1)

= ₹18,73,479 + 1,00,000 + 30,000

= ₹20,03,479

Computation of Ex-Dividend value per Equity Share

(i) Value of ₹10 fully paid Equity Share = $\frac{20,03,479}{1,63,000}$ = ₹ 12.29 per share (approx.)

(ii) Value of ₹ 8 paid-up Equity Share = 12.29 – 2 = ₹ 10.29 per share (approx.)

(iii) Value of ₹ 5 fully paid-up Equity Share = 12.29 x $\frac{5}{10}$ = ₹ 6.15 per share (approx.)

(iv) Value of ₹ 4 paid-up Equity Share = 6.15 - 1 = ₹ 5.15 per share (approx.)

Calculation of Cum-Dividend intrinsic value of different categories of Equity Shares of N Ltd.

Value of Net Assets (including proposed dividend on equity shares)

= ₹18,73,479 + ₹1,50,000

= ₹20,23,479

Net assets (including dividend) available to deemed fully paid-up Equity Shareholders

= Net Assets as computed above + Notional Cash from partly paid-up shares

= ₹20,23,479 + (50,000 x 2 + 30,000 x 1)

= ₹20,23,479 + 1,00,000 + 30,000

= ₹21,53,479

Computation of Cum-Dividend value per share*

(i) Value of ₹10 fully paid Equity Share = $\frac{21,53,479}{1,63,000}$ = ₹13.21 per share (approx).

(ii) Value of ₹8 paid-up Equity Share = 13.21 - 2 = ₹11.21 per share (approx.)

(iii) Value of ₹5 fully paid-up Equity Share = 13.21x $\frac{5}{10}$ = ₹6.605 per share (approx.)

(iv) Value of ₹4 paid-up Equity Share= 6.605 – 1 = ₹5.605 per share (approx.)

Working Notes:

1. Calculation of Average Capital Employed

Fixed Assets:		
Plant and Machinery (including ₹ 36,450 for a Machine charged in 2013)		8,36,450
Land and Building		10,00,000
Furniture & Fixtures (1,00,000 - 4,000)		96,000
Vehicles		2,00,000
		21,32,450
Add : Appreciation @ 5%		1,06.623
		22,39,073
Trade Investment (3,00,000 × $\frac{20}{100}$) × $\frac{80}{100}$		48,000
Current Assets:		
Stock		2,10,000
Debtors (1,95,000-5,000)		1,90,000
Prepaid Expenses		40,000
Advances		45,000
Cash & Bank Balance		2,00,000
		29,72,073
Less : Outside Liabilities:		
12% Debentures	2,00,000	
15% Term Loan	1,50,000	
Deposits	1,00,000	
Bank Loan	50,000	
Creditors	1,50,000	
Outstanding Expenses	20,000	
Provision for Tax	2,00,000	8,70,000
Capital employed at the end of the year i.e. Net Assets		21,02,073
Less: $\frac{1}{2}$ of the current year's Accounting Profit after Tax:		
Profit before Tax	3,80,950	
Less : Tax 40% of ₹ 3,80,950	1,52,380	
	2.28,570	
50% of ₹ 2,28,570		1,14,285
Average capital employed		19,87,788

2. Future Maintainable Profits

Statement of Average Profit

Particulars	**2013**	**2014**	**2015**
Profit after Tax	2,10,000	1,90,000	2,00,000
Profit before Tax (PAT × $\frac{1}{0.50}$)	4,20,000	3,80,000	4,00,000
Add: Capital expenditure charged to revenue	—	50,000	—
Less : Depreciation of the Machinery	5,000	(4,500)	(4,050)
Dividend on Non-Trade Investments	(12,000)	(24,000)	(24,000)
Over-valuation of closing stock	-	(10,000)	—
Add : Overvaluation of opening stock	-	-	10,000
Add: Loss on sale of furniture	-	-	-
(Presumed to be extra ordinary items)	-	-	4,000
Less: Provision for debtors			(5,000)
	4,53,000	3,41,500	3,80,950
Total profit for the three years		11,75,450	
Average Profit = $\frac{₹11,75,450}{3}$		3,91,817	
Less: Depreciation @ 10% on increase in the value of machinery			
8,36,450 × $\frac{5}{100} \times \frac{10}{100}$ = ₹41,823 × $\frac{10}{100}$ i.e.	4,182		
Expected increase in expenditure	20,000		
Annual R & D Expenses anticipated in future	30,000	54,182	
Future Maintainable profit before tax		3,37,635	
Less: Tax @ 40% of 3,37,635		1,35,054	
Future Maintainable Profit After Tax		2,02,581	

3. Computation of Goodwill

	₹
Future Maintainable Profit After Tax	2,02,581
Less: Normal Profit (10% of ₹19,87,788)	1,98,779
Super Profit	3,802
Value of Goodwill = Super Profit × No. of years' purchase = ₹3,802 × 3	11,406

Illustration 22.

Following is the Balance Sheet of Z Ltd. as on 31st March, 2014:

Liabilities	₹ in Lakh	Assets	₹ in Lakh
1,00,000 Equity Shares of ₹10 each	10,00,000	Preliminary expenses	5,00,000
10,000 12% Preference Shares of ₹100 each	10,00,000	Goodwill	15,00,000
General Reserve	6,00,000	Buildings Plant	10,00,000
Profit and Loss Account	4,00,000	Investment in 10% Stock	4,80,000
15% Debentures	10,00,000	Stock	6,00,000
Creditors	8,00,000	Stock-in - trade	4,00,000
		Debtors	1,00,000
		Cash	2,20,000
	48,00,000		**48,00,000**

Additional information are given below:

(a) Nominal value of investment is ₹5,00,000 and its market value is ₹5,20,000.

(b) Following assets are revalued:

(i)	Building	₹32,00,000
(ii)	Plant	₹18,00,000
(iii)	Stock-in-trade	₹4,50,000
(iv)	Debtors	₹3,60,000

(a) Average profit before tax of the company is ₹12,00,000 and 12.50% of the profit is transferred to general reserve, rate of taxation being 50%.

(b) Normal dividend expected on equity shares is 8% while fair return on closing capital employed is 10%.

(c) Goodwill may be valued at three year's purchase of super profits.

(d) Ascertain the value of each equity share under fair value method.

Solution:

1. Calculation of Capital Employed

		₹
Assets:		
Buildings		32,00,000
Plant		18,00,000
Stock		4,50,000
Debtors		3,60,000
Cash		1,00,000
		59,10,000
Less: Liabilities:		
Creditors	8,00,000	
Debentures	10,00,000	18,00,000
TOTAL CAPITAL EMPLOYED		41,10,000

2. Calculation of Actual Profit

Average Profit before Tax (given)	12,00,000
Less: Income from Investment (5,00,000 × 10%)	50,000
	11,50,000
Less: Income Tax @ 50%	5,75,000
Actual Profit	5,75,000

3. Profit for Equity Shareholders

Actual Profit (as calculated above)	5,75,000
Less: Transfer to Reserve @ 12.50%	(71,875)
Less: Preference Dividend	(1,20,000)
Profit available to Equity Shareholders.	3,83,125

4. Normal Profit

10% of Capital Employed

= 10% of ₹41,10,000 = ₹ 4,11,000

5. Super Profit = Actual Profit - Normal Profit

= ₹5,75,000 – ₹4,11,000 = ₹1,64,000

6. Goodwill = ₹1,64,000 x 3 = ₹4,92,000

7. Net Assets for Equity Shareholders

= Capital Employed + Goodwill + Investment – Preference Share Capital

= ₹41,10,000 + ₹4,92,000 + ₹4,80,000 - ₹10,00,000

= ₹40,82,000

Value per share (Based on Intrinsic Value Method)

$$= \frac{₹40,82,000}{1,00,000 \text{ Shares}} = ₹40.82$$

Value per share (Based on Yield Method)

$$\text{Yield on Equity Share} = \frac{\text{Profit for Equity Shareholders}}{\text{Equity Share Capital}} \times 100$$

$$= \frac{₹3,83,125}{10,00,000} \times 100 = 38.31\%$$

$$\text{Value per share} = \frac{38.31}{8} \times 10 = ₹47.89$$

Value of Equity Share Under Fair Value Method

$$= \frac{\text{Intrunsic value + yield value}}{2} = \frac{40.82 + 47.89}{2} = ₹44.36 \text{ (approx)}.$$

Illustration 23.

The Balance Sheet of Q Limited as on 31.12.2015 is as follows :

Liabilities	₹ in Lakh	Assets	₹ in Lakh
1,00,000 Equity shares of ₹10 each fully paid-up	10	Goodwill	5
1,00,000 equity shares of ₹6 each fully paid-up	6	Fixed Assets	15
Reserves & Surplus	4	Other Tangible Assets	5
Liabilities	10	Intangible Assets	
		(Market Value)	3
		Misc. Expenditure to the	
		extent not written off	2
	30		**30**

Fixed assets are worth ₹24 lakhs. Other tangible assets are valued at ₹3 lakhs. The company is expected to settle the disputed bonus claim of ₹1 lakh, not provided for in the accounts. Goodwill appearing in the Balance Sheet is purchased goodwill. It is considered reasonable to increase the value of goodwill by an amount equal to average of the book value and a valuation made at 3 years purchase of average super profit for the last 4 years.

After tax profits and dividend rates were as follows:

Year	PAT (in lakhs) %	Dividend
2012	3.00	11
2013	3.50	12
2014	4.00	13
2015	4.10	14

Normal expectation in the industry to which the company belongs to is 10%. Kamalesh holds 20,000 equity shares of ₹10 each fully paid up and 10,000 equity shares of ₹6 each fully paid up. He wants to sell away his holdings.

(i) Determine the break-up value and market value of both kinds of shares.

(ii) What should be the fair value of shares, if controlling interest is being sold?

Note : Make necessary assumptions, wherever required.

Solution:

(i) Break up value of ₹1 of share capital = $\frac{\text{Net assets available for shareholder}}{\text{Total share capital}}$

$$= \frac{₹28.98 \text{ lakhs}}{₹16.00 \text{ lakhs}} = ₹1.81$$

Breakup value of ₹10 paid up share = 1.81 × 10 = ₹18.10

Breakup value of ₹ 6 paid up share = 1.81 × 6 = ₹10.86

Market value of shares

Average dividend = $\frac{11\% + 12\% + 13\% + 14\%}{4} = 12.5\%$

Market value of Rs. 10 paid up share = $\frac{12.5\%}{10\%} \times 10 = ₹12.50$

Market value of Rs. 6 paid up share = $\frac{12.5\%}{10\%} \times 6 = ₹7.50$

(ii) Breakup value of share will remain as before even if the controlling interest is being sold. But the market value of share will be different as the controlling interest would enable the declaration of dividend upto the limit of disposable profit.

$$\frac{\text{Average Profit}}{\text{Paid up value of shares}} \times 100 = \frac{₹3.4 \text{ lakhs}}{₹16 \text{ lakhs}} \times 100 = 21.25\%$$

Market value of shares:

Fort ₹10 paid up share = $\frac{21.25\%}{10\%} \times 10$ = ₹ 21.25

For ₹6 paid up share = $\frac{21.25\%}{10\%} \times 10 \times 6 = 12.75$

For value of shares = $\frac{\text{Break up value + Market value}}{2}$

Fair value of ₹10 paid up share = $\frac{18.10 + 21.25}{2}$ = 19.68

Fair value of ₹ 6 paid up share = $\frac{18.10 + 12.75}{2}$ = 11.81

Working Notes:

	Particulars		
1	**Calculation of average capital employed**		
	Fixed assets		24.00
	Other tangible assets		3.00
	Intangible assets		3.00
	Less: Liabilities	10	30.00
	Bonus	1	(11.00)
	Net assets (excluding goodwill/Closing capital employed)		19.00
	Less: ½ of profits [½ (4.10- 1.0 (i.e. Disputed Bonus)		(1.55)
	Average Capital Employed		17.45
2.	**Calculation of average super profit for 4 years**		
	Average profit = ¼ [3+3.5+4+4.1 - 1.0(i.e. Bonus)] = ¼ × 13.60		3.400
	Less: Normal Profit 10% of ₹17.45 lakhs		(1.745)
	Super Profit		1.655
3.	**Calculation of goodwill [See Assumption below]**		
	3 years' purchase of average super profit		
	= 3 ×1.655 = ₹ 4.965 lakhs		
	Increase in value of goodwill = ½ (Book value + 3 years super profit)		
	= ½ (5+ 4.965) = ₹4.9825 lakhs		
	Net assets as valued in W.N. 1 including book value of goodwill		19.00
	Add: Goodwill as per the balance sheet	5.00	
	Add: Increase in goodwill (rounded off)	4.98	9.98
	Net Assets available for shareholders.		28.98

Note: Tax effect on disputed bonus and corporate dividend tax has been ignored.

Assumption: Goodwill has been calculated on the basis of average capital employed. Alternatively it may be calculated on the basis of closing capital employed. Accordingly, the closing capital employed will be ₹19 lakhs, super profit will be ₹1.5 lakhs, increase in the value of goodwill will be ₹4.75 lakhs and net assets available for shareholders will be ₹28.75 lakhs. In such a case, the break-up value of ₹1 of share capital will be ₹1.80 (instead of 1.81)

Illustration 24:

The following is the Balance Sheet of K Ltd. as on 31st March, 2016:

Balance Sheet

Liabilities	₹ in Lakh	Assets	₹ in Lakh
3,00,000 Equity shares of ₹10 each fully paid 12.5%	30,00,000	Goodwill	3,00,000
		Building	20,00,000
Redeemable preference shares of ₹100 each fully paid	20,00,000	Plant & Machinery	22,00,000
		Furniture	10,00,000
General Reserve	15,00,000	Investments	16,00,000
Profit & Loss A/c	3,00,000	Stock	12,00,000
Secured Loan	10,00,000	Debtors	20,00,000
Creditors	30,00,000	Bank Balance	4,00,000
		Preliminary Expenses	1,00,000
	1,08,00,000		**1,08,00,000**

Additional Information:

(i) Fixed assets are worth 20% more than book value. Stock is overvalued by ₹1,00,000. Debtors are to be reduced by ₹40,000. Trade investments, which constitute 10% of the total investments are to be valued at 10% below cost.

(ii) Trade investments were purchased on 1.4.2015. 50% of non-trade investments were purchased on 1.4.2014 and the rest on 1.4.2015. Non-trade investments yielded 15% return on cost.

(iii) In 2014 - 2015 Furniture with a book value of ₹1,00,000 was sold for ₹50,000. This loss should be treated as non-recurring or extraordinary item for the purpose of calculating adjusted average profit.

(iv) In 2013 - 2014 new machinery costing ₹2,00,000 was purchased, but wrongly charged to revenue. This amount should be adjusted taking depreciation at 10% on reducing value method.

(v) Return on capital employed is 20% in similar business.

(vi) Goodwill is to be valued at two years purchase of super profits based on simple average profits of last four years.

Profits of last four years are as under:

Year	Amount (in ₹)
2012-2013	13,00,000
2013-2014	14,00,000
2014-2015	16,00,000
2015-2016	18,00,000

(vii) It is assumed that preference dividend has been paid till date.

(viii) Depreciation on the overall increased value of assets (worth 20% more than book value) need not be considered. Depreciation on the additional value of only plant and machinery to be considered taking depreciation at 10% on reducing value method while calculating average adjusted profit.

Find out the intrinsic value of the equity share. Ignore income tax and dividend tax.

Solution:

1. Calculation of Goodwill

(i) Capital Employed

	₹	₹
Fixed assets:		
Building	20,00,000	
Plant and machinery (₹22,00,000 + ₹1,45,800)	23,45,800	
Furniture	10,00,000	
	53,45,800	
Add: 20% Appreciation	10,69,160	
	64,14,960	
Trade investments (₹16,00,000 x 10% x 90%)	1,44,000	
Debtors (₹20,00,000 - ₹40,000)	19,60,000	
Stock (₹12,00,000 - ₹1,00,000)	11,00,000	
Bank Balance	4,00,000	1,00,18,960
Less: Outside liabilities:		
Secured Loan	10,00,000	
Creditors	30,00,000	(40,00,000)
Capital employed		60,18,960

(ii) Future Maintainable Profit

Calculation of Average Adjusted Profit

	2012-2013	**2013-2014**	**2014-2015**	**2015- 2016**
	₹	₹	₹	₹
Profit	13,00,000	14,00,000	16,00,000	18,00,000
Add: Capital Expenditure of Machinery charged to revenue		2,00,000		
Loss on sale of furniture			50,000	
	13,00,000	16,00,000	16,50,000	18,00,000
Less: Depreciation on machinery		(20,000)	(18,000)	(16,200)
Income from non-trade investments (W.N.2)			(1,08,000)	(2,16,000)
Reduction in the value of stock				(1,00,000)
Bad debts				(40,000)
Adjusted Profit	13,00,000	15,80,000	15,24,000	14,27,000
Total adjusted profit for four years				58,31,800
Average profit (Rs. -58,31,800/4)				14,57,950
Less: Depreciation at 10% on Additional Value of Machinery				
(22,00,000 + 1,45,800) × 20% × 10%				(46,916)
Average Adjusted Profit				14,11,034

(iii) Normal Profit 20% on Capital Employed,

i.e. 20% on ₹60,18,960 = ₹ 12,03,792

(iv) Super Profit = Average Adjusted profit-Normal profit

= ₹14,11,034 – ₹ 12,03,792 = ₹ 2,07,242

(v) Goodwill

= 2 years purchase of super profit

= ₹ 2,07,242 × 2 = ₹ 4,14,484

2. Trade investments = ₹16,00,000 × 10% × 90% = ₹ 1,44,000

Non-trade investment = ₹ 16,00,000 - ₹ 1,60,000 = ₹ 14,40,000

Non-trade investment purchased on 1.4.2014 = 50% of ₹ 14,40,000 = ₹ 7,20,000

Non-trade investment purchased on 1.4.2015 = ₹ 14,40,000 - ₹7,20,000 = ₹7,20,000

Income from non-trade investment:

In the year 2014-2015 : 7,20,000 x 15% = ₹ 1,08,000

In the year 2015-2016 : 7,20,000 x 15% = ₹ 1,08,000

7,20,000 x 15% = ₹ 1,08,000

= ₹ 2,16,000

Calculation of Intrinsic Value of Equity Shares of K Ltd.

Net Assets available for Equity Shareholders.

	(₹)	(₹)	(₹)
Goodwill (W.N.1) Sundry fixed assets Trade and non-trade investments (1,44,000 + 14,40,000) Debtors Stock Bank balance			4,14,484 64,14,960 15,84,000 19,60,000 11,00,000 4,00,000
Total Assets			1,18,73,444
Less: Outside liabilities			
Secured loan	10,00,000		
Creditors	30,00,000	40,00,000	
Preference share capital		20,00,000	(60,00,000)
Net assets available for equity shareholders			**58,73,444**

$$\text{Value of a equity shares} = \frac{\text{Net Assets Available to Equity Shareholders}}{\text{Number of Equity Shares}}$$

$$= \frac{₹58,73,444}{3,00,000} = ₹\ 19.59 \text{ (approx)}$$

Illustration 25:

The Balance Sheet of Mulyan Ltd., as on 31st December, 2015 is as follows:

Liabilities		₹ in Lakh	Assets	₹ in Lakh
Share Capital:			Goodwill:	50,000
Equity shares of ₹10 each.	5,00,000		Fixed Assets:	
less, calls in arrear			Machinery	2,30,000
(₹2 for final call)	10,000	4,90,000	Factory shed	3,00,000
8% Preference shares of ₹10 each fully paid		2,00,000	Vehicles	60,000
Reserves and Surplus:			Furniture	25,000
General Reserve		2,00,000	Investments	1,00,000
Profit & Loss A/c		1,40,000	Current Assets:	
Current Liabilities:			Stock in trade	2,10,000
Sundry Creditors		2,70,000	Sundry debtors	3,50,000
Bank Loan		1,00,000	Cash at bank	50,000
			Preliminary Expenses	25,000
		14,00,000		**14,00,000**

Additional Information

(i) Fixed assets are worth 20% above their actual book value, depreciation on appreciated portion of fixed assets is to be ignored for valuation of goodwill.

(ii) Of the investments, 80%, is non-trading and the Balance is trading. All trade investments are to be valued at 20% below cost. A uniform rate of dividend of 10% is earned on all investments.

(iii) For the purpose of valuation of shares, Goodwill is to be considered on the basis of 6 year's purchase of the super profits based on simple average profit of the last 3 years. Profits, after tax @ 50%, are as follows:

Year	₹
2013	1,90,000
2014	2,00,000
2015	2,50,000

In a similar business, return on capital employed is 20%. In 2013, a new furniture costing ₹10,000 was purchased but wrongly charged to revenue.

No effect has yet been given for rectifying the same. Depreciation is charged on furniture @ 10% p.a. (Diminishing Balance Method).

Find out the value of each fully paid and partly paid equity shares.

Solution:

Valuation of an equity share

$$\text{Value of an equity share} = \frac{\text{Net assets available to equity share holders (W.N.6)}}{\text{Number of equity shares}}$$

$$= \frac{9,27,740}{50,000} = 18.5548$$

Value of a ₹ 10 fully paid up share = ₹ 18.5548 per share

Value of ₹ 10 share, ₹ 8 per share paid up = (₹ 18,5548 - ₹ 2) per share

= ₹ 16.5548 per share

Working Notes:

1. Capital employed

	₹	₹
Fixed Assets:		
Machinery	2,30,000	
Factory shed	3,00,000	
Furniture (₹25,000 + ₹7,290)	32,290	
Vehicles	60,000	
	6,22,290	
Add: 20% increase	1,24,458	
	7,46,748	
Trade investments (₹1,00,000 x 20%) x 80%	16,000	
Stock in trade	2,10,000	
Sundry Debtors	3,50,000	
Cash at bank	50,000	13,72,748
Less: Outside liabilities:		
Bank Loan	1,00,000	
Sundry Creditors	2,70.000	(3,70,000)
Capital employed		10,02,748

2. Calculation of average adjusted profit

	2013	2014	2015
Prof it after tax	190,000	2,00,000	2,50,000
Add: Tax @ 50%	1,90,000	2,00,000	2,50,000
Profit before tax	3,80,000	4,00,000	5,00,000
Add: Capital expenditure on furniture	10,000		
Less: Depreciation on furniture (Note)*	(1.000)	(900)	(810)
Income from non-trade investments	(8,000)	(8,000)	(8,000)
	3,81,000	3,91,100	4,91,190
Less: Preliminary expenses (See Note)			(25,000)
	3,81,000	(3,91,100)	4,66,190)
Less: Tax @ 50%	(1,90,500)	(1,95,550)	(2,33.095)
Adjusted profit	(1,90,500)	1,95,550	2,33,095

Note: As per para 56 of AS 26, preliminary expenses are to be charged to profit and loss account as and when they are incurred. It is assumed that preliminary expenses were incurred in the year 2015. Therefore, charged to the profit of the year 2015 only.

	₹
Total adjusted profit for three years (1,90,500 + 1,95,550 + 2,33,095)	6,19,145
Adjusted Average profit (6,19,145/3)	2,06,382

3. Normal profit: 20% on capital employed i.e. 20% on ₹10,02,748 = ₹2,00,550

4. Super profit: Average Adjusted profit - Normal profit

= ₹2,06,382 - ₹2,00,550 = ₹5,832

5. Goodwill: 6 years' purchase of super profit

= ₹5,832 × 6 = ₹34,992

6. Net assets available to equity shareholders

	₹
Capital employed (W.N.1)	10,02,748
Goodwill (W.N.5)	34,992
Add: Non-trade investments	80,000
	11,17,740
Less: Preference share capital	(2,00,000)
	9,17,740
Add: Notional calls received for calls in arrears	10,000
Net assets for equity shareholders	9,27,740

[Note: Furniture is assumed to be purchased at the beginning of the year and therefore, depreciation is charged for the whole year in 2013].

Illustration 26:

The capital structure of VWX Ltd. is as follows as on 31st March, 2015:

Particulars	(₹)
45,000, Equity Shares of 100 each fully paid	45,00,000
12,500, 12% Preference Shares of 100 each fully paid	12,50,000
12% Secured Debentures	12,50,000
Reserves	12,50,000
Profit before Interest and tax during the year	18,00,000
Tax rate	40%

Normally the return on equity shares in this type of industry is 15%. Find out the value of the equity shares subject to the following:

(i) Profit after tax covers fixed interest and fixed dividend at least 4 times.

(ii) Debt equity ratio is at least 2.

(iii) Yield on shares is calculated at 60% of distributed profits and 10% on undistributed profits.

(iv) The company has been paying regularly an equity dividend of 15%.

(v) Risk premium for dividends is generally assumed at 1%.

Solution:

1. Computation of Profit after Tax (PAT) and Retained Earnings

Particulars		₹
Profit before interest and tax (PBIT)		18,00,000
Less: Debentures interest (12,50,000 ×12/100)		(1,50,000)
Profit before tax (PBT)		16,50,000
Less: Tax @ 40%		(6,60,000)
Profit after tax (PAT)		9,90,000
Less: Distributed profits-		
Preference dividend $\left(12,50,000\times\frac{12}{100}\right)$	1,50,000	
Equity dividend $\left(45,00,000\times\frac{15}{100}\right)$	6,75,000	8,25,000
Retained earnings (undistributed profit)		1,65,000

2. Computation of Interest and Fixed Dividend Coverage

$$= \frac{\text{PAT+Debenture interest}}{\text{Debenture interest +Preference dividend}} = \frac{₹9,90,000+₹1,50,000}{₹1,50,000+₹1,50,000} = 3.8$$

This ratio is less than the prescribed ratio i.e. 4.

3. Computation of Debt Equity Ratio

$$\text{Debt Equity Ratio} = \frac{\text{Debt (long term loans)}}{\text{Equity (shareholders' funds)}}$$

$$= \frac{\text{Debentures}}{\text{Preference share capital + Equity share capital + Reserves}}$$

$$= \frac{₹12,50,000}{₹12,50,000 + ₹45,00,000 + ₹12,50,000}$$

$$\text{Debt Equity Ratio} = ₹\frac{12,50,000}{70,00,000} = 0.179$$

The ratio is less than the prescribed ratio i.e. 2.

4. Computation of Actual Yield on Equity Shares

Yield on equity shares is calculated at 60% of distributed profits and 10% of undistributed profits as follows:

	Amt. (₹)
60% of distributed profits (60% of ₹6,75,000)	4,05,000
10% of undistributed profits (10% of ₹1,65,000)	16,500
	4,21,500

Yield on equity shares = $\frac{\text{Yield on shares}}{\text{Equity Share capital}} \times 100 = \frac{4,21,500}{45,00,000} \times 100$ = 9.37%

5. Calculation of Expected Yield on Equity Shares

Normal return expected	15%
Add: Risk premium for low interest and fixed dividend coverage (3.8 < 4)	1% (Note - 1)
Risk adjustment for debt equity ratio not required	Nil (Note - 2)
	16%

Note 1: When interest and fixed dividend coverage is lower than the prescribed norm, the riskiness of equity investors is high. Thus, they should claim additional risk premium over and above the normal rate of return.

Note 2: The debt equity ratio is lower than the prescribed ratio that means outside funds (Debts) are lower as compared to shareholders' funds. Thus, the risk is less for equity shareholders. Therefore, no risk premium is required to be added in such a case.

Value of an Equity Share

$$= \frac{\text{Actual yield}}{\text{Expected yield}} \times \text{Paid up value of a share} = \frac{9.37\%}{16\%} \times 100 = 58.56$$

5.5 VALUATION OF GOODWILL

Goodwill is an intangible fixed asset of an organisation which has to be reflected in its books of accounts on certain circumstances. For this purpose, a money value is required to be attached to this intangible asset. The process of estimating the value of goodwill using certain accepted methodologies is referred to as **valuation of goodwill**.

METHODS OF GOODWILL VALUATION

Average Profit Method:

- As per this method, the value of goodwill depends on the past profit earning capacity of the entity.
- The past profits of certain given number of years are used to determine 'Average Profit'. Such Average Profit may be either 'Simple Average Profit' or 'Weighted Average Profit'.
- Finally, the value of goodwill is determined by multiplying the Average Profit so calculated by certain 'Number of Years' Purchase'.

$\therefore$ Value of Goodwill = Average Profit × No. of Years' Purchase

Student Note:

The variables which influence the valuation of goodwill are discussed hereunder:

- **Profit:** The term 'profit', here, refers to the past profits earned by the firm. These past profits are required to be adjusted/ modified for any abnormal or non-recurring items (whether gain or loss), which are not expected to arise in the future under normal circumstances. The past profit figures are, thus to be used to determine the 'Future Maintainable Profits' that is expected to be earned by the entity.

- **Simple Average Profit:** When there is no definite trend in the past profits, the past profits are simply aggregated and then divided by the number of years to determine the Average Profit. Since, in this case no weights are used on the past profits, the Average Profit, so determined, is referred to as Simple Average Profit.

  $\therefore$ Simple Average Profit = $\frac{P1+P2+\cdots+Pn}{n}$ where, P = Profit of respective year;
  n = Number of years

- **Weighted Average Profit:** When there exists a clear trend (either increasing or decreasing) in the past profits, the past profits are firstly by multiplied by certain 'weights', and then the products are aggregated. Finally, the aggregate figure is divided by the 'aggregate of all the weights' to arrive at the Weighted Average Profit.

  $\therefore$ Weighted Average Profit = $\frac{P1.W1+P2.W2+\cdots\cdots+Pn.Wn}{W1+W2+\cdots\cdots+Wn}$ where, P = Profit of respective year;
  W = Weight of respective year;
  n = Number of years

- **Number of Years' Purchase:** For valuation of goodwill, the average profit determined is usually multiplied by a figure referred to as "Number of Years' Purchase". The phrase 'Number of Years' Purchase' refers to the expected number of future years for which the firm is expected to earn the average profit from the year of purchase. In other words, it is assumed to be the time period during which the entity will enjoy the profit earning capacity.

Illustration 27:

XY Ltd, a partnership firm, earned profits during the past 5 years as follows:

Year	2011	2012	2013	2014	2015
Profits (₹)	27,000	36,000	37,200	42,000	46,800

Determine the value of goodwill in each of the following independent cases:

Case (a): It was decided to value the Goodwill on the basis of 2 years' purchase of average profit of last five years.

Case (b): It was decided to value the Goodwill on the basis of 3½ years' purchase of average profit of last five years after giving weights of 1, 2, 3, 6 and 8 to the profits chronologically.

Case (c): It was decided to value the Goodwill on the basis of 3 years' purchase of weighted average profit of last five years giving maximum weightage to the recent results.

Case (d): It was decided to value the Goodwill on the basis of 2½ years' purchase of simple average profit of last five years. In this regard the following were observed:

(i) an abnormal loss of ₹ 1,800 was charged against the profit of 2013;

(ii) Profit of 2014 included a non-recurring receipt of ₹ 2,500.

(iii) closing stock of 2015 was over-valued by ₹ 2,400.

Solution:

Case (a):

$$\text{Average profit} = \frac{₹27,000 + ₹36,000 + ₹37,200 + ₹42,000 + ₹46,800}{5} = ₹\ 37,800$$

∴ Value of Goodwill = ₹ 37,800 × 2 years' purchase = ₹ 75,600

Case (b):

$$\text{Weighted average profit} = \frac{(₹27,000 \times 1) + (₹36,000 \times 2) + (₹37,200 \times 3) + (₹42,000 \times 6) + (₹46,800 \times 8)}{1+2+3+6+8} = ₹\ 41,850$$

∴ Value of Goodwill = ₹ 41,850 × 3½ years' purchase = ₹ 1,46,475

Case (c):

$$\text{Weighted average profit} = \frac{(₹27,000 \times 1) + (₹36,000 \times 2) + (₹37,200 \times 3) + (₹42,000 \times 4) + (₹46,800 \times 5)}{1+2+3+4+5} = ₹\ 40,840$$

∴ Value of Goodwill = ₹ 40,840 × 3 years' purchase = ₹ 1,22,520

Case (d):

For valuation of goodwill under simple average method, average profit of last few years is to be multiplied by number of year of purchase. Here, the term 'profit' refers to 'Future Maintainable Profits' that the entity can expect to earn in the future. For determining such maintainable profit, past profits are required to be adjusted/ modified for any abnormal or non-recurring items (whether gain or loss), which are not expected to arise in the future under normal circumstances.

In this case,

Profit of 2013 = Profit (as given) + Abnormal loss sustained in 2013 (which cannot be expected to occur in future)

= ₹ 37,200 + ₹ 1,800 = ₹ 39,000

Profit of 2014 = Profit (as given) – Non-recurring receipt of 2014 (which cannot be expected to occur in future)

= ₹ 42,000 – ₹ 2,500 = ₹ 39,500

Profit of 2015 = Profit (as given) – Overvaluation of closing stock (rectification of profit)

= ₹ 46,800 – ₹ 2,400 = ₹ 44,400

$$\text{Simple Average profit} = \frac{₹27,000 + ₹36,000 + ₹39,000 + ₹39,500 + ₹44,400}{5} = ₹\ 37,180$$

∴ Value of Goodwill = ₹ 37,180 × 2½ years' purchase = ₹ 92,950

Super Profit Method:

- As per this method, the value of goodwill depends on the extra (i.e. super) profit earning capacity of an entity.
- Such 'Super Profit' refers to the excess profit earned by the entity over the normal profit that should be earned by a similar firm in the industry.
- Mathematically, Super Profit = Average Future Maintainable Profit – Normal Profit

  i.e. Super Profit = Average Future Maintainable Profit – (Average Capital Employed × Normal rate of return)
- Finally, the value of goodwill is determined by multiplying the Super Profit, so calculated, by certain 'No. of Years' Purchase'.

∴ Value of Goodwill = Super Profit × No. of Years' Purchase

Student Note:

The different variables which influence the valuation of goodwill under 'Super Profit method' are:

- **Super Profit:** Every firm in an industry is expected to earn a normal rate of return. If a particular firm of the industry manages to earn a rate of return that happens to be more than the normal industry rate of return, then such a firm is said to be earning 'Super Profits'. The value of goodwill, under this method, is correlated with this extra profit earning capacity of the firm.
- **Average Future Maintainable Profit:** It refers to the profit that is expected to be earned by the entity in the future under normal circumstances. For this purpose, the past profits that are required to be adjusted/ modified for any abnormal or non-recurring items (whether gain or loss).
- **Capital Employed:** Capital Employed refers to the amount of capital that has been invested in the firm. It is measured as the excess of current value of Total Assets (excluding Goodwill and Fictitious assets) over the current liabilities. Alternatively, it is the aggregate of Owned Capital, Accumulated Profits and Borrowed Capital, if any.
- **Average Capital Employed:** Average Capital Employed is determined by averaging the capital employed at the beginning of the accounting period and that at the end of the accounting period. Mathematically,

  $$\text{Average Capital Employed} = \frac{\text{Opening Capital Employed + Closing Capital Employed}}{2}$$
- **Normal Rate of Return:** It is the rate of return that is usually earned by any firm belonging to a particular industry.
- **Number of Years' Purchase:** For valuation of goodwill, the super profit is usually multiplied by a figure referred to as "Number of Years' Purchase". The phrase 'Number of Years' Purchase' refers to the expected number of future years for which the firm is expected to earn such super profits from the year of purchase.

Illustration 28:

XY Ltd, a partnership firm, earned profits during the past 4 years as follows:

Year	2012	2013	2014	2015
Profits (₹)	42,000	46,000	52,000	46,500

Firm has total assets worth ₹ 82,000 and its current liability includes only creditors of ₹ 12,800. The normal rate return is 10%. Determine the value of goodwill on the basis of 2½ year's purchase of super profits.

Solution:

$$\text{Average Future Maintainable Profit} = \frac{₹42,000 + ₹46,000 + ₹52,000 + ₹46,500}{4} = ₹46,625$$

Here, Capital employed = Total assets – Current Liabilities = ₹ 82,000 – ₹ 12,800 = ₹69,200

Normal profit = Capital employed × Normal rate of return = ₹ 69,200 × 10% = ₹6,920

∴ Super profit = Average Future Maintainable Profit – Normal profit = ₹ 46,625 – ₹ 6,920 = ₹ 39,705

∴ Value of Goodwill = ₹ 39,705 × 2½ years' purchase = ₹ 99,263 (approx.)

Annuity Method:

- This method of goodwill valuation considers the 'time value of money'.
- Under this method, Value of Goodwill = Super Profit × Annuity Value

Student Note:
The different variables which influence the valuation of goodwill under 'Super Profit method' are: • **Super Profit**: It refers to the excess profit earned by the entity over the normal profit that should be earned by a similar firm in the industry. • **Annuity:** Annuity refers to a series of continuous cash flows (either cash inflows or cash outflows) of equal amount that occur in every period, over a specified period of time. • **Annuity Value**: It is determined either from the Annuity Table or may be ascertained from the following formula: Annuity Value = $\frac{(1+r)^n - 1}{r(1+r)^n}$ where, r = Rate of Interest per period, and n = Number of periods.

Illustration 29:

From the following particulars you are required to determine value of goodwill of ABX Ltd.

Super Profit (Computed)	: ₹ 4,50,000
Normal rate of return	: 12%
Present value of annuity of ₹1 for 4 years @ 12%	: 3.0374

Solution:

Value of goodwill = Super profit × P.V of Annuity of ₹ 1for 4 years @ 12%

= ₹ 4,50,000 × 3.0374 = ₹ 13,66,830

Illustration 30:

The following details relate to M/s XYZ, a firm:

Average profit of last four years	: 7,00,000
Average capital employed by the firm	: ₹ 55,00,000
Normal rate of return	: 10%
Present value of annuity of ₹1 for 4 years @ 10%	: 3.1699

Determine the value of goodwill on the basis of annuity of super profit.

Solution:

Super Profit = Average Future Maintainable Profit – Normal Profit

= Average Future Maintainable Profit – (Average Capital Employed X Normal rate of return)

= ₹ 7,00,000 – (₹ 55,00,000 × 10%)

= ₹ 1,50,000

∴ Value of goodwill = Super profit × P.V of Annuity of ₹ 1for 4 years @ 10%

= ₹ 1,50,000 × 3.1699 = ₹ 4,75,485

Capitalisation Method:

- There are two ways of determining the value of goodwill using the capitalisation approach. They are:
  - ✓ Capitalisation of Average Profits; and
  - ✓ Capitalisation of Super Profits.
- **Capitalisation of Average Profits**: When the average profits are capitalised, then firstly, the 'Capitalised Value of the firm' is determined and there from the 'Net Assets' are deducted to arrive at value of goodwill.

  Mathematically, Capitalised Value of the firm = $\frac{\text{Average Future maintainable profit}}{\text{Normal rate of return (\%)}}$; and

Value of Goodwill = Capitalised Value of the firm **Less** Net Assets

- **Capitalisation of Super Profits**: When the super profits are capitalised, then the value of goodwill is directly ascertained.

$$\text{Value of Goodwill} = \frac{\text{Super Profit}}{\text{Normal rate of return (\%)}}$$

Student Note:
The different variables which influence the valuation of goodwill under 'Super Profit method' are: • **Capitalised Value of the firm:** It refers to the standard value of the firm i.e. what ought to be the value of the firm considering its profit earning capacity at the normal rate of return. • **Net Assets:** It refers to the excess of current value of Total Assets (excluding Goodwill and Fictitious assets) over the external liabilities. In other words, it refers to the Net Worth of the entity. • **Super Profit**: It refers to the excess profit earned by the entity over the normal profit that should be earned by a similar firm in the industry.

Illustration 31:

A firm values goodwill under 'Capitalisation of profits' method. Its average profits for past 4 years has been determined at ₹ 72,000. Net Assets and Capital employed in the business is ₹4,80,000 and ₹ 5,00,000 respectively; and its normal rate of return is 12%.

Determine value of goodwill based on:

(a) Capitalisation of Average Profits

(b) Capitalisation of Super Profits

Solution:

(a) **Capitalisation of Average Profits**

$$\text{In this case, Capitalised Value of the Business} = \frac{\text{Expected Average Profit}}{\text{Normal Rate of Return}} = \frac{₹7{,}000}{12\%} = ₹\ 6{,}00{,}000$$

∴ Value of Goodwill = Capitalised Value of the Business ***Less*** Net Assets

= ₹ 6,00,000 – ₹4,80,000 = ₹ 1,20,000

(b) **Capitalisation of Super Profits**

$$\text{In this case, Value of Goodwill} = \frac{\text{Super Profit}}{\text{Normal rate of return (\%)}}$$

Super profit = Average profit – Normal Profit = Average profit – (Capital employed X Normal rate of return)

= ₹ 72,000 – (₹ 5,00,000 × 12%)

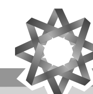
= ₹ 72,000 – 60,000

= ₹ 12,000

$$\therefore \text{Value of Goodwill} = \frac{\text{Super Profit}}{\text{Normal rate of return (\%)}} = \frac{12{,}000}{12\%} = ₹\ 1{,}00{,}000$$

Study Note - 6

SHARE BASED PAYMENTS



This Study Note includes

6.1 Introduction
6.2 Share Based Payment
6.3 Employee Share Based Payment Plans
6.4 Share Based Payment Transaction
6.5 Recognition of Share Based Payment in Financial Statement
6.6 Measurement of Share Based Payment
6.7 Disclosure of Share Based Payment
6.8 Accounting for Share Based Payment Plans

6.1 INTRODUCTION

In recent times, different types of share plans and share option plans have become a common feature of remuneration packages for senior executives, directors and other employees in many countries. Moreover, Shares and share options may also be used to pay suppliers for providing professional services. All these mode of payment are known as **Share-based Payment**.

Share based payments cover all forms of share-based payment for the goods as-well-as for the services supplied by the reporting entity, including:

- employee share or share option schemes;
- share-based payments to parties other than employees that have supplied goods or services to the entity;
- payments to be settled in cash or other assets at amounts that depend on share values, e.g. share appreciation rights.

The accounting for Share-based Pay

Payments" fills a gap in accounting for the recognition and measurement of such transactions. These standards require an entity to reflect in its profit or loss and financial position the effects of share-based payment transactions, including expenses associated with transactions in which share options are granted to employees.

6.2 SHARE BASED PAYMENT

A **share-based payment** is a transaction in which the entity receives goods or services either as consideration for its equity instruments or by incurring liabilities for amounts based on the price of the entity's shares or other equity instruments of the entity.

Employee share-based payments are incentive payments to employees in form of shares. The expression employee share-based payments also include cash incentives to employees, the size of which is linked with value of shares. The payment in form of shares generally involve grant of options to employees to subscribe shares of employer's enterprise at a concessional price, called the exercise price.

The employees gain the excess of market price of share at the time of exercise over the specified exercise price. In case of employee share-based payments in form of cash incentive, the excess of market price on specified future date and a stated price is paid in cash. In either case, the value of incentive depends on increase in share

value, which is the generally accepted indicator financial success of a business. By linking incentives with value of shares, the employee share-based payment plans effectively integrate personal goals of employees with that of the enterprise.

The day a share-based payment plan is announced and accepted by employees is called the grant date and the day, when the employees become entitled to such payments, is called the vesting date. The period between these two dates is called the vesting period. To qualify for the incentives, the employees put in their efforts during the vesting period to fulfill specified vesting conditions, e.g. reaching a specified sales/profit target. Exercise date is the date when an option is exercised by paying the exercise price.

The value of share-based payment depends on the market value of shares on vesting date/exercise date and hence cannot be known with certainty before these dates. Nevertheless, since the share-based payments are payments for services rendered by employees during the vesting period, the value of share-based payments should be recognised as expense during the vesting period, i.e. before value of such payments are known with certainty.

Two principal issues involved in accounting for employee share-based payments are:

(i) Problem of valuation of share-based payments before vesting date; and

(ii) Problem of allocation of the estimated value of share-based payment to a particular accounting period during the vesting period for recognition as expense.

6.3 EMPLOYEE SHARE BASED PAYMENT PLANS

It is an agreement between an entity (or another group entity or a shareholder of a group entity) and another party including an employee) which entitles the other party to receive:

- Equity instruments (including shares or share options) of the entity (or another group entity); or
- Cash (or other assets) for amounts based on the price (or value) of equity instruments of the entity (or another group entity), provided specified vesting conditions (if any) are met.

  "Vest" means to become an entitlement. A party's right to shares of an entity may be free or at a pre-arranged exercise price.

Important Terminology:

Important Terminology:
• **Grant:** Grant of the option means giving an option to the employees to subscribe to the shares of the company.
• **Vesting:** It is the process by which the employee is given the right to apply for shares of the company against the option granted to him in purchase of employee in pursuance of employee stock option scheme (ESOS).
• **Vesting Period:** It is the time period during which the vesting of the option granted to the employee on pursuance of ESOS takes place.
• **Option:** Option means a right but not an obligation granted to an employee in pursuance of ESOS to apply for shares of the company at a pre-determined price.
• **Exercise Period:** It is the time period after vesting within which the employee should exercise his right to apply for shares against the option vested in him in pursuance of the ESOS.
• **Exercise Price:** It is the price payable by the employee for exercising the option granted to him in pursuance of ESOS.
• **Intrinsic Value:** It is the excess of the market price of the share under ESOS over the exercise price of the option (including up-front payment, if any).
• **Fair Value:** It is the amount for which stock option granted or a share offered for purchase could be exchanged between knowledgeable, willing parties in an arm's length transaction.

TYPES OF SHARE BASED PAYMENT PLANS

Share-based payment plans generally take three forms i.e. Employee Stock Option Plans (ESOP), Employee Stock Purchase Plans (ESPP) and Stock Appreciation Rights (SAR).

These are being defined as follows:

- **Employee Stock Option Plan (ESOP):** It is a contract that gives the employees of an enterprise the right, but not obligation, for a specified period to purchase or subscribe to the specified number shares of the enterprise at a fixed or determinable price, called the exercise price.
- **Employee Stock Purchase Plan (ESPP):** Under Employees' Stock Purchase Plans (ESPP), employees are given an option to subscribe to shares of employer in a public issue or otherwise. The exercise price is set at a specified rate of discount on the issue price/ market price on the date of exercise.
- **Stock Appreciation Rights (SAR):** These are the rights that entitle the employees to receive cash or shares for an amount equivalent to the excess of market price on exercise date over a stated price.

6.4 SHARE BASED PAYMENT TRANSACTION

A transaction in a share based payment arrangement in which the entity:

- Receives goods or services from a supplier (including an employee); or
- Incurs an obligation (to the supplier) when another group entity receives those goods or services.

TYPES OF SHARE BASED PAYMENT TRANSACTIONS

There are three types of share-based payment transactions:

- **Equity-settled share-based payment transactions:** Under this type of Share-based Payment transaction, an entity receives services, as consideration for its own equity instruments or it has no obligation to settle the transaction with the supplier.
- **Cash-settled share-based payment transactions:** Under this type of Share-based Payment transaction, the entity acquires services by incurring liabilities for amounts that are based on the price (or value) of equity instruments of the entity or another group entity.
- **Share-based payment transactions with cash alternatives:** Here an entity has a choice of issuing shares or paying cash then the entity shall recognise a liability if it determines that it has an obligation to settle the liability in cash. If on settlement the entity issues shares rather than paying cash then the value of the liability should be transferred to equity.

6.5 RECOGNITION OF SHARE-BASED PAYMENT IN FINANCIAL STATEMENT

An entity shall recognise the goods or services received or acquired in a share-based payment transaction when it obtains the goods or as the services are received.

The entity shall recognise a corresponding increase in equity if the goods or services were received in an equity-settled share-based payment transaction or a liability if the goods or services were acquired in a cash-settled share-based payment transaction.

When the goods or services received or acquired in a share-based payment transaction do not qualify for recognition as assets, they shall be recognised as expenses.

6.6 MEASUREMENT OF SHARE BASED PAYMENT

The measurement of Share-based Payment is as under:

- **In case of equity-settled share-based payment transactions:** the entity shall measure the goods or services received, and the corresponding increase in equity, directly, at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the entity shall measure their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted.
- **In case of cash-settled share-based payment transactions:** The entity shall measure the goods or services acquired and the liability incurred at the fair value of the liability. Until the liability is settled, the entity shall re-measure the fair value of the liability at the end of each reporting period and at the date of settlement, with any changes in fair value recognised in profit or loss for the period.
- **In case of share-based payment transactions with cash alternatives:** For share-based payment transactions in which the terms of the arrangement provide either the entity or the counterparty with the choice of whether the entity settles the transaction in cash (or other assets) or by issuing equity instruments, the entity shall account for that transaction, or the components of that transaction, as a cash-settled share-based payment transaction if, and to the extent that, the entity has incurred a liability to settle in cash or other assets, or as an equity-settled share-based payment transaction if, and to the extent that, no such liability has been incurred.

6.7 DISCLOSURES OF SHARE-BASED PAYMENT

An entity shall disclose information that enables users of the financial statements to understand the nature and extent of share-based payment arrangements that existed during the period. The entity shall disclose atleast the following:

- A description of each type of share-based payment arrangement that existed at any time during the period,
- The number and weighted average exercise prices of share options for each of the following groups of options:
  - ➢ outstanding at the beginning of the period;
  - ➢ granted during the period;
  - ➢ forfeited during the period;
  - ➢ exercised during the period;
  - ➢ expired during the period;
  - ➢ outstanding at the end of the period; and
  - ➢ exercisable at the end of the period.
- For share options exercised during the period, the weighted average share price at the date of exercise. If options were exercised on a regular basis throughout the period, the entity may instead disclose the weighted average share price during the period.
- For share options outstanding at the end of the period, the range of exercise prices and weighted average remaining contractual life. If the range of exercise prices is wide, the outstanding options shall be divided into ranges that are meaningful for assessing the number and timing of additional shares that may be issued and the cash that maybe received upon exercise of those options.
- An entity shall disclose information that enables users of the financial statements to understand how the fair value of the goods or services received, or the fair value of the equity instruments granted, during the period was determined.

- If the entity has measured the fair value of goods or services received as consideration for equity instruments of the entity indirectly, by reference to the fair value of the equity instruments granted, the entity shall disclose at least the following:
  - ✓ **for share options granted during the period**, the weighted average fair value of those options at the measurement date and information on how that fair value was measured, including:
    - (i) the option pricing model used and the inputs to that model, including the weighted average share price, exercise price, expected volatility, option life, expected dividends, the risk-free interest rate and any other inputs to the model, including the method used and the assumptions made to incorporate the effects of expected early exercise;
    - (ii) how expected volatility was determined, including an explanation of the extent to which expected volatility was based on historical volatility; and
    - (iii) whether and how any other features of the option grant were incorporated into the measurement of fair value, such as a market condition.
  - ✓ **for other equity instruments granted during the period** (i.e. other than share options), the number and weighted average fair value of those equity instruments at the measurement date, and information on how that fair value was measured, including:
    - (i) if fair value was not measured on the basis of an observable market price, how it was determined;
    - (ii) whether and how expected dividends were incorporated into the measurement of fair value; and
    - (iii) Whether and how any other features of the equity instruments granted were incorporated into the measurement of fair value.
  - ✓ **for share-based payment arrangements that were modified during the period**:
    - (i) an explanation of those modifications;
    - (ii) the incremental fair value granted (as a result of those modifications); and
    - (iii) Information on how the incremental fair value granted was measured, consistently with the requirements set out in (a) and (b) above, where applicable.
- If the entity has measured directly the fair value of goods or services received during the period, the entity shall disclose how that fair value was determined, e.g. whether fair value was measured at a market price for those goods or services.
- If the entity has rebutted the presumption, it shall disclose that fact, and give an explanation of why the presumption was rebutted.
- An entity shall disclose information that enables users of the financial statements to understand the effect of share-based payment transactions on the entity's profit or loss for the period and on its financial position.
- The entity shall also disclose at least the following:
  - ✓ the total expense recognised for the period arising from share-based payment transactions in which the goods or services received did not qualify for recognition as assets and hence were recognised immediately as an expense, including separate disclosure of that portion of the total expense that arises from transactions accounted for as equity-settled share-based payment transactions;
  - ✓ for liabilities arising from share-based payment transactions:
    - (i) the total carrying amount at the end of the period; and
    - (ii) the total intrinsic value at the end of the period of liabilities for which the counterparty's right to cash or other assets had vested by the end of the period (e.g. vested share appreciation rights).

6.8 ACCOUNTING FOR SHARE BASED PAYMENT PLANS

1. **Accounting for Employee Stock Option Plan (ESOP):**

   The accounting for ESOP involves (i) Valuation of the Stock Options (ii) Recording of the transactions; and (iii) Presentation & Disclosure in financial statement.

(i) Valuation of the Stock Options

- **Value of an option** is the difference between the 'Exercise Price' and the 'Market Value' of the shares on the date of granting the options. To be precise, it is the excess of 'Market Value' over the 'Exercise Price'.
- Mathematically, IV = Market value per share – Exercisable Price per share
- Such valuation is done at the end of the financial year in which the options have been granted.

Gross Value (GV) of employee compensation expenses

$$GV = \text{No. of Options expected to vest} \times \text{Intrinsic Value} \times \frac{\text{Expired Period}}{\text{Vesting Period}}$$

Employee Compensation Expenses to be recognised

= Gross Employees compensation expenses – Expenses already recognized

(ii) Recording of Transactions:

Transaction	Journal Entry
1. Granting of Stock Option	No Journal Entry
2. Recognition of Stock Option Expenses	Employees Stock Option Expenses A/c Dr. To Employees Stock Options Outstanding A/c (Being expenses on …. stock option recognised)
3. Transfer of 'Employees Stock Option Expenses' A/c at the end of accounting period	P/L A/c Dr. To Employees Stock Option Expenses A/c (Being Employees Stock Option expense transferred)
4. Cancellation of options during vesting period	Employees Stock Option Outstanding A/c Dr. To P/L A/c (Being … options cancelled during vesting period)
5. Exercising of Stock Options	Bank A/c Dr. To Employees Stock Option Outstanding A/c (Being money received on …. options exercised)
	Employees Stock Option Outstanding A/c Dr. To Equity Share Capital A/c To Securities Premium Reserve A/c (Being Employees Stock Option Outstanding Account transferred to Equity Share Capital and Securities Premium Reserve Account as per BR. No ... dated …)
6. Lapse of unvested Stock Options at the end of the exercise period	Employees Stock Option Outstanding A/c Dr. To General Reserve/ P/L A/c (Being… unvested options lapsed at the end of exercised period)

(iii) Presentation in financial statement:

In Statement of P/L:	Employees Stock Option Expenses A/c is to be recognised as an expense over the vesting period.
In Balance Sheet:	**During vesting period:** o 'ESOP Outstanding A/c' is to be shown under the head 'Reserves & Surplus' of the Balance Sheet. **After exercise period:** o Lapsed unvested option is to be included with the 'General Reserve' or 'Profit & Loss' under the head 'Reserves & Surplus'.

2. Accounting for Employee Stock Purchase Plan (ESPP):

Valuation of Total fair of ESPP:

Fair Value of ESPP = No. of Shares issued × (Fair Value of a Share - Issue Price)

Expenses are to be recognised over the vesting period in the same way as ESOP.

It is further to be noted that the Fair Value of ESPP can be less than the discount due to post-vesting restrictions on transfers of shares or some other factors.

Recording of Transactions:

Bank A/c	Dr.	[No. of Shares issued × Issue Price]
Employees' Compensation A/c	Dr.	[No. of Shares issued × (Fair Value of Share - Issue Price)]
To Share Capital A/c		[No. of Shares issued × Nominal Value]
To Securities Premium A/c		[No. of Shares issued × (Fair Value of Share - Nominal Value)]

3. Accounting for Stock Appreciation Rights (SAR):

- The SAR's grant date "fair value" is amortized over the SAR's requisite service period (e.g., typically the vesting period).
- "Fair value" is determined using an option pricing model (e.g., Black-Scholes model or Binomial model).
- Any recognized compensation cost may not be reversed after requisite service has been rendered. In addition, no previously recognized compensation cost may be reversed if a vested SAR expires unexercised.
- Previously recognized compensation cost should be reversed if SAR is forfeited due to employee's failure to satisfy service requirement.

Illustration 1.

Ajanta grants 120 share options to each of its 230 employees. Each grant is conditional on the employee working for Ajanta over the next three years. Ajanta has estimated that the fair value of each share option is ₹24. Ajanta estimates that 25% of employees will leave during the three-year period and so forfeit their rights to the share options. Everything turns out exactly as expected.

Calculate the amounts to be recognized as expense during the vesting period.

Solution:

Year	Calculation	Expense for Period (₹)	Cumulative Expense (₹)
1	(27,600 options × 75% × ₹ 24 × 1/3 years)	1,65,600	1,65,600
2	(27,600 options × 75% × ₹ 24 × 2/3 years) – ₹ 1,65,600	1,65,600	3,31,200
3	(27,600 options × 75% × ₹ 24 × 3/3 years) – ₹ 3,31,200	1,65,600	4,96,800

An enterprise should review all estimates taken in consideration for valuation of option. The value of options recognized as expense in an accounting period is the excess of cumulative expense as per latest estimates up to the current accounting period over total expense recognized up to the previous accounting period.

Illustration 2.

The following particulars in respect of stock options granted by a company are available:

Grant date	April1, 2014
Employees covered (Nos.)	525
Options granted per employee (Nos.)	100
Vesting condition: Continuous employment for 3 years	
Nominal value per share (₹)	100
Exercise price per share (₹)	125
Market price per share on grant date (₹)	149
Date of Vesting	March 31, 2017
Date of Exercise	March 31, 2018
Fair value of option per share on grant date (₹)	30

Position on 31/03/15

Estimated annual rate of departure 2%; Number of employees left = 15

Position on 31/03/16

Estimated annual rate of departure 3%; Number of employees left = 10

Position on 31/03/17

Number of employees left = 8; Number of employees entitled to exercise option = 492

Position on 31/3/18

Number of employees exercising the option = 480; Number of employees not exercising the option = 12

Compute expenses to recognize in each year by (i) fair value method (ii) intrinsic value method and show important accounts in books of the company by both of the methods.

Solution:

As per Fair Value Method

Year 2014-15

Fair value of option per share = ₹30

Number of shares expected to be vested = (525 × 0.98 × 0.98 × 0.98) × 100 = 49,400

Fair value = 49,400 x ₹30 = ₹14,82,000

Vesting period = 3 years

Value of option recognized as expense in 2014-15 = ₹14,82,000/3 = ₹4,94,000

Year 2015-16

Fair value of option per share = ₹30

Number of shares expected to be vested = [(525 – 15) × 0.97 × 0.97)] × 100 = 47,986

Fair value = 47,986× ₹ 30 = ₹ 14,39,580

Vesting period = 3 years

Number of years expired = 2 years

Cumulative value of option to recognize as expense in 2014-15 and 2015-16

= (₹ 14,39,580/3)×2 = ₹ 9,59,720

Value of option recognized as expense in 2015-16

= ₹ 9,59,720 – ₹ 4,94,000 = ₹ 4,65,720

Year 2016-17

Fair value of option per share = ₹ 30

Number of shares actually vested under the scheme = 492 ×100 = 49,200

Fair value = 49,200 × ₹ 30 = ₹ 14,76,000

Cumulative value of option to recognize as expense in 3 years = ₹ 14,76,000

Value of option recognized as expense in 2016-17 = ₹ 14,76,000 – ₹ 9,59,720 = ₹ 5,16,280 Year

Year 2017-18

Fair value of option per share = ₹ 30

Number of shares not subscribed = (492 – 480) × 100 = 1,200 Value of option forfeited = 1,200 ×₹ 30

= ₹ 36,000.

Dr. **Employees' Compensation Account** **Cr.**

Year	Particulars	₹	Year	Particulars	₹
2014-15	To ESOP Outstanding A/c	4,94,000	2014-15	By Profit & Loss A/c	4,94,000
2015-16	To ESOP Outstanding A/c	4,65,720	2015-16	By Profit & Loss A/c	4,65,720
2016-17	To ESOP Outstanding A/c	5,16,280	2016-17	By Profit & Loss A/c	5,16,280

Dr. **ESOP Outstanding Account** **Cr.**

Year	Particulars	₹	Year	Particulars	₹
2014-15	To Balance c/d	4,94,000	2014-15	By Employees' Compensation A/c	4,94,000
2015-16	To Balance c/d	9,59,720	2015-16	By Balance b/d	4,94,000
			2016-17	By Employees Compensation A/c	4,65,720
		9,59,720			9,59,720
2016-17	To Balance c/d	14,76,000		By Balance b/d	9,59,720
				By Employees Compensation A/c	5,16,280
		14,76,000			14,76,000
2017-18	To General Reserve A/c (1,200 × 30)	36,000	2017-18	By Balance b/d (49,200 × 30)	14,76,000
	To Share Capital A/c (48,000 × 100)	48,00,000		By Bank A/c (48,000 × 125)	60,00,000
	To Securities Premium A/c (48,000 × 55)	26,40,000			
		74,76,000			74,76,000

Note: Securities Premium

	₹
Exercise price received per share	125
Value of service received per share	30
Consideration received per share	155
Less: Nominal value per share	(100)
Securities premium per share	55

As per Intrinsic Value Method

Year 2014-15

Intrinsic value of option per share = ₹ 149 – ₹ 125 = ₹ 24

Number of shares expected to be vested = (525 × 0.98 × 0.98 × 0.98) x 100 = 49,400

Intrinsic value = 49,400 × ₹ 24 = ₹ 11,85,600

Vesting period = 3 years

Value of option recognized as expense on 2014-15 = ₹ 11,85,600/3 = ₹ 3,95,200

Year 2015-16

Intrinsic value of option per share = ₹ 149 – ₹ 125= ₹ 24

Number of shares expected to be vested = (525 – 15) × 0.97 × 0.97) × 100 = 47,986

Intrinsic value = 47,986 × ₹ 24 = ₹ 11,51,664

Vesting period = 3 years

Number of years expired = 2 years

Cumulative value of option to recognise as expense in 2014-15 and 2015-16

= (₹ 11,51,664/3) × 2 = ₹ 7,67,776

Value of option recognized as expense in 2015-16

= ₹ 7,67,776 – ₹ 3,95,200 = ₹ 3,72,576

Year 2016-17

Intrinsic value of option per share = ₹ 149 – ₹ 125 =₹ 24

Number of shares actually vested = 492 x 100 = 49,200

Intrinsic value =49,200 × ₹ 24 = ₹ 11,80,800

Cumulative value of option to recognize as expense in 3 years = ₹11,80,800 Value of option recognized as expense in 2016-17

= ₹ 11,80,800 – ₹ 7,67,776 = ₹ 4,13,024

Year 2017-18

Intrinsic value of option per share = ₹ 149 – ₹ 125 = ₹ 24

Number of shares not subscribed = (492 – 480) x 100 =1,200

Value of option forfeited = 1,200 x 24 = ₹ 28,800

Dr. **Employees' Compensation Account** **Cr.**

Year	Particulars	₹	Year	Particulars	₹
2014-15	To ESOP Outstanding A/c	3,95,200	2014-15	By Profit & Loss A/c	3,95,200
2015-16	To ESOP Outstanding A/c	3,72,576	2015-16	By Profit & Loss A/c	3,72,576
2016-17	To ESOP Outstanding A/c	4,13,024	2016-17	By Profit & Loss A/c	4,13,024

Dr. **ESOP Outstanding Account** **Cr.**

Year	Particulars	₹	Year	Particulars	₹
2014-15	To Balance c/d	3,95,200	2014-15	By Employees' Compensation A/c	3,95,200
2015-16	To Balance c/d	7,67,776	2015-16	By Balance b/d	3,95,200
				By Employees' Compensation A/c	3,72,576
		7,67,776			7,67,776
2016-17	To Balance c/d	11,80,800	2016-17	By Balance b/d	7,67,776
				By Employees Compensation A/c	4,13,024
		11,80,800			11,80,800
2017-18	To General Reserve A/c (1,200 × 24)	28,800	2017-18	By Balance b/d(49,200x24)	11,80,800
	To Share Capital A/c (48,000x100)	48,00,000		By Bank A/c (48,000x125)	60,00,000
	To Securities Premium A/c (48,000x49)	23,52,000			
		71,80,800			71,80,800

Note: Computation of Securities Premium per share

	₹
Exercise price received per share	125
Value of service received per share	24
Consideration received per share	149
Less: Nominal value per share	(100)
Securities premium per share	49

Illustration 3:

X Ltd. granted 500 stock options to its employees on 01.04.2013 at ₹ 50 per share. The vesting period is 2 ½ years and the maximum exercise period is one year. Market price on that date is ₹ 140 per share. All the options were exercised on 30.06.2016. Pass journal entries giving suitable narrations, if the face value of equity share is ₹ 10 per share. Also show the impact of the above items in the Balance Sheet for the year Mar. 31, 2014 to 2016.

Solution:

X Ltd.

Journal

Date	Particulars		₹	₹
31.3.14	Employees Stock Option Expenses A/c	Dr.	18,000	
	To Employees Stock Option Outstanding A/c			18,000
	(Being expenses on 500 stock options recognised)			
31.3.14	P/L A/c	Dr.	18,000	
	To Employees Stock Option Expenses A/c			18,000
	(Being Employees Stock Options expenses transferred)			
31.3.15	Employees Stock Option Expenses A/c	Dr.	18,000	
	To Employees Stock Option Outstanding A/c			18,000
	(Being expenses on 500 stock options recognised)			
31.3.15	P/L A/c	Dr.	18,000	
	To Employees Stock Option Expenses A/c			18,000
	(Being Employees Stock Options expenses transferred)			
31.3.16	Employees Stock Option Expenses A/c	Dr.	9,000	
	To Employees Stock Option Outstanding A/c			9,000
	(Being expenses on 500 stock options recognised)			
31.3.16	P/L A/c	Dr.	9,000	
	To Employees Stock Option Expenses A/c			9,000
	(Being Employees Stock Options expenses transferred)			
30.6.16	Bank A/c [500 × ₹ 50]	Dr.	25,000	
	To Employees Stock Option Outstanding A/c			25,000
	(Being money received on 500 options exercised)			
30.6.16	Employees Stock Option Outstanding A/c [500×₹ 10]	Dr.	70,000	
	To Equity Share Capital A/c			5,000
	To Securities Premium Reserve A/c [500 × ₹ 130]			65,000
	(Being Employees Stock Option Outstanding Account transferred to equity share capital and Securities Premium Reserve Account)			

Balance Sheet as at 31.03.14 (includes)

Balance Sheet as at 31.3.14 (includes)

Particulars	Note No.	₹
Reserves & Surplus	1	18,000

Notes to Accounts:	
1. Reserves & Surplus	
Employees Stock Option Outstanding	18,000

Balance Sheet as at 31.3.15 (includes)

Particulars	Note No.	₹
Reserves & Surplus	1	18,000

Notes to Accounts:	
1. Reserves & Surplus	
Employees Stock Option Outstanding	36,000

Balance Sheet as at 31.3.16 (includes)

Particulars	Note No.	₹
Reserves & Surplus	1	18,000

Notes to Accounts:	
1. Reserves & Surplus	
Employees Stock Option Outstanding	36,000

Workings:

Calculation of intrinsic value of option = Market price per share – Exercisable price per share = 140 – 50 = ₹ 90

Employee Compensation Expenses to be recognised:

	13-14 (₹)	**14-15 (₹)**	**15-16 (₹)**
Gross Value of employee compensation expenses	18,000	36,000	45,000
$GV = \text{No. of Options expected to vest} \times \text{Intrinsic Value} \times \frac{\text{Expired Period}}{\text{Vesting Period}}$	[500 × 90 × 1/2.5]	[500 × 90 × 2/2.5]	[500 × 90 × 2.5/2.5]
Less: Expenses already recognised upto preceding accounting period	-	18,000	36,000
∴ Expenses to be recognised	18,000	18,000	9,000

Illustration 4:

On April 1, 2014, a company Sky Blue Ltd. offered 100 shares to each of its 1,500 employees at ₹ 40 per share. The employees are given a month to decide whether or not to accept the offer. The shares issued under the plan shall be subject to lock-in on transfers for three years from grant date. The market price of shares of the company on the grant date is ₹ 50 per share. Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at ₹ 48 per share.

On April 30, 2014, 1, 200 employees accepted the offer and paid ₹ 40 per share purchased. Nominal value of each share is ₹ 10.

Record the issue of shares in book of the Sky Blue Ltd. under the aforesaid plan.

Solution:

Fair value of ESPP per share = ₹ 48 – ₹ 40 = ₹ 8; Number of share issued = 1,200 ×100 = 1,20,000; Fair value of ESPP =1,20,000 × ₹ 8= ₹ 9,60,000 Vesting period = One month; Expense recognized in 2014-15 = ₹ 9,60,000.

			₹	₹
April 30,2014	Bank A /c [1,20,000 × ₹ 40]	Dr.	48,00,000	
	Employees' Compensation ExpensesA/c [1,20,000 × 8]	Dr.	9,60,000	
	To Share Capital A/c [1,20,000 × 10]			12,00,000
	To Securities Premium A/c [1,20,000 × 38]			45,60,000

Illustration 5.

A company Amrit Ltd. announced a Stock Appreciation Right on 01/04/14 for each of its 525 employees. The scheme gives the employees the right to claim cash payment equivalent to excess on market price of company's shares on exercise date over the exercise price ₹ 125 per share in respect of 100 shares, subject to condition of continuous employment for 3 years. The SAR is exercisable after 31/03/17 but before 30/06/17. The fair value of SAR was ₹ 21 in 2014-15, ₹ 23 in 2015-16 and ₹ 24 in 2016-17. In 2014-15 the company estimates that 2% of the employees shall leave the company annually. This was revised to 3% in 2015-16. Actually, 10 employees left the company in 2014-15, 5 left in 2015-16 and 3 left in 2016-17. The SAR therefore actually vested to 482 employees. On 30/06/17, when the SAR was exercised, the intrinsic value was ₹ 25 per share.

Show Provision for SAR A/c by fair value method.

Solution:

Dr. **Provision of SARs Account** **Cr.**

Date	Particulars	₹	Date	Particulars	₹
2014-15	To Balance c/d	3,29,700	2014-15	By Employees Compensation Expenses A/c	3,29,700
		3,29,700			3,29,700
2015-16	To Balance c/d	7,06,867	2015-16	By Employee Compensation Expenses A/c	3,77,167
				By Balance b/d	3,29,700
		7,06,867			7,06,867
2016-17	To Balance c/d	11,56,800	2016-17	By Employee Compensation Expenses A/c	4,49,933
				By Balance b/d	7,06,867
		11,56,800			11,56,800
2017-18	To Bank(48,200×25)	12,05,000	2017-18	By Employee Expenses A/c	48,200
				By Balance b/d	11,56,800
		12,05,000			12,05,000

The Provision for SAR is a liability as settlement of SAR is through cash payment equivalent to an excess of market price of company's shares on exercise date over the exercise price.

Working Notes:

Year 2014-15

Number of employees to whom SARs were announced (482+10+5+3) = 500 employees.

Total number of employees after three years, on the basis of the estimation in 2014-15 = (500 x 0.98 x 0.98 × 0.98) =471employees.

No. of SARs expected to vest = 471employees ×100 = 47,100 SAR

Fair value of SARs = 47,100SARs × ₹ 21= ₹ 9,89,100

Vesting period = 3 years

Recognized as expense in 2014-15 = ₹ 9,89,100/3 years = ₹ 3,29,700

Year 2015-16

Total number of employees after three years, on the basis of the estimation in 2015-16 = [(500-10) × 0.97 × 0.97) = 461employees

No. of SARs expected to vest = 461employees ×100 = 46,100 SARs

Fair value of SARs =46,100 SARs × ₹ 23 = ₹ 10,60,300

Vesting period = 3 years

No. of years expired = 2 years

Cumulative value of SARs to be recognized as expense =10,60,300/3 × 2 = ₹ 7,06,867

SARs recognize as expense in 2015-16 = ₹ 7,06,867- ₹ 3,29,700 = ₹ 3,77,167

Year 2016-17

Fair value of SARs = ₹ 24

SARs actually vested = 482 employees x 100 = 48,200 SARs

Fair value = 48,200 SARs × ₹ 24 = ₹ 11,56,800

Cumulative value to be recognized = ₹ 11,56,800

Value of SARs to be recognized as an expense = ₹ 11,56,800 – ₹ 7,06,867 = ₹ 4,49,933

Year 2017-18

Cash payment of SARs = 48,200 SARs ×₹ 25 = ₹ 12,05,000

Value of SARs to be recognized as an expense in 2017-18 = ₹12,05,000 – ₹ 11,56,800 = ₹ 48,200

Illustration 6:

Diamond Ltd. grants 50 stock options to each of its 1,000 employees on 01.04.2011 for ₹20, depending upon the employees at the time of vesting options. The market price of the share is ₹ 50. These options will vest at the end of year 1, if the earning of Diamond Ltd. is 16% or it will vest at the end of the year 2, if the average earning of two years is 13%, or lastly it will vest at the end of the third year, if the average earning of 3 years will be 10%. 2,500 unvested options lapsed on 31.03.2016. 2,000 unvested options lapsed on 31.03.2017 and finally 1,750 unvested options lapsed on 31.03.2018.

Following is earning of Diamond Ltd.:	
Year ended on	Earning
31.03.2016	14%
31.03.2017	10%
31.03.2018	7%

850 employees exercised their vested options within a year and remaining options were un-exercised at the end of the contractual life. Pass journal entries with proper narrations for the above transactions.

Solution:

Journal

Date	Particulars	₹	₹
31.03.2016	Employees compensation expenses A/c Dr.	7,12,500	
	To ESOS outstanding A/c		7,12,500
	(Being compensation expense recognized in respect of the ESOP i.e. 50 options each granted to 1,000 employees at a discount of ₹ 30 each, amortized on straight line basis over the vesting years)		
31.03.2016	Profit and Loss A/c Dr.	7,12,500	
	To Employee compensation expenses A/c		7,12,500
	(Being compensation expense charged to Profit and Loss A/c.)		

			Dr.	Cr.
31.03.2017	Employees compensation expenses A/c	Dr.	1,97,500	
	To ESOS outstanding A/c			1,97,500
	(Being compensation expense recognized in respect of the ESOP)			
31.03.2017	Profit and Loss A/c	Dr.	1,97,500	
	To Employee compensation expenses A/c			1,97,500
	(Being compensation expense charged to Profit and Loss A/c.)			
31.03.2018	Employees compensation expenses A/c	Dr.	4,02,500	
	To ESOS outstanding A/c			4,02,500
	(Being compensation expense recognized inrespect of the ESOP)			
31.03.2018	Bank A/c (850 x 50 x 20)	Dr.	8,50,000	
	ESOS outstanding A/c [(13,12,500/43,750) x 42,500]		12,75,000	
	To Equity Share Capital (42,500 × 10)			4,25,000
	To Securities Premium A/c (42,500 × 40)			17,00,000
	(Being 42,500 options exercised at an exerciseprice of ₹ 50 each)			
31.03.2018	Profit and Loss A/c	Dr.	4,02,500	
	To Employee compensation expenses A/c			4,02,500
	(Being compensation expense charged to Profit and Loss A/c)			
31.03.2018	ESOS outstanding A/c	Dr.	37,500	
	To General Reserve A/c			37,500
	(Being ESOS outstanding A/p on lapse of 1,250 options at the end of exercise of option period transferred to General Reserve A/c)			

Working Note:

Statement showing compensation expenses to be recognized

Particulars	**Year 1 (31.03.2016)**	**Year 2 (31.03.2017)**	**Year3 (31.03.2018)**
Expected vesting period(at the end of the year)	2nd Year	3rd Year	3rd Year
Number of options expected to vest	47,500 Options	45,500 Options	43,750 Options
Total Compensation expenses accrued @30 (i.e. 50 - 20)	14,25,000	13,65,000	13,12,500
Compensation Expenses of the year	7,12,500 [14,25,000 × $^{1}/_{2}$]	9,10,000 [13,65,000×2/ 3]	13,12,500
Less: Compensation Expenses recognized previously	Nil	7,12,500	9,10,000
Compensation expenses to be recognized for the year	7,12,500	1,97,500	4,02,500

Illustration 7.

INDIKAN Ltd. announced a 'Share Based Payment Plan' for its employees, who have completed 3 years of continuous service on 1st April, 2015. The plan is subject to a 3 - year vesting period. The following relevant information is provided to year in this regard:

(i) The eligible employees can either have the option to claim the difference between the exercise price of ₹150 per share and the market price in respect of the share on vesting date in respect of 4,000 shares or such employees are entitled to subscribe to 5,000 shares at the exercise price,

(ii) Any shares subscribed to, by the employees shall carry a 3-year lock-in restriction. All shares carry face value of ₹ 10.

(iii) The current Fair value of the shares at (ii) above is ₹70 and that in respect of freely tradable shares is higher by 25%.

(iv) The Fair value of the shares not subjected to Lock-in restriction at the end of each year increases by a given % from its preceding value as under:

	2015-16	2016-17	2017-18
% of Increase	4	10	14

You are required to draw up the following Accounts under both- options:

(1) Employees' Compensation Expense Account;

(2) Provision for Liability Component Account;

(3) ESOP Outstanding Account.

Solution:

Employees' Compensation Expense Account

Dr. **Cr.**

Year	Particulars	₹	Particulars	₹
2015-16	To Provision for Liability A/c	1,21,333	By P&LA/c	1,21,333
2016-17	To Provision for Liability A/c	1,45,600	By P&LA/c	1,45,600
2017-18	To Provision for Liability A/c	1,89,507	By P&LA/c	1,89,507

Provision for Liability Component Account

Dr. **Cr.**

Year	Particulars	₹	Year	Particulars	₹
2015-16	To balance c/d	1,21,333	2015-16	By Employee Compensation A/c	1,21,333
2016-17	To balance c/d	2,66,933	2016-17	By Balance b/d	1,21,333
				By Employee Compensation A/c	1,45,600
		2,66,933			2,66,933
2017-18	To balance c/d	4,56,440	2017-18	By. Balance b/d	2,66,933
				By Employee Compensation A/c	1,89,507
		4,56,440			4,56,440

Working Notes:

1. Statement of Equity Component and Debt Component in Option

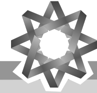
Particulars	₹
Fair Value under Equity Settlement (5,000 × ₹ 70)	3,50,000
Less: Fair Value under cash settlement [4,000 x ₹ 87.50 (₹ 70 + 25% of ₹ 70)] [Liability Component]	3,50,000
Equity component	Nil
Vesting Period	3 Years

2. Statement of expenses to be recognized each year

Particulars	15-16	16-17	17-18
Number of options expected to vest (a)	4,000	4,000	4,000
Fair value estimates per shares at year end (b)	₹ 91	₹ 100.10	₹ 114.11
Total Fair Value of Liability Component (c = a × b)	₹ 3,64,000	₹ 4,00,400	₹ 4,56,440
Total Cumulative Cost of Options	₹ 1,21,333 [(c) ×1/3]	₹ 2,66,933 [(c) × 2/3]	₹ 4,56,440 [(c) × 3/3]
Less: Cumulative Fair value already recognized expenses	-	₹ 1,21,333	₹ 2,66,933
Expenses to be recognized for the period	₹ 1,21,333	₹ 1,45,600	₹ 1,89,507

Study Note - 7

REPORTING THROUGH XBRL (EXTENDED BUSINESS REPORTING LANGUAGE)



This Study Note includes

7.1 Concept of XBRL
7.2 Meaning of XBRL
7.3 Definition of XBRL
7.4 Important XBRL Related Concepts
7.5 Myths Regarding XBRL
7.6 Features of XBRL Reporting
7.7 Benefits of XBRL Reporting
7.8 Users of XBRL
7.9 XBRL International
7.10 XBRL in India

7.1 CONCEPT OF XBRL

XBRL stands for 'e**X**tensible **B**usiness **R**eporting **L**anguage'. XBRL is the open international standard for digital business reporting. It is one of a family of "XML" languages which is becoming a standard means of communicating information between businesses and on the internet.

The basic idea behind XBRL is that instead of treating financial information as a block of text or numeric items, a unique electronically readable tag is attached to each individual financial term. It is not just the data or text that floats around, these individual items move along with an electronic tag. Thus, it is not just the 'content' but also the 'context' is being transmitted XBRL is the international standard for digital reporting of financial, performance, risk and compliance information, although it is also used for many other types of reporting. It offers major benefits to all those who have to create, transmit, use or analyse such business information.

It has been developed and refined over more than a decade ago and supports almost every kind of conceivable reporting. Moreover, it also provides a wide range of features that enhance the quality and consistency of reports, as well as their usability. It provides benefits in the preparation, analysis and communication of business information and is fast becoming an accepted reporting language across the globe.

The change from paper, PDF and HTML based reports to XBRL ones is a little bit like the change from film photography to digital photography, or from paper maps to digital maps. The new format allows you to do all the things that used to be possible, but also opens up a range of new capabilities because the information is clearly defined, platform-independent, testable and digital. Just like digital maps, digital business reports, in XBRL format, simplify the way that people can use, share, analyse and add value to the data. Millions of XBRL documents are getting generated every year, replacing older, paper-based reports with more useful, more effective and more accurate digital versions. [Source: www.xbrl.org]

XBRL is today used for multiple purposes, some of which include:

- Accounting (individual transactions tagged with XBRL Global Ledger);
- Internal Reporting (for drafting of management reports);
- External Reporting (for drafting of financial statements, regulatory reports, corporate tax filings, statistical reports etc.)

7.2 MEANING OF XBRL

XBRL is a language for the electronic communication of business and financial data which is revolutionising the business reporting around the world. The term XBRL includes four terminologies – Extensible, Business, Reporting and Language. These terms are briefly discussed hereunder:

(a) **Extensible**: This term implies that the user can extend the application of a particular business data beyond its original intended purpose. The major advantage in it is that the extended use can be determined even by the users and not just the ones who merely prepare the business data. This is achieved by adding tags which are both human and machine readable – describing what the data is.

(b) **Business:** This platform is relevant to any type of business transaction. It is to be noted that XBRL focus is on describing the financial statements for all kinds of entities.

(c) **Reporting**: The intention behind promoting the use of XBRL is to have all companies report their financial statements in a consolidated manner using the specified formats.

(d) **Language**: XBRL is based on 'e**X**tensible **M**arkup **L**anguage' (XML). It is one of a family of "XML" languages which is becoming a standard means of communicating information between businesses and on the internet. It prescribes the manner in which the data can be "marked-up" or "tagged" to make it more meaningful to human readers as well as to computers-based system.

7.3 DEFINITION OF XBRL

As per **Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015**, Extensible Business Reporting Language" (XBRL), means a standardised language for communication in electronic form to express, report or file financial information by the companies under the Act (i.e. Companies Act, 2013).

7.4 IMPORTANT XBRL RELATED CONCEPTS

1. XML

XML stands for 'e**X**tensible **M**arkup **L**anguage'. It is a markup language for documents containing structured information. A markup language is a mechanism to identify structures in a document.

XML defines a set of rules for encoding documents in a format that is both human-readable and machine-readable. It is a textual data format with strong support (via Unicode) for different human languages.

There are hundreds and thousands of computers programming languages and one among them is XML. Also XML markup language has types of programming languages. There are nearly 200 types of XML markup languages, and XBRL happens to be one of them. XBRL is XML-based and therefore is expected to be widely available in software applications.

Hyper Text Mark-up Language (HTML) is a markup language for describing web documents. HTML is a cornerstone technology used to create web pages as well as to create user interfaces for mobile and web applications. However, this mark-up language suffered from certain limitations, they being – Limited number of Tags, forgiving Browsers, Browser developers may be tempted to add new tags that only work with their product, Cannot customize layout from client side, Product comparison to mention a few. These limitations of HTML gave birth to XML.

It was the World Wide Web Consortium (W3C) where XML group (originally known as the SGML Editorial Review Board) worked and invented XML. The work was started in 1996. On 10th February, 1998 XML version 1.0 recommendation was released.

2. TAXONOMY

Taxonomies are the reporting-area specific hierarchical dictionaries used by the XBRL community. They define the specific tags that are used for individual items of data (such as "net profit"), their attributes and their interrelationships.

As per **Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015**, taxonomy means in XBRL, an elechonic dictionary for reporting the business data as approved by the Central Govemment in respect of any documents or forms indicated in these rules.

Different taxonomies will be required for different business reporting purposes. Some national jurisdictions may need their own reporting taxonomies to reflect local accounting and other reporting regulations. Many different organisations, including regulators, specific industries or even companies, may require taxonomies or taxonomy extensions to cover their own specific business reporting needs.

Taxonomies which have been officially recognized by XBRL International are listed under '**Recognized Taxonomies**'. Some of the recognized taxonomies are:

- India Banking GAAP Taxonomy 2010
- BRAZIL GAAP Commercial and Industrial Taxonomy
- Indonesia Stock Exchange (IDX) Taxonomy 2014
- Japan EDINET Taxonomy 2010
- Canadian Financial Reporting According to Canadian GAAP
- General Purpose Financial Reporting for Profit-Oriented Entities Chilean Laws
- Taxonomie Comptes Annuels (TCA) (France)
- US Governance, Risk and Compliance (GRC) Open Compliance and Ethics Group (OCEG) Taxonomy
- Tata Index for Sustainable Human Development Taxonomy
- MIX Microfinance Taxonomy
- RSC – CCI Scoreboard for Corporate Social Responsibility Taxonomy 2010

7.5 MYTHS REGARDING XBRL

This section clarifies certain myths regarding XBRL. In other words, it is discussed what XBRL is not:

(a) **XBRL is not a set of Accounting Standards**: It needs to be clearly understood that XBRL does not represent a set of accounting standards, which remain the prerogative of the regulatory standards bodies. XBRL is merely a platform on which reporting standards content will reside and be represented.

(b) **XBRL is not a chart of accounts:** It is not a detailed universal chart of accounts. Formulation of a company's chart of accounts is an exercise conducted by its management with regard to its specific business intricacies. XBRL can facilitate the implementation of such structures through its ability to transport data between disparate software applications that might be used within an organizations operational structures.

(c) **XBRL is not a GAAP translator:** It does not provide a mechanism for facilitating a drilldown of existing GAAP information into lower levels of information that would be necessary for translating financial statements from one GAAP to another. The business-reporting document contains the same GAAP information, be it in an XBRL format or an MS word or PDF format.

(d) **XBRL is not a proprietary technology**: XBRL is freely licensed and available to the public.

(e) **XBRL is not a Transaction Protocol**: XBRL deals with business reporting information, not with data capture at the transaction level. It is designated to address issues related to generation and usage of information contained within business reports and begin at the accounting classification level.

7.6 FEATURES OF XBRL REPORING

1. **Clear Definitions**

   XBRL allows the creation of reusable, authoritative definitions, called taxonomies, which capture the meaning contained in all of the reporting terms used in a business report, as well as the relationships between all of the terms. Taxonomies are developed by regulators, accounting standards setters, government agencies and other groups that need to clearly define information that needs to be reported upon. XBRL doesn't limit what kind of information is defined: it's a language that can be used and extended as needed.

2. **Testable Business Rules**

   XBRL allows the creation of business rules that constrain what can be reported. Business rules can be logical or mathematical, or both. These business rules can be used to:

   - Prevent poor quality information being sent to a regulator or third party, by being run by the preparer while the report is in draft stage.
   - Prevent poor quality information being accepted by a regulator or third party, by being run at the point that the information is being received. Business reports that fail critical rules can be sent back to the preparer for review and resubmission.
   - Identifying or highlighting questionable information, allowing prompt follow up, correction or explanation.
   - Creation of ratios, aggregations and other kinds of value-added information, based on the fundamental data provided.

3. **Multi-lingual Support**

   XBRL allows concept definitions to be prepared in as many languages as necessary. Translations of definitions can also be added by third parties. This means that it's possible to display a range of reports in a different language to the one that they were prepared in, without any additional work. The XBRL community makes extensive use of this capability as it can automatically open up reports to different communities.

4. **Strong Software Support**

   XBRL is supported by a very wide range of software from vendors large and small, allowing a very wide range of stakeholders to work with the standard.

7.7 BENEFITS OF XBRL REPORING

The benefits of reporting under XBRL over traditional form are:

1. **Automated Data Processing**: The use of XBRL offers major benefits to the preparers and users of business and financial information by enabling this data to be exchanged and processed automatically by the software. XBRL identification tags reduce and eliminate the need for the data entry operator to manually key data into the software.
2. **More accurate and efficient**: XBRL makes reporting more accurate and more efficient by using comprehensive definitions and accurate data tags. Such data tags allow the preparation, validation, publication, exchange, consumption and analysis of business information of all kinds.
3. **Data Review:** Organisations can use software to automatically validate data electronically received through XBRL. The software can help analyse the data and identify problems that accountants and auditors can examine.
4. **Improved reporting quality:** XBRL provides its users with increased data integrity and uniformity. It also allows for increased transparency of public owned companies' financial records for view by 'interested' parties.

5. **Interchangeable**: Information in reports prepared using the XBRL standard is interchangeable between different information systems in entirely different organisations. This allows for the exchange of business information across a reporting chain. The users who intend to report information, share information, publish information and allow straight through information processing rely on XBRL.

6. **Cost and time savings:** Currently all companies file their reports with regulators using formats like the Portable Document Format (PDF) which has its inherent limitations. Moreover, the costs of sending, receiving, storing, validating and auditing the financial records in this format are comparatively higher. XBRL reduces the involved time and also the cost.

7. **Tagging of transactions**: In addition to allowing the exchange of various business reports, XBRL has the capability to allow the **tagging of transactions** that can themselves be aggregated into XBRL reports. These transactional capabilities allow system-independent exchange and analysis of significant quantities of supporting data. XBRL allows unique tags to be associated with reported facts, which leads to the following advantages:

   - publishing of reports with the confidence that the information contained in them can be consumed and analysed accurately;
   - testing of the reports against a set of business and logical rules, in order to capture and avoid mistakes at their source;
   - using the information in the way that best suits the users' needs, including by using different languages, alternative currencies and in their preferred style
   - providing confidence to the users that the data provided to them conforms to a set of sophisticated pre-defined definitions.

7.8 USERS OF XBRL

XBRL is the international standard for digital reporting. It offers benefits to all those who have to create, transmit, use or analyse such information. XBRL is used in many different ways, for many different purposes. The significant users of XBRL include:

1. **Companies:** Companies are required to provide relevant information to various stakeholders, and to accurately move information amongst them.

2. **Not-for-profit Organisations**: Several not-for-profit organisations, like universities, municipalities etc. opt for reporting under XBRL format.

3. **Accountants:** Accountants use XBRL in support of clients reporting requirements and are required to prepare and present financial statements using XBRL.

4. **Analysts:** Analysts that need to understand relative risk and performance.

5. **Investors:** Investors that need to compare potential investments and understand the underlying performance of existing investments.

6. **Regulatory Authorities:** The different regulatory authorities that use XBRL include:

   - **Financial regulators** that need significant amounts of complex performance and risk information about the institutions that they regulate.
   - **Securities regulators and stock exchanges** that need to analyse the performance and compliance of listed companies and securities, and need to ensure that this information is available to markets to consume and analyse.
   - **Business registrars** that need to receive and make publicly available a range of corporate data about private and public companies, including annual financial statements.

7. **Government agencies:** Government agencies that are in the process of simplifying the process of businesses reporting, reducing red tape (either by harmonising data definitions or consolidating reporting obligations, or both), or improving government reporting by standardising the way that consolidated or transactional reports are prepared.
8. **Tax authorities:** The tax authorities need financial statements and other compliance information from companies in order to process and review their corporate tax affairs.
9. **Statistical and monetary policy authorities:** These authorities that need financial performance information from many different organisations.
10. **Specialist Data Providers:** Specialist data providers that use published information for the purpose of creating comparisons, ratings and other value-added information products for various market participants.

7.9 XBRL INTERNATIONAL

XBRL is managed by ***XBRL International Inc.(XII)***. XBRL International is a global not-for-profit consortium of approximately 600 companies and agencies worldwide working together to build the XBRL language, and promote and support its adoption. It is comprised of jurisdictions which represent countries, regions or international bodies and which focus on the progress of XBRL in their area. The number of established jurisdictions has grown from 7 to 22 over the years. Around 5 jurisdictions, including India are presently in the provisional stage.

It operates mainly through the *XBRL Steering Committee* and has over the years produced a variety of specifications and taxonomies for digitizing financial information in accordance with the accounting rules and other regulations prevailing in different countries. The consortium members meet periodically in international conferences and conduct committee work regularly throughout the week.

This collaborative effort began in 1998 and has produced a variety of specifications and taxonomies to support the goal of providing a standard, XML-based language for digitizing business reports in accordance with the rules of accounting in each country or with other reporting regimes such as banking regulation or performance benchmarking

Presently, XBRL is used around the world, in more than 60 countries.

7.10 XBRL IN INDIA

The XBRL global initiative is led by a non-profit organisation called XBRL International Inc. (XII), which has members from various agencies from more than 164 countries. In India, the Ministry of Corporate Affairs (MCA) has switched over its reporting format to XBRL for Annual Report and Cost Audit report filings. The Reserve Bank of India (RBI) has also moved to XBRL reporting for the Banking Industry while the Securities & Exchange Board of India (SEBI) has mandated reporting by Mutual Funds though XBRL mode. The responsibilities of forming a XBRL national jurisdiction and the implementation of the standards for financial reporting in India have been entrusted to the Institute of Chartered Accountants of India (ICAI).

XBRL India

XBRL India is the Indian Jurisdiction of XBRL International. Its main objective is to promote and encourage the adoption of XBRL in India as the standard for electronic business reporting in India. XBRL India is working closely with regulators, stock exchanges and software companies for promotion of XBRL as a Standard Business Reporting Language. XBRL India is developing taxonomies for specific industries in consultation with the respective regulators viz. Insurance, Power and NBFCs.

Adoption of XBRL in India

XBRL adoption is widespread in India, with the Ministry of Corporate Affairs (annual report and cost audit report filings), the Reserve Bank of India and the Securities and Exchange Board (mutual funds) also having XBRL reporting mandates. The implementation and regulatory framework of XBRL in India is governed by these regulatory agencies.

[A] Adoption of XBRL by Ministry of Corporate Affairs (MCA)

The Ministry of Corporate Affairs (MCA) mandated submission of XBRL in 2011. It is a known fact that introducing new systems requires some time for the market to adapt and settle and it is more challenging when the systems itself undergo significant change before it has been well accepted. The journey of XBRL adoption by MCA brings across the experiences – initial startup, significant change and then stability.

Before the issuance of Companies Act, 2013

In India, the Ministry of Corporate Affairs (MCA) for the first time made it mandatory for certain class of companies to file their Balance Sheets and Profit and Loss Account for the year 2010-11 onwards by using XBRL taxonomy by issuing Circular No. 16/2012 dated 6.7.2012. As per the **Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2011**, the following classes of companies were required to file the Financial Statements in XBRL Form only from the year 2010-2011:

(i) All companies listed in India and their subsidiaries;

(ii) All companies having a paid up capital of ₹ 5 crore (₹ 50 million) and above; or

(iii) All companies having turnover of ₹ 100 crore (₹ 1 billion) or above, excluding power and banking companies, insurance companies, Non-Banking Financial Companies and overseas subsidiaries of these companies.

The circular also contained, by way of an annexure, a host of valuable information about XBRL in the form of Frequently Asked Questions (FAQs) about XBRL. As per the said circular, taxonomies for Indian companies are developed based on the requirements of Schedule VI of Companies Act, Accounting Standards, SEBI Listing requirements, etc. Taxonomies for manufacturing and service sector (referred as Commercial and Industrial, or C&I) and banking sector, is acknowledged by XBRL International. The Institute of Chartered Accountants of India (ICAI), the standards setting body developed taxonomy for Commercial and Industrial companies as per the provisions of Revised Schedule VI to the Companies Act, 1956. It has been developed as per the IFRS architecture 2011.

After the issuance of Companies Act, 2013

In exercise of the powers conferred by sections 469(1) and 469(2) read with section 398 of the Companies Act, 2013, and in supersession of the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2011, except as respects things done or omitted to be done before such supersession, the Central Government issued the **Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015** on 09.09.2015.

Companies required to follow XBRL Reporting

The following class of companies shall file their financial statement and other documents under section 137 of the Companies Act, 2013, with the Registrar in e-form AOC-4 XBRL given in Annexure-I for the financial years commencing on or after April 1, 2014 using the XBRL taxonomy given in Annexure II, namely:

(i) all companies listed with any Stock Exchange(s) in India and their Indian subsidiaries; or

(ii) all companies having paid up capital of rupees five crore or above;

(iii) all companies having turnover of rupees hundred crore or above; or

(iv) all companies which were hitherto covered under the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2011.

Companies exempt from XBRL Reporting

As per the Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Rules, 2015 the following companies are exempt from XBRL filing of their financial statement and other documents:

(i) Banking companies

(ii) Insurance companies

(iii) Power Sector companies; and

(iv) Non-Banking Financial companies.

XBRL & Filing of Cost Audit Report

A company required to furnish cost audit report and other documents to the Central Government under Section 148(6) of the Companies Act, 2013 and rules made thereunder, shall file such report and other documents using the XBRL taxonomy given in Annexure-III to the said Rule for the financial years on or after April 1, 2014 in e-Form CRA-4 specified under the Companies (Cost Records and Audit) Rules, 2014

[B] Adoption of XBRL by Reserve Bank of India (RBI)

The Reserve Bank of India (RBI), India's central bank, oversees a host of critical activities including monetary policy, bank supervision and foreign exchange management. RBI is internationally well regarded for its regulatory acumen that played a key role in the Indian financial sector remaining virtually unscathed during the Asian Financial Crisis and the ongoing international banking and credit crisis. Reserve Bank of India is responsible for implementing the XBRL standard for banks' reporting. RBI had opted for XBRL as the reporting technology for the Basel II reporting norms so as to capture quality information that can be reused across the regulatory functions. Within RBI, XBRL implementation is being regularly monitored by a High Level Steering Committee appointed by the Governor.

[C] Adoption of XBRL by Securities and Exchange Board of India (SEBI)

Securities and Exchange Board of India (SEBI) is in the process of setting up a SEBI Unified Platform for Electronic Reporting and Dissemination (SUPER-D), which will be a XBRL technology based platform for reporting by listed companies, Mutual Funds and other SEBI registered intermediaries. The platform will also be used to disseminate requisite information relating to listed companies, mutual funds and other intermediaries, to the public. SEBI has started a XBRL Pilot Project for filing / reporting by Mutual Funds with SEBI. Under this XBRL MF Pilot Project, SEBI invited all the registered Mutual Fund/Assets Management Companies to participate on voluntary basis as filers for doing XBRL filings of the specified reports to SEBI. These XBRL filings have to be done in addition to the filings under the current system.

[D] Adoption of XBRL by Bombay Stock Exchange (BSE)

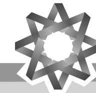
As a part of regulatory compliances, BSE collects data/disclosures in specified formats from its listed companies. With a view to making reporting more accurate and more efficient, BSE has moved towards the XBRL based reporting. BSE became the first stock exchange in India to introduce and implement XBRL based reporting in association with its partner in this endeavor, Microvista Technologies. With implementation of XBRL, BSE is in the club of international stock exchanges that have implemented XBRL based reporting. Keeping in line with continuous improvement, BSE has now made it mandatory for filing of Corporate Governance report and Shareholding Pattern in XBRL mode. Moreover, the BSE is making its taxonomies available online to promote the development of software by the private sector.

References:

- www.xbrl.org
- http://www.mca.gov.in/
- www.rbi.org
- www.bseindia.com

Study Note - 8

GOVERNMENT ACCOUNTING



This Study Note includes

8.1 Government Accounting – an Overview
8.2 General Principles of Government Accounting
8.3 Comparison between Government Accounting and Commercial Accounting
8.4 Government Accounting & Reporting
8.5 Comptroller and Auditor General of India (C&AG)
8.6 Public Accounts Committee (P.A.C)
8.7 Review of Accounts
8.8 Government Accounting Standards Advisory Board (GASAB)
8.9 Government Accounting Standards Issued by Government Accounting Standards Advisory Board (GASAB)
8.10 Indian Government Accounting Standards (IGAS)
8.11 Indian Government Financial Reporting Standards (IGFRS)

8.1 GOVERNMENT ACCOUNTING – AN OVERVIEW

Accounting is the process of recording, classifying and summarizing the financial transactions and communicating the results of its operations and also the financial position to its stake-holders.

Government accounting refers to the system of financial accounting that is applicable to government, its departments, offices and institutions. The accounting system that is put to use in government offices or institutions for the purpose of recording and reporting the financial transactions is referred to as government accounting. It is also referred to as Public Finance Accounting.

According to **Oshisami and Dean,** "Governmental Accounting is the process of recording, analyzing, classifying, summarizing, communicating, and interpreting information about government in aggregate and in detail, reflecting all transactions involving the receipts, transfer, and disposition of government funds and property." -

By the given definition, it is clear that the government account is the systematic and scientific process of recording, presenting, analyzing, summarizing, classifying and communicating the financial transaction of the government offices. It is concerned with keeping a record of government revenue and their proper utilization in different development and administration work. It presents the receipt and payment position of the public fund. It reveals how public funds have been generated and utilized for the welfare of the general public.

It is the systematic process of collecting, recording, classifying, summarizing and interpreting the financial transactions relating to the revenues and expenditures of government institutions/ offices. Thus, simply stated, government accounting is concerned with systematic and scientific recording of government revenues and expenditures.

Therefore, government accounting may be defined as an accounting system used in government institution for the purpose of recording, classifying, summarizing and communicating the financial information regarding the collection and utilization of public funds and properties. It is concerned with keeping records of government revenues and their expenditure in different development and administrative works.

FEATURES OF GOVERNMENT ACCOUNTING

Government Accounting is a unique application area which has certain characteristics of its own. Some of the main features of Government Accounting are discussed as under:

1. **Specific system of accounting:** It is a specific accounting system which is followed by government in its departments, offices and institutions.

2. **Reporting of utilisation of public funds:** The government and its institutions are public institution whose main objective is to provide services to the society and also to maintain law and order in the country. So, the accounting system used by such institutions has to reveal how public funds and properties have been used for that purpose. It is to be noted that government accounting is not done for revealing any profit and loss.

3. **Government Regulations:** Government accounting is maintained according to government rules and regulations. The financial policies, rules and regulations as determined from time to time provide the system of government accounting.

4. **Double Entry System:** Government accounting is based on the principles and assumptions of double entry system of book keeping system. Accordingly, every financial transactionentered into by a government/ government office/ institution are recorded showing their double effects. It implies that for each government financial transaction one aspect of the transaction is debited and the other aspect is credited.

5. **Budget Heads:** All the expenses of government offices are classified into different budget heads and expenditures are made only on approved budget heads.

6. **Budgetary Regulation:** Government expenditures are governed by budgetary regulations. In other words, no government office can make expenditure more than the amount allocated in the budget. Thus, in effect, government accounting gets regulated by the budget.

7. **Mode of Transaction:** All government transactions are supposed to be performed through banks.

8. **Fund-based Accounting:** Apeculiar characteristic of governmental accounting is the employment of separate funds. The government is engaged in an ever-growing number of operations and activities which are quite unrelated to each other. The particular sources of revenue or income often are dedicated to use for a particular phase of the government's operations. The accounts must segregate these specially dedicated resources and isolate them from all other transactions in a separate "fund."

9. **Auditing:** The audit the books of accounts maintained by government departments, offices or institutions are to be audited by a recognised department of the government so as to ensure proper governance and also to prevent misuse and misappropriation of public funds.

OBJECTIVES OF GOVERNMENT ACCOUNTING

The objectives of government accounting are the financial administration of the activities of the government to promote maximisation of welfare in the form of various services. The specific objectives can be stated as under:

1. To record financial transactions of revenues and expenditure relating to the government organizations.

2. To provide reliable financial data and information about the operation of public fund.

3. To record the expenditures as per the appropriate Act, Rules, and legal provisions as set by the government.

4. To avoid the excess expenditures beyond the limit of the budget approved by the government.

5. To help in the preparation of various financial statements and reports.

6. To facilitate the auditing by the concerned government department.

7. To prevent misappropriation of government properties by maintaining the systematic records of cash and store items.

8. To facilitate for estimating the annual budget by providing historical financial data of government and expenditures.

8.2 GENERAL PRINCIPLES OF GOVERMENT ACCOUNTING

The general principles of government accounting are highlighted hereunder:

1. **Classification of expenditures**: The Government Expenditures are classified under Sectors, major heads, minor heads, sub-heads and detailed heads of account. The method of budgeting and accounting under the service heads is not designed to bring out the relation in which Government stands to its material assets in use, or its liabilities due to be discharged at more or less distant dates.

2. **Based on budget**: government accounting is based on the annual budget of the government. In its budget for a year, Government is interested to forecast with the greatest possible accuracy what is expected to be received or paid during the year, and whether the former together with the balance of the past year is sufficient to cover the later.

   Similarly, in the compiled accounts for that year, it is concerned to see to what extent the forecast has been justified by the facts, and whether it has a surplus or deficit balance as a result of the year's transactions. On the basis of the budget and the accounts, Government determines:

   (a) whether it will be justified in curtailing or expanding its activities; and

   (b) whether it can and should increase or decrease taxation accordingly.

3. **End products of government accounting**: In the field of Government accounting, the end products are the monthly accounts and the annual accounts. The monthly accounts serve the needs of the day-to-day administration, while the annual accounts present a fair and correct view of the financial stewardship of the Government during the year.

4. **Period of Accounts**: The annual accounts of the central, state and union territory government shall record transactions, which take place during financial year running from 1st April to 31st March.

5. **Cash basis of accounting**: With the exception of such book adjustments as may be authorized by these rules on the advice of the Comptroller and Auditor General of India (C&AG),the transactions in government accounts shall represents the actual cash receipt and disbursement during a financial year.

6. **Form of Accounts**: The accounts of Government are kept in three parts namely, Consolidated Fund, Contingency Fund and Public Account.

8.3 COMPARISON BETWEEN GOVERNMENT ACCOUNTING AND COMMERCIAL ACCOUNTING

Although the basic principles of financial accounting that are applicable in regular commercial activities apply to the government accounts, there are certain features of governmental accounting which make it quite different from that of regular commercial accounting. The differences between commercial and government accounting have been presented hereunder:

1. **Meaning:** The accounting system applied in the government departments, offices and institutions is referred to as government accounting. While, the system of accounting applied by non-government organizations (whether profit-oriented or non-profit oriented) is known as commercial accounting.

2. **Objective:** Government accounting is maintained by the government offices for recording and reporting the utilisation and position of public funds. Commercial accounting is maintained by business organizations to know the profit or loss for an accounting period and disclose the financial position of the entity.

3. **Scope**: The government accounting happens to be more elaborate that that followed in commercial accounts.

4. **Budget:** Government accounting is directly influenced by the government budgeting system, while commercial accounting does not follow the government budgeting system.

5. **Basis:** Government accounting is prepared on cash basis. On the other hand, commercial accounting may be done on cash basis or accrual basis, or sometimes even on hybrid basis.

6. **Level of Accounting:** Government accounting has the system of central level and operating level accounting. Commercial accounting has no provision of central level and operating level accounting.
7. **Rules and Provisions:** Government accounting is strictly maintained by following the financial rules and provisions as set by the concerned government. Commercial accounting is maintained by following the applicable rules and the 'Generally Accepted Accounting Principles' (GAAP).
8. **Information:** Government accounting provides information to the government about the receipts, deposit, transfer and utilisation of public funds. Commercial accounting provides information to the various stake-holders about the operating result and financial position of the business.
9. **Auditing:** The audit the books of accounts maintained by government departments, offices or institutions are to be audited by a recognised department of the government(namely, the Auditor General Office); while the books of accounts maintained under commercial accounting is audited by any professional auditor.

8.4 GOVERMENT ACCOUNTING AND REPORTING

Controller General of Accounts (CGA) is the apex accounting body in the Government of India. It is the principal Accounts Adviser to the Government of India and is responsible for establishing and maintaining a technically sound management accounting system. The accounts of the Civil Ministries are compiled and maintained by the Pay and Accounts Offices, the basic accounting units.

The Pay and Accounts Offices maintain line item wise accounts of all the transactions involving Consolidated Fund of India, Contingency Fund of India and Public Account of India. Various subsidiary accounts such as Loan accounts, Fund accounts etc. are also maintained by these units.

The accounts compiled by the Pay and Accounts Offices are consolidated on a monthly basis in the Principal Accounts Offices at the Ministry's headquarters. The consolidated accounts of the Ministry are rendered to the Controller General of Accounts. The accounts received from various Ministries are consolidated in the office of the Controller General of Accounts to generate the accounts of the Government of India as a whole.

These monthly accounts are reviewed and a critical analysis of expenditure, revenue collection, borrowings and deficit is prepared for Finance Minister.

Role of CGA: Consolidating monthly accounts of the Government of India and reporting on the fiscal deficit is the primary responsibility of the CGA. The monthly accounts are compiled in the CGA office and a monthly review indicating flow of expenditure, revenue collection, internal and external borrowing and fiscal deficit is prepared for Minister of Finance. A summary of the monthly accounts is also placed on the web. He prepares a critical analysis of expenditures, revenues, borrowings and the deficit for the Finance Minister every month. He also prepares annual Appropriation Accounts and Union Finance Accounts for presentation to the parliament. Ministries, Departments approach the Controller General of Accounts for advice on accounting procedures for new schemes, programmes or activities undertaken by them. The advice rendered by the CGA generally covers aspects related to maintenance of accounts, collection of receipts and it's crediting into Government account, release of payment and it's accounting, creation and operation of funds within Government accounts, banking arrangements for making payments and collecting receipts etc. The advice of the Controller General of Accounts is binding on the Ministries/Departments.

Government Accounting & Information Technology: In a continuous effort towards improving the efficiency and the quality of the services rendered by the Department, Information Technology has been introduced at almost all levels of operations.

At the three levels, namely the Controller General of Accounts, Principal Accounts Offices and the field Pay and Accounts Offices software packages, namely GAINS (Government Accounting Information System), CONTACT (Controller's Accounts) and IMPROVE (Integrated Multimodule Processor for Voucher Entries), are being used to consolidate Government of India Accounts.

The monthly accounts are now published on the Web on the last day of the month following the month of account (i.e. the accounts for Oct 2017 will be available on the last day of November 2017). Efforts are continuing to automate a number of other processes at various levels.

The Systems Group, in the office of the Controller General of Accounts, assists the Controller General of Accounts in the policy formulation and use of Information technology in the accounting offices of the Government. The software support to the organisation is provided by the National Informatics Centre under the Ministry of Planning.

Features of Government Accounting in India

One of the most distinctive features of the Government accounts in India is the minute detail with which the financial transactions are recorded in the account books. All transactions are classified on a six tier functional classification with Major Heads representing a broad function of the Government at the top and an object head representing the activity at the bottom. The intermediate levels represent sub-functions, programmes, schemes and sub-schemes. The functional classification is applicable to receipts as well as payments.

Since the Country follows a Plan based model of economy, the expenditure of Government is divided into Plan and Non-Plan. As the name suggests, the Plan expenditure is directly related to expenditure on schemes and programmes envisages in the plans. The Non-Plan expenditure is the expenditure incurred on establishment and maintenance activities.

Further distinction is made between the expenditure, which under the provisions of the Constitution, is subject to the vote of the legislature and the rest which is charged upon the Consolidated Fund of India.

Since the budget is on an annual basis, the accounts have to conform to it. The accounts are maintained on cash basis. Only the actual receipts realised and the payments made during the year are recorded.

Article of the Constitution provides for creation of a Consolidated Fund of India, Contingency Fund and Public Account.

Accounts of the Government

The Constitution of India provides for the manner in which the accounts of the Government have to be kept. The accounts of Government are kept in three parts namely, Consolidated Fund, Contingency Fund and Public Account. They are discussed as under:

1. **Consolidated Funds of India**

   The Consolidated Funds **is** constituted under Article 266 (1) of the Constitution of India. All revenues received by the Government by way of taxes like Income Tax, Central Excise, Customs and other receipts flowing to the Government in connection with the conduct of Government business i.e. Non-Tax Revenues are credited into the Consolidated Fund. Similarly, all loans raised by the Government by issue of Public notifications, treasury bills (internal debt) and loans obtained from foreign governments and international institutions (external debt) are credited into this fund. All expenditure of the government is incurred from this fund and no amount can be withdrawn from the Fund without authorization from the Parliament. This is the largest of all the three funds.

2. **Public Accounts of India**

   The Public Accounts of India is constituted under Article 266 (2) of the Constitution. The transactions to be recorded in it relate to debt other than those included in the Consolidated Fund of India. The transactions under Debt, Deposits and Advances in this part are those in respect of which Government incurs a liability to repay the money received or has a claim to recover the amounts paid. The transactions relating to 'Remittance' and 'Suspense' shall embrace all adjusting heads. The initial debits or credits to these heads will be cleared eventually by corresponding receipts or payments. The receipts under Public Account do not constitute normal receipts of Government. Parliamentary authorization for payments from the Public Account is therefore not required.

3. Contingency Funds of India

The Contingency Fund of India Fund set by the Government of India under Article 267 of the Constitution of India. It records the transactions connected with Contingency.It is held on behalf of President by the Secretary to the Government of India, Ministry of Finance, Department of Economic Affairs. The corpus of this fund is ₹ 500 crores. Advances from the fund are made for the purposes of meeting unforeseen expenditure which are resumed to the Fund to the full extent as soon as Parliament authorizes additional expenditure. Thus, this fund acts more or less like an imprest account of Government of India.

8.5 COMPTROLER AND AUDITOR GENERAL OF INDIA (C&AG)

The Comptroller and Auditor General (C&AG) of India is an authority, established by the Constitution under Constitution of India/Part V Chapter V/Sub-part 7B/Article 148, who audits all receipts and expenditure of the Government of India and the state governments, including those of bodies and authorities substantially financed by the government. The CAG is also the external auditor of Government-owned corporations and conducts supplementary audit of government companies, i.e., any non-banking/ non-insurance company in which Union Government has an equity share of at least 51 per cent or subsidiary companies of existing government companies. Comptroller and Auditor General (C&AG) is the guardian or care-taker of the national purse. He is appointed by the President of India for a tenure of 6 years.

The constitution has instituted the British system of responsible government in India. The substance of responsibility is that the executive i.e. the Prime Minister and the Cabinet remains answerable for all their activities to the popularly elected chamber of the legislature. The responsibility becomes empty unless financial activities of the government are subject to parliamentary scrutiny. For this it is imperative that there should be an independent authority to examine and scrutinize the financial transactions of the government. Since he is the impartial head of the audit and accounts system of India, it is essential that he should be independent of executive control.

With this object in view, the Government of India Act of 1935, made the Auditor General of India irremovable except "in like manner and on like grounds as a judge of the Federal Court." The office of the Comptroller and Auditor General is an adaptation of the office of the Auditor General under the Act of 1935.Articles 148 to 151 of the Indian constitution create and regulate the office of Comptroller and Auditor General of India. The office of the Comptroller and Auditor General is considered as "pivotal" to the control of entire financial system of the country. Dr. B. R. Ambedkar felt that the Comptroller and Auditor General of India shall be the most important officer under the constitution of India.

ROLE, FUNCTION AND DUTIES OF THE COMPTROLLER & AUDITOR GENERAL (C&AG)

The role, function and duties of the Comptroller and Auditor General (CAG) are elaborated by the Comptroller and Auditor General's (Duties, Powers and Conditions of Service)Act, 1971 (56 of 1971).An amendment of this act in 1976 has relieved him from preparing the accounts of the government. As per Sec. 10 of the said Act, the role/ duties of the C&AG has been discussed as under:

1. **Comptroller and Auditor General to compile accounts of Union and States:** The role of the C&AG includes:

    - **Compilation of accounts**: Compiling the accounts of the Union and of each State from the initial and subsidiary accounts rendered to the audit and accounts offices under his control by treasuries, offices or departments responsible for the keeping of such accounts; and
    - **Keeping accounts**: Keeping such accounts in relation to any of the matters specified in the above clause as may be necessary.

    However, the President may, after consultation with the Comptroller and Auditor General, by order, relieve him from the responsibility for compiling:

    (i) the said accounts of the Union (either at once or gradually by the issue of several orders); or

    (ii) the accounts of any particular services or departments of the Union;

(iii) relieve him from the responsibility for keeping the accounts of any particular class or character.

Moreover, the Governor of a State with the previous approval of the President and after consultation with Comptroller and Auditor General, by order, relieve him from the responsibility for compiling:

(i) the said accounts of the State (either at once or gradually by the issue of several orders); or

(ii) the accounts of any particular services or departments of the State.

2. **Comptroller and Auditor General to prepare and submit accounts to the President Governors of States and Administrators of Union territories having Legislative Assemblies**: The Comptroller and Auditor-General shall from the accounts compiled by him or by the Government or any other person responsible in that behalf prepare in each year accounts (including, in the case of accounts compiled by him, appropriation accounts) showing under the respective heads the annual receipts and disbursements for the purpose of the Union, of each State and of each Union territory having a Legislative Assembly, and shall submit those accounts to the President or the Governor of a State or Administrator of the Union territory having a Legislative Assembly, as the case may be on or before such dates as he may, with the concurrence of the Government concerned, determine.

   However, the President may, after consultation with the Comptroller and Auditor-General, by order, relieve him from the responsibility for the preparation and submission of the accounts relating to annual receipts and disbursements for the purpose of the Union or of a Union territory having a Legislative Assembly. Further the Governor of a State may, with the previous approval of the President and after consultation with the Comptroller and Auditor-General, by order, relieve him from the responsibility for the preparation and submission of the accounts relating to annual receipts and disbursements for the purpose of the State.

3. **Comptroller and Auditor General to give information and render assistance to the Union and States**: The Comptroller and Auditor-General shall, in so far as the accounts, for the compilation or keeping of which he is responsible, enable him so to do, give to the Union government, to the State Governments or to the Governments of Union Territories having Legislative Assemblies, as the case may be, such information as they may, from time to time, require, and render such assistance in the preparation of their annual financial statements as they may reasonably ask for.

4. **General provisions relating to audit**: It shall be the duty of the Comptroller and Auditor-General:

   - to audit all expenditure from the Consolidated Fund of India and of each State and of each Union territory having a Legislative Assembly and to ascertain whether the moneys shown in the accounts as having been disbursed were legally available for and applicable to the service or purpose to which they have been applied or charged and whether the expenditure conforms to the authority which governs it;
   - to audit all transactions of the Union and of the States relating to Contingency Funds and Public Accounts;
   - to audit all trading, manufacturing, profit and loss accounts and balance-sheets and other subsidiary accounts kept in any department of the Union or of a State; and in each case to report on the expenditure, transactions or accounts so audited by him.

5. **Audit of receipts and expenditure of bodies or authorities substantially financed from Union or State Revenues**: Where anybody or authority is substantially financed by grants or loans from the Consolidated Fund of India or of any State or of any Union territory having a Legislative Assembly, the Comptroller and Auditor-General shall, subject to the provisions of any law for the time being in, force applicable to the body or authority, as the case may be, audit all receipts and expenditure of that body or authority and to report on the receipts and expenditure audited by him.

   However, Comptroller and Auditor-General may with the previous approval of the President or the Governor of a State or the Administrator of a Union territory having a Legislative Assembly, as the case may be, audit all receipts and expenditure of any body or authority where the grants or loans to such body or authority from the Consolidated Fund of India or of any State or of any Union territory having a Legislative Assembly, as the case may be in a financial year is not less than rupees one crore.

6. **Functions of Comptroller and Auditor General in the case of grants or loans given to other authorities or bodies**: Where any grant or loan is given for any specific purpose from the Consolidated Fund of India or of any State or of any Union territory having a Legislative Assembly to any authority or body, not being a foreign State or international organisation, the Comptroller and Auditor-General shall scrutinise the procedures by which the sanctioning authority satisfies itself as to the fulfillment of the conditions subject to which such grants or loans were given. For this purpose the C&AG shall have right of access, after giving reasonable previous notice, to the books and accounts of that authority or body.

   However, the President, the Governor of a State or the Administrator of a Union territory having a Legislative Assembly, as the case may be, may, where he is of opinion that it is necessary so to do in the public interest, by order, relieve the Comptroller and Auditor-General, after consultation with him, from making any such scrutiny in respect of anybody or authority receiving such grant or loan.

   Except where he is authorised so to do by the President, the Governor of a State or the Administrator of Union territory having a Legislative Assembly, as the case may be, the Comptroller and Auditor-General shall not have, while exercising the powers conferred on him by sub-section (1), right of access to the books and accounts of any corporation to which any such grant or loan as is referred to in subsection (1) is given if the law by or under which such corporation has been established provides for the audit of the accounts of such corporation by an agency other than the Comptroller and Auditor-General:

   Moreover, such authorisation shall be made except after consultation with the Comptroller and Auditor-General and except after giving the concerned corporation a reasonable opportunity of making representations with regard to the proposal to give to the Comptroller and Auditor-General right of access to its books and accounts.

7. **Audit of receipts of Union or of States**: It shall be the duty of the Comptroller and Auditor-General to audit all receipts which are payable into the Consolidated Fund of India and of each State and of each Union territory having a Legislative Assembly and to satisfy himself that the rules and procedures in that behalf are designed to secure an effective check on the assessment, collection and proper allocation of revenue and are being duly observed and to make for this purpose such examination of the accounts as he thinks fit and report thereon.

8. **Audit of accounts of stores and stock**: The Comptroller and Auditor-General shall have authority to audit and report on the accounts of stores and stock kept in any office or department of the Union or of a State.

9. **Powers of Comptroller and Auditor General in connection with audit ofaccounts**: The Comptroller and Auditor General shall in connection with the performance of his duties under this Act, have authority:

   - to inspect any office of accounts under the control of the union or of a State, including treasuries, and such offices responsible for the keeping of initial or subsidiary accounts, as submit accounts to him;
   - to require that any accounts, books, papers and other documents which deal with or form the basis of or an otherwise relevant to the transactions to which his duties in respect of audit extend, shall be sent to such place as he may appoint for his inspection;
   - to put such questions or make such observations as he may consider necessary, to the person in charge of the office and to call for such information as he may require for the preparation of any account or report which it is his duty to prepare.

   The person in charge of any office or department, the accounts of which have to be inspected and audited by the Comptroller and Auditor-General, shall afford all facilities for such inspection and comply with requests for information in as complete a form as possible and with all reasonable expedition.

10. **Audit of Government companies and corporations**: The duties and powers of the Comptroller and Auditor-General in relation to the audit of the accounts of Government companies shall be performed and exercised by him in accordance with the provisions of the Companies Act, 1956 (1 of 1956).

    The duties and powers of the Comptroller and Auditor-General in relation to the audit of the accounts of corporations (not being companies) established by or under law made by Parliament shall be performed and exercised by him in accordance with the provisions of the respective legislations.

The Governor of a State or the Administrator of a Union territory having a Legislative Assembly may, where he is of opinion that it is necessary in the public interest so to do, request the Comptroller and Auditor-General to audit the accounts of a corporation established by law made by the Legislature of the State or of the Union territory, as the case may be, and where such request has been made, the Comptroller and Auditor-General shall audit the accounts of such corporation and shall have, for the purposes of such audit, right of access to the books and accounts of such corporation. However, no such request shall be made except after consultation with the Comptroller, and Auditor-General and except after giving reasonable opportunity to the corporation to make representations with regard to the proposal for such audit.

11. **Laying of reports in relation to accounts of Government companies and corporations:** The reports of the Comptroller and Auditor-General, in relation to audit of accounts of a Government company or a corporation referred to in section 19, shall be submitted to the Government or Governments concerned. The Central Government shall cause every report received by it under sub-section (1) to be laid, as soon as may be after it is received, before each House of Parliament. The State Government shall cause every report received by it under sub-section (1) to be laid, as soon as may be after it is received, before the Legislature of the State.

12. **Audit of accounts of certain authorities or bodies**: Where the audit of the accounts of anybody or authority has not been entrusted to the Comptroller and Auditor-General by or under any law made by Parliament, he shall, if requested so to do by the President, or the Governor of a State or the Administrator of a Union territory having a Legislative Assembly, as the case may be, undertake the audit of the accounts of such body or authority on such terms and conditions as may be agreed upon between him and the concerned Government and shall have, for the purposes of such audit, right of access to the books and accounts of that body or authority. However, no such request shall be made except after consultation with the Comptroller and Auditor-General.

8.6 PUBLIC ACCOUNTS COMMITTEE (P.A.C)

The Public Accounts Committee (P.A.C.) is a committee of selected members of Parliament, constituted by the Parliament of India.

In the Indian parliamentary form of governance, the legislature has the power to ensure "that the appropriated money is spent economically, judiciously and for the purpose for which it was sanctioned". Even though the Comptroller and Auditor General of India (C&AG) is to audit the accounts of the government and to ensure the propriety of the money spent, yet its report is further examined by the special committee of the parliament, is known as Public Account Committee.

The Committee entrusted with the responsibility of examining the accounts of the Government. The Government expenditures are thoroughly examined and ensured that the Parliamentary limits are not breached. It examines the report of Accounts of the union government submitted by the Comptroller and Auditor General of India (C&AG), to the President for the purpose of auditing of the revenue and the expenditure of the Government of India. The Public Accounts Committee in India thus ensures Parliamentary control over government expenditure.

The Public Accounts Committee was first set up in India in 1921 under the Montague Chelmsford Reforms. The basic function of the committee had been to ensure that the expenditure had been incurred for the intended purposes as authorised by the authority concerned. Presently, it is formed every year with a strength of not more than 22 members, out of which 15 members are from Lok Sabha (the lower house of the Parliament), and 7 members are from Rajya Sabha (the upper house of the Parliament). The term of office of the members is one year.

Constitution of Public Accounts Committee (P.A.C)

The Committee consists of not more than 22 members comprising15 members elected by Lok Sabha every year from amongst its members according to the principle of proportional representation by means of single transferable vote, and not more than 7 members of Raj ya Sabha elected by that House in like manner are associated with the Committee. Thus, the present P.A.C is a joint committee of the two Houses.

The Chairman is appointed by the Speaker of Lok Sabha from amongst its members of Lok Sabha. Since 1967, the chairman of the committee is selected from the opposition. Earlier, it was headed by a member of the ruling party.

However, it is to be noted that, a Minister is not eligible to be elected as a member of the Committee. If a member after his election to the Committee is appointed a Minister, he ceases to be a member of the Committee from the date of such appointment.

Role of Public Accounts Committee (P.A.C)

1. **Role regarding examination of the C&AG report:** The chief function of P.A.C. is to examine the audit report of Comptroller and Auditor General (C&AG) after it is laid in the Parliament. C&AG assists the Committee during the course of investigation.

2. **Role regarding unauthorized expenditures or excess expenditures**: In examining the report of the Comptroller and Auditor General of India (C&AG), the committee has to satisfy itself that:

   - the expenditures made by the government, were authorized by the Parliament; and

   - the expenditures under any head has not crossed the limits of parliamentary authorization.

   It is to be noted that, every expenditure made by the government must be sanctioned by the Parliament. Thus, it is the role of the committee to bring to the notice of the Parliament instances of unauthorized expenditures or expenditures beyond sanctioned limits.

3. **Role regarding spending of money by ministries**: The committee not only ensures that ministries spend money in accordance with parliamentary grants, it also brings to the notice of the Parliament instances of extravagance, loss, in fructuous expenditure and lack of financial integrity in public services. However, the committee cannot question the polices of the government. It only concerns itself with the execution of policy on its financial aspects.

4. **Scrutinizing the audit reports of public corporations:** A new dimension has been added to the function of the P.A.C. by entrusting it with the responsibility of scrutinizing the audit report of public corporations.

5. **Scrutinising the working process of ministries and public corporations**: In examining the accounts and audits of the ministries and public corporations, the Committee gets the opportunity to scrutinize the process of their working. It points out the weakness and shortcomings of the administration of ministries and public corporations Criticisms of the P.A.C. draw national attention. This keeps the ministries and public corporations sensitive to the criticisms of the P.A.C. Thus, it is wrong to suppose that the P.A.C. is only an instrument of financial control, it is as well an instrument of administrative control.

8.7 REVIEW OF ACCOUNTS

The accounts of Government Companies set up under the provisions of the Companies Act (including Government Insurance Companies and deemed Government Companies) are audited by the Comptroller and Auditor General of India (C&AG) under the provisions of Section 143 of the Companies Act, 2013. Under these provisions, the C&AG:

(i) shall appoint statutory auditor of a Government company,

(ii) may conduct supplementary or test audit of accounts of a Government Company, and

(iii) may comment upon the report of the statutory auditor. In addition he issues directions to the statutory auditors regarding the manner in which the accounts of a Government Company are to be audited.

The accounts certified by the Statutory Auditors (Chartered Accountants) appointed by the Central Government on the advice of the CAG under the Companies Act, 2013 are subjected to supplementary or test audit by officers of the CAG and CAG gives his comments or supplements the report of the Statutory Auditors. The Companies Act, 2013 empowers the CAG to issue directions to the Statutory Auditors on the manner in which the Company's accounts shall be audited.

8.8 GOVERMENT ACCOUNTING STANDARDS ADVISORY BOARD (GASAB)

The accounting systems, the world over, are being revisited with an emphasis on transition from rule to principle based standards and migration from cash to accrual based system of accounting. The GASAB, as a nodal advisory body in India, is taking similar action to formulate and improve standards of government accounting and financial reporting and enhance accountability mechanisms.

The Government Accounting Standards Advisory Board (GASAB) was constituted by the Comptroller and Auditor General of India (C&AG) with the support of Government of India through a notification dated August 12, 2002. This Board was constituted to establish and improve the standards of governmental accounting and financial reporting, and enhance the accountability mechanisms. The decision to set-up GASAB was taken in the backdrop of the new priorities emerging in the Public Finance Management and to keep pace with International trends. The new priorities focus on good governance, fiscal prudence, efficiency & transparency in public spending.

Structure of GASAB

The Board has high level representation from the important accounting heads in Government, Ministry of Finance, Department of Post, Finance Secretaries of states, RBI and heads of premier accounting & research organizations. The board consists of the following members:

1. Deputy Comptroller and Auditor General (Government Accounts) as Chairperson
2. Financial Commissioner, Railways
3. Member (Finance) Telecom Commission, Department of Telecom
4. Secretary, Department of Post
5. Controller General of Defence Accounts
6. Controller General of Accounts
7. Additional / Joint Secretary (Budget), Ministry of Finance, Government of India
8. Deputy Governor, Reserve Bank of India, or his nominee

9-12. Principal Secretary (Finance) of four States, by rotation

13. Director General, National Council of Applied Economic Research(NCAER), New Delhi
14. President, Institute of Chartered Accountants of India (ICAI), or his nominee
15. President, Institute of Cost and Works Accountants of India, or his nominee
16. Principal Director in GASAB, as Member secretary.

Responsibilities of GASAB

GASAB, inter alia, has the following responsibilities:

1. To formulate and improve standard of Government accounting and financial reporting in order to enhance accountability mechanisms.
2. To formulate and propose standards that improve the usefulness of financial reports based on the needs of the users.
3. To keep the standards current and reflect change in the Governmental environment.
4. To provide guidance on implementation of standards.
5. To consider significant areas of accounting and financial reporting that can be improved through the standard setting process.
6. To improve the common understanding of the nature and purpose of information contained in the financial reports.

8.9 GOVERMENT ACCOUNTING STANDARDS ISSUED BY GOVERNMENT ACCOUNTING STANDARD ADVISORY BOARD (GASAB)

The mission of the Government Accounting Standards Advisory Board (GASAB) is to formulate and recommend Indian Government Accounting Standards (IGASs) for cash system of accounting and Indian Government Financial Reporting Standards (IGFRS) for accrual system of accounting, with a view to improving standards of Governmental accounting and financial reporting which will enhance the quality of decision-making and public accountability.

GASAB has been developing two types of Accounting Standards, namely Indian Government Accounting Standards (IGAS) and Indian Government Financial Reporting Standards (IGFRS)for the Government. These standards have been developed to address the issues related with the existing cash system of accounting and its migration to the accrual system of accounting in future.

8.10 INDIAN GOVERMENT ACCOUNTING STANDARDS (IGAS)

The standards being developed to make existing cash system of accounting more transparent are called Indian Government Accounting Standards (IGAS).The Indian Government Accounting Standards (IGAS), formulated by the Government Accounting Standards Advisory Board (GASAB) and notified by the Ministry of Finance, Government of India are:

- Guarantees given by Governments: Disclosure Requirements (IGAS 1);
- Accounting and Classification of Grants-in-aid (IGAS 2)
- Loans and Advances made by Governments (IGAS 3)

The Indian Government Accounting Standards (IGAS), approved by the Government Accounting Standards Advisory Board (GASAB) and under consideration of Government of India, are:

- Foreign Currency Transactions and Loss/Gain by Exchange Rate Variations (IGAS 7);
- Government Investments in Equity (IGAS 9);
- Public Debt and Other Liabilities of Governments: Disclosure Requirement (IGAS 10).

IGAS – 1 GURANTEES GIVEN BY GOVERNMENTS: DISCLOSURE REQUIREMENTS

Introduction: The Union Government and the State Governments give Guarantees for repayment of borrowings within such limits, if any, as may be fixed upon the security of the Consolidated Fund of India or of the State, as the case may be, in terms of articles 292 and 293 of the Constitution.

Guarantees are also given by the Union Government

- for payment of interest on borrowings, repayment of share capital;
- payment of minimum annual dividend; and
- payment against agreements for supplies of materials and equipments on credit basis on behalf of the State Governments, Union territories, local bodies, railways, Government companies or corporations, joint stock companies, financial institutions, port trusts, electricity boards and co-operative institutions.

Guarantees are also given by the Union Government to the Reserve Bank of India, other banks and financial institutions:

- for repayment of principal and payment of interest;
- cash credit facility;
- financing seasonal agricultural operations; and
- for providing working capital in respect of companies, corporations, co-operative societies and co-operative banks.

Further, guarantees are also given in pursuance of agreements entered into by the Union Government with international financial institutions, foreign lending agencies, foreign Governments, contractors and consultants towards repayment of principal, payment of interest and payment of commitment charges on loans.

The Union Government also gives performance guarantees for fulfillment of contracts or projects awarded to Indian companies in foreign countries as well as foreign companies in foreign countries besides counter-guarantees to banks in consideration of the banks having issued letters of credit to foreign suppliers for supplies or services rendered by them on credit basis in favour of companies or corporations.

Furthermore, guarantees are given by the Union Government to railways, and electricity boards for due and punctual payment of dues and freight charges by the companies and corporations.

Similarly, guarantees are also given by the State Governments and Union Territory Governments (with legislature).

As the statutory corporations, Government companies, co-operative institutions, financial institutions, autonomous bodies and authorities are distinct legal entities, they are responsible for their debts. Their financial obligations may be guaranteed by a Government and thus the Government has a commitment to see that these are fulfilled.

When these entities borrow directly from the market, it reduces a Government's budgetary support to them and the magnitude of a Government's borrowings. However, it adds to the level of Guarantees given by the Governments. In consideration of the Guarantees given by the Governments, the beneficiary entities are required to pay guarantee commission or fee to the Governments. The Guarantees have an important economic influence and result in transactions or other economic flows when the relevant event or conditions actually occur. Thus, Guarantees normally constitute contingent liability of the Governments.

Objective: The objective of this Standard is to set out disclosure norms in respect of Guarantees given by the Union, the State Governments and Union Territory Governments (with legislature) in their respective Financial Statements to ensure uniform and complete disclosure of such Guarantees.

Scope: The scope of this standard is stated as under:

- This Standard applies to preparation of the Statement of Guarantees for inclusion and presentation in the Financial Statements of the Governments. Financial Statements should not be described as complying with this Standard unless these comply with all its requirements.
- The Authority in the Government which prepares the Statement of Guarantees for inclusion and presentation in the Financial Statements shall apply this Standard. The Accounting Authority is responsible for inclusion and presentation of the Statement of Guarantees in the Financial Statements as provided by the Authority in the Government.

Important Definitions:

- **Accounting Authority:** It means the Authority which prepares the Financial Statements of the Government
- **Authority in the Government:** It means the tracking (monitoring) unit or Authority for Guarantees and in its absence, the Ministry or the Department of Finance, as the case may be.
- **Automatic Debit Mechanism:** It means the arrangement whereby the Government's cash balance is affected on a specified date or on the occurrence of specified events to meet certain obligations arising out of Guarantees given by it.
- **Financial Statements:** It means the Annual Finance Accounts of the Governments.
- **Guarantee:** It means an accessory contract, by which the promisor undertakes to be answerable to the promisee for the debt, default or miscarriage of another person, whose primary liability to the promisee must exist or be contemplated.
- **Structured Payment Arrangement:** It means the arrangement whereby the Government agrees to transfer funds to the designated account in case the beneficiary entity fails to ensure availability of adequate funds for servicing the debts, as per stipulations.

Disclosure:

The Financial Statements of the Union Government, the State Governments and the Union Territory Governments (with legislature) shall disclose the following:

- maximum amount for which Guarantees have been given during the year, additions and deletions (other than invoked during the year) as well as Guarantees outstanding at the beginning and end of the year;
- amount of Guarantees invoked and discharged or not discharged during the year:
- details of Guarantee commission or fee and its realisation; and
- other material details.

The Financial Statements of the Union Government, the State Governments and the Governments of Union Territories (with legislature) shall disclose in the notes the following details concerning class or sector of Guarantees:

- limit, if any, fixed within which the Government may give Guarantee;
- whether Guarantee Redemption or Reserve Fund exists and its details including disclosure of balance available in the Fund at the beginning of the year, any payments made and balance at the end of the year;
- details of subsisting external foreign currency guarantees in terms of Indian rupees on the date of Financial Statements;
- details concerning Automatic Debit Mechanism and Structured Payment Arrangement, if any;
- whether the budget documents of the Government contain details of Guarantees:
- details of the tracking unit or designated authority for Guarantees in the Government; and
- other material details.

Effective date:

This Indian Government Accounting Standard becomes effective for Financial Statements covering periods beginning on or after 1-4-2010 for class-wise disclosures in the Financial Statements of the Union Government and sector-wise disclosures in the Financial Statements of the State Governments and Union Territory Governments (with legislature).

IGAS — 2 ACCOUNTING AND CLASSIFICATION OF GRANTS-IN-AID

Introduction: Grants-in-aid are payments in the nature of assistance, donations or contributions made by one government to another government, body, institution or individual. Grants-in-aid are given for specified purpose of supporting an institution including construction of assets.

The general principle of grants-in-aid is that it can be given to a person or a public body or an institution having a legal status of its own. Such grants-in-aid could be given in cash or in kind used by the recipient agencies towards meeting their operating as well as capital expenditure requirement.

Grants-in-aid are given by the Union Government to State Governments and by the State Governments to the Local Bodies discharging functions of local government under the Constitution. This is based on the system of governance in India, which follows three-tier pattern:

- with the Union Government at the apex,
- the States in the middle, and
- the Local Bodies (LBs) consisting of the Panchayati Raj Institutions (PRIs) and the Urban Local Bodies (ULBs) at the grass root level.

Accounts of these three levels of Government are separate and consequently the assets and liabilities of each level of government are recorded separately. Grants-in-aid released by the Union Government to the State Governments are paid out of the Consolidated Fund of India as per Articles 275 and 282 of the Constitution. The Union Government releases grants-in-aid to the State/ Union Territory Government under Central Plan Schemes and Centrally Sponsored Schemes. Sometimes, the Union Government disburses funds to the State Governments in

the nature of Pass-through Grants that are to be passed on to the Local Bodies. Funds are also released directly by the Union Government to District Rural Development Agencies (DRDAs) and other specialized agencies including Special Purpose Vehicles (SPVs) for carrying out rural development, rural employment, rural housing, other welfare schemes and other capital works schemes like construction of roads, etc.

The 73rd and 74th Constitutional Amendment Acts envisage a key role for the Panchayati Raj Institutions (PRIs) and the Urban Local Bodies (ULBs) in respect of various functions such as education, health, rural housing, drinking water, etc.

The State Governments are required to devolve funds, functions and functionaries upon them for discharging these functions. The extent of devolution of financial resources to these bodies is to be determined by the State Finance Commissions. Such funds received by the Local Bodies from the State Governments as grants-in-aid are used for meeting their operating as well as capital expenditure requirements. The ownership of capital assets created by Local Bodies out of grants-in-aid received from the States Government lies with the Local Bodies themselves.

Apart from Grants-in-aid given to the State Governments, the Union Government gives substantial funds as Grants-in-aid to other agencies, bodies and institutions. Similarly, the State Governments also disburse Grants-in-aid to agencies, bodies and institutions such as universities, hospitals, cooperative institutions and others. The grants so released are utilized by these agencies, bodies and institutions for creation of capital assets as well as for meeting day-to-day operating expenses.

Objective:

The objectives of this Standard are:

- to prescribe the principles for accounting and classification of Grants-in-aid in the Financial Statements of Government both as a grantor as well as a grantee.
- to prescribe practical solutions to remove any difficulties experienced in adherence to the appropriate principles of accounting and classification of Grants-in-aid by way of appropriate disclosures in the Financial Statements of Government.

Scope:

This Standard applies to the Union Government and the State Governments in accounting and classification of Grants-in-aid received or given by them. The Financial Statements should not be described as complying with this Standard unless they comply with all the requirements contained therein. This Standard encompasses cases of Pass-Through Grants such as Grants-in-aid given by the Union Government to State Governments and by the State Governments to the Local Bodies discharging functions of local government under the Constitution.

Important Definitions:

- **Accounting Authority:** It is the authority which prepares the Financial Statements of the Government
- **Financial statements:** It means the Annual Finance Accounts of the Governments.
- **Grants-in-aid:** The Grants-in-aid are payments, transfers of funds, in cash or in kind, in the nature of donations or contributions by one government (grantor) to another government, body, institution or individual (grantee).
- **Government:** Itmeans all departments and ministries of a Government taken together, whether of the Union Government or State Government or Union Territory Government with Legislature.
- **Local Bodies:** It includes Panchayati Raj Institutions and Urban Local Bodies under the provisions of Article 243 and Schedule 12 of the Constitution.
- **Pass-Throuah Grants:** It means grants-in-aid given by the Union Government to the State Governments for transfer to an ultimate grantee.

Recognition:

- **Grants-in-aid in cash** shall be recognised in the books of the grantor at the time cash disbursements take place. Grants-in-aid in cash shall be recognised in the books of the grantee at the time cash receipts take place.

- **Grants-in-aid in kind** shall be recognized in the books of the grantor at the time of their receipt by the grantee. Moreover, it shall be recognized in the books of the grantee at the time of their receipt by the grantee.

Disclosure:

- In order to ascertain the extent of Grants-in-aid disbursed by the grantor to the grantee for the purpose of creation of capital assets, the Financial Statements of the grantor shall disclose the details of total funds released as Grants-in-aid and funds allocated for creation of capital assets by the grantee during the financial year, in the form of an Appendix to the Financial.
- This will enhance transparency and lead to improved disclosure of information in the Financial Statements of the grantor. Such disclosures shall also enable the users of Financial Statements to assess the quantum of future capital formation activity to be undertaken by different grantees supported by funds from the Government.

Effective Date: This Indian Government Accounting Standard becomes effective for the Financial Statements covering periods beginning from 1.4.2011.

IGAS — 3 LOANS AND ADVANCES MADE BY GOVERNMENT

Introduction: The Government of India has been empowered under proviso (2) of Article 293 of the Constitution of India to make loans to the States, subject to such conditions as may be laid down by or under any law made by Parliament, any sums required for the purpose of making such loans being chargeable to the Consolidated Fund of India.

The Union Government has been providing financial assistance to the State Governments, a substantial portion of which is in the form of loans. These loans are advanced to the States both in the form of plan and non-plan assistance intended for both developmental and non-developmental purposes. Loans are also provided by the Union Government to Foreign Governments, Government companies and Corporations, Non-Government institutions and Local bodies. The Union Government also disburses recoverable advances to Government servants.

The State Governments disburse loans to Government Companies, Corporations, Local Bodies, Autonomous Bodies, Cooperative Institutions, Statutory Corporations, quasi-public bodies and other non-Government/private institutions. The State Governments also disburse recoverable advances to Government servants.

Objective: The objectives of the Standard are:

- to lay down the norms for Recognition, Measurement, Valuation and Reporting in respect of Loans and Advances made by the Union and the State Governments in their respective Financial Statements to ensure complete, accurate, realistic and uniform accounting practices, and
- to ensure adequate disclosure on Loans and Advances made by the Governments consistent with best international practices.

Scope: This Standard applies to Loans and Advances given by the Government for incorporation and presentation in the Financial Statements of the Government. Financial Statements shall not be described as complying with this Standard unless they comply with all the requirements contained therein. This standard shall apply only to government accounts being maintained on a cash basis.

Important Definitions:

- **Accounting Authority:** It is the authority which prepares the Financial Statements of the Governments.
- **Accounting Period:** It means the period covered by the Financial Statements.
- **Advances:** These are loans made to Government servants.
- **Carrying amount:** It means the net amount which the debtor owes the creditor at any point of time and it reflects the historical cost of the loan and subsequent cash flows resulting in either decrease due to repayments or write-offs or increase due to additional disbursements.
- **Cash Basis of Accounting:** It means the accounting transactions of an entity represent the actual cash receipts and disbursements during a financial year as distinguished from the amount due to or by the entity during the same period.

- **Charged and Voted Loans and Advances:** All loans to State Governments and a part of the same to Union Territory Governments made by the Union Government are 'charged' loans whereas all other loans and advances are 'voted' loans and advances.
- **Consolidated Fund of India:** It is the fund referred to in clause (1) article 266 of the Constitution of India.
- **Financial Statements:** It means the Annual Finance Accounts of the respective Governments.
- **Government:** It means the Union Government or any State Government or Government of any Union territory with Legislature.
- **Historical Cost**: It is the original book value of loans and advances.
- **Loanee Entity**: It is an entity in whose favor a loan or an advance is sanctioned by the Government.
- Loanee Group: It consists of a group of loanee entities of similar nature and characteristics.
- **Loans:** These are the assistance by the Governments by providing money, goods or services directly or indirectly to the beneficiary entities which entails a contractual right to receive back equivalent moneys along with interest thereon, if any, as per terms and conditions of the loan agreements.
- **Major Heads of Account:** It represents the functions of Government as per the 'List of Major and Minor Heads of Account of Union and States.
- **Minor Heads of Account:**It represents various programmes or schemes undertaken by departments of Government to achieve the objectives of the function represented by the major head as per the 'List of Major and Minor Heads of Account of Union and States.
- **Sub-Major Heads of Account:** It represents the sub-functions of Government. It is under the Major Heads and as per the 'List of Major and Minor Heads of Account of Union and States.
- **Plan Loans:** These are the loans sanctioned by the Government for plan purposes;
- **Sector:**It consists of a grouping of specific functions or services as per the 'List of Major and Minor Heads of Account of Union and States.
- **Write-off**:These are when a competent authority remits or writes off any loan owing to its irrecoverability or otherwise, whereby irrecoverable portion of loan is transferred from the debt head of account to an expenditure head as loss to the Government.

Recognition:

- A loan shall be recognized by the disbursing entity as an asset from the date the money is actually disbursed and not from the date of sanction and if a loan is disbursed in installments then each installment shall be treated as a separate loan for the purpose of repayment of principal and payment of interest, except where the competent authority specifically allows consolidation of the installments into a single loan at the end of the concerned financial year.
- The loans converted into equity shall be treated as conversion and shall lead to a reduction in the outstanding loan amount
- The debt assumption due to invocation of guarantees shall be treated as disbursement of loan, unless otherwise so specified.

Measurement and Valuation:

- Historical Cost measurement shall be the basis for accounting and reporting on loans and advances made by Governments.
- As of the last date of accounting period of Financial Statements, the carrying amount of loans shall undergo revision an account of additional disbursement and repayments or write-offs during the accounting period.

Disclosure:

- The Financial Statements of the Union and State Governments shall disclose the Carrying Amount of loans and advances at the beginning and end of the accounting period showing additional disbursements and repayments or write-offs.
- An additional column in the relevant Financial Statements shall also reflect the amount of interest in arrears and this amount shall not be added to the closing balance of the loan which shall be in nature of an additional disclosure.
- The Financial Statements of the Union Government shall disclose the following details under 'Loans and Advances made by the Union Government' in the Annual Finance Accounts of the Union Government:
  - ✓ the summary of Loans and Advances showing Loanee group-wise details;
  - ✓ the summary of Loans and Advances showing Sector-wise details;
  - ✓ The summary of repayments in arrears from Governments and other loanee entities.
- The Financial Statements of the Union Government shall disclose the following details under 'Detailed Statement of Loans and Advances made by the Union Government in the Annual Finance Accounts of the Union Government -
  - ✓ the detailed statement of Loans and Advances showing the Major Head;
  - ✓ the detailed Statement of repayments in arrears from State or Union territory Governments;
  - ✓ the detailed Statement of repayments in arrears from other Loanee entities.
- The Financial Statements of the Union Government shall disclose the following details under 'Additional Disclosures' in the Annual Finance Accounts of the Union Government:
- The fresh Loans and Advances made during the year.
- the Financial Statements of the State Governments shall disclose the following details under 'Statement of Loans and Advances made by the State Governments' in the Annual Finance Accounts of the State Government
  - ✓ the summary of Loans and Advances showing Loanee group-wise details;
  - ✓ the summary of Loans and Advances showing Sector-wise details;
  - ✓ the summary of repayments in arrears from Loanee entities.
- The Financial Statements of the State Governments shall disclose the following details under 'Detailed Statement of Loans and Advances made by the State Government in the Annual Finance Accounts of the State Government:
  - ✓ the detailed statement of Loans and Advances showing the Major Head and Minor Head-wise details;
  - ✓ the detailed Statement of repayments in arrears from Loanee entities.
- The Financial Statements of the State Governments shall disclose the details relating to fresh Loans and Advances made during the year under 'Additional Disclosures' in the Annual Finance Accounts of the State Government.

Effective Date: This Indian Government Accounting Standard becomes effective for the Financial Statements covering periods beginning from 1.4.2011.

IGAS — 7 FOREIGN CURRENCY TRANSACTIONS AND LOANS OR GAIN BY EXCHANGE RATE VARIATION

Introduction: Government Accounting Rules, 1990 require that the accounts of the Government shall be maintained in Indian currency i.e., Indian rupees. Indian rupee is the reporting currency for the financial statements of the Government.

All transactions of the Union and State Governments taking place in other countries are passed periodically by the Indian Embassies/ Missions to India and brought to account finally in the Indian books after they have been converted into rupees.

All transactions taking place with foreign Governments or foreign entities or international agencies in foreign currency are also to be recorded in the reporting currency applying exchange rate on the date of transaction.

The missions and embassies of India abroad incur expenditure on their operations including the pay and other entitlements of the officials employed there. They also make payments on behalf of other Ministries and Departments relating to defense, commerce, education as well as public sector undertakings and State Governments. These involve foreign currency transactions and loss or gain due to difference between exchange rate applicable and exchange rate internally adopted by Government like official rate of exchange or salary rate of exchange. Government may use various rates of exchange internally determined for foreign currency transactions that might give rise to loss or gain for accounting purpose.

Under Article 292 of the Constitution of India, the executive power of the Union extends to borrowing upon the security of the Consolidated Fund of India within such limits, if any, as may from time to time be fixed by the Parliament by law and to the giving of guarantees within such limits, if any, as may be so fixed. The Union Government may have bilateral and multi-lateral transactions involving foreign currency. This may involve borrowing or lending involving repayment of principal and payment of interest denominated in foreign currency and loss or gain by exchange rate variation.

In case of foreign currency loans to various projects, particularly by the World Bank, there are different procedures for disbursement. These are (i) Reimbursement through Special Account, (ii) Reimbursement outside Special Account, and (iii) Direct payment/ Commitment procedure. The Direct payment/ Commitment procedure involves direct payment of foreign currency to contractor/ supplier/ consultants from the loan/ credit funds the World Bank, as opted by the project implementing agency. The rupee equivalent of the foreign currency paid directly from the loan/credit is recoverable from the project implementing agency. However, under externally aided projects the Union Government releases 'additional central assistance towards disbursements under this procedure. But the rupee amount of the foreign currency paid directly from the loan/credit is recoverable from the project implementing agency.

Government may float or may enter into agreement with designated bank(s), for example, the State Bank of India to float schemes involving foreign currency denominated bonds/ deposits, such as 'The NRI Bonds', 'India Millennium Deposits' and 'Resurgent India Bonds' for subscription by the Non-Resident Indians, Overseas Corporate Bodies or Banksacting in fiduciary capacity on their behalf. The proceeds may not flow into the Consolidated Fund and are either kept in the Public Account as in the case of the NRI Bonds or acquired by the Reserve Bank of India. Rupees securities issued to the international financial institutions such as the Asian Development Bank, International Bank of Reconstruction and Development (World Bank), International Development Association, International Fund for Agricultural Development, African Development Bank are accounted for under 'internal debt' of the Central Government that may require repayment on encashment of rupee securities in convertible currencies giving rise to exchange difference.

Foreign currency transactions for acquisition of Special Drawing Rights (SDRs) at the IMF are accounted for under Special Deposit and Accounts-SDR at the IMF-Exchange Rate.

Objective: The objective of this standard is to provide accounting and disclosure requirements of foreign currency transactions and financial effects of exchange rate variations in terms of loss or gain in the financial statements. It also deals with the requirements of disclosure of foreign currency external debts and the rate applied for disclosure. The principal issues in accounting and reporting for foreign currency transactions are to decide which exchange rate to apply and how to recognise in the financial statements the financial effects of exchange rate variations in terms of loss or gain.

Scope: The Accounting Authority which prepares and presents the financial statements of the Government under the cash basis of accounting, as defined in the Government Accounting Rule 21 of GAR 1990 and Government Financial Rule 68 of GFR 2005 should apply this Standard:

(a) in accounting and disclosure for transactions in foreign currencies;

(b) in accounting and disclosure for financial effects of exchange variations in terms of loss or gainby exchange rate variation, and

(c) in disclosure of foreign currency external debts and the rate(s) applied for disclosure.

Financial statements should not be described as complying with this Standard unless they comply with all its requirements.

This Standard shall apply to foreign currency transactions of the Union Government as well as that of the State Governments.

This Standard deals with presentation of expenditure and revenue in terms of loss or gain by exchange rate variations arising from foreign currency transactions. It also deals with disclosure of foreign currency external debt.

This Standard does not deal with disclosure requirements of external guarantees. The requirements of disclosure of details of subsisting external guarantees in terms of Indian rupees on the date of financial statements have been dealt with in IGAS1 “Guarantees given by Governments: Disclosure Requirements’.

The Reserve Bank of India is the custodian of foreign currency and foreign exchange reserves and this Standard does not deal with foreign currency reserves.

Important Definitions:

- **Accounting Authority:** It is the authority which prepares the financial statements of the Government.
- **Capital Account:** It means a division of Government accounts wherein receipts and expenditure of capital nature are accounted for.
- **Closing Rate:** It is the exchange rate on the last working day of the period for which the financial statement is prepared.
- **Consolidated Fund of India or Consolidated Fund of State:** It means the Consolidated Fund referred to in Article 266 (I) of the Constitution of India.
- **Cross Currency Swap Agreement:** Itis a financial agreement between two parties to exchange a stream of principal and interest payments in one currency for a stream of principal and interest payments in another currency.
- **Direct Payment Procedure:** It involves direct payment of foreign currency to contractor / supplier / consultants, from the loan / credit funds of the World Bank, as opted by the project implementing agency.
- **Exchange Rate:** It is the ratio for exchange of two currencies.
- **Exchange Rate Variation:** It means change in the ratio for exchange of two currencies;
- **Exchange Difference:** It is the difference resulting from reporting the same number of units of a foreign currency in the reporting currency at different exchange rates.
- **External Guarantee:** It means a guarantee against liability denominated in foreign currency.
- **Financial Statements:** It means the Annual Finance Accounts of the Governments.
- **Foreign Currency:** It means a currency other than the reporting currency of the Government.
- **Forward Rate:** It means the specified exchange rate for exchange specified by the terms of agreement for exchange of two currencies at a specified future date.
- **Government:** It means the Central (Union) Government or a State Government, or a Union Territory Government;
- **Government Accounts:** It mean the form and divisions of accounts and accounting records in which all transactions ofGovernment are accounted for.
- **Guarantee:** It is an accessory contract, by which the promisor undertakes to be answerable to the promisee for the debenture default or miscarriage of another person, whose primary liability to the promisee must exist or be contemplated.
- **Indian Currency:** It means currency which is expressed or drawn in Indian rupees.
- **Official Rate of Exchange:** It means official accounting rateof exchange between Indian rupees and foreign currencies determined and issued by the Ministry of External Affairs, Government ofIndia periodically.
- **Public Account:** It means the Public Account of India referred to in Article 266(2) of the Constitution of India;
- **Public Sector Undertaking:** It means government companies incorporated under the Companies Act, 1956 and Statutory Corporations set up under the specific Acts of Parliament and State Legislatures, as the context may imply.
- **Reporting Currency:** It means Indian Rupees.

- **Revenue Account:** It means a division of Government accounts wherein receipts and expenditure of revenue nature are accounted for.
- **Salary Rate of Exchange:** It means the rate of exchange between the reporting currency and foreign currency fixed by Ministry of External Affairs, Government of India for disbursement of salary of the officials posted at Mission abroad.
- Special Drawing Right means the international reserve asset created by the International Monetary Fund.

Foreign Currency Transactions: A Foreign currency transaction of Government is a transaction which is denominated in or requires settlement in a foreign currency. This may include:

- transactions arising due to operations of the missions and embassies abroad and receipts and payments made by them including those on behalf of other Ministries and Departments relating to defence, commerce, education as well as public sector undertakings and State Governments;
- bilateral and multi-lateral foreign currency transactions involving borrowing or lending including debt servicing;
- purchasing/ selling goods or services where purchase/ sale price is denominated in foreign currency;
- transactions arising from the schemes involving foreign currency such as 'The NRI Bonds', the flow of which goes to Government account;
- transactions for acquisition of Special Drawing Rights at the International Monetary Fund and quota contributions to IMF and the transactions under Financial Transaction Plan;
- rupees securities issued to the international financial institutions which are accounted for under the head internal debt of the Central Government but requiring repayment on encashment of rupee securities in convertible currencies.

A foreign currency transaction of Government shall be reported in the reporting currency by applying to the foreign currency amount, exchange rate between the reporting currency and the foreign currency at the date of receipts and payments.

The exchange rate at the date of receipts and payments is the rate as determined by the Government of India for the purpose viz., salary rate, official rate, etc. or else the rate as indicated by the Reserve Bank of India in its buying and selling rate as may be appropriate, issued every day.

Treatment of Loss or Gain by Exchange Rate Variation: This standard set out the following accounting treatment required by this Standard with respect to loss or gain by exchange rate variations and exchange difference on different types of foreign currency transactions.

- All losses or gains by exchange rate variation in respect of Government transactions in foreign currencies shall be recognised as revenue loss or gain.
- Government may have losses or gains by exchange rate variations on its operating activities like operation of its missions abroad as mentioned in paragraph 2 above or due to contractual commitments to bear the financial effect of exchange rate variations as part of its fiscal and economic policy.
- Loss or gain arising out of transactions for acquisition of Special Drawing Rights at the International Monetary Fund shall be reported in the financial statements.
- Exchange difference may arise out of Government's financing activities like borrowing of loans denominated inforeign currencies and issuing of rupees securities. External borrowings of the Government are recorded at the historical rate of exchange i.e., rate of exchange prevailing at the date of transaction. As most of the loans have long repayment period(s), their repayment extends over several years. Meanwhile, exchange rate(s) may undergo significant changes. If the exchange rate is higher at the time of repayment, repayment of loans in Indian rupees exceed the rupee amount of loan drawn.

In case repayment of loans, at the end of loan period the balance, if any, remaining in external debt head may be cleared adjusting the same under appropriate revenue or expense head for exchange rate fluctuations or to miscellaneous Government Account head.

Disclosure:

The financial statements shall disclose rates of exchange adopted internally by the Government for different types of foreign currency transactions including forward contract rate, if any, along with their basis as part of Statement of Accounting Policies.

The financial statements shall disclose the following details of foreign loans in the format given in paragraph 30:

(a) loans outstanding on historical cost basis at the beginning and end of the year;

(b) loans outstanding on closing rate basis at the beginning and end of the year;

(c) loans outstanding in foreign currency units at the beginning and end of the year;

(d) additions during the year in foreign currency terms and in Indian Rupee along with the rate of exchange adopted;

(e) discharge during the year showing separately the amounts in foreign currency units, on historical basis and

(f) current rate of exchange basis;

(g) loss or gain on repayment of loans due to variation of exchange rate;

(h) amount outstanding at the end of the year in foreign currency units, on historical basis and on closing rate basis;

(i) interest paid on external debt; and

(j) closing rate of exchange applied.

Financial statements shall disclose in the notes the following:

(a) category-wise gross figure of loss and gain by exchange rate variation for the financial year;

(b) loss and gain by exchange rate variation separately for Capital Head transactions and Revenue Head transactions;

(c) amount of loan and exchange difference in respect of fully repaid loans; and

(d) amount of loss or gain, if any, on cross-currency swap agreements.

Effective Date: This Indian Government Accounting Standard shall be effective for financial statements for the periods commencing from the 1st April subsequent to the date of notification of the standard by Government.

IGAS — 9 GOVERNMENT INVESTMENTS IN EQUITY

Introduction:

The Union Government, State Governments, and Governments of Union Territories with Legislatures (hereinafter called Government), make investments in entities like Government companies, Statutory Corporations, other Joint Stock Companies and Cooperative Banks/ Societies etc. In addition, the Union Government also invests in international bodies and authorities like the International Monetary Fund, Asian Development Fund, and International Finance Corporation.

Government's investments in equity include direct investment in share capital, conversion of outstanding loans (principal and interest) against the entity into equity, and conversion of dividends declared by the entity, but not received, into equity. This standard covers all such investment in equity, and does not cover investment in the loan capital of the entity.

Objective:

The objective of the Standard is to lay down the norms for recognition, measurement,and reporting of investments of the Government in the Financial Statements so that the financial statements provide a true and fair view of investments of the Government, consistent with best international practices.

Scope:

This Standard applies to investments made in different investee entities by the Government for incorporation, and presentation in the Financial Statements. This standard will apply only to Government accounts being maintained on cash basis.

It applies to investment in equity of the investee entities and not in debt, like debentures, bonds, and such other instruments which are normally accounted for by the investee entities as long term and short term debt. The Financial Statements shall not be considered as giving a true arid fair view of investments unless they comply with this Standard.

Important Definitions:
• **Accounting Authority:** It is the authority that prepares the financial statements of the Government. • Accounting Period: It means the financial year covered by the financial statements, which is normally from 01 April to 31 March. • **Bonus Shares:** These are the shares issued free of cost to the shareholders by an investee entity by capitalising its reserves and / or the security premiums as per the requirement of the relevant law. • **Cash Basis of Accounting:** It is one wherein the accounting transactions of the Government represent the actual cash receipts and disbursements during a financial year as distinguished from the amount due to *or from* the investee entity during the same period. • **Disinvestment/ divestment / retirement of-Government Equity:** It means the sale or transfer of equity shares by the Government. • **Equity Share:** It is a share, which is not a preference share. • **Financial Statements:** It means the Annual Finance Account of the respective Government. • **Government:** It means the Union Government or any State Government or Government of any Union Territory with Legislature. • **Government Investment in Equity:** It includes investment in equity shares obtained by the Government on payment of cash or in exchange of any other asset; exercise of a right granted by the investee; issuance of bonus shares by the investee entity; reinvestment of dividends; or conversion of loans into equity. • **Historical Cost:** It is the cost of acquisition of equity shares. • **Investee Entity:** It is an entity in which an investment is made by the Government. • **Investee Group:** It consists of a group of investee entities of similar nature and characteristics that can be collectively and distinctively addressed such as Statutory Corporations, Joint Stock Companies, International Bodies, State Cooperative Banks/other banks, Cooperative Societies, Employees Consumer Cooperative Societies, etc. • **Preference Shares:** It mean those shares which have the following two characteristics: • (a) that with respect to dividends, carry a preferential right to be paid a fixed amount or an amount calculated at a fixed rate; (b) that with respect to capital, they carry, over the equity share hotter, on winding up or repayments of capital, a preferential right to be repaid the amount of the capital paid up or deemed to have been paid up. • **Right Shares:** These are the allotment of shares on the issue of fresh capital by an investee entity to which a shareholder, by virtue of his holding, is entitled to, certain shares on payment in the investee enterprise in proportion to the number of shares already held by him.

Recognition:

An investment in equity shall be recognised by the Government as an asset from the date on which the investment details are entered in the books of the entity.

Loans converted into equity and dividends declared but not distributed by the investee entity, converted into equity shall be treated as equity investments from the date on which such conversion takes plate, i.e. from the date on which details of conversion are entered in the books of the investee entity.

Measurement:

- The method of initial measurement of investments in the financial statements of theGovernment is the historical cost of the investment. Where investment in equity is acquired on payment of cash including on exercise of rights granted by the investee, the historical cost is the amount of cash disbursed. Historical cost of Bonus shares is nil as there is no payment of cash. In case the Government acquires equity shares in consideration of any other asset, e.g., land, the historical cost of such investment shall be the face value of the equity shares. Where the equity shares are acquired on reinvestment of dividends, the historical cost of such shares is the amount of dividends against which the shares are allotted. Historical cost of equity shares acquired on conversion of loans is the amount of the loan outstanding (principal and interest) against which such shares are allotted.
- Total market value of the investments will be calculated on the basis of the price quoted on the last day of the financial year in the primary market of trading of that particular stock or in case the quoted price is not available on that date, the price on the date at which it was last quoted before the closing of the financial year. This will be applicable to the listed companies whose shares are regularly traded on a recognised stock exchange during the year.
- Investments subsequent to initial measurement shall also be reflected in the financial statements at historical cost.
- The total amount of investments on the last date of an accounting period shall be the investments at the beginning of the period with additions and disinvestment / sale of investments during the period.

Disclosure:

The Financial Statements of the Government shall disclose the amount of investments at the beginning and at the end of the accounting period showing additional investments, disinvestments / divestments or retirement /write town of capital / transfer of share, if any.

They will reflect the additions made during the year by way of investments to the opening balance and disinvestments/ divestments there from, for arriving at the closing balance.

Types of investments are specifically mentioned and acquisitions of investments in terms of exchange of goods/ other assets are also recorded.

The amount of dividend received shall be reflected as revenue of the period.

The Financial Statements of the Government shall disclose the following details under the statement of 'Investments made by the Government':

(i) Detailed Statement of Investments made investee Entity wise.

(ii) Detailed Statement of Disinvestments / divestments / retirement of capital / transfer of shares made Investee Entity wise.

(iii) Summary of Investments: Investee group-wise (such as Statutory Corporations, Joint Stock Companies, Cooperative Banks, etc.

(iv) Additional disclosures of investee entities which have not submitted accounts and / or have suffered a loss during the preceding three consecutive years.

The detailed statement of investments, Investee entity wise in the Financial Statementswhich the entity belongs, the Ministry or Department under which the investee is functioning, whether the enterprise is in operation or not etc. Details of disinvestment / divestments / retirement of capital / transfer of share during the year are reported in the Statement of disinvestment / retirement of capital, investee entity wise. While indicating the type and number of units, the units acquired, and those allotted as bonus shares, shall be depicted separately along with year of allotment. The statements shall also disclose the total paid up capital of the entity. This would help indicate the extent of government control and whether the investment has increased or decreased.

Moreover, where the units of investments are traded in the market, the amount of investment in terms of market value may also be disclosed. The price quoted on the last day of the financial year in the primary market of trading of that particular stock orin case the quoted price is not available on that date, the price on the date at which it was last quoted before the closing of the financial year may be taken into account.

The amount of dividend received and credited to Government revenue shall also be reported entity wise. In case the dividend received pertains to previous accounting periods, the year to which the amounts actually pertain are disclosed by way of a foot note.

Additional disclosures shall include the investments and disinvestments / divestments / retirement of capital / transfer of shares made during the reporting period. In addition, disclosures shall be made by way of a note to accounts in respect of investments in entities which have made a net loss i.e., loss after interest and taxes in the previous accounting period along with remarks where further investments have been made during the reporting period. Where the accounts of the investee entities are in arrears for more than three consecutive years, the fact should be disclosed, along with remarks in cases where the G6vernment has invested in the entity during the reporting period.

Effective date:

This Indian Government Accounting Standard becomes effective for the financial statements covering periods beginning from the 01 April of the year following the notification of the Standard by the Government.

IGAS — 10 PUBLIC DEBT AND OTHER LIABILITIES OF GOVERNMENTS: DISCLOSURE REQUIREMENTS

Introduction:

In terms of Article 292 of the Constitution, the executive power of the Union extends to borrowing upon the security of the Consolidated Fund of India within such limits, if any, as may from time to time be fixed by Parliament by Law. Article 293(1) of the Constitution provides a similar provision in respect of State Governments. Section 48A(1) of the Government of Union Territory Act 1963 and Section 47A(1) of Government of NCT of Delhi Act 1991, also provides for borrowing upon the security of the Consolidated Fund of the Union Territory concerned or Consolidated Fund of the Capital within such limits, if any, as may be fixed by Parliament by law and the stipulations indicated therein.

Objective:

The objective of the IGAS isto lay down the principles for identification, measurement and disclosure of public debt and other obligation of Union and the State Governments including Union Territories with legislatures in their respective financial statements.

It ensures consistency with international practices for accounting of public debt in order to ensure transparency and disclosure in the financial statements of Government for the benefit of various stake holders.

Scope:

- The proposed IGAS shall apply to the financial statements prepared by the Union and State Governments and Union Territories with legislature.
- The IGAS shall also cover "other obligations" as defined in paragraph 4 of this standard relating to definitions. The IGAS shall not include in its ambit, guarantees and other contingent liabilities and non-binding assurances.

Important Definitions:

- **Accounting Authority**: It means the authority who prepares the Financial Statements of the Governments.
- Accounting Period: It means the period covered by the Financial Statements.
- **Cash Basis of Accounting:** It is that wherein accounting transactions of the Union Government, State Government and Government of Union Territory with legislature represent the actual cash receipts and disbursement during a financial year as distinguished from the amounts due to or by the relevant Government, subject to the exceptions as may be authorized under the Government Accounting Rules 1990 or by any general or special orders issued by the Central Government on the advice of the Comptroller & Auditor General of India.
- **Consolidated Fund of India**: It is the fund referred to in Article 266(1) of the Constitution of India.
- **Consolidated Fund of a State:** It is the fund referred to in Article 266(1) of the Constitution of India.
- **Consolidated Fund of Union Territories with Legislature**: It is the fund referred to in Section 47(1) of the Union Territories Act, 1963 and Section 46(1) of the Government of National Capital Territory of Delhi Act, 1991.
- **Public Account of India:** It is the fund referred to in Article 266(2) of the Constitution of India.
- **Public Account of a State:** It is the fund referred to in Article 266(2) of the Constitution of India.
- **Public Account of Union Territory:** It is the Public Account referred to in Section 47A (1) and Section 46A (1) of the Government of Union Territories Act, 1963 and the Government of National Capital Territory of Delhi Act, 1991 respectively.
- **Financial Statements:** It means the Annual Finance Accounts of the Union Government, State Governments and Union Territories with legislature. It would also include appropriate statements, schedules and notes to the above statements.
- **Government:** It means the Union Government or any State Government or Government of any Union Territory with Legislature.
- **Face Value:** It is the contract value of the Public Debt or other obligations.
- **Public Debt:** It includes internal and external debts of the Central Government, State Governments and Government of the Union Territory with legislature, as applicable.
- **Other Obligations:** It refers to the net outcome of the receipt and payment transactions arising in the public account. It does not include transactions categorized as Remittances, Suspense and Miscellaneous and Cash Balance.

Measurement & Valuation:

The Public Debt and Other Obligations incurred by Governments shall be accounted and reported on the basis of Face Value. For the purpose of reporting external debt, changes in the Balance at the end of the Accounting Period arising from variations in the rate of exchange shall also be reported.

Disclosure:

The financial statements of the Union Government, State Governments and the Union Territories with legislature shall disclose the following details concerning Public Debt and other obligations:

(a) the opening balance, additions and discharges during the year, closing balance and net change in rupee terms with respect to internal debt;

(b) the opening balance, additions and discharges during the year, closing balance and net change in rupee terms with respect to external debt, wherever applicable;

(c) the opening balance, receipts and disbursements during the year, closing balance and net change in rupee terms with respect of other obligations.

The Financial Statements of the Union Government and the State governments shall disclose the following details regarding servicing of debt and related parameters for the current year, preceding year and net change in rupee terms with respect to:

(a) Interest paid by the governments on public debt, small saving, provident funds, and reserve funds and on other obligations.

(b) Interest received on loans to State and Union Territory Governments, departmental Commercial Undertakings, PSUs and other Undertaking including Railways, Post & Telegraph.

(c) Interest received on other Loans, from investments of cash balances and other items.

External debt of the Central Government shall be classified according to source indicating the currency of transaction. Measurement of face value shall be in respect of both the currency of agreement and Indian rupees. It should also disclose the outstanding in terms of exchange rate prevailing at the end of the accounting period.

Effective date:

This Indian Government Accounting Standard becomes effective for the Financial Statements covering periods beginning on 1st April of the year after the notification of the Standard by the Government.

8.11 INDIAN GOVERNMENT FINANCIAL REPORTING STANDARDS (IGFRS)

The standards being developed for accrual system of accounting in the Government are called the Indian Government Financial Reporting Standards (IGFRS).

Accrual based Accounting Standards, i.e., Indian Government Financial Reporting Standards (IGFRS), approved by the Government Accounting Standards Advisory Board (GASAB) under consideration of Government of India:

- IGFRS 1: Presentation of Financial Statements
- IGFRS 2: Property, Plant & Equipment
- IGFRS 3: Revenue from Government Exchange Transactions
- IGFRS 4: Inventories
- IGFRS 5: Contingent Liabilities (other than guarantees) and Contingent Assets: Disclosure Requirements.[1]

Formulation of some other IGFRSs/IGASs is under progress

IGFRS 1: Presentation of Financial Statements

IGFRS 1 has prescribed the manner of presentation of financial statements by Government entities that follow accrual basis of accounting. It sets out over all requirement for the presentation of financial statements, guidance for their structure and minimum requirements for the content of financial statements presented under the accrual basis of accounting.

IGFRS 2: Property, Plant and Equipment

This standard has prescribed the accounting treatment for property, plant and equipment (PPE) so that users of financial statements can obtain information regarding an entity's investment in its property, plant and equipment and any changes in such investment. The principal issues in accounting for property, plant and equipment are the timing of recognition of the assets, the determination of their carrying amounts and the depreciation charges and impairment losses to be recognised in relation to them. In addition, this standard aims at categorising assets according to their nature and also aims to provide for depreciation of assets, taking into account their usage over the life of the assets. The Accounting Standard is essentially an adaptation to Indian requirements of International Public Sector Accounting Standard (EPSAS 17) issued by IFAC on Property, Plant and Equipment. It also envisaged to provide guidance to pilot studies and the eventual development of a common reporting framework under accrual basis for the Union and the States. The IGFRS are subject to revision by GASAB based on experiences with pilot studies.

1 http://gasab.gov.in/gasab accessed on 20.06.2016

IGFRS 3: Revenue from Government Exchange Transaction

This Standard lays down the principles to be followed for recognition and measurement of revenue from exchange transactions by government entities under accrual basis of accounting, wherein transactions and other events are recognised when they occur (and not only when cash or its equivalent is received or paid). It is envisaged to provide guidance to the pilot studies and eventual development of a common reporting framework under accrual basis for Union and the States. The IGFRS could be revised by GASAB based on pilot studies.

IGFRS 4: Inventories

This standard has prescribed the accounting treatment for inventories. A primary issue in accounting for inventories is the amount of cost to be recognized as an asset and carried forward until the related revenues are recognized. This Standard provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories. This Standard aims at using accrual principles of accounting for inventories – both at the stage of charging as expense and depicting the closing stock in the financial statements at the end of the reporting period.

The Accounting Standard has derived inputs from Indian Accounting Standards (Ind AS 2), IPSAS 12 and IAS 2 (International Accounting Standards). The Standard is envisaged to provide guidance to the pilot studies and eventual development of a common reporting framework under accrual basis for the Union and the States. The IGFRS 4 could be revised by GASAB based on pilot studies.

IGFRS 5: Contingent Liabilities (other than guarantees) and Contingent Assets: Disclosure Requirements

This standard has laid down the principles for disclosure requirements of Contingent Liabilities (other than guarantees) and Continent Assets for both the Union and the State Governments including Union Territories with Legislatures, in their respective Financial Statements in order to ensure uniform and appropriate disclosure of such liabilities and assets. It also ensures consistency with international best practices leading to transparency and improved quality of disclosure in the financial reports of Governments for the benefit of various stakeholders. An important objective of the IGFRS is to ensure that Governments portray the risks associated with contingent liabilities and contingent assets in a transparent manner. The purpose of this standard is to provide for disclosure requirements of contingent liabilities (other than guarantees) and contingent assets of Governments in the financial

Statements. Disclosure of contingent liability is relevant from the point of view of knowing what risk of future liability the government carries. Disclosure of contingent assets is relevant in knowing what possible assets may accrue to government.