PAPER – 1: ADVANCED ACCOUNTING

QUESTIONS

PART – I: Multiple Choice Questions based on Case Scenarios

1. Surya Ltd. Has a two fixed asset, FA1 is being carried in the balance sheet for ₹ 600 lakhs and FA 2 is being carried at ₹ 300 lakhs

   As at 31st March 2024, the value in use for FA 1 is ₹ 500 lakhs and the net selling price is ₹ 550 lakhs. The Company did upward revaluation last year for ₹ 20 lakhs for FA 1.

   As at 31st March 2024, the value in use for FA 2 is ₹ 350 lakhs and the net selling price is ₹ 320 lakhs.

   (a) How much is the total Impairment loss for current year for FA 1:

   (i) ₹ 100 Lakhs

   (ii) ₹ 50 Lakhs

   (iii) ₹ 30 lakhs

   (iv) Nil

   (b) How much impairment loss will be charged to profit and loss for current year for FA1:

   (i) ₹ 100 Lakhs

   (ii) ₹ 50 Lakhs

   (iii) ₹ 30 lakhs

   (iv) Nil

(c) How much is the total Impairment loss for current year for FA 2:

(i) ₹ 50 Lakhs

(ii) ₹ 30 Lakhs

(iii) ₹ 20 lakhs

(iv) Nil

(d) What will be the carrying value on 1st April 2024 for FA 1:

(i) ₹ 550 Lakhs

(ii) ₹ 530 Lakhs

(iii) ₹ 520 lakhs

(iv) ₹ 500 lakhs

General MCQs

2. The debit or credit balance of "Foreign Currency Monetary Item Translation Difference Account"

(a) Is shown as "Miscellaneous Expenditure" in the Balance Sheet

(b) Is shown under "Reserves and Surplus" as a separate line item

(c) Is shown as "Other Non-current" in the Balance Sheet

(d) Is shown as "Current Assets" in the Balance Sheet

Part II - Descriptive Questions

Applicability of Accounting Standards

AS 1

3. ABC Ltd. was making provision for non-moving inventories based on no issues for the last 12 months up to 31.3.2023.

The company wants to provide during the year ending 31.3.2024 based on technical evaluation:

Total value of inventory	₹ 100 lakhs
Provision required based on 12 months issue	₹ 3.5 lakhs
Provision required based on technical evaluation	₹ 2.5 lakhs

Does this amount to change in Accounting Policy? Can the company change the method of provision?

AS 3

4. Classify the following activities as (1) Operating Activities, (2) Investing Activities, (3) Financing Activities (4) Cash Equivalents.

    a. Proceeds from long-term borrowings.

    b. Proceeds from Trade receivables.

    c. Trading Commission received.

    d. Redemption of Preference Shares.

    e. Proceeds from sale of investment

    f. Interim Dividend paid on equity shares.

    g. Interest received on debentures held as investment.

    h. Dividend received on shares held as investments.

    i. Rent received on property held as investment.

    j. Dividend paid on Preference shares.

    k. Marketable Securities

AS 5

5. During the course of the last three years, a company owning and operating Helicopters lost four Helicopters. The company's accountant felt that after the crash, the maintenance provision created in respect of the respective helicopters was no longer required, and proposed to write it back to the Profit and Loss account as a prior period item.

    Is the company's proposed accounting treatment correct? Discuss.

AS 7

6. Rose Constructions undertake to construct a·bridge for the Government of Uttar Pradesh. The construction commenced during the financial year ending 31.03.2024 and is likely to be completed by the next financial year. The contract is for a fixed price of ₹ 12 crore with an escalation clause. You are given the following information for the year ended 31.03.2024:

Cost incurred upto 31.03.2024	₹ 4 crore
Cost estimated to complete the contract	₹ 6 crore

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

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

AS 9

7. Mithya Ltd. entered into agreement with Satya Ltd. for sale of goods costing ₹ 8 lakh at a profit of 20% on cost. The sale transaction took place on 1st February, 2024. On the same day, Satya Ltd. entered into another agreement with Mithya Ltd. to resell the same goods at ₹ 10.80 lakh on 1st August, 2024. State the treatment of this transaction in the financial statements of Mithya Ltd. as on 31.03.2024. The pre-determined re-selling price covers the holding cost of Satya Ltd. Give the Journal Entries as on 31.03.2024 in the books of Mithya Ltd.

AS 10

8. MS Ltd. has acquired a heavy machinery at a cost of ₹ 1,00,00,000 (with no breakdown of the component parts). The estimated useful life is 10 years. At the end of the sixth year, one of the major components, the turbine requires replacement, as further maintenance is uneconomical. The remainder of the machine is perfect and is expected to last for the next four years. The cost of a new turbine is ₹ 45,00,000. The discount rate assumed is 5%.

   Can the cost of the new turbine be recognised as an asset, and, if so, what treatment should be used?

AS 11

9. Bansal Company Ltd. imported raw material worth US Dollars 12,000 on 15th January, 2024 when the exchange rate was ₹ 68 per US Dollar. The payment for the transaction was made on 5th May, 2024 when exchange rate was ₹ 64 per US Dollar. At the year end, 31st March, 2024, the rate of exchange was ₹ 65 per US Dollar. The accountant of the company

passed entry on 31st March, 2024 adjusting the cost of raw material consumed for the difference between ₹ 64 and ₹ 68 per US Dollar. Discuss whether this treatment is justified as per the provisions of AS-11 (Revised).

AS 14

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

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

AS 16

11 How will interest be capitalized when qualifying assets are funded by borrowings in the nature of bonds that are issued at a discount?

    X Ltd. issued in year 1, a 3 year 10% p.a. (interest paid annually) bond with a face value of ₹ 1,00,000 at a price of ₹ 90,000 to finance a qualifying asset which is ready for intended use at the end of year 2. Compute the amount of borrowings costs to be capitalized if the company uses for amortization of discount straight line basis

AS 17

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

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

AS 18

13. Will transactions with related parties, for services provided/received free of cost, be required to be disclosed?

A Limited has a corporate communications department, which centralises the public relations function for the whole group of A Limited and its subsidiaries. No charges are, however, levied by A Limited on its subsidiaries and accordingly, these transactions are not given accounting recognition. Would these constitute related party transactions requiring disclosure under AS 18 in the standalone financial statements of A Limited?

AS 19

14. Money Limited leased a machine to Hello Limited on the following terms:

		(₹ in lakh)
(i)	Fair value of the machine	24.00
(ii)	Lease term	5 years
(iii)	Lease rental per annum	4.00
(iv)	Guaranteed residual value	0.8
(v)	Expected residual value	1.5
(vi)	Internal rate of return	15%

Discounted rates for 1st year to 5th year are 0.8696, 0.7561, 0.6575, 0.5718, and 0.4972 respectively.

Ascertain Unearned Finance Income.

AS 20

15. XYZ Limited has a wholly owned subsidiary BC Limited. The Group prepares consolidated Financial Statements for the year ended 31st March, 2024. XYZ Limited (in its separate financial statements) has incurred a loss of ₹ 2 crore during the year, while the consolidated profit for the group during the year is ₹ 40 lakh.

XYZ Limited has 5,00,000 shares outstanding as at 31st March, 2024. Further, it has granted options to issue equity shares as at that date. In respect of such options, 1,00,000 shares are considered to be the shares issued for no consideration. There are no changes in income or

expenses that are expected from the issue of equity shares on exercise of these options.

Calculate Basic and Diluted EPS for XYZ Limited for separate financial statements and for the Group.

AS 22

16. ABC Ltd. prepares its accounts annually on 31st March. On 1st April, 2022, it purchases a machine at a cost of ₹ 1,50,000. The machine has a useful life of three years and an expected scrap value of zero. Although it is eligible for a 100% first year depreciation allowance for tax purposes, the straight line method is considered appropriate for accounting purposes. ABC Ltd. has profits before depreciation and taxes of ₹ 2,00,000 each year and corporate tax rate is 40 percent each year.

    The purchase of machine at a cost of ₹ 1,50,000 in 2022 gives rise to a tax saving of ₹ 60,000. The corporate tax rate has been assumed to be same in each of the three years. Calculate deferred tax and pass necessary journal entries.

    What will be the amount of deferred tax, if the substantively enacted tax rates for 2022, 2023 and 2024 are 40%, 35% and 38% respectively.

AS 23

17. A Ltd. invested ₹ 1,00,000 to acquire 10% stake (Investment I) in B Ltd. and later invested ₹ 3,00,000 to acquire additional 20% (Investment II). The net asset value of the B ltd. at the respective investment dates was ₹ 7,50,000 and ₹ 12,50,000 respectively. Determine whether B Ltd. is an associate of A Ltd. Also, calculate goodwill arising on the acquisition of the associate.

AS 24

18. What are the disclosure and presentation requirements of AS 24 for discontinuing operations?

    Give four examples of activities that do not necessarily satisfy criterion (a) of paragraph 3 of AS 24, but that might do so in combination with other circumstances.

AS 26

19. During 2023-2024, an enterprise incurred costs to develop and produce a routine, low risk computer software product, as follows:

	Amount (₹)
Completion of detailed programme and design (Phase 1)	25,000
Coding and Testing for establishing technical feasibility (Phase 2)	20,000
Other coding costs (Phase 3)	42,000
Testing costs (Phase 4)	12,000
Product masters for training materials (Phase 5)	13,000
Duplication of computer software and training materials, from product masters (2,000 units) (Phase 6)	40,000
Packing the product (1,000 units) (Phase 7)	11,000

After completion of phase 2, it was established that the computer software is technically feasible for the market. What amount should be capitalized as software costs in the books of the company, on the Balance Sheet date?

AS 29

20. During the year, QA Ltd. delivered manufactured products to customer K. The products were faulty and on 1st October, 2023 customer K commenced legal action against the Company claiming damages in respect of losses due to the supply of faulty product. Upon investigating the matter, QA Ltd. discovered that the products were faulty due to defective raw material procured from supplier F. Therefore, on 1st December, 2023, the Company commenced legal action against F claiming damages in respect of the supply of defective raw materials.

QA Ltd. has estimated that it's probability of success of both legal actions, the action of K against QA Ltd. and action of QA Ltd. against F, is very high.

On 1st October, 2023, QA Ltd. has estimated that the damages it would have to pay K would be ₹ 5 crore. This estimate was revised to ₹ 5.2

crore as on 31st March, 2024 and ₹ 5.25 crore as at 15th May, 2024. This case was eventually settled on 1st June, 2022, when the Company paid damages of ₹ 5.3 crore to K.

On 1st December, 2023, QA Ltd. had estimated that it would receive damages of ₹ 3.5 crore from F. This estimate was revised to ₹ 3.6 crore as at 31st March, 2024 and ₹ 3.7 crore as on 15th May, 2024. This case was eventually settled on 1st June, 2022 when F paid ₹ 3.75 crore to QA Ltd. QA Ltd. had, in its financial statements for the year ended 31st March, 2024, provided ₹ 3.6 crore as the financial statements were approved by the Board of Directors on 26th April, 2024.

(i) Whether the Company is required to make provision for the claim from customer K as per applicable AS? If yes, please give the rationale for the same.

(ii) If the answer to (a) above is yes, what is the entry to be passed in the books of account as on 31st March, 2024?

(iii) What will the accounting treatment of the action of QA Ltd. against supplier F as per applicable AS?

SUGGESTED ANSWERS/HINTS

Case Scenario and MCQ

Q. No.		Hints
1.	**(a)**	**(ii)**
	(b)	**(iii)**
	(c)	**(iv)**
	(d)	**(i)**
2.	**(b)**	

Descriptive Question

3. The decision of making provision for non-moving inventories on the basis of technical evaluation does not amount to change in accounting policy. Accounting policy of a company may require that provision for non-moving inventories should be made. The method of estimating the amount of

provision may be changed in case a more prudent estimate can be made. In the given case, considering the total value of inventory, the change in the amount of required provision of non-moving inventory from ₹ 3.5 lakhs to ₹ 2.5 lakhs is also not material. The disclosure can be made for such change in the following lines by way of notes to the accounts in the annual accounts of ABC Ltd. for the year 2023-24:

"The company has provided for non-moving inventories on the basis of technical evaluation unlike preceding years. Had the same method been followed as in the previous year, the profit for the year and the corresponding effect on the year end net assets would have been lower by ₹ 1 lakh."

4. Operating Activities: b, c.

Investing Activities: e, g, h, i.

Financing Activities: a, d, f, j.

Cash Equivalents: k

5. The balance amount of maintenance provision written back to profit and loss account, no longer required due to crash of the helicopters, is not a prior period item because there was no error in the preparation of previous periods' financial statements. The term 'prior period items', as defined in AS 5 (revised) "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies", refer only to income or expenses which arise in the current period as a result of errors or omissions in the preparation of the financial statements of one or more prior periods. The balance amount left in the provision created earlier is not as a result of error in the past. So it will not be considered as prior period item. Such write back of provision is not an ordinary feature of the business, it shall be considered as an extra-ordinary item.

As per paragraph 8 of AS 5, extraordinary items should be disclosed in the Statement of Profit and Loss as a part of net profit or loss for the period. The nature and the amount of each extraordinary item should be separately disclosed in the Statement of Profit and Loss in a manner that its impact on current profit or loss can be perceived. Hence, the amount so written-back (if material) should be disclosed as an extraordinary item as per AS 5 rather than as prior period items.

6.

	₹ in crore
Cost of construction of bridge incurred upto 31.3.2024	4.00
Add: Estimated future cost	6.00
Total estimated cost of construction	10.00
Contract Price (12 crore x 1.05)	12.60 crore

Stage of completion

Percentage of completion till date to total estimated cost of construction

= (4/10)×100 = 40%

Revenue and Profit to be recognized for the year ended 31st March, 2024 as per AS 7:

Proportion of total contract value recognized as revenue

= Contract price x percentage of completion

= ₹ 12.60 crore x 40% = ₹ 5.04 crore

Profit for the year ended 31st March, 2024 = ₹ 5.04 crore – ₹ 4 crore = 1.04 crore.

7. In the given case, Mithya Ltd. concurrently agreed to repurchase the same goods from Satya Ltd. on 1st February, 2024. Also the re-selling price is pre-determined and covers purchasing and holding costs of Satya Ltd. Hence, the transaction between Mithya Ltd. and Satya Ltd. on 1st February, 2024 should be accounted for as financing rather than sale. The resulting cash flow of ₹ 9.60 lakh received by Mithya Ltd., cannot be considered as revenue as per AS 9 "Revenue Recognition".

Journal Entries in the books of Mithya Ltd.

			₹ in lakh	
1.2.2024	Bank Account	Dr.	9.60	

	To Advance from Satya Ltd*.			9.60
	(Being advance received from Satya Ltd. amounting [₹ 8 lakh + 20% of ₹ 8 lakh = 9.60 lakh] under sale and re-purchase agreement)			
31.3.2024	Financing Charges Account	Dr.	0.40	
	To Satya Ltd.			0.40
	(Financing charges for 2 months [(10.80 – 9.60) x 2/6]			
31.3.2024	Profit and Loss Account	Dr.	0.40	
	To Financing Charges Account			0.40
	(Being amount of finance charges transferred to P& L Account)			

8. The new turbine will produce economic benefits to MS Ltd., and the cost is measurable. Hence, the item should be recognised as an asset. The original invoice for the machine did not specify the cost of the turbine; however, the cost of the replacement ₹ 45,00,000 can be used as an indication (usually by discounting) of the likely cost, six years previously.

Statement showing cost of new turbine and machine after 6th year

			₹
Cost of machines recognized on purchase			1,00,00,000
Less: Depreciation charged for 6 years	[(1,00,00,000/ 10) x 6]		(60,00,000)
			40,00,000

* The balance of Satya Ltd.'s account will be disclosed as an advance under the heading liabilities in the balance sheet of Mithya Ltd. as on 31st March, 2024.

Less: Current cost of turbine to be derecognized:			
Cost of Turbine before 6 years	[45,00,000 x {1 / $(1.05)^6$}]	33,57,900	
Less: Depreciation for 6 years	[(33,57,900 / 10) x 6]	(20,14,740)	(13,43,160)
Add: Cost of new turbine to be recognised			45,00,000
Revised carrying amount of machine			71,56,840

9. As per AS 11, 'The Effects of Changes in Foreign Exchange Rates', initial recognition of a foreign currency transaction is done in the reporting currency by applying the exchange rate at the date of the transaction. Accordingly, on 15th January, 2024, the raw material purchased and its creditors will be recorded at US dollar 12,000 × ₹ 68 = ₹ 8,16,000.

Also, on balance sheet date such transaction is reported at closing rate of exchange, hence it will be valued at the closing rate i.e. ₹ 65 per US dollar (USD 12,000 x ₹ 65 = ₹ 7,80,000) at 31st March, 2024, irrespective of the payment made for the same subsequently at lower rate in the next financial year.

The difference of ₹ 3 (65 – 68) per US dollar i.e. ₹ 36,000 (USD 12,000 x ₹ 3) will be shown as an exchange gain in the profit and loss account for the year ended 31st March, 2024 and will not be adjusted against the cost of raw materials.

In the subsequent year on settlement date, the company would recognize or provide in the Profit and Loss account an exchange gain of ₹ 1 per US dollar, i.e. the difference from balance sheet date to the date of settlement between ₹ 65 and ₹ 64 per US dollar i.e. ₹ 12,000.

Hence, the accounting treatment adopted by the Accountant of the company is incorrect i.e. it is not in accordance with the provisions of AS 11.

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

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

Computation of Purchase Consideration

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

11. As per AS 16, "Borrowing costs are interest and other costs incurred by an enterprise in connection with the borrowing of funds". Further, as per para 4 (b) of the standard, "amortization of discounts or premiums relating to borrowings" as a component of borrowing costs. Thus, the borrowing costs comprise the periodic interest payable on the bonds in question and the amount of discount amortised during the period.

Paragraph 6 of the Statement, inter-alia, states that "Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalized as part of the cost of that asset".

Further, paragraph 19 states that "Capitalisation of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete". Thus, only that portion of the amortised discount should be capitalised as part of the cost of a qualifying asset which relates to the period during which acquisition, construction or production of the asset takes place.

Straight line basis

(Amount in ₹)

Years	Interest	Amortisation of discount	Total borrowing costs
Year 1	10,000	3,333	13,333
Year 2	10,000	3,333	13,333
Year 3	10,000	3,334	13,334

In the above case, the amount of borrowing costs capitalized would be ₹ 13,333 in Year 1 and Year 2. The borrowing costs of ₹ 13,334 incurred in Year 3 would be expensed since the asset is ready for its intended use at the end of Year 2.

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

13. These transactions would require disclosure under AS 18 in the standalone financial statements of A Limited. As per paragraph 10 of AS 18, a related party transaction is "a transfer of resources or obligations between related parties, regardless of whether or not a price is charged". In the given situation, there is a transfer of resources from A Limited to its subsidiaries, though no price is charged for the same. Hence, it will constitute as related party transaction and will require disclosure in the financial statements of A Ltd.

14. As per AS 19 on Leases, **unearned finance income** is the difference between (a) the **gross investment** in the lease and (b) the present value of minimum lease payments under a finance lease from the standpoint

of the lessor; and any unguaranteed residual value accruing to the lessor, at the interest rate implicit in the lease.

Where:

(a) **Gross investment** in the lease is the aggregate of (i) minimum lease payments from the stand point of the lessor and (ii) any unguaranteed residual value accruing to the lessor.

Gross investment = Minimum lease payments + Unguaranteed residual value

= [Total lease rent + Guaranteed residual value (GRV)] + Unguaranteed residual value (URV)

= [(₹ 4,00,000 × 5 years) + ₹ 80,000] + ₹ 70,000
= ₹ 21,50,000 (a)

(b) Table showing present value of (i) Minimum lease payments (MLP) and (ii) Unguaranteed residual value (URV).

Year	MLP inclusive of URV ₹	Internal rate of return (Discount factor @ 15%)	Present Value ₹
1	4,00,000	0.8696	3,47,840
2	4,00,000	0.7561	3,02,440
3	4,00,000	0.6575	2,63,000
4	4,00,000	0.5718	2,28,720
5	4,00,000	0.4972	1,98,880
	80,000 (GRV)	0.4972	39,776
	20,80,000		13,80,656 (i)
	70,000 (URV)	0.4972	34,804 (ii)
	21,50,000	(i)+ (ii)	14,15,460(b)

Unearned Finance Income (a) - (b) = ₹ 21,50,000 – ₹ 14,15,460 = ₹ 7,34,540.

15. Computation of earnings per share

Particulars	**Consolidated financial statements**	**Standalone financial statements of XYZ Limited**
Basic earnings/(loss) per share	₹ 8 [40,00,000/5,00,000]	(₹ 40) [2,00,00,000/ 5,00,000]
Diluted earnings/ (loss) per share	₹ 6.66 [40,00,000/ 6,00,000]	(₹ 40) [2,00,00,000/ 5,00,000]

As per paragraph 39 of AS 20 "Potential equity shares should be treated as dilutive when, and only when, their conversion to equity shares would decrease net profit per share from continuing ordinary operations.

In the above case, if the exercise of options was considered for separate financial statements of XYZ Limited, the diluted loss per share would have reduced to ₹ 33.33 [2,00,00,000/6,00,000]. As this is antidilutive, the options would not be treated as potentially dilutive equity shares. Accordingly, in the separate financial statements of XYZ Limited, the Diluted EPS would be same as Basic EPS.

16. If the cost of machine is spread over three years of its life for accounting purposes, the amount of the tax saving should also be spread over the same period as shown below:

Statement of Profit and Loss

(for the three years ending 31st March, 2022, 2023, 2024)

		(₹ in thousand)		
		2022	**2023**	**2024**
	Profit before depreciation and taxes	200	200	200
Less:	Depreciation for accounting purposes	50	50	50
	Profit before taxes	150	150	150
Less:	Tax expense			
	Current tax:			
	0.40 x (200 -150)	20		

	0.40 x 200		80	80
	Deferred tax:			
	Tax effect of timing differences originating during the year leading to DTL			
	0.40 (150-50)	40		
	Tax effect of timing differences reversing during the year			
	0.40 (0-50)	-	(20)	(20)
	Tax expense	60	60	60
	Profit after tax	90	90	90
	Net timing differences	100	50	0
	Deferred tax liability balance	40	20	0

In 2022, the amount of depreciation allowed for tax purposes exceeds the amount of depreciation charged for accounting purpose by ₹ 1,00,000 and, therefore, taxable income is lower than the accounting income. This gives rise to a deferred tax liability of ₹ 40,000. In 2023 and 2024 accounting income is lower than taxable income because the amount of depreciation charged for accounting purposes exceeds the amount of depreciation allowed for tax purposes by ₹ 50,000 each year. Accordingly, deferred tax liability is reduced by ₹ 20,000 each in both the years. As may be seen, tax expense in based on the accounting income of each period.

In 2022, the profit and loss account is debited and deferred tax liability account is credited with the amount of tax on the originating timing difference of ₹ 1,00,000 while in each of the following two years, deferred tax liability account is debited and profit and loss account is credited with the amount of tax on the reversing timing difference of ₹ 50,000.

The following Journal entries will be passed:

Year 2022			
Profit and Loss A/c	Dr.	20,000	

To Current tax A/c (Being the amount of taxes payable for the year 2022 provided for)			20,000
Profit and Loss A/c To Deferred tax liability A/c (Being the deferred tax liability created for originating timing difference of ₹ 1,00,000)	Dr.	40,000	40,000
Year 2023			
Profit and Loss A/c To Current tax A/c (Being the amount of taxes payable for the year 2023 provided for)	Dr.	80,000	80,000
Deferred tax liability A/c To Profit and Loss A/c (Being the deferred tax liability adjusted for reversing timing difference of ₹ 50,000)	Dr.	20,000	20,000
Year 2024			
Profit and Loss A/c To Current tax A/c (Being the amount of taxes payable for the year 2024 provided for)	Dr.	80,000	80,000
Deferred tax liability A/c To Profit and Loss A/c (Being the deferred tax liability adjusted for reversing timing difference of ₹ 50,000)	Dr.	20,000	20,000

Presentation:

In the year 2022, the balance of deferred tax account i.e. ₹ 40,000 would be shown separately from the current tax payable for the year in terms of paragraph 30 of AS 22. In the year 2023, the balance of deferred tax liability account would be ₹ 20,000 and be shown separately from the current tax payable for the year as in year 2022. In year 2024, the balance of deferred tax liability account would be nil.

If the rate of tax changes, it would be necessary for the enterprises to adjust the amount of deferred tax liability carried forward by applying the tax rate that has been enacted or substantively enacted by the balance sheet date on accumulated timing differences at the end of the accounting year

The amount of deferred tax liability would be computed as follows:

The deferred tax liability carried forward each year would appear in the balance sheet as under:

31st March, 2022 = 0.40 (1,00,000) = ₹ 40,000

31st March, 2023 = 0.35 (50,000) = ₹ 17,500

31st March, 20224 = 0.38 (Zero) = ₹ Zero

Accordingly, the amount debited (credited) to the profit and loss account (with corresponding credit or debit to deferred tax liability) for each year would be as under:

31st March, 2022 Debit = ₹ 40,000

31st March, 2023 (Credit) = ₹ (22,500)

31st March, 2024 (Credit) = ₹ (17,500)

17. As per para 3 of AS 23 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. Significant influence may be gained by share ownership, statute or agreement. As regards share ownership, if an investor holds, directly or indirectly through subsidiary(ies), 20% or more of the voting power of the investee, it is presumed that the investor has significant influence, unless it can be clearly demonstrated that this is not the case. In this case, A Ltd. has invested 30 % in B Ltd. so B Ltd. is to be considered as an associate of A Ltd.

The goodwill arising on the acquisition of the associate will be computed as follows:

		₹
Investment I		1,00,000
Share of net assets	(10 percent of ₹ 7,50,000)	(75,000)

Goodwill (A)		25,000
Investment II		3,00,000
Share of net assets	(20 percent of ₹ 12,50,000)	(2,50,000)
Goodwill (B)		50,000
Total goodwill (A + B)		75,000

18. **(i)** An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event (as defined in paragraph 15) occurs:

(a) a description of the discontinuing operation(s);

(b) the business or geographical segment(s) in which it is reported as per AS 17, Segment Reporting;

(c) the date and nature of the initial disclosure event;

(d) the date or period in which the discontinuance is expected to be completed if known or determinable;

(e) the carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;

(f) the amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;

(g) the amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto; and

(h) the amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

(ii) Para 3 of AS 24 "Discontinuing Operations" explains the criteria for determination of discontinuing operations. According to Paragraph 9 of AS 24, examples of activities that do not necessarily

satisfy criterion (a) of paragraph 3, but that might do so in combination with other circumstances, include:

(i) Gradual or evolutionary phasing out of a product line or class of service;

(ii) Discontinuing, even if relatively abruptly, several products within an ongoing line of business;

(iii) Shifting of some production or marketing activities for a particular line of business from one location to another; and

(iv) Closing of a facility to achieve productivity improvements or other cost savings.

An example in relation to consolidated financial statements is selling a subsidiary whose activities are similar to those of the parent or other subsidiaries.

19. As per para 44 of AS 26, costs incurred in creating a computer software product should be charged to research and development expense when incurred until technological feasibility/asset recognition criteria has been established for the product. Technological feasibility/asset recognition criteria have been established upon completion of detailed programme design or working model. In this case, ₹ 45,000 would be recorded as an expense (₹ 25,000 for completion of detailed program design and ₹ 20,000 for coding and testing to establish technological feasibility/asset recognition criteria). Cost incurred from the point of technological feasibility/asset recognition criteria until the time when products costs are incurred are capitalized as software cost (₹ 42,000 + ₹ 12,000 + ₹ 13,000) ₹ 67,000. Duplication of computer software and training materials, from product masters and packing the products are the cost incurred after development phase. Hence, the same shall be expensed off during the year it is incurred.

20. **(i)** Yes, QA Ltd. is required to make provision for the claim from customer K as per AS 29 since the claim is a present obligation as a result of delivery of faulty goods manufactured. Also, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligations. Further, a reliable estimate of ₹ 5.2 crore can be made of the amount of the

obligation while preparing the financial statements as on 31st March, 2024.

(ii) Statement of Profit and Loss A/c Dr. ₹ 5.2 crore

To Current Liability A/c ₹ 5.2 crore

(iii) As per para 30 of AS 29, QA Ltd. shall not recognise a contingent asset. Here the probability of success of legal action is very high but there is no concrete evidence which makes the inflow virtually certain. Hence, it will be considered as contingent asset only and shall not be recognized.