CASE STUDIES ON ACCOUNTING & AUDITING STANDARDS

by

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1) ACCOUNTING STANDARD (AS - 21) :

Balance Sheet as at 31st March, 2003

Liabilities	A Ltd.	B Ltd.	C Ltd.	Assets	A Ltd.	B Ltd.	C Ltd.
Share Capital				Fixed Assets			
(Face Value Rs. 10/-)	5000	2000	1000				
				INVESTMENTS			
Reserve & Surplus	4000	2000	0	In B Ltd. (60%)	1000	0	0
Loans	1000	1000	1000	In C Ltd. (60%)	0	1000	0
CURRENT LIABILITIES				**CURRENT ASSETS**			
Payable to A	0	0	1000	Receivable from A	0	1000	0
Payable to B	1000	0	0	Receivable from C	1000	0	0
Others	1000	1000	2000	Others	5000	2000	2000
				Profit & Loss A/c	0	0	2000
Total (Rs.)	12000	6000	5000	Total (Rs.)	12000	6000	5000

Profit & Loss A/c for the year ending 31st March, 2003

Particulars	A Ltd.	B Ltd.	C Ltd.	Particulars	A Ltd.	B Ltd.	C Ltd.
RAW MATERIAL				**SALES**			
From A	0	2000	1000	To B Ltd.	2000	0	0
From B	0	0	1000	To C Ltd.	1000	1000	0
Others	6000	2000	0	Others	9000	5000	3000
Other Expenses	2000	1000	2000	Net Loss	0	0	1000
Tax - Current	1000	500	0				
Tax - Deferred	1000	200	0				
Net Profit	2000	300	0				
Total (Rs.)	12000	6000	4000	Total (Rs.)	12000	6000	4000

Particulars of Investments in Subsidiaries are as under :

Acquisition by A Ltd. in B Ltd.

Date of Purchase	% of Holding	No. of Shares	Purchase Value	Net Assets of B Ltd.
01.04.1999	30	60	400	2000
01.04.2000	30	60	600	3000

Acquisition by B Ltd. in C Ltd.

Date of Purchase	% of Holding	No. of Shares	Purchase Value	Net Assets of B Ltd.
01.04.2000	60	60	1000	1000

a) Should A Ltd. consolidate the Accounts of C Ltd., as per AS-21? Its effective holding in C Ltd.

b) Compute :

- Goodwill & Capital Reserve
- Minority Interest in Net Assets & Profits/ Losses
- Revenue Reserves & Surplus

c) Can goodwill & capital reserve arising on consolidation of different subsidiaries be set off or not ?

d) C Ltd. has negative net worth and is incurring losses should goodwill on consolidation be amortised / written off?

2) ACCOUNTING STANDARD (AS-22) :

a) What is the tax effect of sale of fixed assets, considering the block of assets approach followed in the Income-Tax Act, 1961 ? Company A has a block of assets with the written down value of Rs.1,00,000 on April 1, 20X1 for tax purposes. The book value of the assets for accounting purposes is also Rs.1,00,000. The assets are depreciated on written down value basis at 25 percent per annum for both accounting and tax purposes. Of the entire block, assets costing Rs.5,000 on April1, 20X1, were sold for Rs.10,000 on March 31, 20X3. Compute the deferred tax asset/ liability assuming tax rate of 40 percent .

b) What is the tax effect of an upward revaluation of fixed assets where the increase in net book value arising on revaluation of fixed assets is credited directly to revaluation reserve as per the requirements of AS-10 and the depreciation is charged on revalued amount ?

c) If there is a huge deferred tax liability arising from difference in book value and tax base of fixed assets and also there is a huge deferred tax asset arising from unabsorbed depreciation or carry forward of losses under tax laws, whether the deferred tax liability and the deferred tax asset can be set off against each other ?

d) If MAT U/s 115 JB is applicable in the current year, would it have any effect on deferred tax assets/ liabilities at the year end ?

e) Under the following situations, what would be the effect on reversible adverse tax differences (deferred tax liabilities) carried forward at the year – end ?

- The assessee is likely to enjoy tax-holiday U/s-80-1A or 80-1B in future years ;
- The assessee is likely to enjoy tax benefits U/s-10A or 10B in future years;

- The assessee is likely to be under MAT situation U/s-115 JB of the Income-Tax Act in future years ;

f) How should the deferred tax assets arising from long-term losses be recognized?

3) AUDITING & ASSURANCE STANDARD (AS-26) :

State True or False :

i) Audit Engagement Letter (AEL) is normally issued by the Auditee,

ii) AEL is not essential for a Company Audit where the object and scope of audit is governed by Statute.

iii) AEL should be sent before the commencement of the engagement.

iv) AEL should include :

a. Obejctive of Audit

b. Management's Responsibility to maintain Accounts

c. Fact that Audit do not cover Frauds & Errors

d. Audit Procedures

e. Manner of Payment of Fees

v) AEL is not required for Branch Audits.

vi) AEL should be issued on Reappointment every year.

vii) Engagements may be changed on the request of the management which provides lower level of assurance.

4) ACCOUNTING STANDARD (AS-26) :

State True or False :

i) AS-26 applies to :

a) Research & Development

b) Intangible Assets for Sale in Ordinary Course

c) Goodwill arising on amalgamation

d) Licenses

e) Motion picture films

f) Exp. on exploration of oil, minerals etc.

g) Soft-wares

h) Expenditure on VRS

ii) Intangible Asset should be recognized irrespective of its future economic benefits to the enterprise ;

iii) Internally generated intangible assets should not be recognized ;

iv) All expenses during development phase of intangible asset arising from development should be recognized ;

v) Intangible asset should be amortised in ten years irrespective of its availability for use.

5) ACCOUNTING STANDARD (AS- 5, 6 & 10);

- M/s XYZ have been the Auditors of My Fertilizer Limited (a govt. company due for divestment) for the past three years and this is their fourth year ;

- During the first year of their audit, Auditor had observed that the company was not capitalizing Machinery Spares in terms of the relevant Accounting Standard ;

- Accordingly, he had qualified his report in respect of non-compliance with the Accounting Standard and Non-provision of depreciation on the spares not capitalised;

- During the year 2002-03 since the company is due to be divested, as per the government instructions in this regard, all the non-compliances with the Accounting Standards have to be removed ;

- Accordingly, the company has decided to comply with the provisions of the Accounting Standard by capitalizing the spares and depreciating the same during the year as per Schedule-XIV to the Companies Act, 1956 ;

Auditor is now faced with the following situation :

a) The company has disclosed the same as a "Change in the accounting policy" in terms of AS-5 quantifying the effect on the current years operations of the Company. Would it amount to a change in accounting policy?

b) The company has calculated the depreciation since the date of purchase and debited the entire amount to the current years P&L. Whether correct?

c) If (b) is correct, should depreciation relating to earlier years be shown as prior period expense?

d) During the year 2003-04 the machinery spares is used and another set of machinery spares is purchased. The cost of new spares be capitalised or be charged to revenue?

6) ACCOUNTING STANDARD (AS-23) :

State True or False :

i) AS 23 implies consolidation of financial statements of Associates in financial statements of a group;

ii) A subsidiary is an associate of holding company ;

iii) Goodwill / Capital Reserve arising on acquisition of interests in associates are shown separately in group financial statements ;

iv) The post acquisition change in the investor's share of net assets of the associate is adjusted from carrying amount of the investment ;

v) AS 23 does not apply to investments in associates acquired and held for sale in near future .

7) (AS–7) (REVISED) :

A Ltd. has entered into a Builder Agreement with the owner of a land for construction of 46 flats during the year 2002-03 ? Although the AS-7 (Revised) is to come into effect in respect of all contracts entered into during accounting periods commencing on or after 01.04.2003, the company intends to apply the AS w.e.f. the current year. Till the previous year the company was following 'Completed Contract Method' of Accounting for circular projects.

The issues to be considered are :-

a) Whether AS-7 (Revised) would apply to the Builders Agrement ? (Para-2 of AS-7)

b) If yes, how 'Percentage of Completion Method' be applied in view of the fact that sale price of unsold completed flats as at the year end cannot be estimated? (Para-21 to Para-30 of AS-7)

c) Does Company have an option of following 'Completed Contract Method' even during the year?

8A) (AS-27) :

A holds 51% in C, and B holds 49% in C, and there is a Joint Venture agreement between A & B for Joint Control over C. Should AS-27 be applicable for A's investment in C ?

8B) ACCOUNTING STANDARD (AS-18) :

a) Where the head of an operating division (e.g. purchase, sales, finance) who is not a member of the board, should he be covered under the "Related Party Relationship"?

b) Whether a non-executive director should be considered as a Related Party?

8C) ACCOUNTING STANDARD (AS-19) :

In the case of a finance lease between two Indian Companies, should the lessor or the lessee record the leased asset in the fixed assets register maintained pursuant to Section 209 of the Companies Act, 1956 ?

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