AS 7

CONSTRUCTION CONTRACTS

Q 1 RTP MAY 2024

The following data is provided for M/s. Raj Construction Co.

(i) Contract Price – ₹ 85 lakhs

(ii) Materials issued – ₹ 21 Lakhs out of which Materials costing ₹ 4 Lakhs is still lying unused.at the end of the period.

(iii) Labour Expenses for workers engaged at site – ₹ 16 Lakhs (out of which ₹1 Lakh is still unpaid)

(iv) Specific Contract Costs = ₹ 5 Lakhs

(v) Sub-Contract Costs for work executed – ₹ 7 Lakhs, Advances paid to Sub-Contractors – ₹ 4 Lakhs

(vi) Further Cost estimated to be incurred to complete the contract –₹ 35 Lakhs

You are required to compute the Percentage of Completion, the Contract Revenue and Cost to be recognized as per AS-7.

Solution

Computation of contract cost

	₹ Lakh	₹ Lakh
Material cost incurred on the contract (net ofclosing stock)	21-4	17
Add: Labour cost incurred on the contract (including outstanding amount)		16
Specified contract cost	given	5
Sub-contract cost (advances should not be considered)		7
Cost incurred (till date)		45
Add: further cost to be incurred		35
Total contract cost		80

Percentage of completion = Cost incurred till date/Estimated total cost

= ₹ 45,00,000/₹ 80,00,000

= 56.25%

Contract revenue and costs to be recognized

Contract revenue (₹ 85,00,000x56.25%) = ₹ 47,81,250

Contract costs = ₹ 45,00,00

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Q 2 RTP NOV 2023

AP Ltd., a construction contractor, undertakes the construction of commercial complex for Kay Ltd. AP Ltd. submitted separate proposals for each of 3 units of commercial complex. A single agreement is entered into between the two parties. The agreement lays down the value of each of the 3 units, i.e. ₹50 Lakh ₹60 Lakh and ₹75 Lakh respectively. Agreement also lays down the completion time for each unit.

Solution

As per AS 7 'Construction Contracts', when a contract covers a number of assets, the construction of each asset should be treated as a separate construction contract when:

(a) separate proposals have been submitted for each asset;

(b) each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and

(c) the costs and revenues of each asset can be identified.

Therefore, AP Ltd. is required to treat construction of each unit as a separate construction contract as the above-mentioned conditions of AS 7 are fulfilled in the given case.

Q 3 RTP MAY 2022

B Ltd. undertook a construction contract for ₹ 50 crores in April, 2020. The cost of construction was initially estimated at ₹ 35 crores. The contract is to be completed in 3 years. While executing the contract, the company estimated that the cost of completion of the contract would be ₹ 53 crores.

Can the company provide for the expected loss in the financial Statements for the year ended 31st March,

2021? Explain.

Solution-

As per para 35 of AS 7 "Construction Contracts", when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately. Therefore, the foreseeable loss of ₹ 3 crores (₹ 53 crores less ₹ 50 crores) should be recognized as an expense immediately in the year ended 31st March, 2021. The amount of loss is determined irrespective of

(i) Whether or not work has commenced on the contract;

(ii) Stage of completion of contract activity; or

(iii) The amount of profits expected to arise on other contracts which are not treated as a single construction contract in accordance provisions of AS 7.

Q 4 MTP 1 NOV 2023

Rajendra undertook a contract ₹ 20,00,000 on an arrangement that 80% of the value of work done, as certified by the architect of the contractee should be paid immediately and that the remaining 20% be retained until the Contract was completed.

In Year 1, the amounts expended were ₹ 8,60,000, the work was certified for ₹ 8,00,000 and 80% of this was paid as agreed. It was estimated that future expenditure to complete the Contract would be ₹ 10,00,000.

In Year 2, the amounts expended were ₹ 4,75,000. Three-fourth of the work under contract was certified as done by December 31st and 80% of this was received accordingly. It was estimated that future expenditure to complete the Contract would be ₹ 4,00,000.

In Year 3, the amounts expended were ₹ 3,10,000 and on June 30th, the whole Contract was completed.

Show how Contract revenue would be recognized in the P & L A/c of Mr. Rajendra each year.

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Solution ₹

Year 1

Actual expenditure	8,60,000
Future estimated expenditure	10,00,000
Total Expenditure	18,60,000

$$\% \text{ of work completed} = \frac{8,60,000}{18,60,000} \times 100 = 46.24\% \text{ (rounded off)}$$

Revenue to be recognized = 20,00,000 x 46.24% = ₹ 9,24,800

Year 2

Actual expenditure	4,75,000
Future Expenditure	4,00,000
Expenditure incurred in Year 1	8,60,000
	17,35,000

$$\% \text{ of work completed} = \frac{4,75,000 \quad 8,60,000}{17,35,000} = 76.95\% \text{ (rounded off)}$$

Revenue to be recognized (cumulative) = 20,00,000 x 76.95%	= 15,39,000
Less: revenue recognized in Year 1	= (9,24,800)
Revenue to be recognized in Year 2	₹ 6,14,200

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Year 3

Whole contract got completed therefore total contract value less revenue recognized up to year 2 will be amount of revenue to be recognized in year 3 i.e. 20,00,000 – 15,39,000 (9,24,800 + 6,14,200) = ₹4,61,000.

Note: Calendar year has been considered as accounting year.

Q5 MTP 2 NOV 2023, MTP MAY 2023

Akar Ltd. signed on 01/04/22, a construction contract for ₹ 1,50,00,000. Following particulars are extracted in respect of contract, for the period ending 31/03/23.

- Materials used ₹ 71,00,000
- Labour charges paid ₹ 36,00,000
- Hire charges of plant ₹ 10,00,000
- Other contract cost incurred ₹ 15,00,000
- Labour charges of ₹ 2,00,000 are still outstanding on 31.3.23.
- It is estimated that by spending further ₹ 33,50,000 the work can be completed in all respect.

You are required to compute profit/loss for the year to be taken to Profit & Loss Account andadditional provision for foreseeable loss to be recognized as per AS 7.

Solution

Statement showing the amount of profit/loss to be taken to Profit and Loss Account andadditional provision for the foreseeable loss as per AS 7

	Cost of Construction	₹	₹
	Material used		71,00,000
	Labour Charges paid	36,00,000	
Add:	Outstanding on 31.03.2023	2,00,000	38,00,000
	Hire Charges of Plant		10,00,000
	Other Contract cost incurred		15,00,000
	Cost incurred upto 31.03.2023		1,34,00,000
Add:	Estimated future cost		33,50,000
	Total Estimated cost of construction		1,67,50,000
	Degree of completion (1,34,00,000/1,67,50,000 x 100)		80%
	Revenue recognized (80% of 1,50,00,000)		1,20,00,000
	Total foreseeable loss (1,67,50,000 – 1,50,00,000)		17,50,000
Less:	Loss for the current year (1,34,00,000 – 1,20,00,000)		14,00,000
	Loss to be provided for		3,50,000

Q6 MAY 2023 EXAM

Fisher Construction Co. obtained a contract for construction of a commercial complex. The following details are available in records of a company for the year ended 31st March, 2023:

Particulars	Amount in lakhs
Total contract price	24000
Work certified	12500
Work not certified	2500
Estimated further cost to completion of work	17500

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Progress payment received	11000
Progress payment to be received	3000

Applying the provisions of AS 7, you are required to compute:

(i) Profit / Loss for the year ended 31st March, 2023.

(ii) Contract work in progress at the end of financial year 2022-2023.

(iii) Revenue to be recognized out of the total contract value.

(iv) Amount due from/ to customers as at the year end.

Solution

	(₹ In lakhs)
(i) Profit or Loss for the year ended 31.03.2023	32,500
Total cost of construction (12,500 + 2,500 + 17,500)Less:	(24,000)
Total contract price	8,500
Total foreseeable loss to be recognized as expense	

According AS 7, when it is probable that total contract costs will exceed total contract revenue; the expected loss should be recognized as an expense immediately.

	(₹ in lakhs)
(ii) Contract work-in-progress i.e. cost incurred to date are ₹ 15,000 lakhs	
Work certified	12,500
Work not certified	2,500
Contract work in progress at the end of 2022-23	15,000

(iii) Proportion of total contract value recognized as revenue:

For this, cost incurred till 31.03.2023 is 46.154% (15,000/32,500 x 100) to total costs of construction.

Therefore, Proportion of total contract value recognized as revenue is

46.154% of ₹ 24,000 lakhs = ₹ 11,076.96 lakhs

Or 46.15% (Approx.) of ₹ 24,000 lakhs = ₹ 11,076 lakhs

(iv) Amount due from/ to customers =

(Contract costs + Recognised profits - Recognised Losses)

- (Progress payments received + Progress payments to be received)

= (15,000 + Nil - 8,500) - (11,000 + 3,000) ₹ in lakhs

= [6,500 - 14,000] ₹ in lakhs

Amount due to customers = ₹ 7,500 lakhs

Q7 RTP MAY 2023

On 1st December, 2021, GR Construction Co. Ltd. undertook a contract to construct abuilding for ₹ 45 lakhs. On 31st March, 2022, the company found that it had already spent ₹ 32.50 lakhs on the construction. Additional cost of completion is estimated at ₹ 15.10 lakhs. What amount should be charged to revenue in the final accounts for the year ended31st March, 2022 as per provisions of AS-7?

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Solution

	₹ in lakhs
Cost of construction incurred till date	32.50
Add: Estimated future cost	15.10
Total estimated cost of construction	47.60

Percentage of completion till date to total estimated cost of construction

= (32.50/47.60) 100 = 68.28%

Proportion of total contract value recognised as revenue for the year ended31st March, 2022 per AS 7 (Revised)

= Contract price x percentage of completion

= ₹ 45 lakh x 68.28% = ₹ 30.73 lakhs.

	(₹ in lakhs)
Total cost of construction	47.60
Less: Total contract price	(45.00)
Total foreseeable loss to be recognized as expense	2.60

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

Q 8 MTP 2 MAY 2023

PRZ & Sons Ltd. are Heavy Engineering contractors specializing in construction of dams. From the records of the company, the following data is available pertaining to year ended31st March, 2023:

	(₹ crore)
Total Contract Price	2,400
Work Certified	1,250
Work pending certification	250
Estimated further cost to completion	1,750
Stage wise payments received	1,100
Progress payments in pipe line	300

Using the given data and applying the relevant Accounting Standard you are required to:

(i) Compute the amount of profit/loss for the year ended 31st March, 2023.

(ii) Arrive at the contract work in progress as at the end of financial year 2022-23.

(iii) Determine the amount of revenue to be recognized out of the total contract value.

(iv) Work out the amount due from/to customers as at year end.

Solution

(i)	Calculation of profit/ loss for the year ended 31st March, 2023	(₹ in crores)
	Total estimated cost of construction (1,250 + 250 + 1,750)	3,250
	Less: Total contract price	(2,400)
	Total foreseeable loss to be recognized as expense	850

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

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(ii)	Contract work-in-progress i.e. cost incurred to date	(₹ in crores)
	Work certified	1,250
	Work not certified	250
		1,500

(iii) **Proportion of total contract value recognised as revenue**

Percentage of completion of contract to total estimated cost of construction

= (1,500 / 3,250) 100 = 46.15%

Revenue to be recognized till date = 46.15% of ₹ 2,400 crores = ₹ 1,107.60 crores.

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

= ₹ [1,500 + Nil – 850 – (1100 + 300)] crores

= ₹ [1,500 – 850 – 1,400] crores

Amount due to customers (shown as liability) = ₹ 750 crores.

Q 9 RTP NOV 2022

On 1st December, 2020, "Sampath" Construction Limited undertook a contract to construct a building for ₹ 108 lakhs. On 31st March, 2021 the company found that it had already spent ₹ 83.99 lakhs on the construction. A prudent estimate of additional cost for completion was ₹ 36.01 lakhs.

You are required to compute the amount of provision for foreseeable loss, which must be made in the Final Accounts for the year ended 31st March, 2021 based on AS 7 "Accounting for Construction Contracts."

Solution

Calculation of foreseeable loss for the year ended 31st March, 2021

(as per AS 7 "Construction Contracts")

	(₹ in lakhs)
Cost incurred till 31st March, 2021	83.99
Prudent estimate of additional cost for completion	36.01
Total cost of construction	120.00
Less: Contract price	(108.00)
Foreseeable loss	12.00

According to AS 7 (Revised 2002) "Construction Contracts", when it is probable that total contract costs will exceed total contract revenue; the expected loss should be recognized as an expense immediately. Therefore, amount of ₹12 lakhs is required to be provided for in the books of Sampath Construction Ltd. for the year ended 31st March, 2021.

Q 10 MTP NOV 2022

On 1st December, 2019, Mahindra Construction Co. Ltd. undertook a contract to construct a building for ₹ 170 lakhs. On 31st March, 2020, the company found that it had already spent ₹ 1,29,98,000 on the construction. Prudent estimate of additional cost for completion was ₹ 64,02,000. Calculatetotal estimated loss on contract and what should be shown in statement of profit and loss account as contract revenue and contract cost in the final accounts for the year ended 31 st March, 2020, as per provision of Accounting Standard 7 (Revised).

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Solution

	₹
Cost incurred till 31st March, 2020	129,98,000
Prudent estimate of additional cost for completion	64,02,000
Total cost of construction	194,00,000
Less: Contract price	(170,00,000)
Total foreseeable loss	24,00,000

As per AS 7 Construction Contracts, when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately. Hence the foreseeable loss of ₹ 24,00,000 should be recognized as an expense immediately in the year ended 31st March 2020.

Contract work in progress = 129,98,000/194,00,000 X 100= 67%

Proportion of contract value recognized as turnover as per AS7

= 67% of ₹ 170,00,000 = ₹ 113,90,000.

Q 11 MTP NOV 2022

The following data is provided for M/s. Raj Construction Co.

(i) Contract Price – ₹ 85 lakhs

(ii) Materials issued – ₹ 21 Lakhs out of which Materials costing ₹ 4 Lakhs is still lying unused.at the end of the period.

(iii) Labour Expenses for workers engaged at site – ₹ 16 Lakhs (out of which ₹ 1 Lakh is still unpaid)

(iv) Specific Contract Costs = ₹ 5 Lakhs

(v) Sub-Contract Costs for work executed – ₹ 7 Lakhs, Advances paid to Suh-Contractors – ₹ 4 Lakh

(vi) Further Cost estimated to be incurred to complete the contract – ₹ 35 Lakhs

You are required to compute the Percentage of Completion, the Contract Revenue and Cost to be recognized as per AS-7.

Solution

Computation of contract cost

	₹ Lakh	₹ Lakh
Material cost incurred on the contract (net of closing stock)	21-4	17
Add: Labour cost incurred on the contract (including outstandingamount)		16
Specified contract cost	given	5
Sub-contract cost (advances should not be considered)		7
Cost incurred (till date)		45
Add: further cost to be incurred		35
Total contract cost		80

Percentage of completion = Cost incurred till date/Estimated total cost

= ₹ 45,00,000/₹ 80,00,000

= 56.25%

Contract revenue and costs to be recognized

Contract revenue (₹ 85,00,000x56.25%) = ₹ 47,81,250

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Contract costs = ₹ 45,00,000

Q 12 MAY 2022 EXAM

Grace Ltd., a firm of contractors provided the following information in respect of a contract for the year ended on 31st March,2022:

Particulars	(₹ in '000)
Fixed Price Contract with an escalation clause	35,000
Work Certified	17,500
Work not Certified (includes ₹ 26,25,000 for materials issued, out ofwhich material lying unused at the end of the period is ₹ 1,40,000) Estimated further cost to completion	3,815
Progress Payment Received	17,325
Payment to be Received	14,000
Escalation in cost is by 8% and accordingly the contract price isincreased by 8%	4,900

From the above information, you are required to:

(i) Compute the contract revenue to be recognized.

(ii) Calculate Profit /Loss for the year ended 31st March,2022 and additional provision for loss to be made, if any, for the year ended 31st March,2022.

Solution

(a) Calculation of total estimated cost of construction

		₹ in thousand
Cost of Contract incurred till date		
Work certified	17,500	
Work not certified (3,815 thousand - 140 thousand)	3,675	21,175
Add: Estimated future cost		17,325
Total estimated cost of construction		38,500
Contract Price (35,000 thousand x 1.08)		37,800

Stage of completion

Percentage of completion till date to total estimated cost of construction = [Cost of workcompleted till date / total estimated cost of the contract] x 100

= [₹ 21,175 thousand / ₹ 38,500 thousand] x 100= 55%

Revenue to be recognized for the year ended 31stMarch, 2022

Proportion of total contract value recognized as revenue = Contract price x percentage ofcompletion = ₹ 37,800 thousand x 55% = ₹ 20,790 thousand

Loss to be recognized for the year ended 31stMarch, 2022

Loss for the year ended 31stMarch, 2022 = Cost incurred till date - Revenue to berecognized for the year ended 31st March, 2022

= ₹ 21,175 thousand - ₹ 20,790 thousand = ₹ 385 thousand

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Provision for loss to be made at the end of 31st March, 2022

		₹ in thousand
Total estimated loss on the contract		
Total estimated cost of the contract	38,500	
Less: Total revised contract price	(37,800)	700
Less: Loss recognized for the year ended 31st March,2022		(385)
Provision for loss to be made at the end of 31st March,2022		315

Q 13 MTP 1 MAY 2022

Sarita Construction Co. obtained a contract for construction of a dam. The following details are available in records of company for the year ended 31st March, 2021:

	₹ In Lakhs
Total Contract Price	12,000
Work Certified	6,250
Work not certified	1,250
Estimated further cost to completion	8,750
Progress payment received	5,500
Progress payment to be received	1,500

Applying the provisions of Accounting Standard 7 "Accounting for Construction Contracts" you are required to compute:

(i) Profit/Loss for the year ended 31st March, 2021.

(ii) Contract work in progress as at end of financial year 2020-21.

(iii) Revenue to be recognized out of the total contract value.

(iv) Amount due from/to customers as at the year end.

Solution

(i)	Loss for the year ended, 31st March, 2021	(₹ in lakhs)
	Amount of foreseeable loss	
	Total cost of construction (6,250 + 1,250 + 8,750)	16,250
	Less: Total contract price	(12,000)
	Total foreseeable loss to be recognised as expense	4,250

According to AS 7, when it is probable that total contract costs will exceed total contract revenue,the expected loss should be recognised as an expense immediately.

Loss for the year ended, 31st March, 2021 amounting ₹ 4,250 will be recognized.

(ii)	Contract work-in-progress as on 31.3.21	(₹ in lakhs)

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	Contract work-in-progress i.e. cost incurred to date are ₹ 7,500 lakhs:	
	Work certified	6,250
	Work not certified	1,250
		7,500

(iii) Proportion of total contract value recognised as revenue

Cost incurred till 31.3.21 is 46.15% (7,500/16,250 100) of total costs of construction.

Proportion of total contract value recognised as revenue:

46.15% of ₹ 12,000 lakhs = ₹ 5,538 lakhs

(iv) Amount due from/to customers at year end

(Contract costs + Recognised profits – Recognised Losses) – (Progress payments received + Progress payments to be received)

= [(7,500 + Nil – 4,250) – (5,500 + 1,500)] ₹ in lakhs = [3,250 – 7,000] ₹ in lakhs

Amount due to customers = ₹ 3,750 lakhs

Q 14 MTP 2 MAY 2022

Bricks Ltd. signed on 01/04/21, a construction contract for ₹ 1,50,00,000. Following particulars are extracted in respect of contract, for the period ending 31/03/22:

- Materials issued ₹ 75,00,000
- Labour charges paid ₹ 36,00,000
- Hire charges of plant ₹ 10,00,000
- Other contract cost incurred ₹ 15,00,000
- Out of material issued, material lying unused at the end of period is ₹ 4,00,000
- Labour charges of ₹ 2,00,000 are still outstanding on 31.3.22.
- It is estimated that by spending further ₹ 33,50,000 (including material unused ₹ 4,00,000), the work can be completed in all respect.

You are required to compute profit/loss to be taken to Profit & Loss Account and additional provision for foreseeable loss as per AS 7.

Solution

Statement showing the amount of profit/loss to be taken to Profit and Loss Account andadditional provision for the foreseeable loss as per AS 7

	Cost of Construction	₹	₹
	Material Issued	75,00,000	
Less:	Unused Material at the end of period	4,00,000	71,00,000
	Labour Charges paid	36,00,000	
Add:	Outstanding on 31.03.2022	2,00,000	38,00,000
	Hire Charges of Plant		10,00,000
	Other Contract cost incurred		15,00,000
	Cost incurred upto 31.03.2022		1,34,00,000
Add:	Estimated future cost		33,50,000
	Total Estimated cost of construction		1,67,50,000

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	Degree of completion (1,34,00,000/1,67,50,000 x 100)	80%
	Revenue recognized (80% of 1,50,00,000)	1,20,00,000
	Total foreseeable loss (1,67,50,000 - 1,50,00,000)	17,50,000
Less:	Loss for the current year (1,34,00,000 - 1,20,00,000)	14,00,000
	Loss to be provided for	3,50,000

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