Paper-16: Advanced Financial Accounting & Reporting

Time Allowed: 3 Hours **Full Marks: 100**

The figures in the margin on the right side indicate full marks.

Working Notes should form part of the answer.

"Whenever necessary, suitable assumptions should be made and indicated in answer by the candidates."

Part A questions are compulsory. Attempt all of them

Part B has seven question. Attempt any five of them

Part A (25 marks)

1. **(a) In each of the cases given below, one out of four alternatives is correct. Indicate the correct answer (= 1 mark)and give workings/reasons briefly in support of your answer (= 1 mark): [10×2=20]**

(i) The records of Win Now Stock Ltd. shows that, Net Profit for the current year is ₹398.40 lakhs, No. of Equity Shares outstanding 200 lakhs, No. of 8% Convertible Debentures of ₹100 each 3 lakhs, All the Debentures are convertible into 10 equity shares, Tax Rate 30%, As per AS 20, Diluted Earnings Per Share will be :

A. ₹ 1.70
B. ₹ 1.76
C. ₹ 1.80
D. None of these

Answer:

A — ₹1.70.

Adjusted Net Profit for the current year (398.40 + 24 - 7.2) = ₹ 391.2 lakhs.
No. of equity shares resulting from conversion of debentures: 30,00,000 Shares.
No. of equity shares used to compute diluted EPS: (2,00,00,000 + 30,00,000) = 230,00,000 Shares.
Diluted earnings per share: (391,20,000/230,00,000) = ₹ 1.70.

(ii) X Ltd. holds 61% of Y Ltd., Y Ltd. holds 51% of W Ltd., Z Ltd. holds 49% of W. Ltd. and 45% shares of Q Ltd. As per AS 18, Related Parties are :

A. X Ltd., Y Ltd. & W Ltd;
B. X Ltd. & Z Ltd;
C. Y Ltd. & Z Ltd;
D. X Ltd. & Y Ltd. only.

Answer: (A) — X Ltd., Y Ltd. & W Ltd.

X Ltd., Y Ltd. & W Ltd. are related to each other. Z Ltd. & W Ltd. and Z Ltd. & Q Ltd. are related to each other by virtue of Associate relationship. However, neither X Ltd. nor Y Ltd. is related to Z Ltd. and vice versa.

(iii) Fast Ltd. has an asset, which is carried in the Balance Sheet on 31.3.2014 at ₹1,200 lakh. As at that date value in use is ₹ 900 lakh. If the net selling price is ₹850 lakh, recoverable amount of the Asset as per AS-28 will be:

A. ₹ 850 lakh
B. ₹ 900 lakh
C. ₹ 300 lakh
D. None of the above

Answer:

B — ₹900 lakh.

Recoverable amount is higher of Value in use ₹900 lakh and net selling price ₹850 lakh.
Recoverable amount = ₹900 lakh.

(iv) A firm obtained a contract for construction of a railway bridge. Following information is available for the year ended 31.3.2014:

Total contract Price = ₹ 3,000 lakhs
Work certified = ₹ 1,600 lakhs
Work not certified = ₹ 920 lakhs
Estimated further cost to completion = ₹ 760 lakhs
Progress payment received = ₹ 1,400 lakhs
What will be the foreseeable loss to be shown in the accounts of 2013-14 as per AS-7?

A. ₹280 lakhs
B. ₹1,120 lakhs
C. ₹200 lakhs
D. None of the above

Answer:

A — ₹280 lakhs.

Total cost of construction ₹(1,600 + 920 + 760)	= ₹3,280 lakhs
Less: Total contract price	₹3,000 lakhs
So, foreseeable loss to be recognised in 2013 – 2014	= ₹280 lakhs

(v) As per records of Popular Ltd. Accounting Profit ₹12,00,000, Book Profit as per MAT ₹7,00,000, Profit as per Income Tax Act ₹1,20,000, Tax Rate 20%, MAT Rate 7.50%. As per AS-22, Deferred Tax Asset/Liability will be :

A. ₹ 2,40,000
B. ₹ 2,16,000
C. ₹ 48,000
D. ₹ 2,68,500

Answer:

B — ₹ 2,16,000.

Tax as per accounting profit 12,00,000 × 20%	= ₹2,40,000

Tax as per Income-tax Profit 1,20,000 × 20% = ₹24,000
Therefore, Deferred Tax liability as on 31.03.2014 = ₹2,40,000 – ₹24,000 = ₹2,16,000.

(vi) Gayatri Ltd. purchased 1,500 shares of Savita Ltd. in December, 2011 at ₹ 100 each and paid brokerage at 1%. In September, 2012 Savita Ltd. issued bonus shares at one share for every three held by the Shareholders. If Gayatri Ltd. sold 1,000 shares in March, 2013 at ₹ 110 per share and paid a brokerage of 1%, what would be the carrying cost of investment in Savita Ltd. after the sale of shares as per AS-13?
A. ₹ 75,750
B. ₹ 41,500
C. ₹ 42,700
D. None of the above

Answer:

A — ₹ 75,750

Cost of acquisition of 1,500 shares : 1,500 x 100	= ₹ 1,50,000
Brokerage paid @ 1 %	= ₹ 1,500
	₹ 1,51,500
Cost of acquisition of 500 bonus shares	NIL
Carrying cost of 2,000 shares in Savita Ltd.	₹ 1,51,500
Weighted average cost of 1,000 shares sold	
(1,51,500 / 2,000) x 1,000	₹ 75,750
Carrying cost of investment in Savita Ltd.	₹ 75,750

(vii) Mittal Ltd. had acquired 75% share of Mitali Ltd. for ₹ 27 lakh. The Net Assets of Mitali Ltd. on the day are ₹ 24 lakh. During the year Mittal Ltd. sold the investment for ₹ 32 lakh and Net Assets of Mitali Ltd. on the date of disposal was ₹ 40 lakh. The Profit/Loss on disposal of this investment to be recognized in consolidated financial statement is
A. Profit ₹ 800 lakh
B. Profit ₹ 200 lakh
C. Loss ₹ 700 lakh
D. Insufficient Information

Answer:

C — Loss ₹ 7.00 lakh

		₹ in Lakh
Proceeds from the sale of investment		32.00
Less: Mittal Ltd."s Share in net Assets (40 lakh x 0.75)		= 30.00
		2.00
Less: Goodwill in the Consolidated Financial Statement		
Cost of Investment	27.00	
Less: Mittal Ltd."s share in net asset on the date		
(24 lakh x 0.75)	18.00	
		9.00
		(7.00)

(viii) The following data apply to a company's defined benefit pension plan for the year:

	Amount (₹)
Fair market value of plan assets (beginning of year)	**20,000**
Fair market value of plan assets	**28,500**
Employer Contribution	**7,000**
Benefit Paid	**5,000**

The actual return on plan assets is:

A. ₹20,000
B. ₹28,500
C. ₹ 8,500
D. ₹ 6,500

Answer:

D — ₹6,500.

The actual return is computed as follows: Amount (₹)

Fair market value of plan assets (end of year)		28,500
Fair market value of plan assets (beginning of year)		20,000
Change in plan assets		8,500
Adjusted for		
Employer contributions	7,000	
Less: Benefit Paid	5,000	2,000
Actual return on plan assets		6,500

(ix) On 1st April, 2013 Good Morning Ltd. offered 100 shares to each of its 500 employees at ₹ 50 per share. The employees are given a month to decide whether or not to accept the offer. The shares issued under the plan (ESPP) 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 dated is ₹60 per share. Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at ₹56 per share.
On 30th April, 2013 400 employees accepted the offer and paid ₹30 per share purchased. Normal value of each share is ₹10.
The amount of expense to be recognised on 2013-2014 is:
A. ₹2,40,000;
B. ₹4,00,000;
C. ₹20,00,000;
D. ₹18,40,000.

Answer:

Fair value of an ESPP = ₹56 - ₹50 = ₹6.00
Number of shares issued = 400 employees X 100 shares / employee= 40,000 shares
Fair value of ESPP which will be recognized as expenses in the year 2013-2014
= 40,000 shares X ₹ 6 = ₹2,40,000

Vesting period = 1 month

Expenses to be recognized on 2013-2014 is ₹ 2,40,000.

(x) Vishal Ltd. uses horses to transport material from one place to another place on hilly area where construction activity is going on. It purchases horses worth ₹1,00,000 for transporting material on 1.4.2013. Useful life of horses was estimated 5 years, therefore company decided to write off depreciation on horses as per Straight Line Method over 5 years. Depreciation for the year 2014 will be:

A. ₹20,000
B. ₹1,00,000
C. NIL
D. None of the above.

Answer:

C — NIL.

As per AS – 6, Depreciation Accounting is not applicable to Live Stock.

(b) 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 buyers. Comment on the valuation of the stocks by the company. [5]

Answer:

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.

Part B (75 marks)

2. HJ Ltd. made an offer to acquire all the Shares of LJ Ltd., to be satisfied by the allotment of 5 Shares in HJ Ltd. at ₹ 25 per Share for every 4 Shares in LJ Ltd. By the date of expiration of the offer, which was on 1.1.2013, Shareholders owning 75% of the Shares LJ Ltd. accepted the offer and the acquisition was effective from that date.

The accounting date of LJ Ltd. was on 31st March in each year, but to conform with HJ Ltd. the accounts were prepared to 30.06.2013, covering the Fifteen Months to the date.
The draft summarized accounts of the Companies on 30.06.2013 which do not include any of Shares in LJ Ltd. were as follows –

Particulars	HJ Ltd. (₹)	LJ Ltd.(₹)
Equity and Liabilities		
(1) Shareholders' Funds:		
(a) Share Capital -Authorised	3,00,000	75,000
- Issued & Fully paid (₹ 10)	1,50,000	60,000
(b) Reserves & Surplus		
- General Reserve	55,000	---
- Profit & Loss A/c	62,000	20,000
(2) Current Liabilities:		
(a) Other Current Liabilities	27,000	7,000
(b) Short Term Provisions		
- Provision for Taxation	33,000	6,000
Total	**3,27,000**	**93,000**
Assets		
(1) Non-Current Assets:		
(a) Fixed Assets - Tangible		
(i) P & M at Cost	50,000	12,000
Less: Depreciation	18,000	3,000
	32,000	9,000
(ii)Freehold Prop,(at cost)	2,00,000	38,000
(b) Non-Current Investments		
(Quoted Invt at Cost)	7,000	-
(2) Current Assets:		
(a) Inventories	32,000	21,000
(b) Trade Receivables - Drs	41,000	17,000
(c)Cash & Cash Equivalents	15,000	8,000
Total	**3,27,000**	**93,000**

Profit & Loss Account - Period ending 30.06.2013

	Particulars	HJ Ltd. (₹)	LJ Ltd.(₹)
	Period	12 Months	15 Months
	Balance brought forward	14,000	12,000
Add:	Profit for the period	80,000	18,000
	Total	94,000	30,000
	Taxation for the period	32,000	6,000
	Interim Dividend paid, 30th Nov 2012	---	4,000
	Balance Carried forward	62,000	20,000
	Total	94,000	30,000

The Directors of HJ Ltd recommended a final dividend of 20% to the Shareholders on register as on 30.06.2013. The Directors of LJ Ltd proposed a final dividend of 12.50% payable on 30.09.2013.

You are required to prepare the Consolidated Balance Sheet of HJ Ltd. and LJ Ltd. as on 30.06.2013. [15]

Answer:

A. Basic Information

Company Status	Dates	Holding Status
Holding Company = HJ Subsidiary = LJ	Acquisition: 01.01.2013 Consolidation: 30.06.2013	Holding Company = 75% Minority Interest = 25%

B. Computation of Purchase Consideration - Cost of Investment in LJ in HJ's books

Particulars	₹
Number of Shares Acquired (75% of 6,000 Shares)	4,500
Exchange Ratio (5 Shares in HJ Ltd for 4 Shares of LJ Ltd)	
Number of Shares issued by HJ Ltd (5/4 x 4,500)	5,625
Issue Price Per Share	25
Total Purchase Consideration (5,625 Shares x ₹ 25 Per Share)	1,40,625
Part of Equity Share Capital (5,625 Shares x ₹ 10 Per Share)	56,250
Part of Securities Premium (5,625 Shares x ₹ 15 Per Share)	84,375

C. Analysis of Profit and Loss Account of LJ Ltd.

Balance on 30.06.2013 ₹ 20,000
Less: Proposed Dividend (₹ 60,000 x 12.5%) ₹ 7,500
Corrected Balance ₹ 12,500

Balance on 01.04.2012 (Preceding B/ Sheet) ₹ 12,000 — Capital Profit
- Group Interest-Pre = 12,000 x 75% = 9,000
- Minority Interest = 12,000 x 25% = 3,000

Profit for 15 Months (01.04.12 to 30.06.13 i.e. upto consolidation) (balancing figure) ₹ 500
- 01.04.12 to 31.12.12: ₹ 500 x 9/15 = ₹ 300 Capital Profit
  - GI-Pre = 300x75% =225
  - MI = 300x25% =75
- 01.03.13 to 30.06.13: ₹ 500 x 6/15 = ₹ 200 Revenue Profit
  - GI-Pre = 200x75% =150
  - MI = 200x25% =50

Total Capital Profits: ₹ 12,000 + 300 = ₹ 12,300, Total Revenue Profits: ₹ 200

D. Consolidation of Balances

Particulars	Total	Minority Interest	Pre-Acquisition	Post Acquisition	
LJ (Holding 75%, Minority 25%)				**Gen. Res.**	**P&L A/c**
Equity Capital	60,000	15,000	45,000		
Profit and Loss A/c	12,500	3,125	9,225		150
Share of Proposed Dividend	7,500	1,875	3,375 7500x(9/15)x75%]		2,250 7,500x(6/15)x75%]
Minority Interest		20,000			
Total [Cr]			57,600	---	2,400
Cost of Investment [Dr.]			(1,40,625)		
Parent's Balances				55,000	62,000
Proposed Dividend [(₹1,50,000x20%)+ New Shares ₹56,250 x 20% x 6/12)]					(35,625)

For Consolidated Balance Sheet		20,000	83,025 (Goodwill)	55,000	28,775

E. Consolidated Balance Sheet of HJ Ltd. and its subsidiary LJ Ltd. as at 30.06.2013

	Particulars as at 30th June	Note	This Year	Prev. Year
I	EQUITY AND LIABILITIES			
(1)	Shareholders' Funds:			
	(a) Share Capital	1	2,06,250	
	(b) Reserves & Surplus	2	1,68,150	
(2)	Minority Interest		20,000	
(3)	Current Liabilities			
	(a) Other Current Liabilities (27,000 + 7,000)		34,000	
	(b) Short Term Provisions	3	74,625	
	Total		5,03,025	
II	ASSETS			
(1)	Non-Current Assets			
	(a) Fixed Assets (i) Tangible Assets	4	2,79,000	
	(ii)Intangible Assets - Goodwill on Consolidation		83,025	
	(b) Non-Current Investments - Quoted at Cost		7,000	
(2)	Current Assets			
	(a) Inventories = 32,000 + 21,000		53,000	
	(b) Trade Receivables = 41,000 + 17,000		58,000	
	(c) Cash & Cash Equivalents = 15,000 + 8,000		23,000	
	Total		5,03,025	

Notes to the Balance Sheet

Note 1: Share Capital

Particulars	This Year	Prev. Year
Authorised: ....Equity Shares of ₹ 10 each		
Issued, Subscribed & Paid up: [₹ 1,50,000 + (5,625 Shares x ₹ 10)] (Of the above, 5,625 Shares were issued for Non-Cash Consideration)	2,06,250	
Total	2,06,250	

Note 2: Reserves and Surplus

Particulars	This Year	Prev. Year
(a) Securities Premium	84,375	
(b) Other Reserves - General Reserve	55,000	
(c) Surplus (Balance in P & L A/c)	28,775	
Total	1,68,150	

Note 3: Short Term Provisions

Particulars	This Year	Prev. Year
(a) Proposed Dividend (HJ)	35,625	
(b) Provision for Taxation (33,000 + 6,000)	39,000	
Total	74,625	

Note 4: Tangible Assets

Particulars	This Year	Prev. Year

(a) Freehold Property (2,00,000 + 38,000) (b) Plant & Machinery (32,000 + 9,000)	2,38,000 41,000	
Total	2,79,000	

3. Sea Fish Ltd. was hugely unsuccessful and had to be reconstructed. For this purpose, Testy Sea Foods Ltd. was incorporated with an Authorised Capital of ₹ 5,00,000 broken into 50,000 Shares of ₹10 each. The Shareholders of Sea Fish Ltd. were to receive 2 shares of ₹10 each credited as ₹ 6 paid for every 3 Shares held. The balance of ₹ 4 was to be paid as to ₹ 2 application and ₹ 2 on allotment.

The Trial Balance of Sea Fish Ltd. on the date of reconstruction was as follows-

Particulars	₹	₹
Share Capital 50,000 Shares of ₹ 10 each, fully paid		**5,00,000**
Patent Rights	**2,50,000**	
Sundry Debtors / Creditors	**1,45,000**	**1,50,000**
Stock	**70,000**	
Cash at Bank	**15,000**	
Preliminary Expenses	**20,000**	
Profit & Loss A/c	**1,50,000**	
Total	**6,50,000**	**6,50,000**

Preferential Creditors amount to ₹20,000 and were to be settled in full in Cash. The Balance amounts due to other Creditors were to be settled as under:

Creditors for ₹ 80,000 — ₹ 50,000 in Cash
Creditors for ₹ 50,000 — ₹ 50,000 in 10% Debentures

Liquidation Expenses amounted to ₹ 3,000 which met by Testy Sea Foods Ltd.
Fractions of Shares in all amounted to 133.33 Shares in terms of Shares of Tasty Sea Foods Ltd. for which cash was paid. The other Shares were duly allotted and all payments due in respect of them received by Testy Sea Foods Ltd.
5,000 of the unissued shares offered, were taken up and paid for in Cash by the General Public.
Close the books of the Sea Fish Ltd. and open the books of Testy Sea Foods Ltd. Give the Balance Sheet of Tasty Sea Foods Ltd. The value of Patent Rights can be adjusted to the required extent. [15]

Answer:

1. Computation of purchase Consideration

Number of Shares outstanding in Sea Fish Ltd.	50,000
Number of Shares to be issued by Testy Sea Foods Ltd.	
Two Shares of Testy Sea Foods Ltd. for three shares of Marsh $2 \times \frac{50,000}{3}$	33,333.33
Hence, Purchase Consideration [33,333.33 Shares × ₹ 6]	₹2,00,000
Issuable by Cash [133.33 Shares × ₹ 6]	₹800
Issuable by Equity Shares [33,200 × ₹6]	**₹1,99,200**

2. Journal Entries in the books of Testy Sea Foods Ltd.

	Particulars		Debit	Credit
1.	Business Purchase A/c	Dr.	2,00,000	
	To Liquidator of Sea Fish Ltd.			2,00,000
	(Being Business of Sea Fish Ltd. purchased for ₹ 2,00,000)			
2.	Patent Rights (Balancing Figure) A/c	Dr.	90,000	
	Stock-in-Trade	Dr.	70,000	
	Cash at Bank	Dr.	15,000	
	Trade Debtors	Dr.	1,45,000	
	To Creditors			1,20,000
	To Business Purchase			2,00,000
	(Being incorporation of Assets and Liabilities of Sea Fish Ltd. and the balance amount adjusted against Patent Rights Account)			
3.	Bank A/c	Dr.	66,400	
	To Share Application money			66,400
	(Being Share Application Money on 33,200 Shares received @ ₹2 per Share)			
4.	Liquidator of Sea Fish Ltd.	Dr.	2,00,000	
	Share Application money	Dr.	66,400	
	To Equity Share Capital			2,65,600
	To Bank			800
	(Being amt due to Liquidator of Sea Fish Ltd. discharged by Issue of Equity Shares of ₹10 each, ₹6 paid up and by Cash and transfer of Share Application money to Share Capital)			
5.	Equity Share Allotment	Dr.	66,400	
	To Equity Share Capital			66,400
	(Being Allotment Money of ₹ 2 per Share due on 33,200 Shares)			
6.	Bank A/c	Dr.	66,400	
	To Equity Share Allotment			66,400
	(Being Share Allotment Money received on 33,200 Shares @ ₹ 2 per Share)			
7.	Sundry Creditors	Dr.	1,20,000	
	To Bank			70,000
	To 10% Debentures			50,000
	(Being amount due to Sundry Creditors settled by payment in Cash and issue of 10% Debentures)			
8.	Patent A/c	Dr.	3,000	
	To Bank			3,000
	(Being expenses of liquidation of Sea Fish Ltd. incurred)			
9.	Bank A/c	Dr.	50,000	
	To Share Application Money			50,000
	(Being application money received on 5,000 Shares at ₹ 10 per Share from Public Issue)			
10.	Share Application Money A/c	Dr.	50,000	
	To Equity Share Capital			50,000
	(Being Shares Application Money transferred to Equity Share Capital)			

3. Computation of cash and Cash Equivalets:

	Particulars	₹	₹
	Opening Balance		15,000
Add:	Share Application Money	66,400	

	Equity Share Allotment Share Application Money	66,400 50,000	1,82,800
Less:	Liquidators Sea Fish Ltd. Payment to Sundry Creditors Liquidation Expenses	(800) (70,000) (3,000)	(73,800)
	Total		**1,24,000**

4. Balance Sheet of Testy Sea Foods Ltd. (after take over)

	Particulars as at 31st March	Note	This Year	Prev. Yr
I	**EQUITY AND LIABILITIES**			
(1)	Shareholders' Funds: Share Capital	**1**	3,82,000	
(2)	Non-Current Liabilities Long Term Borrowings (Debentures)		50,000	
	Total		4,32,000	
II	**ASSETS**			
(1)	**Non-Current Assets**			
(2)	Fixed Assets: - Intangible Assets - Patents (90,000 + 3,000)		93,000	
	Current Assets			
	(a) Inventories		70,000	
	(b) Trade Receivables - Debtors		1,45,000	
	(c) Cash & Cash Equivalents		1,24,000	
	Total		4,32,000	

Notes to the balance Sheet: **Note 1: Share Capital**

Particulars	This Year	Prev. Year
Authorised: 50,000 Equity Shares of ₹ 10 each	5,00,000	
Issued, Subscribed & Paid up: 38,200 Equity Shares of ₹10 each (Of the Above, 33,200 Shares of ₹6 each were issued for Non-Cash Consideration)	3,82,000	
Total	3,82,000	

4. The balance Sheet of NM Traders Ltd. as on 31.12.2012 is as follows –

Equity & Liabilities	₹
(1) Shareholders' Funds:	
(a) Share capital (₹100 each)	
(i) 4,500 Equity Shares	**4,50,000**
(ii) 1,500 6% Preference Shares	**1,50,000**
(b) Reserves & Surplus - P & L Account	**7,50,000**
(2) Non- current Liabilities:	
Long term Borrowings - 5% Debenture	**3,00,000**
(3) Current Liabilities:	
Trade Payable - Sundry creditors	**2,39,250**

Total	18,89,250
Assets	₹
(1) Non-current Assets:	
(a) Fixed Assets:	
(i) Tangible Assets	
- Freehold Properties	3,75,000
- Plant and Machinery	1,50,000
(ii) Intangible Assets – Goodwill	1,50,000
(b) Non-Current Investments(Quoted)	
- Returns 10% on cost	3,00,000
(2) Current Assets:	
(a) Inventories	2,70,000
(b) Trade receivables – debtors	2,99,250
(c) Cash & Cash Equivalents	3,45,000
Total	18,89,250

Profits for the three years 2011, 2012, 2013 after charging the Debenture Interest but before providing for Preference Dividend, were ₹ 2,20,500, ₹ 3,22,500, and ₹ 2,40,000 respectively.

- **Preference Shares are payable on Liquidation.**
- **The Purchaser wants to acquire all the 4,500 Equity Shares.**

- **The price for Equity Shares is to be based on the following assumptions -**

(i) Normal Return of 10% on Net Asset (at revised valuation) attributable to Equity Shares.
(ii) Goodwill to be calculated at 3 times the adjusted average Super Profits of the 3 years referred above.
(iii) Debentures will be redeemed at a discount of 25% prior to the Sale of the Business, and in order to provide fund for this purpose, Investments will be sold out.
(iv) Value of Freehold Property is agreed to be ascertained on the basis 8% return. The current rental value is ₹ 50,400.
(v) A claim of ₹ 8,250 was omitted to be provided in the year 2013.
(vi) Market Value of Quoted Investments was ₹ 3,75,000.
(vii) Non-recurring Profits are to be eliminated. 10% of the Profits for 2012 referred to above arose from a transaction of non-recurring nature.
(viii) A Provision of 5% on Sundry Debtors was made in 2013 is no longer required (the provision when made was taken into account for purpose of Income Tax at 50%)

Prepare a valuation for the Company's Shares (from the point of view of the purchaser) after taking into account the revised values and valuation of Goodwill based on 3 years Purchase of Super Profits based on the Average Profits of the last three years. [15]

Answer:

A. Computation of Future Maintainable Equity Earnings

Particulars	2011	2012	2013
Profit after Tax	2,20,500	3,22,500	2,40,000
Less: Non-recurring Expenditure (10% × 3,22,500)	-	(32,2500)	-
Claims unaccounted , now accounted	-	-	(8,250)
Add: Provision for Bad-debts not required (2,99,250 × 5/95)	-	-	15,750

Less: Tax Provision at 50% on the above (15,750 - 8,250) × 50%	-	-	(3,750)
Adjusted Profit after Tax	2,20,500	2,90,250	2,43,750
Average Profits = $\frac{2,20,500 + 2,90,250 + 2,43,750}{3}$			2,51,500
Add: Interest on Debentures (No Longer receivable) (₹3,00,000×5%×50%) (After Tax)			7,500
Less: Income from Investments (No Longer receivable) (₹3,00,000×5%×50%)(After Tax)			(15,000)
Future Maintainable Profits before Preference Dividend			2,44,000
Less: Preference Dividend			(9,000)
Future Maintainable Equity Earnings			2,35,000

Note:

- Sundry Debtors as per B/s reflects the net balance after deducting 5% provision. Since Net Debtors of ₹2,99,250 reflect 95% of the Total Debtors Amount, Provision = ₹ 2,99,250 x 5/95 = ₹ **15,750.**
- Simple Average is taken due to fluctuating / oscillating trend of profits.

B. Computation of Capital Employed

Particulars	₹	₹
Freehold Property (Capitalisation of Rental Value of ₹ 50,400 at 8%)		6,30,000
Plant & Machinery		1,50,000
Stock		2,70,000
Sundry Debtors = $\frac{₹2,99,250}{(100\% - \text{Provision at } 5\%)}$		3,15,000
Bank [Balance 345 + Investment sale 375 – Debenture Redemption 225)		4,95,000
Total Assets		**18,60,000**
Less: Outside Liabilities (excluding Equity Shareholders' Funds)		
Sundry Creditors [₹ 2,39,250 + Unaccounted Claim of ₹ 8,250]	2,47,500	
Preference Shareholders [Share Capital + Dividend Due]	1,59,000	
Additional Tax Liability due to unaccounted claim & provision written back	3,750	**4,10,250**
Net Worth of Equity Share Holders on B/s date		**14,49,750**

Note:

- Since Normal Return is 10% on the Net Assets' available to Equity Shares (given), Future Maintainable Equity Earnings should be compared with the Expected Equity Earnings. Hence, Net worth of Equity Shareholders (i.e. after deducting Preference Shareholders' dues) is considered.
- Goodwill in the Balance Sheet should not be considered for computing net worth for Goodwill computation.
- Redemption value of debentures = Face Value ₹ 3,00,000 - 25% Discount = ₹ 2,25,000.

C. Computation of Super Profits and Goodwill

Particulars	₹
Future Maintainable Equity Earnings	2,35,000
Less: Normal Earnings = Normal Return x Capital Employed = 10% x 14,49,750	(1,44,975)
Super Profit i.e. Excess Earnings available for Equity Sharholders	**90,025**
Goodwill at 3 years purchase of Super Profits = ₹ 90,025 x 3 years	**2,70,075**

Note: Alternatively, Average Capital Employed can be considered as Proxy for Future Capital Employed to determine normal earnings.

D. Valuation of Shares

Particulars	₹
(a) Net Worth attributable to Equity Holders (calculated above)	14,49,750
(b) Goodwill	2,70,075
(c) Total Net Assets of Equity Shareholders	**17,19,825**
(d) Number of Equity Shares	4,500 shares
(e) Value per Equity Share	**₹ 382.18**

5. (a) P Ltd. own 80% of S and 40% of J. J is Jointly Controlled Entity. Balance Sheet of four Companies as on 31.03.14 are-

(₹ in lakhs)

I. Equity &Liabilities	P	S	J
Share Capital ₹1 equity share	**1,000**	**400**	**800**
Reserves and Surplus – Retained earnings	**3,400**	**3,400**	**3,600**
Trade payables-creditors	**200**	**300**	**250**
Total	**4,600**	**4,100**	**4,650**
II. Assets	**P**	**S**	**J**
Non-current assets – fixed assets	**1,000**	**800**	**1,400**
Non-current Investments			
Investment in S	**800**	**-**	**-**
Investment in J	**600**	**-**	**-**
Current assets	**2,200**	**3,300**	**3,250**
Total	**4,600**	**4,100**	**4,650**

P Ltd acquired Shares in S many years ago when retained earnings of S were ₹520. P Ltd acquired its shares in J at the beginning of the year when retained earnings of J were ₹400. The Balance of Goodwill relating to S had been written off three years ago. The value of Goodwill in J remains unchanged. Prepare the Consolidated Balance Sheet of P Ltd as on 31.03.2014 as per AS-21 and 27. [9]

Answer:

A. Basic Information

Company	**S Ltd.**	**J Ltd.**
Nature	Subsidiary	Jointly Controlled Entity
Nature of Consolidation	Total Consolidation	Proportionate Consolidation
1 Group Interest	80%	40%
Minority Interest	20%	Not Applicable

B. Analysis of Reserves

S Ltd	
DOC 3400	
DOA	DOA to DOC
520	2880
Pre	Post

J Ltd	
DOC 3600	
DOA	DOA to DOC
400	3200
Pre	Post

C. Consolidation of Balances

(Credit balance in Positive. Debit balances in Negative)

Particulars	Minority of S	Invst. in S (Pre Acqn.)	Invst. in 3 (Pre Acqn.)	Retained Profits
Balance as per Balance Sheet	-	(800)	(600)	
Share in Equity Capital	80 [400 × 20%]	320 [400 × 80%]	320 [800 × 40%]	3,400 -
Share in Pre Acquisition Profits	104 [520 × 20%]	416 [520 × 80%]	160 [400 × 40%]	-
Capital Reserve / (Goodwill) Share in Pre Acquisition Value (320 + 320)	-	**(64)**	**(120)**	
Share in Post Acquisition Reserves From S From J [3200 x 40%] Goodwill Adjusted Earlier	 576 [2880 × 20%]	 64		 2304 [2880 × 80%] 1280 (64)
For Consolidated Balance Sheet	**760**	**-**	**(120)**	**6,920**
	Minority Interest		**Goodwill**	**Retained Earnings**

D. Consolidated Balance Sheet of P as on 31.03.2014.

(₹ in lakhs)

	Particulars as at 31st March	Note	This Year	Prev. Yr
I	**EQUITY AND LIABILITIES**			
(1)	**Shareholders' Funds**:			
	(a) Share Capital (1,000 Equity Shares of ₹ 1 each)		1,000	
	(b) Reserves & Surplus Surplus (Balance in P&L A/c)		6,920	
(2)	**Minority Interest**		760	
(3)	**Current Liabilities**			
	Trade Payables Creditors [P 200 + S 300 + J (0.4 × 250)]		600	
	Total		**9,280**	

II	**ASSETS**			
(1)	**Non-Current Assets**			
	(a) Fixed Assets:			
	(i) Tangible Assets [P 1,000 + S 800 + J(0.4 × 1,400)]		2,360	
	(ii) Intangible Assets - Goodwill on Consolidation (120 + 120)		240	
(2)	**Current Assets** = [P 2,200 + S 3,300 + J (0.4 x 3,250)]		6,800	
	Total		**9,280**	

(b)(i) Compute Goodwill if - Future Maintainable Profit before Tax is ₹30 Lakhs; Normal After Tax Rate of Return is 20%; Actual Capital Employed is ₹93 Lakhs and the Tax rate is 30%.

(ii) Compute Goodwill under Annuity Method, based on 3 years purchase of Discounted Super Profits if - Future Maintainable Profit after Tax is ₹30 Lakhs; Normal Pre-tax Rate of Return is 20%; Capital Employed is ₹120 Lakhs; Tax rate is 30% and the Discount Rate is 15%.

[3+3=6]

Answer:

(i)

Particulars	**₹ Lakhs**
(a) Future Maintainable Profits After Tax = FMPBT **Less** 30% Tax = ₹ 30 Lakhs - 30%	21.00
(b) Normal Capital = $\frac{\text{FMPAT}}{\text{Normal Post Tax Rate of Return}} = \frac{\text{`21.00 lakhs}}{20\%}$	105.00
(c) Actual Capital Employed (given)	93.00
(d) Goodwill = (b - c)	**12.00**

(ii)

Particulars	**₹ Lakhs**
(a) Future Maintainable Profits after Tax (given)	30.00
(b) Normal Profit = Actual Capital Employed x Normal Post Tax Rate of Return	16.80
(c) Super Profits = (a - b)	13.20
(d) Annuity Factor for 3 years at 15%	2.283
(e) Goodwill under Annuity Method = Present Value of Super Profits for 3 years = (c x d)	**30.14**

6. (a) Compute EVA of Vikram Ltd. for 3 years from the information given - (in ₹ Lakhs)

Year	**1**	**2**	**3**

Average Capital Employed	₹3,000.00	₹3,500.00	₹4,000.00
Operating Profit before Interest (adjusted for Tax Effect)	₹850.00	₹1,250.00	₹1,600.00
Corporate Income Taxes	₹80.00	₹70.00	₹120.00
Average Debt ÷ Total Capital Employed (in %)	40.00	35.00	13.00
Beta Variant	1.10	1.20	1.30
Risk Free Rate (%)	12.50	12.50	12.50
Equity Risk Premium (%)	10.00	10.00	10.00
Cost of Debt (Post Tax) (%)	19.00	19.00	20.00

[10]

Answer:

EVA Statement of Vikram Ltd.

Particulars	Year 1	Year 2	Year 3
(i) Cost of Equity (K_e) = Risk Free Rate + (Beta x Equity Risk Premium)	12.5 + (1.1 x 10) = 23.50%	12.5 + (1.2 x 10) = 24.50%	12.5 + (1.3 x 10) = 25.50%
(ii) Cost of Debt (K_d) (given)	19.00%	19.00%	20.00%
(iii) Debt-Equity Ratio (Debt=given, Equity is bal. fig)	40% & 60%	35% & 65%	13% & 87%
(iv) WACC = [(K_d) x Debt % + (K_e) x Equity%]	**21.70%** (19 x 40% + 23.50 x 60%)	**22.58%** (19 x 35% + 24.50 x 65%)	**24.79%** (20 x 13% + 25.50 x 87%)
(v) Average Capital Employed (given)	3,000.00	3,500.00	4,000.00
(vi) Capital Charge (Fair Return to Providers of Capital i.e. Average Capital Employed x	₹3,000 x 21.70% = ₹651.00	₹3,500 x 22.58% = ₹790.30	₹4,000 x 24.79% =₹ 991.60
(vii) Operating Profit before Taxes & Interest	**₹850.00**	**₹1,250.00**	**₹1,600.00**
(viii) **Less:** Taxes Paid	₹80.00	₹70.00	₹120.00
(ix) Operating Profit after Taxes (This is the return	₹770.00	₹1,180.00	₹1,480.00
(x) Capital Charge (computed in 6 above)	₹651.00	₹790.30	₹991.60
(xi) Economic Value Added (ix) – (x)	**₹119.00**	**₹389.70**	**₹488.40**
(xii) EVA as a % of Average Capital Employed	**3.96%**	**11.13%**	**12.21%**

(b) From the following details, compute according to Lev and Schwartz (1971) model, the value of human resources of skilled employees group.

(i) Annual average earning of an employee till the retirement age	**₹2,00,000**
(ii) Age of Retirement	**65 years**
(iii) Discount rate	**15%**
(iv) No. of employees in the group	**20**
(v) Average age	**62 years**

[5]

Answer:

Particulars	
(i) Average Annual Earning till retirement	**₹2,00,000**
(ii) Annuity Factor for 3 years at 15%	**2.2832**

(iii) No. of employees	20
(iv) Value of Human Resource of Skilled Employees group (i)×(ii)×(iii)	91,32,800

Note: As the employees are 62 years (Average) , there are 3 more years for them i.e., till 65 years of age to retire. Hence the average earning is discounted for 3 years at 15%.

7. The following abridged Balance Sheet as at 31.03.2013 pertains to Jupiter Ltd. (₹Lakhs)

Equity & Liabilities	₹
(1) Shareholders' Funds:	
(a) Share Capital - Equity Share Capital	
(i) 180 Lakhs Shares of ₹10, fully paid up	1,800
(ii) 90 Lakhs Shares of ₹10, ₹8 paid up	720
(iii) 150 Lakhs Shares of ₹5, fully paid up	750
(b) Reserves & Surplus	5,628
(2) Non-Current Liabilities:	
Long Term Borrowings - Secured Loans	4,500
(3) Current Liabilities:	
(a) Other Current Liabilities	1,242
(b) Short Term Provisions	960
Total	15,600
Assets	
(1) Non-Current Assets:	
(a) Fixed Assets:	
(i) Tangible Assets	11,166
(ii) Intangible Assets - Goodwill	420
(b) Other Non-Current Assets	
- Miscellaneous Expenditure	171
(2) Current Assets:	
(a) Short Term Loans & Advances	943
(b) Other Current Assets	2,900
Total	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 -

- **Intrinsic Value on the basis of Book Values of Assets and Liabilities including Goodwill,**
- **Value per Share on the basis of Dividend Yield. Normal Rate of Dividend in the concerned Industry is 15%, whereas Jupiter Ltd has been paying 20% Dividend for the last four years and is expected to maintain it in the next few years, and**
- **Value per Share on the basis of EPS, For the year ended 31st March, 2013 the Company has earned ₹1,371 Lakhs 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.**

[15]

Answer:

A. Computation of Capital employed **(₹ in Lakhs)**

Particulars	Amount	Amount
Goodwill at Cost Other fixed assets Current Assets Loans and advances		420 11,166 2,900 943
Total assets Less: Outside liabilities Secured loans .' Current liabilities Provisions	 4,500 1,242 960	**15,429** **6,702**
Capital employed attributable to Equity Share Holders		**8,727**

B. Computation of Value per Share under Intrinsic Value Method **(₹ in Lakhs)**

Particulars	Amount
Capital employed as on valuation Date i.e. Balance Sheet Date **Add:** Notional call on shares partly paid up (90 Lakhs shares x ₹ 2 per share)	8,727 180
Net assets available to equity shareholders [A]	**8,907**
Equivalent value of equity share capital (at par value) 180 + 90 Lakhs Shares of ₹ 10 150 Lakhs Shares of ₹ 5	 2,700 750
Face value of equity share capital [B]	**3,450**
Value per share of ₹1 = $\frac{A}{B} = \frac{₹8,907}{₹3,450}$	₹2.58
Value per Share	
₹ 10 Share, fully paid-up = ₹ 10 x ₹ 2.58	**₹ 25.80**
₹ 10 Share, *X* 8 paid-up = ₹ 25.80 **Less** × 2 Unpaid	**₹ 23.80**
₹ 5 Share, fully paid-up = ₹ 5 x ₹ 2.58	**₹ 12.90**

Note: Unpaid amount on partly paid up shares is assumed to be called up in the immediate future.

C. Computation of Value per Share under Dividend Yield Method (₹ in lakhs)

Particulars	
Company's Dividend rate Normal industry dividend	20% **15%**

Value per share	
₹ 10 Shares, fully paid up = $\frac{₹10 \times 20\%}{15\%}$	**₹ 13.33**
₹ 10 Shares, ₹ 8 paid up = $\frac{₹8 \times 20\%}{15\%}$	**₹ 10.67**
₹ 5 Shares, Fully paid up = $\frac{₹5 \times 20\%}{15\%}$	**₹6.67**

Note: Dividend is payable only on the paid up value. Hence under dividend - yield Method, the value per share for different Categories of shares, should be taken on pro- rata basis, as indicated above.

Particulars	₹ in Lakhs
Profit after Tax for the year	1,371
Paid up Equity share capital [1,800+720+750]	**15%**
Company's EPS for a share of ₹1 = $\frac{`1,371}{`3,270}$	**0.42**
Value per share = $\frac{\text{Face Value} \times \text{Company EPS per ₹1}}{\text{Market EPS}}$	
₹ 10 Shares, fully paid up = $\frac{₹10 \times 0.42}{0.20}$	**₹ 21.00**
₹ 10 Shares, ₹ 8 paid up = $\frac{₹8 \times 0.42}{0.20}$	**₹ 16..80**
₹ 5 Shares, fully paid up = $\frac{₹5 \times 0.42}{0.20}$	**₹10.50**

Summary of value per under different methods

Particulars	Intrinsic value method	Dividend yield method	EPS method
₹ 10 Shares, fully paid up	₹25.80	₹13.33	₹21.00
₹ 10 Shares, ₹ 8 paid up	₹23.80	₹10.67	₹16.80
₹ 5 Shares, fully paid up	₹12.90	₹6.67	₹10.50

Note: Under Intrinsic Value / Net Assets Method, the difference between fully and partly paid up share will reflect the uncalled amount. However, under Dividend and EPS methods, the difference between the fully and partly paid up shares will be proportional to the paid up value.

8. Write short notes on any three of the following: [3×5=15]

(a) Treatment of refund of Government grants;

(b) Disclosure requirement as per AS 24 (Discontinuing Operations);

(c) Objections to Segmental Reporting;

(d) "Grant Date" and "Vesting Conditions" as per IFRS-2.

Answer:

(a) Treatment of refund of Government grants:

Answer:

As per AS 12 "Accounting for Government Grants", government grant that becomes refundable should be treated as an extraordinary item. The amount refundable in respect of a government grant related to revenue is applied first against any unamortized deferred credit remaining in respect of the grant. To the extent that the amount refundable exceeds any such deferred credit, or where no deferred credit exists, the amount is charged immediately to profit and loss statement.

The amount refundable in respect of a government grant related to a specific fixed asset is recorded by increasing the book value of the asset or by reducing the capital reserve or the deferred income balance, as appropriate, by the amount refundable.

In the first alternative, *i.e.,* where the book value of the asset is increased, depreciation on the revised book value is provided prospectively over the residual useful life of the asset. Where a grant which is in the nature of promoters' contribution becomes refundable, in part or in full, to the government on non-fulfillment of some specified conditions, the relevant amount recoverable by the government is reduced from the capital reserve.

(b) Disclosures requirement as per AS 24 (Discontinuing Operations):

Initial disclosure event

Information about planned discontinuance must be disclosed in the first set of financial statement immediately after the "initial disclosure event", initial disclosure event is the event out of these two and whichever occurs earlier –

- Entering into an agreement to sell substantially all the assets of the discontinuing operation.
- Approving and announcing of the discontinuance plan.

Presentation and Disclosure

Initial disclosure:

First disclosure after initial disclosure event occurs about the discontinuing operations:
Description of the discontinuing operation.
Business or geographical segments in which it is reported.
Date and nature of initial disclosure event.
Timing of expected completion of discontinuance.
Carrying amount of total assets and liabilities to be disposed of.
Amount of revenue and expense attributable to discontinuing operation.
Amount of pre-tax profit or loss and tax expense attributable to discontinuing operation.
Net cash flows after initial disclosure event occurs about the discontinuing operations.

Other disclosure:

When an enterprise disposes of assets or settles liabilities attributable to a discontinuing operation, the following other informations are also disclosed.

- Amount of gain or loss recognized on the disposal of assets or settlement of liabilities and related income-tax.
- Net selling price from the sale of those net assets for which the enterprise has entered into binding sale agreements and the expected timing thereof and carrying amount of those assets.

(c)Objections to Segmental Reporting:

The possible objections to Segmental Reporting can be enumerated as below:

(i) It is generally felt that Segmental Revenues and Expenses are not distinguishable objectively in many cases. Revenues of a weak product line may be derived only because of the existence of a strong product line. Also many joint costs are only separable arbitrarily.
(ii) Much of segmental results depend on the inter-departmental transfer pricings which are not always logically established.
(iii) Various segments of an enterprise may use common resources which makes it difficult to arrive at a segment wise performance ratio.
(iv) Since the users are not in position to know the proper base for cost allocation, the segment results would be less than meaningful.
(v) The last objection consists of the competitive implications to the firm. Some academics contend that company secrets will be disclosed while others referred to the competitive hardship suffered by some firms if segmented data is required. Suppose that Company X, a small company, has a segment identical to one in Company Y, a huge conglomerate. Company X would have to disclose the segment while Company Y would not because the segment is not considered material to Y's operations.

However, considering the problems of joint cost allocation, often it is suggested to follow a contribution margin approach for reporting segmental results. By this only identifiable costs are deducted from segment revenues and gross segment margins may only be indicated. But for all practical purposes, this becomes a useless exercise when proportion of identifiable cost is insignificant.

(d) "Grant Date" and "Vesting Conditions" as per IFRS-2:

"Grant Date" is the date at which the entity and the employee (or other party providing similar services) agree to share based payment arrangement signifying by shared understanding of the terms and conditions of stock option. The term 'agree' is used in usual sense - there must be 'offer' and ' acceptance'. Therefore, the date on which the entity makes the offer becomes the grant date as 'acceptance' is either by explicit arrangement to which the employees have already agreed to implicit evidenced by commencement of their work.

Vesting Conditions:

These are conditions which are to be satisfied by the counterparty to be entitled to receive cash, other assets or equity instruments of the entity under share based payment arrangement. Examples of vesting conditions:
(i) service condition- an employee should complete a minimum period of service from the grant date;

(ii) performance condition - an employee should achieve a specified sales target or profit target.

However, no vesting condition other than market condition should be taken into account for the purpose of determining fair value of stock option.