Paper 18 – Corporate Financial Reporting

Whenever necessary suitable assumptions may be made and disclosed by way of note.

Working Notes should form part of the answers

Answer all the questions.

1. Answer any two of the following: [2×5]

(a) Differentiate the following items with reference to 'Accounting Standards' (AS applicable in India) and International Financial Reporting Standards (IFRS):
(i) Extra ordinary items

(ii) Contingencies. [5]

Answer:

Accounting Standards applicable in India	International Financial Reporting Standards
Extraordinary Items	
Events or transactions, clearly distinct from the ordinary activities of the entity, which are not expected to recur frequently and regularly, are termed as extra-ordinary items. Disclosure of the nature and amount of such item is required in the income statement to perceive the impact of current and future profits.	IAS 1 prohibits presentation of any items of income or expense as extraordinary.
Contingencies	
Contingent Liabilities are disclosed unless the probability of outflow is remote. Contingent gains are neither recognized nor disclosed.	Unrecognized possible losses and possible gains are disclosed.

(b) What are the need for convergent of AS with IFRS? [5]

Answer:
Convergence of Accounting Standards with IFRS: In general, convergence of Accounting Standards (AS) with International Financial Reporting Standards (IFRS) means to achieve harmony with IFRS. The term convergence can be considered as "to design and maintain national accounting standards in a way that financial statements prepared in accordance with national AS are in convergence with IFRS". IAS I require financial statements to comply with all requirements of IFRS. This does not mean that IFRS should be adopted word by word. The local standard setters can add disclosure requirements or can remove some requirements which do not create non compliance with IFRS. Thus, convergence with IFRS means adoption of IFRS with exceptions wherever necessary.

(c) Explain the difference between the GAAP and IFRS with regards to Cash Flow Statement. [5]

Answer:

Cash Flow Statement

Indian GAAP	IFRS
Mandatory for listed companies and those companies which fall in the category of Level-1 corporate entities.	Mandatory for all entities preparing their financial statements in accordance with IFRS as it is a component of a complete set of financial statements.
AS 3 permits use of "Direct" or "Indirect" method. However, SEBI mandates listed companies to present cash flows from operating activities in a cash flow statement according to the "indirect method" only.	Cash flow from operating activities may be presented using either direct or indirect method. However, IAS 7 encourages entities to report cash flows from operating activities using the direct method.
There is no specific guidance on treatment of bank overdraft by AS 3. In general, bank overdrafts are' treated as financing activities in cash flow statement. However, demand deposits with bank are treated as cash.	Bank borrowings are normally treated as part of financing activities. However, bank overdrafts that are repayable on demand and that form an integral part of an entity's cash management are treated as cash equivalents under IAS 7".
As per AS 3, interest and dividend paid are treated as cash outflow under financing activities and interest and dividend received are treated as cash inflow from investing activities. AS 3 does not provide any option with regard to classification of interest paid or received.	Under IAS 7, interest and dividend, whether received or paid, may be classified as operating or financing activities dependent upon classification which reflects the economic nature of transactions and in a manner consistent from period to period.
In AS 3, the cash flows associated with extraordinary items may be classified as arising from operating, investing or financing activities as appropriate and will be disclosed separately.	IFRS does not classify any item as extraordinary item. Hence, no provision related to cash flows from extra-ordinary item has been discussed in IAS 7.

2. (a) Given below are the summarized Balance Sheets of A Ltd. and T Ltd. as on 31.12.2013. T Ltd. was merged with A Ltd. with effect from 1.1.2014 and the merger was in the nature of purchase.

Summarised Balance Sheets as on 31.12.2013

Equity and Liabilities	A Ltd. ₹	T Ltd. ₹	Assets	A Ltd. ₹	T Ltd. ₹
Share Capital:			Fixed Assets	9,50,000	4,00,000
Equity Shares of ₹10 each	7,00,000	2,50,000	Investments (Non-trade)	2,00,000	50,000
General Reserve	3,50,000	1,20,000	Inventory	1,20,000	50,000
Surplus (P & L A/c)	2,10,000	65,000	Trade receivables	75,000	80,000
Export Profit Reserve	70,000	40,000	Advance Tax	80,000	20,000
12 % Debentures	1,00,000	1,00,000	Cash & Bank Balances	2,75,000	1,30,000
Trade payables	30,000	55,000			
Prov. for Taxation	1,00,000	50,000			
Proposed Dividend	1,40,000	50,000			
	17,10,000	7,30,000		17,00,000	7,30,000

A Ltd. would issue 12% Debentures to discharge the claims of the debenture holders of T Ltd. at par. Non-trade investments of A Ltd. fetched @25% while those of T Ltd. fetched @18%. Profit before of A Ltd. and T Ltd. during 2011, 2012 and 2013 and were as follows:

	A Ltd. ₹	T Ltd. ₹
2011	5,25,000	1,50,000
2012	5,75,000	1,90,000
2013	6,25,000	2,00,000

Goodwill may be calculated on the basis of capitalisation method taking 20% as normal rate of return for profit before tax. Purchase consideration is discharged by A Ltd. on the basis of intrinsic value per share. Prepare Balance Sheet of A Ltd. after merger. [15]

Solution:

Balance Sheet of A Ltd. (after merger with T Ltd.)

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	9,24,000
(b) Reserves and Surplus	2	13,50,960
(2) Non-Current Liabilities		
Long-term borrowings	3	2,00,000
(3) Current Liabilities		
(a) Trade payables	4	85,000
(b) Other Current Liabilities	5	2,90,000
Total		28,49,960
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	6	13,50,000
Intangible assets (Goodwill) [WN1]		3,80,000
(b) Non-current Investments (2,00,000+,50,000)		2,50,000
(c) Other non-current assets	7	40,000
(2) Current assets		
(a) Inventories (1,20,000 + 50,000)		1,70,000
(b) Trade Receivables (75,000 + 80,000)		1,55,000
(c) Cash & Cash equivalents (2,75,000+1,30,000-40)		4,04,960
(d) Other current assets	8	1,00,000
Total		28,49,960

Notes to Accounts

			(₹)	(₹)
1.	**Share Capital**			
	92,400 Equity Shares of ₹10 each [70,000+22,400]			9,24,000
	(Of the above shares, 22,400 shares were issued to the vendors otherwise than cash)			
2.	**Reserves and surplus**			
	General Reserve		3,50,000	
	P&LA/c		2,10,000	
	Securities Premium [22,400 x [40.40-10]		6,80,960	
	Export profit reserve	70,000		
	Add: Balance of T Ltd.	40,000	1,10,000	13,50,960

3.	**Long Term Borrowings**		
	12% Debentures	1,00,000	
	Add: 12% debentures issued at par other than cash	1,00,000	2,00,000
4.	**Trade payables**		
	Trade payables	30,000	
	Add: Taken over	55,000	85,000
5.	**Other Current Liabilities**		
	Provision for Taxation 1,00,000		
	Add: Provision for Taxation of T Ltd. 50,000	1,50,000	
	Proposed dividend*	1,40,000	2,90,000
6.	**Tangible assets**		
	Fixed Assets	9,50,000	
	Add: Taken over	4,00,000	13,50,000
7.	**Other non-current assets**		
	Amalgamation Adjustment A/c [on a/c of export profit reserve]		40,000
8.	**Other current assets**		
	Advance Tax (80,000 + 20,000)		1,00,000

Working Notes

(1) Valuation of Goodwill

(i) Capital Employed

	₹	A Ltd. ₹	₹	T Ltd. ₹
-Assets as per Balance Sheet		17,00,000		7,30,000
Less: Non-trade Investment		(2,00,000)		(50,000)
Net Assets to be considered for G/W		15,00,000		6,80,000
Less: Liabilities				
12% Debentures	1,00,000		1,00,000	
Trade payables	30,000		55,000	
Provision for Taxation	1,00,000	(2,30,000)	50,000	(2,05,000)
Capital Employed		12,70,000		4,75,000

* It is assumed that the amount of proposed dividend has already been declared.

(ii) Average Profit Before Tax

		A Ltd. ₹		T Ltd. ₹
2011		5,25,000		1,50,000
2012		5,75,000		1,90,000
2013		6,25,000		2,00,000
		17,25,000		5,40,000
Simple Average		5,75,000		1,80,000
Less: Non-trading income*		(50,000)		(9,000)
		5,25,000		1,71,000
(iii) Goodwill Capitalised value of average profit	$\frac{5,25,000}{20}$ x100	26,25,000	$\frac{1,71,000}{20}$ x100	8,55,000
Less. Capital Employed [From (i)above]		(12,70,000)		(4,75,000)
Goodwill		13,55,000		3,80,000

* For A Ltd. (2,00,000 @ 25 %) and T Ltd. (50,000 @ 18 %)

(2) Intrinsic Value per Share

		A Ltd. ₹		T Ltd. ₹
Goodwill [WN 1]	13,55,000		3,80,000	
Other Assets	17,00,000	30,55,000	7,30,000	11,10,000
Less: Liabilities				
12% Debentures	1,00,000		1,00,000	
Trade payables	30,000		55,000	
Provision for Tax	1,00,000	(2,30,000)	50,000	(2,05,000)
Net Assets		28,25,000		9,05,000
Intrinsic value per share [Net Assets / No. of Shares]		28,25,000 / 70,000 =₹ 40.40 (rounded off)		9,05,000 / 25,000 =₹ 36.20

(3) Purchase Consideration & discharge

Intrinsic Value of T Ltd. [a]	36.20 per share
No. of shares [b]	25,000
Purchase Consideration c= [a x b]	₹ 9,05,000
Intrinsic Value of A Ltd. [d]	₹ 40.40 per share
No. of shares to be issued [c / d]	22,400.99
No. of shares to be issued [rounded off]	22,400.00
Cash for fractions	₹ 40 [₹ 9,05,000-(22,400x40.40)]

OR,

(b) The following are the summarized Balance Sheets of X Ltd and Y Ltd as on 31st December 2013.

(Amount in ₹)

Equity and Liabilities	X Ltd	Y Ltd	Assets	X Ltd	Y Ltd
(1) Shareholders' Funds:			**(1) Non-Current Assets:**		
(a) Share Capital			**(a) Fixed Assets**	**7,00,000**	**5,00,000**
(i)Equity Shares of ₹10 each	**6,00,000**	**6,00,000**	**(b)Non-Current Investments**		
(ii)10% Pref. Shares of ₹10 each	**2,00,000**	**2,00,000**	**(i)6,000 Shares of Y Ltd**	**80,000**	
			(ii)10,000 Shares of X Ltd		**1,60,000**
(b) Reserves & Surplus	**3,00,000**	**4,00,000**	**(2) Current Assets:**		
(2) Non-Current Liabilities:			**(a) Inventories**	**2,40,000**	**6,40,000**
- Long Term Borrowings (12% Debentures)	**2,00,000**	**3,00,000**	**(b) Trade Receivables**		
			(i) Debtors	**3,60,000**	**3,80,000**
(3) Current Liabilities:			**(ii) Bills Receivable**	**60,000**	**40,000**
- Trade Payables			**(c)Cash & Cash Equivalents**	**1,10,000**	**80,000**
(i) Sundry Creditors	**2,20,000**	**2,50,000**			
(ii) Bills Payable	**30,000**	**50,000**			
Total	**15,50,000**	**18,00,000**	**Total**	**15,50,000**	**18,00,000**

Fixed Assets of both the Companies are to be revalued at 15% above Book Values and Stock and Debtors are to be taken over at 5% less than their Book Values. Both the Companies are to pay 10%

Equity Dividends, Preference Dividends having been paid already. After the above transactions are given effect to, X Ltd will absorb Y Ltd on the following terms -

(a) 8 Equity Shares of ₹10 each will be issued by X Ltd, at par against 6 Shares of Y Ltd.

(b) 10% Preference Share of Y Ltd will be paid off at 10% Discount, by issue of 10% Preference Shares of ₹100 each of X Ltd at par.

(c) 12% Debenture Holders of Y Ltd are to be paid off at a 8% Premium by 12% Debentures in X Ltd, issued at a Discount of 10%.

(d) ₹ 30,000 to be paid by X Ltd to Y Ltd for Liquidation Expenses.

(e) Sundry Creditors of Y Ltd, include ₹20,000 due to X Ltd.

Prepare: (a) Statement of Purchase Consideration payable by X Ltd, (b) Balance Sheet of X Ltd after its absorption of Y Ltd. [15]

Solution:

1. Computation of Purchase Consideration

Equity Shares held by outsiders in Y Ltd = Total Shares 60,000 Less Shares held by X Ltd 6,000	54,000 Shares
Equity Shares to be issued by X Ltd to Outside Shareholders in Y Ltd = 54,000 x 8/6	72,000 Shares
Less: Shares already held by Y Ltd	10,000 Shares
Hence, Balance additional Equity Shares to be issued now by X Ltd	62,000 Shares
To Equity Shareholders of X Ltd i.e. Value of Equity Shares = 62,000 Shares x ₹10 To 10% Preference Shareholders of Y Ltd (₹ 2,00,000 Less 10% Discount) [18,000 10% Preference Shares of X Ltd of ₹10 each at Par)	₹ 6,20,000 ₹ 1,80,000
Total Purchase Consideration	**₹ 8,00,000**

2. Journal Entries in the books of X Ltd

	Particulars		Debit	Credit
1.	Business Purchase	Dr.	8,00,000	
	To Liquidator of Y Ltd			8,00,000
	(Being Business of Y Ltd purchased as a going concern)			
2.	Fixed Assets (5,00,000 + 15% upward revaluation)	Dr.	5,75,000	
	Stock (6,40,000 - 5%)	Dr.	6,08,000	
	Debtors (3,80,000 - 5%)	Dr.	3,61,000	
	Bills Receivable	Dr.	40,000	
	Cash and Bank (80,000-60,000 Dividend Paid+10,000 Dividend received)	Dr.	30,000	
	To Debentureholders A/c (including 8% Premium Payable) (3,00,000 + 8%)			3,24,000
	To Sundry Creditors			2,50,000
	To Bills Payable			50,000
	To Business Purchase			8,00,000
	To Investments in Y Ltd. (cancellation of own invt. on absorption)			80,000
	To Capital Reserve			1,10,000
	(Being Sundry Assets & Liabilities of Y Ltd taken over)			
3.	12% Debentureholders A/c	Dr.	3,24,000	
	Discount on Issue of Debentures	Dr.	36,000	
	To 12% Debentures [3,24,000 ÷ 90%]			3,60,000
	(Being 12% Debentures of Y Ltd taken over at 8% premium, now settled by 13% own debentures at 10% discount)			

4.	Capital Reserve A/c Dr. To Y Ltd (Being Y Ltd's Expenses met and adjusted out of Capital Reserve)	30,000	 30,000
5.	Y Ltd A/c Dr. To Cash / Bank A/c (Being amount due to Y Ltd's for Realisation Expenses settled)	30,000	 30,000
6.	Liquidator of Y Ltd A/c Dr. To Equity Share Capital To 10% Preference Share Capital (Being the settlement of Purchase Consideration to Y Ltd)	8,00,000	 6,20,000 1,80,000
7.	Sundry Creditors A/c Dr. To Sundry Debtors A /c (Being elimination of Inter-Company Owings / Balances)	20,000	 20,000

3. Balance Sheet of X Ltd (after absorption)

	Particulars as at 31st December	Note	This Year	Prev. Yr
I	**Equity and Liabilities**			
(1)	Shareholders' Funds:			
	(a) Share Capital	1	16,00,000	
	(b) Reserves & Surplus	2	4,31,000	
(2)	Non-Current Liabilities			
	Long Term Borrowings - 12% Debentures (2,00,000 + 3,60,000)		5,60,000	
(3)	Current Liabilities			
	Trade Payables (i) Creditors (2,20,000 + 2,50,000 - 20,000)		4,50,000	
	(ii) Bills Payable (30,000 + 50,000)		80,000	
	Total		**31,21,000**	
II	**Assets**			
(1)	Non-Current Assets			
	(a) Fixed Assets: - Tangible Assets (8,05,000 + 5,75,000)		13,80,000	
	(b) Other Non-Current Assets - Misc. Exp. (Discount on issue of Debentures)		36,000	
(2)	Current Assets			
	(a) Inventories (2,40,000 + 6,08,000)		8,48,000	
	(b) Trade Receivables (i) Debtors (3,60,000 + 3,61,000 - 20,000)		7,01,000	
	(ii) Bills Receivable (60,000 + 40,000)		1,00,000	
	(c) Cash & Cash Equivalents (1,10,000+30,000-60,000+6,000-30,000)		56,000	
	Total		**31,21,000**	

Notes to the Balance Sheet

Note 1: Share Capital	This Year	Prev. Year
Authorised: ………………… Equity Shares of ₹ 10 each …………………10% Preference Shares of ₹ 10 each		

Issued, Subscribed & Paid up:		
1,22,000 Equity Shares of ₹10 each (Of the above, 62,000 Equity Shares were issued for non-cash consideration under a scheme of amalgamation)	12,20,000	
38,000 10% Preference Shares of ₹10 each (Of the above, 18,000 Preference Shares were issued for non-cash consideration under a scheme of amalgamation)	3,80,000	
Total	**16,00,000**	

Note 2: Reserves and Surplus			This Year	Prev. Year
(a)	Capital Reserve	(1,10,000 - 30,000)	80,000	
(b)	Revaluation Reserve	(own assets revalued) (7,00,000 x 15%)	1,05,000	
(c)	Other Reserves	(3,00,000 - 60,000 + 6,000)	2,46,000	
	Total		**4,31,000**	

3. (a) As on 30th June, 2012 the draft balance sheets of the companies showed, the following position:

	R Ltd. ₹	K Ltd. ₹	C Ltd. ₹
Fixed assets	**2,70,000**	**60,000**	**70,000**
Investments at cost	**3,20,000**	**1,50,000**	**10,000**
	5,90,000	**2,10,000**	**80,000**
Current assets:			
Inventory	**1,10,480**	**36,840**	**61,760**
Trade Receivables	**2,20,140**	**69,120**	**93,880**
Balances at bank	**2,62,580**	**16,540**	**52,610**
	5,93,200	**1,22,500**	**2,08,250**
Less: Current liabilities:			
Trade payables	**2,24,120**	**73,130**	**78,190**
Taxation	**60,000**	**—**	**22,000**
Proposed dividends	**2,00,000**	**60,000**	**40,000**
	4,84,120	**1,33,130**	**1,40,190**
Net current assets / (liabilities)	**1,09,080**	**(10,630)**	**68,060**
	6,99,080	**1,99,370**	**1,48,060**
Financed by:			
Issued ordinary shares of ₹10 each	**4,00,000**	**1,50,000**	**80,000**
Capital reserve	**1,00,000**	**—**	**23,000**
Revenue reserve	**1,99,080**	**49,370**	**45,060**
	6,99,080	**1,99,370**	**1,48,060**

You also obtain the following information:

(i) K Ltd. acquired 6,800 shares in C Ltd. at ₹22 per share in 2009 when the balance on capital reserve was ₹15,000 and on revenue reserve ₹30,500 consolidated.

(ii) R Ltd. purchased 8,000 shares in K Ltd. in 2009 when the balance on the revenue reserve was ₹40,000. R Ltd. purchased a further 4,000 shares in K Ltd. in 2010 when the balance on the revenue reserve was ₹45,000. R Ltd. held no other investments on 30th June, 2012.

(iii) Proposed dividends from subsidiary companies are included in the figure for Trade Receivables in the accounts of the parent companies.

Prepare the consolidated balance sheet of R Ltd. and its subsidiaries as on 30th June, 2012, together with the consolidation schedules. [15]

Solution:

Consolidated Balance Sheet of R Ltd. as on 30th June, 2012

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	4,00,000
(b) Reserves and Surplus	2	3,20,584
(2) Minority Interest (W.N iv)		65,918
(3) Current Liabilities		
(a) Trade Payables (2,24,120 + 73,130 + 78,190)		3,75,440
(c) Short term Provisions	3	82,000
(b) Other current liabilities	4	2,18,000
Total		**14,61,942**
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
(i) Tangible assets(2,70,000 + 60,000 + 70,000)		4,00,000
(ii) Intangible assets	5	2,09,592
(b) Non-current investment(W.N v)		10,400
(2) Current assets		
(a) Inventories (1,10,480 + 36,840 + 61,760)		2,09,080
(b) Trade Receivables(W.N vi)		3,01,140
(c) Cash & Cash equivalents (2,62,580 + 16,540 + 52,610)		3,31,730
Total		**14,61,942**

Notes to Accounts

			₹
1.	**Share Capital**		
	40,000 equity shares of ₹10 each		4,00,000
2.	**Reserves and Surplus**		
	Revenue Reserve (1,99,080 + 16,064)	2,15,144	
	Capital reserve(1,00,000 + 5,440)	1,05,440	3,20,584
3.	**Short term provisions**		
	Provision for Taxation (60,000 + 22,000)		82,000
4.	**Other current liabilities**		
	Proposed Dividend*		
	Minority Shareholders	18,000	
	Holding Company	2,00,000	2,18,000
5.	**Intangible assets**		
	Goodwill (W.N iii)		2,09,592

* Proposed dividend is shown under current liability assuming that the dividend has already been declared.

Working Notes:

Analysis of profit

(i) C Ltd.

	Capital Profit ₹	Capital Reserve ₹	Revenue Reserve ₹

Capital Reserve in 2009	15,000		
Increase in Capital Reserve		8,000	
Revenue Reserve in 2009	30,500		
Increase in Revenue Reserve			14,560
	45,500	8,000	14,560
Minority Interest 15%	6,825	1,200	2,184
Share of K	38,675	6,800	12,376

(ii) K Ltd.

Revenue Reserve in 2009	40,000		
Increase in Revenue Reserve			9,370
Share in C Ltd,		6,800	12,376
	40,000	6,800	21,746
Minority interest (20%)	8,000	1,360	4,349
	32,000	5,440	17,397
Less: (5,000 x $\frac{4}{15}$) for second acquisition treated as capital	+1,333		-1,333
	33,333		16,064

(iii) Cost of Control / Goodwill

Cost of Investment in C	1,49,600	
Cost of Investment in k	3,20,000	
Less:		4,69,600
Paid up value of shares		
in C	68,000	
in K	1,20,000	
Capital profits in		
C	38,675	
K	33,333	
		2,60,008
Goodwill		2,09,592

(iv) Minority Interest

	(20%) K Ltd.	(15%) C Ltd.
Capital	30,000	12,000
Capital Reserve	1,360	1,200
Revenue Reserve	4,349	2,184
Capital Profit	8,000	6,825
	43,709	22,209

(v) Investment

K Limited	1,50,000	
Less: Cost of C Limited (6,800 x ₹ 22)	(1,49,600)	400
C Limited		10,000
		10,400

(vi) Trade Receivables

R Limited		2,20,140
Less: Dividend from K Limited		(48,000)
		1,72,140
K Limited	69,120	
Less: Dividend from C Limited	(34,000)	35,120
C Limited		93,880
		3,01,140

OR

(b) Given below are the Separate Balance Sheets and Profit and Loss Statements of H Ltd. and its subsidiary S Ltd.:

Separate Balance Sheets of H Ltd. and S Ltd as on 31.3.2012		
	H Ltd. 31.3.2012 (₹ in lacs)	**S Ltd. 31.3.2012 (₹ in lacs)**
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Equity Share capital	**2000**	**1000**
(b) Reserves and Surplus	**12600**	**1838**
(2) Non-current Liabilities		
(a) Long Term Borrowings	**2000**	**2700**
(b) Deferred Tax Liabilities	**600**	**450**
(c) Other Long Term Liabilities	**350**	**300**
(d) Long term provisions	**400**	**300**
(4) Current Liabilities		
(a) Short term Borrowings	**300**	**200**
(b) Trade payables	**120**	**100**
(c) Other Current Liabilities	**370**	**100**
(d) Short term provisions	**340**	**300**
Total	**19080**	**7288**
II. Assets		
(1) Non-current Assets		
(a) Fixed Assets		
(i) Tangible Assets	**6000**	**3000**
(ii) Intangible Assets	**200**	**100**
(iii) Capital Work in Progress	**3000**	**2000**
(b) Non-current Investments	**4000**	**200**
(c) Long term Loans and Advances	**3000**	**200**

(d) Other Non-current Assets	100	200
(2) Current Assets		
(a) Current Investments	500	200
(b) Inventories	450	400
(c) Trade Receivables	200	150
(d) Cash and Cash equivalents	1080	50
(e) Short term Loans and Advances	300	600
(f) Other Current Assets	250	188
Total	19080	7288

Profit and Loss Statement for the year ended on 31.3.2012	₹ in lacs	₹ in lacs
I. Revenue from Operations	11000	5000
II. Other Income	800	200
III. Total Revenue	11800	5200
IV. Expenses	7220	3660
Cost of materials consumed	5500	2400
Purchase of stock-in-trade	300	200
Changes in inventories of finished goods, work in progress and stock in trade	-500	-300
Employee Benefits Expense	1100	800
Finance Costs	200	140
Depreciation and Amortization Expense	320	220
Other Expenses	300	200
V. Profit Before Exceptional and Extraordinary Items and tax	4580	1540
VI. Exceptional Items	50	30
VII. Profit before Extraordinary Items and tax	4630	1570
VIII. Extraordinary items	10	2
IX. Profit before Tax	4620	1568
X. Tax Expense	1386	470
(1) Current tax	220	100
(2) Deferred tax	50	20
XI. Profit/(Loss) for the Period from Continuing Operations	3234	1098
XII. Profit/(Loss) from Discontinuing Operations	0	-80
XIII. Tax Expense of discontinuing operations	0	20
XIV. Profit/(Loss) from Discontinuing Operations (after tax)	0	-60
XV. Profit/(Loss) for the Period	3234	1038

H Ltd. acquired 80% of shares of S Ltd. on 1.4.2011. Balance of reserve and surplus as on the date of acquisition was ₹1000 lacs. H Ltd. paid ₹ 2000 lacs for this acquisition. S Ltd. paid dividend of ₹200 lacs during 2011-12 for the accounting year 2010-11.

As on 31.3.2012 the following inter-company transactions are recorded:

(i) H Ltd. sold goods to S Ltd. amounting to ₹900 lacs which is included in raw materials consumed of S Ltd.
(ii) Trade receivables of H Ltd. include an amount of ₹50 lacs due from S Ltd.
(iii) Non-current and current borrowings of S Ltd. are from H Ltd.

(iv) Finance cost of S Ltd. represents interest on money borrowed from H Ltd.
Applying consolidation procedures explained in AS 21, prepare consolidated financial statements.

[15]

Solution:

Computation of Goodwill

	₹ in lacs	₹ in lacs
Share of net assets acquired on the date of acquisition		
Equity share capital	1000	
Reserves & Surplus	800	
80% thereof		1440
Purchase consideration less dividend adjustment		1840
Goodwill		400

Computation of Minority Interests

	₹ in lacs
20% of share capital	200
20% of pre-acquisition reserve less dividend	160
Share of profit	208
	568

Consolidated Profit and Loss Statement

	₹ in lacs
I. Revenue from Operations	15100
II. Other Income	860
III. Total Revenue	15960
IV. Expenses	9840
Cost of materials consumed	7000
Purchase of stock-in-trade	500
Changes in inventories of finished goods, work in progress and stock in trade	-800
Employee Benefits Expense	1900
Finance Costs	200
Depreciation and Amortization Expense	540
Other Expenses	500
V. Profit Before Exceptional and Extraordinary Items and tax	6120
VI. Exceptional Items	80
VII. Profit before Extraordinary Items and tax	6200
VIII. Extraordinary items	12
IX. Profit before Tax	6188
X. Tax Expense	1856
(1) Current tax	320
(2) Deferred tax	70

XI. Profit/(Loss) for the Period from Continuing Operations	4332
XII. Profit/(Loss) from Discontinuing Operations	-80
XIII. Tax Expense of discontinuing operations	20
XIV. Profit/(Loss) from Discontinuing Operations (after tax)	-60
XV. Profit/(Loss) for the Period	4272
Share of Parent	4064
Minority Interest (20% of ₹1038 lacs)	208

Consolidated Balance Sheet as on 31.3.2012

	₹ in lacs
I. Equity and Liabilities	
(1) Shareholders' Funds	
(a) Equity Share capital	2000
(b) Reserves and Surplus	13430
(c) Money received against share warrant	0
Minority Interest	0
(2) Share Application Money Pending Allotment	568
(3) Non-current Liabilities	
(a) Long Term Borrowings	2000
(b) Deferred Tax Liabilities	1050
(c) Other Long Term Liabilities	650
(d) Long term provisions	700
(4) Current Liabilities	
(a) Short term Borrowings	300
(b) Trade payables	170
(c) Other Current Liabilities	470
(d) Short term provisions	640
Total	**21978**
II. Assets	
(1) Non-current Assets	
(a) Fixed Assets	
(i) Tangible Assets	9000
(ii) Intangible Assets	700
(iii) Capital Work in Progress	5000
(b) Non-current Investments	2360
(c) Long term Loans and Advances	500
(d) Other Non-current Assets	300
(2) Current Assets	
(a) Current Investments	700
(b) Inventories	850
(c) Trade Receivables	300
(d) Cash and Cash equivalents	1130
(e) Short term Loans and Advances	700
(f) Other Current Assets	438

Total	21978

4. (a) S Ltd. is considering buying the business of B Ltd.; the final accounts of which for the last three years were as follows:

Draft Profit and Loss Accounts for the years ended 31st Dec.

	2011	2012	2013
Sales	2,20,000	2,08,000	2,24,000
Less: Material consumed	1,00,000	95,000	1,12,000
Business expenses	80,000	80,000	82,000
Depreciation	12,000	13,000	14,000
Net Profit	28,000	20,000	16,000

Draft Balance Sheets as at 31st Dec.

	2010 ₹	2011 ₹	2012 ₹	2013 ₹
Fixed Assets, at cost	1,00,000	1,20,000	1,40,000	1,80,000
Less: Depreciation	(70,000)	(82,000)	(95,000)	(1,09,000)
	30,000	38,000	45,000	71,000
Inventory-in-trade	16,000	17,000	18,500	21,000
Trade receivables	21,000	24,000	26,000	28,000
Cash in hand and at Bank	32,000	11,000	28,000	13,200
Prepaid Expenses	1,000	500	2,000	1,000
	1,00,000	90,500	1,19,500	1,34,200
Equity Capital	50,000	50,000	70,000	70,000
Securities Premium	—	—	5,000	5,000
General Reserve	16,000	24,000	26,000	42,000
Debentures	20,000	—	—	—
Trade payables	11,000	13,000	14,000	14,000
Accrued Business Expenses	3,000	3,500	4,500	3,200
	1,00,000	90,500	1,19,500	1,34,200

S Ltd. wishes the offer to be based upon trading cash flows rather than book profits. By trading cash flow is meant cash received from Trade receivables less cash paid to Trade payables and for business expenses (excluding depreciation), together with an allowance for average annual expenditure on fixed assets of ₹20,000 per year.

The actual expenditure on fixed assets is to be ignored, as is any cash received or paid out on the issue or redemption of shares or debentures.

S Ltd. wishes the trading cash flow to be calculated for each of the years 2011, 2012 and 2013, and for these to be combined using weighting of 20% for 2011, 30% for 2012 and 40% for 2013 to give an average annual trading cash flow.

S Ltd. considers that the average annual trading cash flow should show a return of 10% on its investment.

You are required to calculate:

(a) the trading cash flow for each of the years 2011, 2012 and 2013;
(b) the weighted average annual trading cash flow
(c) the price which Smith Ltd. should offer for the business. [10]

Solution:

(a) Trading Cash flow of B Ltd.

	2011 ₹	2012 ₹	2013 ₹
Profit earned during the years	28,000	20,000	16,000
Add : Depreciation (As given in P & L Statement)	12,000	13,000	14,000
Increase in Trade payables	2,000	1,000	—
Increase in Accrued Business Expenses	500	1,000	—
Decrease in Prepaid Expenses	500	—	1,000
(A)	43,000	35,000	31,000
Less: increase in Inventory	1,000	1,500	2,500
Increase in Trade receivables	3,000	2,000	2,000
Increase in Prepaid Expenses	—	1,500	—
Decrease in Accrued Business Expenses	—	—	1,300
(B)	4,000	5,000	5,800
Gross Trading Cash flow (A)-(B)	39,000	30,000	25,200
Less: Adjustment for allowance for average expenditure in fixed assets	(20,000)	(20,000)	(20,000)
Trading Cash Flow	19,000	10,000	5,200

b) Weighted average annual trading Cash flow

Year	Trading cash flow	Weight	Weighted Trading Cash flow
2009	19,000	20%	3,800
2010	10,000	30%	3,000
2011	5,200	40%	2,080
Total	**34,200**		8,880

c) Price Smith Ltd, should offer for the business

Return on Investment = 10%

Weighted Average annual cash flow = ₹8,880

Therefore, the price to be offered will be= $\frac{\text{Average Annual Cash Flow}}{\text{Return on Investment}} = \frac{₹8,880}{10\%} =$ ₹88,800.

OR,

(b)(i) The acquiree possesses a show room on operating lease in a prime location of the city @ ₹1 million rent p.a. for a period of 3 years. It is a non- cancellable lease. Its current market value is ₹2 million p.a. But the lease is non- transferable. Should the acquirer recognize any intangible assets? Discount factor: 10%. [5]

Answer:

In the case "the amount by which the lease terms are favourable compares with the terms of current market transactions for the same or similar items is an intangible asset that meet the contractual-legal criterion for recognition of intangibles separately from goodwill, even though the acquirer cannot sell or otherwise transfer the lease contract. An intangible under the title 'operating lease right' may be recognised at the PV of annuity of ₹1 million for 3 years.

Value of intangible = ₹1 million x 2.4869 = ₹2.49 million.

(ii) X Ltd. and Y Ltd. merged together under the following terms and conditions:

All assets and liabilities of Y Ltd. will be transferred to X Ltd. and such assets and liabilities will be presented in the financial statements of X Ltd. After merger, X Ltd. will rename as XY Ltd. Y Ltd. has 100 million equity shares of ₹10 each of which X Ltd. holds 20% of shares. 9% of the shareholders objected to this merger. Their claims are discharged paying cash at 6 months average price. Claims of other equity shareholders were discharged by issuance of shares of X Ltd. However, debentures of ₹100 million required to be discharged since the debenture holders did not agree to the merger.

Can this merger be classified as amalgamation in the nature of merger? [5]

Answer:

As per AS 14, amalgamation in the nature of merger is an amalgamation which satisfies all the following conditions.

(i) All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.

(ii) Shareholders holding not less than 90% of the face value of the equity shares of the transferor company (other than the equity shares already held therein, immediately before the amalgamation, by the transferee company or its subsidiaries or their nominees) become equity shareholders of the transferee company by virtue of the amalgamation.

(iii) The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.

(iv) The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company.

(v) No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies.

In the given case, 9% dissenting shareholders works out to be 9/80 i.e. 11.25% of the shareholders other than the acquiring company. Also debenture holders to be paid in cash. Therefore, all the conditions stated above are not satisfied. This amalgamation cannot be classified as amalgamation in the nature of merger.

5. (a) ABC Ltd. grants 1000 employees stock options on 1.4.2010 at ₹40, when the market price is ₹160. The vesting period is 2 ½ years and the maximum exercise period is one year. 300 unvested options lapse on 1.5.2012. 600 options are exercised on 30.6.2013.100 vested options lapse at the end of the exercise period.

Pass necessary journal entries giving suitable narrations. [10]

Solution:

Journal Entries

Date	Particulars	Debit (₹)	Credit (₹)
01.04.2010	Deferred Employees Compensation Expense A/c Dr. To Employee Stock Options Outstanding A/c (Being granting of 1000 Equity Shares under Employees Stock Option Scheme at an issue price of ₹40, against the current market price of ₹160, option valued at ₹120 i.e. difference between the Fair Market Value and the Option Issue Price. Option Cost to be amortized over the vesting period of 2 ½ years)	1,20,000	 1,20,000
31.03.2011	Employee Compensation Expense A/c Dr. To Deferred Employee Compensation Expenses A/c (Being amortization of Employee Compensation Expense i.e. Option Cost to the extent of expense relating to Financial Year 2004-05 = ₹1,20,000 x 1 Year ÷ 2 ½ Years)	48,000	 48,000
31.03.2012	Employee Compensation Expense A/c Dr. To Deferred Employee Compensation Expenses A/c (Being amortization of Employee Compensation Expense i.e. Option Cost to the extent of expense relating to Financial Year 2005-06 = ₹1,20,000 x 1 Year ÷ 2 ½ Years)	48,000	 48,000
01.05.2012	Employee Stock Options Outstanding A/c Dr. To Deferred Employee Compensation Expenses A/c To General Reserve A/c (Being Lapse of 300 unvested Options, to the extent of Employees Compensation Expense amortized (i.e. ₹ 28,800 = ₹ 96,000 x 300 Shares / 1000 Shares), transferred to General Reserve, to the extent not amortized (₹ 7,200 = ₹ 24,000 x 300 Shares /1000 Shares), reversed against Employees Stock Options Outstanding) **[Also See Note]**	36,000	 7,200 28,800
30.09.2012	Employee Compensation Expense A/c Dr. To Deferred Employee Compensation Expenses A/c (Being amortization of Employee Compensation Expense on eligible Unvested Options at the end of vesting period i.e. Option Cost to the extent of expense relating to Financial Year 2006-07 = ₹1,20,000 x y2 Year ÷ 2½ Years x 700 Shares ÷1000 Shares)	16,800	 16,800
30.06.2013	Bank A/c (600 Shares x Exercise Price ₹40) Dr. Employee Stock Option Outstanding A/c Dr. To Paid up Equity Share Capital (600 x 10) To Securities Premium A/c (Being exercise of 600 Options at ₹40 per share. Shares deemed to be issued at Fair Value of ₹120 per Share per ₹10 Share. ₹110 per share transferred to Securities Premium Account)	24,000 72,000	 6,000 90,000

01.10.2013	Employee Stock Options Outstanding A/c Dr. To General Reserve A/c (Being 100 Vested options lapsed at the end of expiry period, balance in Stock Options Outstanding transferred to General Reserve)	12,000	12,000

Note:

1. The above journal entries have been proposed based on the Guidance Note on Accounting for Employee Share Based Payments (2011).
2. **Lapse during Vesting Period:** Under Para 18, lapse of options during the Vesting Period (i.e. between 01.04.2010 to 30.09.2012) should be adjusted cumulatively i.e. accounted for by suitably reducing the amount to be expensed off subsequent to the date of lapsing. In the instant case, option cost amortized already is in excess of the option cost on eligible options. Therefore, the difference is transferred to General Reserve, applying the guidance in Para 22 (i.e. lapse of options after the vesting date)

Lapse after Vesting Date: As per Para 22, lapse of options after the vesting date (during the exercise period), the balance standing to the credit of Stock Options Outstanding should be transferred to General Reserve. In no case, the amount already amortized be written back to the Profit and Loss Account.

OR,

(b)(i) A Mutual Fund raised 100 Lakhs on April 1,2013 by issue of 10 Lakh units of ₹ 10 per unit. The fund invested in several Capital Market instruments to build a portfolio of ₹90 Lakhs. The initial expenses amounted to ₹6 Lakhs. During April, 2013 the fund sold certain securities of Cost ₹38 Lakhs for ₹40 Lakhs and purchased certain other securities for ₹28.20. The fund management expenses for the month amounted to ₹4.50 Lakhs of which ₹0.25 Lakh was in arrears. The dividend earned was ₹1.20 Lakhs. 75% of the realized earnings were distributed. The market value of the portion on 30.04.2013 was ₹101.90 Lakh. Determine NAV per unit. [5]

Solution:

Computation of Net Asset Value

Particulars	₹ in lakhs
Opening Bank Balance (100 - 90 - 6)	4.00
Add: Proceeds from Sale of Securities	40.00
Add: Dividend Received	1.20
Less: Cost of Securities	(28.20)
Less: Fund Management Expenses (4.50 - 0.25)	(4.25)
Less: Capital Gains distributed [75% of (40 - 38)]	(1.50)
Less: Dividends distributed (75% of 1.20)	(0.90)
Closing Bank Balance	**10.35**
Add: Closing Market value of Portfolio	101.90
Less: Arrears of expenses	(0.25)
Closing Net Assets	**112.00**
Net Asset Value (₹112.00 Lakhs ÷ 10,00,000 units)	**11.20 per unit**

(ii) The Capital Structure of Nidhi Ltd is as under:

- **80,00,000 Equity Shares of ₹10 each = ₹ 800 Lakhs**
- **1,00,000 12% Preference Shares of ₹250 each = ₹250 Lakhs**
- **1,00,000 10% Debentures of ₹500 each = ₹500 Lakhs**
- **Term Loan from Bank (at 10%) = ₹450 Lakhs.**

The Company's Profit and Loss Account for the year showed a balance PAT of ₹100 lakhs, after appropriating Equity Dividend at 20%. The Company is in the 30% tax bracket. Treasury Bonds carry 6.5% interest and beta factor for the Company may be taken at 1.5. The long run market rate of return may be taken at 16.5%. Calculate EVA. [5]

Solution:

1. Profit and Loss Statement

Particulars	Computation	₹ in Lakhs
Profit before Interest and Taxes	**Balancing figure**	**509.29**
Less: Interest on Debentures	10% x ₹500 Lakhs	50.00
Interest on Bank Term Loan	10% x ₹450 Lakhs	45.00
Profit before Tax	(₹ 290.00 ÷ 70%)	414.29
Less: Tax at 40%	(₹ 290.00 ÷ 70%) x 30%	124.29
Profit after Tax	**Reverse working**	290.00
Less: Preference Dividend	12% x ₹250 Lakhs	30.00
Residual Earnings for Equity Shareholders	**Reverse working**	260.00
Less: Equity Dividend	20% x ₹ 800 Lakhs	160.00
Net Balance in P & L Account	**Given**	100.00

2. Computation of Cost of Equity: K_e = Risk Free Rate + Beta × (Market Rate - Risk Free Rate)

= 6.5% + [1.5 (16.5% - 6.5%)] = 21.5%.

3. Computation of WACC:

Component	Amount	Ratio	Individual Cost	WACC
Equity	₹ 800 Lakhs	800 ÷2000 = 40.0%	K_e = 21.5%	8.60%
Preference	₹ 250 Lakhs	250 ÷ 2000 = 12.5%	K_p = 12%	1.50%
Debt	₹ 950 Lakhs	950 ÷ 2000 = 47.5%	K_d = Interest x (100 - Tax Rate) = 10% x (100% - 30%) = 7%	3.33%
Total	**₹ 2,000 Lakhs**		K_o =	**13.43%**

4. Computation of EVA:

Particulars	₹ Lakhs
Profit before Interest and Taxes (from WN 1)	509.29
Less: Tax (as computed above)	124.29
Net Operating Profit After Taxes i.e. Return to Providers of Capital	385.00
Less: Capital Charge (Fair Return to providers of Capital)	2,000 x 13.43% = 268.60
Economic Value Added	**116.40**

6. (a)(i) From the following details, compute the total value of human resources of skilled and unskilled group of employees according to Lev and Schwartz (1971) model.

Particulars	Skilled	Unskilled
(i) Annual average earning of an employee till the retirement	₹60,000	₹40,000
(ii) Age of retirement	60 years	60 years
(iii) Discount rate	15%	15%
(iv) No. of employees in the group	30	40
(v) Average age	57 years	58 years

[8]

Solution:

Particulars	Skilled	Unskilled
1. Average Age	57 years	58 years
2. Age of Retirement	60 years	60 years
3. Remaining Period of employment	3 years	2 years
4. Annual Earnings / Employee	60,000	40,000
5. Annuity Factor at 15% for 3 / 2 Years	2.2832	1.6257
6. Value of Employees = Present Value of future earnings of employees = Annual Earnings x Annuity Factor		
(a) Skilled: (60,000 x Annuity Factor at 15% for 3 years)	**₹ 1,36,992**	
(b) Unskilled: (40,000 x Annuity Factor at 15% for 2 years)		**₹ 65,028**
7. No. of employees	**30**	**40**
8. Therefore, total Value of Human Resources	**₹ 41,09,760** (1,36,992 x 30 employees)	**₹ 26,01,120** (65,028 x 40 employees)

Total Value of Human Resources

Skilled	₹ 41,09,760
Unskilled	₹ 26,01,120
Total	**₹67,10,880**

(ii) Explain the disclosure requirement under AS 27 'Financial Reporting of Interest in Joint Ventures'.

[7]

Answer:

Disclosure requirement under AS 27

In separate Financial Statements and CFS

- aggregate amount of contingent liability of the venturer in relation to its interest in the joint venture and share of the venturer in each contingent liability incurred jointly with other venturers.
- Contingent liability that has arisen on account of contingent liability of other venturers.
- Share in contingent liabilities of the joint ventures themselves.
- Aggregate amount of any capital commitment of the venturer and share of the venturer in the capital commitment incurred jointly with other venturers.
- Venturers share of capital commitments of the joint ventures themselves.
- The list of all joint ventures and description of interest in significant joint ventures.
- In its separate financial statements the venturer should disclose the aggregate amount of each assets, liabilities, income and expenses related to interest in jointly controlled entities.

OR,

(b)(i) The following particulars in respect of Stock Options granted by a Company are available.

Grant date	**April 1,2010**
Number of Employees covered	**500**
Number of Options granted per employee	**100**
Fair Value of Option per share on grant date (₹)	**50**

The Vesting Period shall be determined as below:

1. **If the Company earns ₹ 120 Crores or above after taxes in 2010-11, the Options will vest on 31.03.2011.**
2. **If condition (a) is not satisfied but the Company earns ₹ 250 Crores or above after taxes in aggregate in 2010-11 and 2011-12, the Options will vest on 31.03.2012.**
3. **If conditions (a) and (b) are not satisfied but the Company earns ₹ 400 Crores or above after taxes in aggregate in 2010-11, 2011-12 and 2012-13, the Options will vest on 31.03.2013.**

Position on 31.03.2011	**Position on 31.03.2012**
(a) Company earned₹ 115 Crores after taxes in 2010-11 **(b) Company expects to earn ₹ 140 Crores in 2011-12 after taxes** **(c) Expected vesting date: 31.03.2012** **(d) No. of employees expected to be entitled to Option = 474**	**(a) Company earned ₹ 130 Crores after taxes in 2011-12** **(b) Company expects to earn ₹ 160 Crores in 2012-13 after taxes** **(c) Expected vesting date: 31.03.2013** **(d) No. of employees expected to be entitled to Option = 465**
Position on 31.03.2013 **(a) The Company earned ₹ 165 Crores after taxes in 2012-13** **(b) No. of employees on whom Option actually vested = 450**	

Compute the expenses to recognize in each year. [10]

Solution:

1. Year 2010-11

Profit for the Period	₹ 115 Crores
Therefore, Option will vest on	31.03.2012
Hence, vesting period is	2 Years
Fair Value of Option per share	₹50
Number of Shares actually vested under the Scheme = [474 Employees x 100 Shares]	47,400
Total Fair Value = 47,400 Shares x ₹50	₹23,70,000
Value of Option recognized as expense in 2010-11 = ₹23,70,000/2	**₹11,85,000**

2. Year 2011-12

Cumulative Profits for 2010-11 and 2011-12 (115 Crores + 130 Crores)	₹ 245 Crores
Therefore, Option will vest on	31.03.2013
Hence, vesting period is	3 Years
Fair Value of Option per share	₹50
Number of Shares expected to vest under the Scheme = 465 Employees x 100 Shares	46,500
Fair Value of Options expected to vest = 46,500 x ₹50	₹ 23,25,000
Cumulative value of Option to recognize as expense for Two Years = (23,25,000 / 3 Years) x 2 Years	15,50,000
Less: Value of Option recognized as expense in 2010-11	(11,85,000)
Value of Option recognized as expense in 2011-12	**₹ 3,65,000**

3. Year 2012-13

Fair Value of Option per share Number of Shares expected to vest under the Scheme = 450 Employees x 100 Shares Total Fair Value of the Options vesting = 45,000 x ₹50 Total Vesting Period	₹50 45,000 ₹ 22,50,000 3 Years
Cumulative value of Option to recognize in 10-11,11-12 and 12-13 **Less:** Value of Option recognized as expense in 10-11 and 11-12	22,50,000 (15,50,000)
Value of Option recognized as expense in 2012-13	**₹7,00,000**

(ii) While closing its books of accounts on 31.03.2013 a Non-Banking Financial Company has its advances classified as follows:

Particulars	₹in Lahks
Standard Assets	**25,200**
Sub-Standard Assets	**2,010**
Secured portion of Doubtful Debts:	
- **Upto one year**	**480**
- **One year to three years**	**135**
- **More than three years**	**45**
Unsecured Portion	**145**
Loss Assets	**72**

Calculate the amount of provision to be made against the advances. [5]

Solution:

Computation of amount of provision

Particulars	Loan ₹ Lakhs	Provision %	Provision ₹ Lakhs
Standard Assets	25,200	0.25%	63.00
Sub-Standard Assets	2,010	10%	201.00
Secured Portion of Doubtful Debts:			
- Upto one year	480	20%	96.00
- One year to three years	135	30%	40.50
- More than three years	45	50%	22.50
Unsecured Portion	145	100%	145.00
Loss Assets	72	100%	72.00
Total			**640.00**

7. (a) From the following summarized Balance Sheet of A Ltd. and its subsidiary B Ltd., prepare a consolidated Balance Sheet as on 31st December, 2011.

Equity and Liabilities	A Ltd.	BLtd.	Assets	A Ltd.	BLtd.
Share Capital			**Sundry Assets**	**1,86,000**	**64,000**
Equity Shares of₹ 10 each	**2,00,000**	**40,000**	**Shares in B Ltd. 1,200**		
Profit on sale of shares	**6,000**		**shares at ₹15 each**	**36,000**	
Profit and Loss A/c					
Brought forward	**12,000**	**14,400**			
For the year	**4,000**	**9,600**			

	2,22,000	64,000		2,22,000	64,000

A Ltd. bought in earlier year 3,200 equity shares in B Ltd. @ 15 when the Profit and Loss Account balance in B Ltd. was ₹8,800. A sold 800 shares @₹22.50, credited the difference between the sale proceeds and cost to 'Profit on sale of investment account' on 30th June, 2009 and crediting the balance to the investment account. Profit during the year accrued uniformly. [10]

Solution:

Consolidated Balance Sheet of A Ltd., and its subsidiary B Ltd. as at 31st December, 2011

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	2,00,000
(b) Reserves and Surplus	2	31,120
(2) Minority Interest (W.N iii)		25,600
Total		2,56,720
II. Assets		
(1) Non-current assets		
Fixed assets		
(i) Tangible assets (1,86,000 + 64,000)		2,50,000
(ii) Intangible assets	3	6,720
Total		2,56,720

Notes to Accounts

			₹
1.	**Share Capital**		
	20,000 equity shares of ₹ 10 each		2,00,000
2.	**Reserves and Surplus**		
	Profit & Loss Account **(W.N** iv)		31,120
3.	**Intangible assets**		
	Goodwill (W.N ii)		6,720

Working Notes:

(i) Analysis of Profit of B Ltd.

	Capital Profit	Revenue Profit
P/L A/c Balance on the date of acquisition	8,800	
Increase in the balance after acquisition (14,400 – 8,800)		5,600
Profit for the year		9,600
	8,800	15,200
Less: Minority Interest (40 per cent)	3,520	6,080
Share of A Ltd	5,280	9,120

(ii) Cost of Control

Cost of Investments		36,000
Less: Paid-up value of shares	24,000	
Share of Capital Profits	5,280	(29,280)
Goodwill		6,720

(iii) Minority Interest (40 per cent)

Paid-up value of shares held	16,000

Share of Capital Profits	3,520
Share of Revenue Profits	6,080
	25,600

(iv) Consolidated Revenue Profit

Balance as per Profit and Loss A/c of A Ltd.	16,000
Add: Profit on sale of shares	6,000
	22,000
Share in Revenue Profit of B Ltd.	9,120
	31,120

(v) Investments in B Ltd.

Particulars	₹	Particulars	₹
To Balance b/d	48,000	By Bank	18,000
To Profit on Sale	6,000	By Balance c/d	36,000
	54,000		54,000

OR,

(b)(i) H Ltd. sold goods to its 100% subsidiary S. Ltd. amounting to ₹1,00,000 - cost ₹1,03,000 which is lying in the godown of S Ltd. at the year end. It is found that market value of such goods is ₹105,000 at the year end and in the normal course of business it is possible to realize only ₹1,05,000. Therefore, inventory was valued at cost by S Ltd. which is ₹1,00,000. For S Ltd. cost remains lower than the net realizable value. While preparing consolidated balance sheet how should H Ltd. eliminate unrealized loss in terms of Paragraph 17, AS 21? [5]

Answer:

Paragraph 17 of AS 21 states that "Unreleased losses resulting from intragroup transactions that are deducted in arriving at the carrying amount of assets are also eliminated unless cost cannot be recovered".

In this case cost of goods lying in the inventory can be recovered, whereas H Ltd. has already booked a loss of ₹3,000 on sale of goods S Ltd. For the purpose of Group accounts, the goods should be shown at cost, i.e. ₹1,03,000 which is lower of the cost and net realizable value. Therefore, while preparing consolidated financial statements ₹3000 should be added to the inventory.

(ii) A Ltd. holds 35% of voting right in B Ltd. But it has been analyzed that—

(a) Majority members of the Board of B Ltd. are representatives of A Ltd. "

(b) 80% of the purchase transactions of B Ltd. are with A Ltd. in a term unfavourable to B Ltd. Market price of the goods purchased is at least 10% less than at what rate the transactions are agreed upon with outside parties.

(c) Another 30% of the voting right of the company are with various financial institutions, which are supporting the existing management to protect their interest.

(d) Another 20% of the voting right are held by X Ltd. and its subsidiaries.

(e) Balance 15% of the voting right are with miscellaneous investors.

Should B Ltd. be treated as a subsidiary of A Ltd.? [5]

Answer:

This is a general management pattern of many group companies in India. Golden shares are held by group companies to keep control over the majority of the Board of Directors. In all these cases proper identification holding - subsidiary relationship is necessary. Section 4 of the Companies Act, 1956 may not provide useful guidance to ascertain 'control' in accounting sense.

There are cases where, a company controls the majority of the composition of the Board of Directors if representatives of the financial institutions are not counted. This creates problem in identifying control although "control" vests with a company with the tacit support of the financial institutions. If it proved that A Ltd. enjoys economic benefit over B Ltd. there remains a strong evidence that there exists control of A Ltd. over B Ltd. even if it does not enjoy more than one-half of the voting power, and it does not have majority representation in the Board of Directors of B Ltd. It is, of course, challenging to identify subsidiaries on the basis of "control over the composition of Board of Directors to obtain economic benefit".

8.(a)(i) Explain the objectives and scope of Indian Government Accounting Standard – 7 'Foreign Currency Transaction and Loss or Gain by Exchange Rate variance. [7]

Answer:

Objective

Government may have foreign currency transactions and loss or gain arising due to exchange rate variations. The objective of this standard is to provide accounting and disclosure requirements of foreign currency transactions and financial effects of exchange rate variations in terms of loss or gain in the financial statements. It also deals with the requirements of disclosure of foreign currency external debts and the rate applied for disclosure.

The principal issues in accounting and reporting for foreign currency transactions are to decide which exchange rate to apply and how to recognise in the financial statements the financial effects of exchange rate variations in terms of loss or gain.

Scope

The Accounting Authority which prepares and presents the financial statements of the Government under the cash basis of accounting, as defined in the Government Accounting Rule 21 of GAR 1990 and Government Financial Rule 68 of GFR 2005 should apply this Standard:

(a) in accounting and disclosure for transactions in foreign currencies;

(b) in accounting and disclosure for financial effects of exchange variations in terms of loss or gain by exchange rate variation, and

(c) in disclosure of foreign currency external debts and the rate(s) applied for disclosure.

Financial statements should not be described as complying with this Standard unless they comply with all its requirements. This Standard shall apply to foreign currency transactions of the Union Government as well as that of the State Governments. This Standard deals with presentation of expenditure and revenue in terms of loss or gain by exchange rate variations arising from foreign currency transactions. It also deals with disclosure of foreign currency external debt. This Standard

does not deal with disclosure requirements of external guarantees. The requirements of disclosure of details of subsisting external guarantees in terms of Indian rupees on the date of financial statements have been dealt with in IGAS1 "Guarantees given by Governments: Disclosure Requirements'. The Reserve Bank of India is the custodian of foreign currency and foreign exchange reserves and this Standard does not deal with foreign currency reserves.

(ii) What are the roles of Public Accounts Committee as constituted by Parliament? [8]

Answer:

The role of the Public Accounts Committee is to assess the integrity, economy, efficiency and effectiveness of government financial management. It achieves this by:

- examining Government financial documents; and
- considering the reports of the Auditor - General.

A significant amount of the committee's work involves following up matters raised in the reports to Parliament by the Auditor - General. This ensures that public sector financial issues are scrutinised for the benefit of the Parliament and the public.

While scrutinising the Appropriation Accounts of the Government of India and the Reports of the Comptroller and Auditor General thereon, it is the duty of the Committee to satisfy itself—

– that the moneys shown in the accounts as having been disbursed were legally available for and applicable to the service or purpose to which they have been applied or charged;
– that the expenditure conforms to the authority which governs it; and
– that every re-appropriation has been made in accordance with the provisions made in this behalf under rules framed by competent authority.

An important function of the Committee is to ascertain that money granted by Parliament has been spent by Government "within the scope of the demand". The functions of the Committee extend "beyond the formality of expenditure to its wisdom, faithfulness and economy". The Committee thus examines cases involving losses, nugatory expenditure and financial irregularities.

It is also the duty of the PAC to examine the statement of accounts of autonomous and semi-autonomous bodies, the audit of which is conducted by the Comptroller & Auditor General either under the directions of the President or by a Statute of Parliament.

OR,

(b)(i) Write a note on Indian Government Accounting Standard – 8, Contingent Liabilities (other than Gurantees) and Contingent Assets. [10]

Answer:

The purpose of the proposed IGAS on Contingent Liabilities (other than guarantees) and Contingent Assets is to provide for disclosure requirements of contingent liabilities (other than guarantees) and contingent assets of Governments in the financial statements. Disclosure of contingent liability is relevant from the point of view of knowing what risk of future liability the government carries. Disclosure of contingent assets is relevant in knowing what possible assets may accrue to government.

Under cash basis of accounting and financial reporting, generally, cash receipts and cash payments and cash balance are reported. However, in some jurisdictions additional information on financial assets and financial liabilities may also be reported. Financial assets such as loans and advances and

investments made by governments and financial liabilities in the nature of long-term debt are reported. Further, governments may disclose certain types of contractual obligations such as guarantees, which are not present liability. Certain possible assets such as revenue in arrears, which are under litigation, may also be disclosed. These are contingent because actual position of liability or asset will be confirmed only when related future events become certain. Disclosure of such information is relevant from the point of view of assessing possible future liability in case of contingent liability and future economic benefits and service potential in case of contingent assets. Guarantees given and other such uncertain liabilities relate to contingent liability and revenue in arrears under litigation and such other uncertain assets relate to contingent assets.

Objective

The objective of the proposed IGAS on the subject is to lay down the principles for disclosure requirements of Contingent Liabilities (other than guarantees) and Continent Assets of both the Union and the State Governments including Union Territories with Legislatures, in their respective Financial Statements in order to ensure uniform and appropriate disclosure of such liabilities and assets. It also ensures consistency with international best practices leading to transparency and improved quality of disclosure in the financial reports of Governments for the benefit of various stakeholders. An important objective of the proposed IGAS is to ensure that Governments portray the risks associated with contingent liabilities and contingent assets in a transparent manner.

Scope

The proposed IGAS shall apply to both the Union and the State Governments including Union Territories with Legislatures in preparation of their financial reports. The IGAS shall not include in its ambit guarantees (including letters of comfort) for which IGAS 1 would apply. The standard also excludes treatment of off budget borrowings, for which a separate statement may be developed, when found necessary.

(ii) State the responsibilities of the Government Accounting Standards advisory Board. [5]

Answer:

Responsibilities of the Board

- To establish and improve standard of Government accounting and financial reporting in order to enhance accountability mechanisms.
- To formulate and propose standards that improve the usefulness of financial reports based on the needs of the users.
- To keep the standards current and reflect change in the Governmental environment;
- To provide guidance on implementation of standards.
- To consider significant areas of accounting and financial reporting that can be improved through the standard setting process.
- To improve the common understanding of the common understanding of the nature and purpose of information contained in the financial reports.