

## PAPER – 1: FINANCIAL REPORTING

### PART – I : RELEVANT AMENDMENTS, NOTIFICATIONS AND ANNOUNCEMENTS

#### A. Applicable for May, 2015 examination

##### 1. Amendment to Schedule VII to the Companies Act, 2013

The Central Government vide Notification No. G.S.R. 568(E) dated 6<sup>th</sup> August, 2014, made amendments in Schedule VII to the Companies Act, 2013, wherein it has added "slum area development" as one of the avenue for contribution for CSR.

The term 'slum area' shall mean any area declared as such by the Central Government or any State Government or any other competent authority under any law for the time being in force.

Further, MCA vide notification no. G.S.R. 741(E) dated 24<sup>th</sup> October, 2014 has made further amendments to Schedule VII to the Companies Act, 2013 by notifying two more avenues for incurring eligible expenditure under CSR requirements for companies. According to the said notification, the contributions to the "Swach Bharat Kosh set up for the promotion of sanitation" and "contributions to the Clean Ganga Fund set up for rejuvenation of river Ganga" will also be considered as eligible expenditure qualifying for CSR.

##### 2. Securities and Exchange Board of India (Share Based Employee Benefits) Regulations, 2014

SEBI vide Circular No. LAD-NRO/GN/2014-15/16/1729 dated 28<sup>th</sup> October, 2014 has formulated the SEBI (Share Based Employee Benefits) Regulations, 2014 which replaces the SEBI (Employees Stock Option Plan) Guidelines, 1999. The said Regulations deal with various provisions relating to employee stock option schemes, employee stock purchase schemes, stock appreciation rights schemes, general employee benefits schemes and retirement benefit schemes formulated by listed companies. The regulations deal with definition of eligible employees, formation of compensation committee, shareholders approvals variation of terms of issue, listing, compliances etc. For the complete text of this notification please refer to the link: [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1414568485252.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1414568485252.pdf)

##### 3. Amendment to the Rule 6 of the Companies (Accounts) Rules, 2014

The Central Government vide Notification No. GSR... (E) dated 14<sup>th</sup> October, 2014, has amended the Companies (Accounts) Rules, 2014 by inserting two provisos in its Rule 6. Rule 6 talks about the manner of consolidation for the companies mandated to prepare the consolidated financial statements under section 129(3) of the Companies Act, 2013.

1. According to the first proviso added therein, an intermediate wholly-owned subsidiary company whose immediate parent is a company incorporated in India

would not be required to comply with the requirements of the Rule 6 of the Companies (Accounts) Rules, 2014.

However, the intermediate wholly-owned subsidiary company whose immediate parent is a company incorporated outside India is required to comply with the requirements of the Rule 6.

2. According to the second proviso added therein, those companies which do not have any subsidiary but have one or more associates or joint ventures or both, have been exempted from preparing Consolidated Financial Statements for the financial year 2014-15.

**4. Schedule III related disclosures made in the stand-alone financial statements not to be repeated in CFS – Clarification**

Under the Act, the requirements of Schedule III would apply to preparation of stand-alone financial statements as well as to the preparation of Consolidated Financial Statements.

While AS 21, 'Consolidated Financial Statements', inter alia, provides that certain information required under Schedule III to the Companies Act, 2013 given in the notes to the stand-alone financial statements of the parent and/or the subsidiary, need not be included in the Consolidated Financial Statements.

MCA has resolved the conflict between the accounting standards and the Act by providing a clarification in this regard vide Circular No. 39/2014, dated 14<sup>th</sup> October, 2014, after consulting with the ICAI.

The clarification mentions that Schedule III of the Act read with the applicable accounting standards does not envisage a company while preparing its Consolidated Financial Statements to repeat the disclosures made by it under the stand-alone financial statements used for consolidation. In the Consolidated Financial Statements, the company would need to give all disclosures relevant to Consolidated Financial Statements only.

**5. Amendment to the Companies (Corporate Social Responsibility Policy) Rules, 2014**

The Central Government vide Notification No. G.S.R. 644(E) dated 12<sup>th</sup> September, 2014, has amended sub-rule (6) of Rule 4 of the Companies (Corporate Social Responsibility Policy) Rules, 2014.

Earlier sub-rule (6) of Rule 4 states that Companies may build CSR capacities of their own personnel as well as those of their Implementing agencies through Institutions with established track records of at least three financial years but such expenditure shall not exceed five percent of total CSR expenditure of the company in one financial year. This sub rule has now been amended and states that such expenditure will include expenditure on administrative overheads also.

**6. Amendment to Schedule II to the Companies Act, 2013**

The Central Government vide Notification No. G.S.R. 627(E) dated 29<sup>th</sup> August, 2014 has amended Schedule II to the Companies Act, 2013 dealing with the useful lives of assets for calculation of depreciation. The said amendments will be voluntary for companies in respect of financial year commencing on or after 1<sup>st</sup> April, 2014 and mandatory for financial statements in respect of financial years commencing on or after 1<sup>st</sup> April, 2015.

**7. Clarification on Accounting Standard 10 - Capitalization of Cost**

MCA, vide general circular no. 35/2014 dated 27<sup>th</sup> August, 2014, has received a number of representations seeking clarifications on capitalization of borrowing costs incurred during extended delay in commercial production for reasons beyond the developer's control and whether capitalization of power plant should be unit wise or project wise.

On consultation with the Accounting Standard Board of the ICAI, MCA has clarified that AS 10 'Accounting for Fixed Assets' and AS 16 'Borrowing Costs' prescribe the principles of capitalization of various costs.

According to AS 10, only such expenditure should be capitalized and form part of the cost of the fixed asset which increase the worth of the asset. Cost incurred during extended delay in commencement of commercial production after the plant is otherwise ready does not increase the worth of the fixed assets. Therefore, such cost cannot be capitalized.

AS 16, inter alia provides guidance with regard to capitalization where some units of a project are complete and ready for commercial production while construction continues for the other units. In such a case, cost should be capitalized in relation to that part once the part is ready for commercial production.

MCA further clarified that AS 10 and AS 16 are applicable irrespective of whether the power projects are 'Cost Plus Projects' or 'Competitive Bid Projects'.

**8. Insertion of Paragraph 46 for Entities Other than Companies**

In line with para 46 inserted by the MCA for corporate entities, the Council of the ICAI has also inserted Paragraph 46 in AS 11 for Entities other than Companies in the month of February, 2014, which is as follows:

46(1) In respect of accounting periods commencing on or after 7th December, 2006 (such option to be irrevocable and to be applied to all such foreign currency monetary items), the exchange differences arising on reporting of long-term foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, in so far as they relate to the acquisition of a depreciable capital asset, can be added to or deducted from the cost of the asset and should be depreciated over the balance life of the asset, and in other cases, can be accumulated in a "Foreign Currency Monetary Item Translation Difference

Account" in the enterprise's financial statements and amortized over the balance period of such long-term asset or liability, by recognition as income or expense in each of such periods, with the exception of exchange differences dealt with in accordance with the provisions of paragraph 15.

(2) To exercise the option referred to in sub-paragraph (1), an asset or liability shall be designated as a long-term foreign currency monetary item, if the asset or liability is expressed in a foreign currency and has a term of twelve months or more at the date of origination of the asset or the liability:

Provided that the option exercised by the enterprise should disclose the fact of such option and of the amount remaining to be amortized in the financial statements of the period in which such option is exercised and in every subsequent period so long as any exchange difference remains unamortized."

#### 9. Modification of Guidelines on Mortgage Guarantee Companies (MGCs)

In the wake of representations received from the industry and keeping in view the long – term beneficial impact of development of the Mortgage Guarantee industry, RBI vide Notification No. RBI/2014-15/170 DNBS (PD) CC. No.20/MGC/03.011.001/2014-15, dated August 08, 2014, has decided to make certain modifications to the existing Guidelines on Mortgage Guarantee Companies (MGCs) as under:

- (a) *Capital Adequacy*: While calculating the capital adequacy of the MGC, the mortgage guarantees provided by the MGCs may be treated as Contingent Liabilities and the credit conversion factor applicable to these Contingent Liabilities will be fifty percent as against the present applicable credit conversion factor of hundred percent.
- (b) *Contingency Reserve*
  - i. If provision made towards losses exceed 35% of the premium or fee earned during a financial year, the Contingency Reserves could go to a minimum of 24% of the premium or fee earned, such that the aggregate of Provisions made towards Losses and Contingency Reserves is at least 60% of the premium or fee earned during a financial year.
  - ii. A MGC can utilize the Contingency Reserves without the prior approval of RBI for the purpose of meeting and making good the losses suffered by the mortgage guarantee holders. Such a measure can be initiated only after exhausting all other avenues and options to recoup the losses.
- (c) *Classification on Investments*: It has now been decided that investments made by MGCs towards Government securities, quoted or otherwise, government guaranteed securities and bonds not exceeding the MGC's capital may be treated as "Held To Maturity (HTM)" for the purpose of valuation and accounted for accordingly. Investment classified under HTM need not be marked to market and will be carried at acquisition cost, unless it is more than the face value, in which case the premium should be amortised over the period remaining to maturity. The

book value of the security should continue to be reduced to the extent of the amount amortised during the relevant accounting period. However, if any security out of this HTM category is traded before maturity, the entire lot will be treated as securities held for trade and will have to be marked to market.

- (d) *Provision for Loss on invoked Guarantees:* In case the provisions already held for loss on invoked guarantees are in excess of the contract wise aggregate of 'amount of invocation' (after adjusting the realizable value of the assets held by the company in respect of each housing loan), the excess may be reversed. However, the reversal can be done only after full recovery /closure of the invoked guarantee amount or after the account becomes standard.

#### 10. Relevant Section of the Companies Act, 2013

The relevant Sections of the Companies Act, 2013 notified up to 30th September 2014 are applicable for May, 2015 Examination.

#### 11. Schedule III to the Companies Act, 2013

Students may note that Schedule III to the Companies Act, 2013 gives general instructions for preparation of balance sheet and statement of profit and loss of a company. Schedule III to the Companies Act, 2013, also contains general instructions for preparation of consolidated financial statements, at its end in addition to Part I - Balance Sheet and Part II - Statement of Profit and Loss. Students are advised to go through complete Schedule III to the Companies Act, 2013 carefully for preparation of financial statements of companies including consolidated financial statements.

*Students may refer Schedule III to the Companies Act, 2013 on the Institute's website [www.icaai.org](http://www.icaai.org)>>Students>>Bos knowledge portal>>Final Course>>Paper 1 Financial Reporting>>Additional Reading Material>>Schedule III to the Companies Act, 2013.*

#### 12. Buy Back of Securities (Amendment) Regulations, 2013

In exercise of the powers conferred under section 30 of the Securities and Exchange Board of India Act, 1992, SEBI made Securities and Exchange Board of India (Buy-back of Securities) (Amendment) Regulations, 2013 to amend the Securities and Exchange Board of India (Buy back of Securities) Regulations, 1998.

The important provisions of the new regulations (applicable for listed companies) are:

- (i) No offer of buy-back for fifteen per cent or more of the paid up capital and free reserves of the company shall be made from the open market.
- (ii) A company shall not make any offer of buyback within a period of one year reckoned from the date of closure of the preceding offer of buy-back, if any.
- (iii) The company shall ensure that at least fifty per cent of the amount earmarked for buy-back is utilized for buying back shares or other specified securities.

These new regulations can be downloaded from the link [http://203.199.247.102/cms/sebi\\_data/attachdocs/1375961931576.pdf](http://203.199.247.102/cms/sebi_data/attachdocs/1375961931576.pdf)

## **B. Not applicable for May, 2015 examination**

### **Ind ASs issued by the Ministry of Corporate Affairs**

To bring Indian standards at par with the IAS/IFRS, some of the earlier Accounting Standards and Guidance Notes have been revised or are under the process of revision. However, at present, the Accounting Standard Board in consultation with the Ministry of Corporate Affairs (MCA) for convergence of Indian Accounting Standards with International Financial Reporting Standards (IFRS), has placed on its website 35 Ind ASs which are in actual issued in correspondence to IFRS with certain carve outs. This was done in the year 2011. Earlier the government of India planned to implement the Ind ASs to various corporate in the phase manner. However, due to certain implementation issues like the requirements of various laws and Act prevailing in India which were not in consonance with the Ind AS, the implementation of Ind AS get was deferred.

At that time it was also decided that there will be two separate sets of Accounting Standards viz. (i) Indian Accounting Standards converged with the IFRS – standards which are being converged by eliminating the differences of the Indian Accounting Standards vis-à-vis IFRS (known as Ind AS) and (ii) Existing Notified Accounting Standards.

The Ind ASs have been prepared by National Advisory Committee on Accounting Standards (NACAS) and with its recommendation submitted to Ministry of Corporate Affairs (MCA). The final recommended Ind ASs (as on 2011) have certain carve outs. The carve outs have been made to fill up the gap/differences in application of Accounting Principles Practices and economic conditions prevailing in India.

#### **A. Carve-outs which are due to differences in application of accounting principles and practices and economic conditions prevailing in India.**

##### **1. Ind AS 21: The Effects of Changes in Foreign Exchange Rates**

It requires recognition of exchange differences arising on translation of monetary items from foreign currency to functional currency directly in profit or loss.

#### **Carve out**

Ind AS 21 permits an option to recognise exchange differences arising on translation of certain long-term monetary items from foreign currency to functional currency directly in equity. In this situation, Ind AS 21 requires the accumulated exchange differences to be amortised to profit or loss in an appropriate manner.

**Note:** ICAI has proposed the removal of this carve out on the ground that as per IFRS 9, only those exposures can qualify for hedge accounting which have impact on the statement of profit and loss. Where an entity follows the option by not recognising the gains and losses on foreign exchange fluctuations in profit or loss

but directly in equity, such an entity would not be able to use hedge accounting as per IFRS 9. It was felt that, in any case, the option is conceptually inappropriate as the entity is able to defer the gains/losses arising from foreign exchange risks. At present, the said proposal is under consideration of the MCA.

## 2. Ind AS 28: Investment in Associates

1. Paragraph 25 require that difference between the reporting period of an associate and that of the investor should not be more than three months, in any case.

### Carve out

The phrase 'unless it is impracticable' has been added in the relevant requirement i.e., paragraph 25 of Ind AS 28.

2. IAS 28 requires that for the purpose of applying equity method of accounting in the preparation of investor's financial statements, uniform accounting policies should be used. In other words, if the associate's accounting policies are different from those of the investor, the investor should change the financial statements of the associate by using same accounting policies.

### Carve out

The phrase, 'unless impracticable to do so' has been added in the relevant requirements i.e., paragraph 26 of Ind AS 28.

**Note:** The ICAI proposed the removal of this carve-out on the ground that impracticability to obtain financial statements prepared in accordance with the uniform accounting policies of the investor and as on the date on which the financial statements of the investor are drawn (except the time gap permitted by the standard) may be considered as the investor may not have significant influence over the investee. In other words, in such a case, it may be difficult to establish that the investor is having significant influence over the investee and, therefore, investee may not be regarded as an associate of the investor. Accordingly, the ICAI is of the view that term 'unless impracticable' should be deleted. At present, the said proposal is under consideration of the MCA.

## 3. Ind AS 32- Financial Instruments in Presentation Part

A Carve out is an exception has been included to the definition of 'financial liability' in paragraph 11 (b) (ii), Ind AS 32 to consider the equity conversion option embedded in a convertible bond denominated in foreign currency to acquire a fixed number of entity's own equity instruments as an equity instrument if the exercise price is fixed in any currency. This exception is not provided in IAS 32.

**4. Ind AS 39- Financial Instruments: Recognition and Measurement**

IAS 39 requires all changes in fair values in case of financial liabilities designated at fair value through Profit and Loss at initial recognition shall be recognised in profit or loss. IFRS 9 which will replace IAS 39 requires these to be recognised in 'other comprehensive income'

**Carve out**

A proviso has been added to paragraph 48 of Ind AS 39 that in determining the fair value of the financial liabilities which upon initial recognition are designated at fair value through profit or loss, any change in fair value consequent to changes in the entity's own credit risk shall be ignored.

**5. Ind AS 103, Business Combinations**

IFRS 3 requires bargain purchase gain arising on business combination to be recognised in profit or loss.

**Carve out**

Ind AS 103 requires the same to be recognised in other comprehensive income and accumulated in equity as capital reserve, unless there is no clear evidence for the underlying reason for classification of the business combination as a bargain purchase, in which case, it shall be recognised directly in equity as capital reserve.

**6. Ind AS 101, First-time Adoption of Indian Accounting Standards****(i) Presentation of comparatives in the First-time Adoption of Indian Accounting Standards (Ind AS) 101 (corresponding to IFRS 1)**

IFRS 1 defines transitional date as beginning of the earliest period for which an entity presents full comparative information under IFRS. It is this date which is the starting point for IFRS and it is on this date the cumulative impact of transition is recorded based on assessment of conditions at that date by applying the standards retrospectively except to the extent specifically provided in this standard as optional exemptions and mandatory exceptions. Accordingly, the comparatives, i.e., the previous year figures are also presented in the first financial statements prepared under IFRS on the basis of IFRS.

**Carve out**

Ind AS 101, requires an entity to provide comparatives as per the existing notified Accounting Standards. It is provided that, in addition to aforesaid comparatives, an entity may also provide comparatives as per Ind AS on a memorandum basis.

**(ii) Presentation of reconciliation**

IFRS 1 requires reconciliations for opening equity, total comprehensive income, cash flow statement and closing equity for the comparative period to explain the transition to IFRS from previous GAAP.

**Carve out**

Ind AS 101 provides an option to provide a comparative period financial statements on memorandum basis. Where the entities do not exercise this option and, therefore, do not provide comparatives, they need not provide reconciliation for total comprehensive income, cash flow statement and closing equity in the first year of transition but are expected to disclose significant differences pertaining to total comprehensive income. Entities that provide comparatives would have to provide reconciliations which are similar to IFRS.

**(iii) Cost of Non-current Assets Held for Sale and Discontinued Operations on the date of transition on First-time Adoption of Indian Accounting Standards (Ind AS)****Carve out**

Ind AS 101 provides transitional relief that while applying Ind AS 105 - Non-current Assets Held for Sale and Discontinued Operations, an entity may use the transitional date circumstances to measure such assets or operations at the lower of carrying value and fair value less cost to sell.

**(iv) Foreign currency gains/losses on translation of long term monetary items****Carve out**

Ind AS 101 provides that on the date of transition, if there are long-term monetary assets or long-term monetary liabilities mentioned in paragraph 29A of Ind AS 21, an entity may exercise the option mentioned in that paragraph regarding spreading over the unrealised Gains/Losses over the life of Assets/Liabilities either retrospectively or prospectively. If this option is exercised prospectively, the accumulated exchange differences in respect of those items are deemed to be zero on the date of transition.

**(v) Financial instruments existing on transition date****Carve out**

Ind AS 101 provides that the financial instruments carried at amortised cost should be measured in accordance with Ind AS 39 from the date of recognition of financial instruments unless it is impracticable (as defined in Ind AS 8) for an entity to apply retrospectively the effective interest method or the impairment requirements of Ind AS 39. If it is impracticable to do so then the fair value of the financial asset at the date of transition to Ind-ASs shall be the new amortised cost of that financial asset at the date of transition to Ind ASs. Ind

AS 101 provides another exemption that financial instruments measured at fair value shall be measured at fair value as on the date of transition to Ind AS.

**(vi) Definition of previous GAAP under Ind AS 101 First time Adoption of Indian Accounting Standards**

IFRS 1 defines previous GAAP as the basis of accounting that a first-time adopter used immediately before adopting IFRS.

**Carve out**

Ind AS 101 defines previous GAAP as the basis of accounting that a **first-time adopter** used immediately before adopting Ind ASs for its reporting requirements in India. For instance, for companies preparing their financial statements in accordance with the existing Accounting Standards notified under the Companies (Accounting Standards) Rules, 2006 shall consider those financial statements as previous GAAP financial statements.

**(vii) Cost of Property, Plant and Equipment (PPE), Intangible Assets, Investment Property, on the date of transition of First-time Adoption of Indian Accounting Standards.**

Ind AS 101 provides an entity an option to use carrying values of all assets as on the date of transition in accordance with previous GAAP as an acceptable starting point under Ind AS.

**B. Carve-outs for specific industries**

**7. Ind AS 18-Revenue**

On the basis of principles of the IAS 18, IFRIC 15 on Agreement for Construction of Real Estate, prescribes that construction of real estate should be treated as sale of goods and revenue should be recognised when the entity has transferred significant risks and rewards of ownership and has retained neither continuing managerial involvement nor effective control.

**Carve out**

IFRIC 15 has not been included in Ind AS 18, Revenue. Such agreements have been scoped out from Ind AS 18 and have been included in Ind AS 11, Construction Contracts.

**8. Ind AS 18- Revenue**

**Carve out**

A footnote has been added in paragraph 1 to Ind AS 18, Revenue, that for rate regulated entities, this standard shall stand modified, where and to the extent the recognition and measurement of revenue of such entities is affected by recognition and measurement of regulatory assets/liabilities as per the Guidance Note on the subject being issued by the Institute of Chartered Accountants of India.

### 9. Ind AS 19 Employee Benefits vis-à-vis IFRSs/IASs restricting options

According to Ind AS 19 the rate to be used to discount post-employment benefit obligation shall be determined by reference to the market yields on government bonds, whereas under IAS 19, the government bonds can be used only where there is no deep market of high quality corporate bonds. To illustrate treatment of gratuity subject to ceiling under Indian Gratuity Rules, an example has been added in Ind AS 19. IAS 19 permits various options for treatment of actuarial gains and losses for post employment defined benefit plans whereas Ind AS 19 requires recognition of the same in other comprehensive income, both for post-employment defined benefit plans and other long-term employment benefit plans. The actuarial gains recognised in other comprehensive income should be recognised immediately in retained earnings and should not be reclassified to profit or loss in a subsequent period.

In a significant step towards convergence of Indian accounting standards with the IFRS, the Ministry of Corporate Affairs (MCA) on January 2, 2015 announced a roadmap for adoption of Indian Accounting Standards (Ind AS) which is closely aligned with the International Financial Reporting Standards (IFRS), as issued by International Accounting Standards Board (IASB).

In pursuance of the Budget statement, the Ministry of Corporate Affairs, Government of India after wide consultations with various stakeholders and regulators, on January 2, 2015 has announced a revised Road Map for companies other than Banking Companies, Insurance Companies and Non-Banking Finance Companies (NBFCs) for implementation of Indian Accounting Standards (Ind AS) converged with the International Financial Reporting Standards (IFRS).

According to it, the Indian Accounting Standards (Ind ASs) shall be applicable to the companies as follows:

- (i) On voluntary basis for financial statements for accounting periods beginning on or after April 1, 2015, with the comparatives for the periods ending 31st March, 2015 or thereafter;
- (ii) On mandatory basis for the accounting periods beginning on or after April 1, 2016, with comparatives for the periods ending 31st March, 2016, or thereafter, for the companies specified below:
  - (a) Companies whose equity and/or debt securities are listed or are in the process of listing on any stock exchange in India or outside India and having net worth of ₹ 500 Crore or more.
  - (b) Companies other than those covered in (ii) (a) above, having net worth of ₹ 500 Crore or more.

- (c) Holding, subsidiary, joint venture or associate companies of companies covered under (ii) (a) and (ii) (b) above.
- (iii) On mandatory basis for the accounting periods beginning on or after April 1, 2017, with comparatives for the periods ending 31st March, 2017, or thereafter, for the companies specified below:
- (a) Companies whose equity and/or debt securities are listed or are in the process of being listed on any stock exchange in India or outside India and having net worth of less than rupees 500 Crore.
- (b) Companies other than those covered in paragraph (ii) and paragraph (iii)(a) above that is unlisted companies having net worth of rupees 250 crore or more but less than rupees 500 Crore.
- (c) Holding, subsidiary, joint venture or associate companies of companies covered under paragraph (iii) (a) and (iii) (b) above.

However, Companies whose securities are listed or in the process of listing on SME exchanges shall not be required to apply Ind AS. Such companies shall continue to comply with the existing Accounting Standards unless they choose otherwise.

- (iv) Once a company opts to follow the Indian Accounting Standards (Ind AS), it shall be required to follow the Ind AS for all the subsequent financial statements.
- (v) Companies not covered by the above roadmap shall continue to apply existing Accounting Standards prescribed in Annexure to the Companies (Accounting Standards) Rules, 2006.

The issuance of Ind AS is a significant step towards the implementation of converged standards in India. **However, Ind ASs are not made applicable for May, 2015 examination.**

## PART – II : QUESTIONS AND ANSWERS

### QUESTIONS

#### AS 2

1. (a) Hema Ltd. is in the business of manufacturing computers. During the year ended 31<sup>st</sup> March, 2015 the company manufactured 550 computers, it has the policy of valuing finished stock of goods at a standard cost of ₹ 1.8 lakhs per computer. The details of the cost are as under:

|  | <i>(₹ in lakhs)</i> |
|--|---------------------|
| Raw material consumed  | 400                 |
| Direct Labour  | 250                 |
| Variable production overheads                                  | 150                 |
| Fixed production overheads (including interest of ₹ 100 lakhs) | 290                 |

Compute the value of cost per computer for the purpose of closing stock and also comment on the policy of valuation of inventory adopted by Hema Ltd.

**AS 3**

- (b) A Finance House Ltd. purchased commercial paper (CP) of ₹ 100 crores on 28<sup>th</sup> February, 2015 for 89 days maturity. There is a ready market for sale/purchase of commercial paper. While preparing cash flow statement for the financial year ended on 31.3.2015, Finance House Ltd. showed CP of ₹ 100 crores under Investing Activities.

**AS 5**

2. (a) At March 31, 2015, High Ltd. was holding long-lived assets, which it intended to sell. The company appropriately recognized a loss in 2014-15 related to these assets. State whether on High Ltd.'s Income Statement for the year ended March 31, 2015, this loss should be reported as
- (a) An extraordinary item.
  - (b) A component of income from continuing operations before income-taxes to be disclosed separately.
  - (c) A separate component of selling or general and administrative expenses, disclosed net of tax benefit.
  - (d) A component of gain (loss) from sale of discontinued operations, disclosed net of income-taxes.

**AS 6**

- (b) In the books of Optic Fiber Ltd., plant and machinery stood at ₹ 6,32,000 on 1.4.2014. However, on scrutiny it was found that machinery worth ₹ 1,20,000 was included in the purchases on 1.6.2014. On 30.6.2014 the company disposed a machine having book value of ₹ 1,89,000 on 1.4.2014 at ₹ 1,75,000 in part exchange of a new machine costing ₹ 2,56,000. The company charges depreciation @ 20% WDV on plant and machinery.

You are required to calculate:

- (i) Depreciation to be charged to the Profit and Loss Account.
- (ii) Book value of Plant and Machinery A/c as on 31.3.2015.
- (iii) Loss on exchange of machinery.

**AS 7**

3. (a) Vatika Ltd. has undertaken bridge construction contract wherein, bridge will be constructed in 3 years. The details of the contracts are as follows:
- (i) Initial contract revenue ₹ 900 crores

(ii) Initial contract cost ₹ 800 crores

|                                    | Years       |             |             |
|------------------------------------|-------------|-------------|-------------|
|                                    | I           | II          | III         |
|                                    | ₹ in crores | ₹ in crores | ₹ in crores |
| Estimated contract cost            | 805         |             |             |
| Increase in contract revenue       | -           | 20          |             |
| Estimated additional increase cost | -           | 15          |             |
| Contract cost incurred upto        | 161         | 584         | 820         |

At the end of year II cost incurred includes ₹ 10 crores, for material stored at the sites to be used in year III to complete the project.

State the amount of revenue, expenses and profit to be recognized in the Statement of Profit and Loss in these three years.

#### AS 9

- (b) When will the revenue be recognized in the case of inter divisional transfers?
- (c) Sarita Publications publishes a monthly magazine on the 15<sup>th</sup> of every month. It sells advertising space in the magazine to advertisers on the terms of 80% sale value payable in advance and the balance within 30 days of the release of the publication. The sale of space for the March 2015 issue was made in February 2015. The magazine was published on its scheduled date. It received ₹ 2,40,000 on 10.3.2015 and ₹ 60,000 on 10.4.2015 for the March 2015 issue.

Discuss in the context of AS 9 the amount of revenue to be recognized and the treatment of the amount received from advertisers for the year ending 31.3.2015. What will be the treatment if the publication is delayed till 2.4.2015?

#### AS 10

4. (a) On 1.4.2015, Orbit Ltd. had sold some of its fixed assets for ₹ 100 lakhs whose written down value was ₹ 250 lakhs. These assets were revalued earlier. As on 1.4.2015, the revaluation reserve corresponding to these assets stood at ₹ 200 lakhs. The profit on sale of property ₹ 200 lakhs shown in the profit and loss statement presented the transfer of this amount. Loss on sale of asset was included in cost of goods sold. Comment on the above accounting treatment done by Orbit Ltd. in light of the relevant accounting standards.

#### AS 11

- (b) Path Ltd. purchased a fixed asset for US \$ 50 lakhs on 01.04.2014 and the same was fully financed by the foreign currency loan [i.e. US \$] repayment in five equal instalments annually. (Exchange rate at the time of purchase was 1 US \$=₹ 60).

As on 31.03.2015 the first instalment was paid when 1 US \$ fetched ₹ 62.00. The entire loss on exchange was included in cost of goods sold. Path Ltd. normally provides depreciation on fixed assets at 20% on WDV basis and exercised the option to adjust the cost of asset for exchange difference arising out of loan restatement and payment. Calculate the amount of exchange loss and its treatment and depreciation.

**AS 12**

5. (a) Power Ltd. has acquired a generator on 1.4.2013 for ₹ 100 lakhs. On 2.4.2013, it applied to Indian Renewal Energy Development Authority (IREDA) for a subsidy. The subsidy was granted in June, 2014 after the accounts for 2013-14 were finalized. The company has not accounted for the subsidy for the year ended 31.3.2014.

State

- (i) Is this a prior period item?
- (ii) How should the subsidy be accounted in the accounting year 2014-15?
- (iii) Would your opinion differ, if the sanction letter for subsidy was received in June 2014 before the accounts for 2013-14 were approved by the Board of Directors?
- (iv) Would your opinion differ had the company made many similar applications in the past and on all occasions, it has received the subsidy applied for?

**AS 13**

- (b) A company is engaged in the business of refining, transportation and marketing of petroleum products. During the financial year ended March 31<sup>st</sup>, 2015, the company acquired controlling interest from Government of India in another public sector undertaking @ ₹ 1,551 per share as against the book value of ₹ 192.58 per share and market value of ₹ 876 per share as on February 18, 2015.

Thus the strategic premium of ₹ 675 per share has been paid considering various tangible and intangible factors.

The above investment in the shares of the acquired company has been considered as long term strategic investment and, therefore, has been accounted for at cost, i.e. at ₹ 1,551 per share in the financial statements. No provision for diminution in value has been made in the books of account.

As per the requirement of Schedule III to the Companies Act, 2013, the aggregate market value of the quoted shares has been properly reflected in the financial statements.

On March 28, 2015, the acquired shares were quoted at ₹ 880 per share on BSE and the current market price as on July 18 was around ₹ 300.

Considering the tangible and intangible benefits the Management is of the view that there is no permanent diminution in the value of the strategic investment in the acquired company, as the same has been considered as a long-term investment. Therefore, there is no need for provision for diminution in the value of the shares of the acquired company.

Required:

- (i) Whether the accounting treatment 'at cost' under the head 'Long Term Investments' without providing for any diminution in value is correct and in accordance with the provisions of AS 13.
- (ii) If not, what should have been the accounting treatment in such a situation particularly considering the fact that there is no material change in circumstances and strength of the acquired company which further supported the expected benefits from such synergy? Whether the reduction in market value should be considered in isolation for ascertaining the value of such investment or not? What methodology should be adopted for ascertaining the provision for diminution in the value of investment, if any?
- (iii) If any provision for diminution in the value is to be made, whether such provision should be charged to the profit and loss account or whether same can be considered as deferred expenditure and amortised over a period of 5 years. Whether it is open for the company to charge off such diminution in the value in the books of account instead of creating provision.
- (iv) Whether the premium paid for strategic benefits for investment described in facts of the case, can be accounted for separately in the books of account keeping in view that AS 13 specifies that long term investments should be recorded at cost and there is no specific provision in the standard in respect of accounting for premium paid for strategic benefits.

#### AS 16

6. (a) A company capitalizes interest cost of holding investments and adds to cost of investment every year, thereby understating interest cost in profit and loss account. State whether the accounting done by the company is usual or not?

#### AS 17

- (b) Whether interest expense relating to overdrafts and other operating liabilities identified to a particular segment should be included in the segment expense or not?

In case interest is included as a part of the cost of inventories where it is so required as per AS 16, read with AS 2 and those inventories are part of segment assets of a particular segment, state whether such interest would be considered as a segment expense.

**AS 18**

7. (a) P Ltd. has 60% voting right in Q Ltd. Q Ltd. has 20% voting right in R Ltd. Also, P Ltd. directly enjoys voting right of 14% in R Ltd. R Ltd. is a listed company and regularly supplies goods to P Ltd. The management of R Ltd. has not disclosed its relationship with P Ltd.

How would you assess the situation from the view point of AS 18 on 'Related Party Disclosures'?

**AS 19**

- (b) A machine having expected useful life of 6 years, is leased for 4 years. Both the cost and the fair value of the machinery are ₹ 7,00,000. The amount will be paid in 4 equal instalments and at the termination of lease, lessor will get back the machinery. The unguaranteed residual value at the end of the 4<sup>th</sup> year is ₹ 70,000. The IRR of the investment is 10%. The present value of annuity factor of ₹ 1 due at the end of 4<sup>th</sup> year at 10% IRR is 3.169. The present value of ₹ 1 due at the end of 4<sup>th</sup> year at 10% rate of interest is 0.683.

State with reasons whether the lease constitutes finance lease and also compute the unearned finance income.

**AS 20**

8. (a) In the following list of shares issued, for the purpose of calculation of weighted average number of shares, from which date weight is to be considered:
- (i) Equity Shares issued in exchange of cash,
  - (ii) Equity Shares issued as a result of conversion of a debt instrument,
  - (iii) Equity Shares issued in exchange for the settlement of a liability of the enterprise,
  - (iv) Equity Shares issued for rendering of services to the enterprise,
  - (v) Equity Shares issued in lieu of interest and/or principal of an other financial instrument,
  - (vi) Equity Shares issued as consideration for the acquisition of an asset other than in cash.

Also define Potential Equity Share.

**AS 24**

- (b) Qu Ltd. is in the business of manufacture of Passenger cars and commercial vehicles. The company is working on a strategic plan to shift from the Passenger car segment over the coming 5 years. However, no specific plans have been drawn up for sale of neither the division nor its assets. As part of its plan it will reduce the production of passenger cars by 20% annually. It also plans to commence another

new factory for the manufacture of commercial vehicles plus transfer of employees in a phased manner.

- (i) You are required to comment if mere gradual phasing out in itself can be considered as a 'Discontinuing Operation' within the meaning of AS 24.
- (ii) If the company passes a resolution to sell some of the assets in the passenger car division and also to transfer few other assets of the passenger car division to the new factory, does this trigger the application of AS 24 ?
- (iii) Would your answer to the above be different if the company resolves to sell the assets of the Passenger Car Division in a phased but time bound manner?

#### AS 25

9. (a) On 30.6.2014, X Limited incurred ₹ 3,00,000 net loss from disposal of a business segment. Also on 31.7.2014, the company paid ₹ 80,000 for property taxes assessed for the calendar year 2014. How should the above transactions be included in determination of net income of X Limited for the six months interim period ended on 30.9.2014?

#### AS 28

- (b) A significant raw material used for plant Y's final production is an intermediate product bought from plant X of the same enterprise. X's products are sold to Y at a transfer price that passes all margins to X. 80% of Y's final production is sold to customers outside the reporting enterprise. 60% of X's final production is sold to Y and the remaining 40% is sold to customers outside the reporting enterprise.

For each of the following cases, what are the cash-generating units for X and Y?

Case 1: X could sell the products it sells to Y in an active market. Internal transfer prices are higher than market prices.

Case 2: There is no active market for the products X sells to Y.

#### AS 29

10. (a) WZW Ltd. is in dispute involving allegation of infringement of patents by a competitor company who is seeking damages of a huge sum of ₹ 1000 Lakhs. The directors are of the opinion that the claim can be successfully resisted by the company. How would you deal the same in the Annual Accounts of the company?

#### Guidance Note

- (b) Futura Ltd. had the following items under the head "Reserves and Surplus" in the Balance Sheet as on 31<sup>st</sup> March, 2015:

|                            | Amount ₹ in lakhs |
|----------------------------|-------------------|
| Securities Premium Account | 80                |
| Capital Reserve            | 60                |
| General Reserve            | 90                |

The company had an accumulated loss of ₹ 250 lakhs on the same date, which it has disclosed under the head "Statement of Profit and Loss" as an asset in its Balance Sheet. Comment on accuracy of this treatment in line with Schedule III to the Companies Act, 2013.

#### IFRS vis a vis AS applicable in India

11. (a) Explain the treatment of the following items with reference to Existing Accounting Standards (as applicable in India) vis-a-vis IFRS:
- (1) Consolidated Financial Statements
  - (2) Joint Arrangements
- (b) Who are the beneficiaries of convergence with IFRS in India?

#### Corporate Financial Reporting

- (c) Explain the role of SEBI with respect to Corporate Financial Reporting.

#### Accounting for Corporate Restructuring – Business Acquisition

12. AB Ltd. and CD Ltd. two private companies, decide to amalgamate their business into a new holding company EF Ltd., which was incorporated on 1<sup>st</sup> August, 2014 with an authorised capital of ₹ 40,00,000 in equity shares of ₹ 10 each. The new company plans to commence operations on 1<sup>st</sup> October, 2014.

From the information given below, and assuming that all transactions are completed by 31<sup>st</sup> March, 2015, you are required to:

- (a) Prepare Projected Statement of Profit & Loss of EF Ltd. for the six months ending 31<sup>st</sup> March, 2015.
- (b) Prepare Projected Balance Sheet of EF Ltd. as on 31<sup>st</sup> March, 2015.
- (c) Show the computation of number of shares to be issued to the former shareholders of AB Ltd. and CD Ltd.

#### Information

- (1) EF Ltd. will acquire the whole of the Equity share capital of AB Ltd. and CD Ltd. by issuing its fully paid own shares.
- (2) The number of shares to be issued is to be calculated by multiplying the future annual maintainable profits available to the Equity shareholders in each of the two companies by agreed price earnings ratios.

The following information is relevant:

|                                       | <i>AB Ltd. (₹)</i> | <i>CD Ltd. (₹)</i> |
|---------------------------------------|--------------------|--------------------|
| Equity Shares of ₹ 10 each fully paid | 10,00,000          | 4,00,000           |
| 8% Cumulative Preference shares       |                    | 1,00,000           |

|   |          |          |
|---|----------|----------|
| 10% Debentures  | 2,00,000 |          |
| Future annual maintainable pre tax profits (before interest/dividend) | 2,30,000 | 1,12,000 |
| Price Earnings Ratio  | 10 times | 8 times  |

- (3) Shares in the holding company are to be issued to the shareholders in subsidiary companies at a premium of 20% and thereafter these shares will be marketed on the stock exchange.
- (4) It is expected that the Group profits of the new company in 2014-15 will be at least ₹ 4,50,000 but that will be required as additional working capital to facilitate expansion. Accordingly it is planned to make a further issue of 37,500 Equity shares to the public for cash at a premium of 30% on 1st February, 2015. The new shares will not rank for interest/dividend to be paid on 31st March, 2015.
- (5) Out of the proceeds of the right issue EF Ltd. will advance ₹ 2,50,000 to AB Ltd. and ₹ 2,00,000 to CD Ltd. on 1st February, 2015 for working capital. These advances will carry interest @ 15% p.a. to be paid monthly.
- (6) Preliminary Expenses are estimated at ₹ 8,000 and Administrative Expenses for the half-year ended 31st March, 2015 at ₹ 16,000 but this expenditure will be covered by temporary overdraft facility. It is estimated that Interest on Bank Overdraft cost will be ₹ 1,600 in the first six months.
- (7) A provision for ₹ 7,500 should be made for Directors Fee for the half-year.
- (8) On 31st March, 2015, Interim Dividends on Equity Shares, will be paid by AB Ltd. @ 5%, by CD Ltd. @ 4.4% and by EF Ltd. @ 4%.
- (9) Income tax is to be taken @50% for calculation of number of shares. However, ignore tax effect while preparing Projected Statement of Profit and Loss.

#### Consolidated Financial Statements

13. A Ltd. acquired 70% of equity shares of B Ltd. on 1.4.2008 at cost of ₹ 10,00,000 when B Ltd. had an equity share capital of ₹ 10,00,000 and reserves and surplus of ₹ 80,000. In the four consecutive years, B Ltd. fared badly and suffered losses of ₹ 2,50,000, ₹ 4,00,000, ₹ 5,00,000 and ₹ 1,20,000 respectively. Thereafter in 2012-13, B Ltd. experienced turnaround and registered an annual profit of ₹ 50,000. In the next two years i.e. 2013-14 and 2014-15, B Ltd. recorded annual profits of ₹ 1,00,000 and ₹ 1,50,000 respectively. Show the minority interests and cost of control at the end of each year for the purpose of consolidation.

**Consolidated Financial Statements of Subsidiary, Associate and Joint Venture Companies**

14. The following information relates to the results of the parent and subsidiary (jointly) and the investment in associate and joint venture:

Summarised Balance Sheet as at 31.3.2015

|                                     | <i>Holding and subsidiary</i> | <i>Associate</i> | <i>Joint Venture</i> |
|-------------------------------------|-------------------------------|------------------|----------------------|
| Called up equity shares of ₹ 1 each | 1,00,000                      | 40,000           | 10,000               |
| General reserve                     | 40,000                        |                  | -                    |
| Profit and loss account             | 37,000                        | 27,000           | 83,000               |
| Minority Interest                   | 20,000                        | -                | -                    |
| Creditors                           | 20,000                        | 32,000           | 6,000                |
| Provision for tax                   | 9,000                         | 11,000           | 7,000                |
| Proposed dividend                   | <u>10,000</u>                 | <u>-</u>         | <u>4,000</u>         |
|                                     | <u>2,36,000</u>               | <u>1,10,000</u>  | <u>1,10,000</u>      |
| Fixed assets                        | 1,95,000                      | 74,000           | 41,000               |
| Investments:                        |                               |                  |                      |
| 8,000 shares in Associate           | 15,000                        | -                | -                    |
| 5,000 shares in Joint Venture       | 5,000                         | -                | -                    |
| Current assets                      | <u>21,000</u>                 | <u>36,000</u>    | <u>69,000</u>        |
|                                     | <u>2,36,000</u>               | <u>1,10,000</u>  | <u>1,10,000</u>      |

Profit and Loss account for the year ended 31.3.2015

|                                      | <i>Holding and subsidiary</i> | <i>Associate</i>  | <i>Joint venture</i> |
|--------------------------------------|-------------------------------|-------------------|----------------------|
| Turnover                             | 3,00,000                      | 4,00,000          | 2,00,000             |
| <i>Less:</i> Cost of sales           | <u>(2,14,000)</u>             | <u>(2,80,000)</u> | <u>(1,40,000)</u>    |
| Gross profit                         | 86,000                        | 1,20,000          | 60,000               |
| <i>Less:</i> Administration expenses | <u>(53,200)</u>               | <u>(90,000)</u>   | <u>(20,000)</u>      |
| Operating profit                     | 32,800                        | 30,000            | 40,000               |
| <i>Less:</i> Exceptional charge      | (5,400)                       | (3,000)           | (1,000)              |
| <i>Add:</i> Dividends from Associate | 1,600                         |                   |                      |
| Dividends from Joint venture         | <u>5,000</u>                  | <u>        </u>   | <u>        </u>      |

|   |                 |                |                |
|---|-----------------|----------------|----------------|
| Profit before taxation                      | 34,000          | 27,000         | 39,000         |
| <i>Less:</i> Tax                            | <u>(7,000)</u>  | <u>(8,000)</u> | <u>(6,000)</u> |
| Profit after taxation                       | 27,000          | 19,000         | 33,000         |
| <i>Less:</i> Minority interest              | (2,000)         | -              | -              |
| Dividend paid                               | -               | (8,000)        | (6,000)        |
| Dividend proposed                           | <u>(10,000)</u> | <u>-</u>       | <u>(4,000)</u> |
| Retained profit for the year                | 15,000          | 11,000         | 23,000         |
| <i>Add:</i> Retained profit brought forward | <u>22,000</u>   | <u>16,000</u>  | <u>60,000</u>  |
| Retained profit carried forward             | <u>37,000</u>   | <u>27,000</u>  | <u>83,000</u>  |

You are given the following additional information:

- (a) The parent company purchased its investment in the associate two years ago when the balance on the profit and loss account was ₹ 17,000. The useful life of the goodwill is estimated at ten years and there are no signs of impairment of the goodwill.
- (b) The parent company entered into a joint venture to access a lucrative market in the former East Germany. It set up a company two years ago and has 50 per cent of the voting rights of the company set up for this joint venture.

Prepare the consolidated balance sheet and profit and loss account for the Group for the year ended 31.3.2015.

### Financial Instruments

15. Friendly Ltd. granted ₹ 100 lakhs as loan to its employees on 1<sup>st</sup> January, 2014 at a concessional rate of interest of 4 per cent per annum on the condition that the loan is to be repaid in five equal annual instalments along with interest thereon. You are informed that the prevailing lending rate for such risk profiles is 10% p.a. You are required to find out at what value the loan should be recognized initially and the amount of annual amortization till closure thereof. Show Journal Entries with appropriate narrations that will be recorded in the company's books in the year 2014.

[Present value of an Indian Rupee at a discount rate of 10 per cent per annum for 5 years will be .9090, .8263, .7512, .6829 and .6208 which is to be adopted for the purpose of calculation].

### Share Based Payments

16. Kush Ltd. announced a Share Based Payment Plan for its employees who have completed 3 years of continuous service, on 1<sup>st</sup> April, 2010. The plan is subject to a 3 years vesting period. The following information is supplied to you in this regard:

- (i) The eligible employees can either have the option to claim the difference between the exercise price of ₹ 144 per share and the market price in respect of the share on vesting date in respect of 5,000 shares or such employees are entitled to subscribe to 6,000 shares at the exercise price.
- (ii) Any shares subscribed to by the employees shall carry a 3 year lock in restriction. All shares carry face value of ₹ 10.
- (iii) The current fair value of the shares at (ii) above is ₹ 60 and that in respect of freely tradeable shares is higher by 20%.
- (iv) The fair value of the shares not subjected to lock in restriction at the end of each year increases by a given % from its preceding value as under:

|               | Year 2010-11 | Year 2011-12 | Year 2012-13 |
|---------------|--------------|--------------|--------------|
| % of Increase | 6            | 10           | 15           |

You are required to draw up the following accounts under both options:

- (I) Employee Compensation Account,  
 (II) Provision for Liability Component Account,  
 (III) ESOP Outstanding Account.

#### Mutual Fund

17. (a) On 1.4.2014, a mutual fund scheme had an outstanding of 18 lakhs units of face value of ₹ 10 each. The scheme earned ₹ 162 lakhs in 2014-15, out of which ₹ 90 lakhs was earned in the first half of the year. On 30.9.2014, 2 lakh units were sold at a "NAV" of ₹ 70.

Pass Journal entries for sale of units and distribution of dividend at the end of 2014-15.

#### NBFC

- (b) While closing its books of account on 31<sup>st</sup> March, 2015 a non-banking finance company has its advances classified as follows:

| <i>Particulars</i>                 | <i>₹ in lakhs</i> |
|------------------------------------|-------------------|
| Standard Assets                    | 16,800            |
| Sub-Standard Assets                | 1,340             |
| Secured portion of doubtful debts: |                   |
| - Upto one year                    | 320               |
| - One year to three years          | 90                |
| - More than three years            | 30                |

|                                     |    |
|-------------------------------------|----|
| Unsecured portion of doubtful debts | 97 |
| Loss Assets                         | 48 |

Calculate the amount of provision, which must be made against the advances.

### Valuation of Shares

18. Yogesh Ltd. showed the following performance over 5 years ended 31<sup>st</sup> March, 2015:

| Year Ended on<br>31st March | *Net profit<br>before tax |     | Prior period<br>adjustment | Remarks                                    |
|-----------------------------|---------------------------|-----|----------------------------|--|
|                             | ₹                         |     | ₹                          |  |
| 2011                        | 4,00,000                  | (-) | 1,00,000                   | Relating to 2009-10                        |
| 2012                        | 3,50,000                  | (-) | 2,50,000                   | Relating equally to<br>2009-10 and 2010-11 |
| 2013                        | 6,50,000                  | (+) | 1,50,000                   | Relating to 2011-12                        |
| 2014                        | 5,50,000                  | (-) | 1,75,000                   | Relating to 2011-12                        |
| 2015                        | 6,00,000                  | (-) | 1,00,000                   | Relating to 2011-12                        |
|                             |                           | (+) | 25,000                     | Relating to 2013-14                        |

\*Net profit before tax is after debiting or crediting the figures of loss (-) or gains (+) mentioned under the columns for prior period adjustments.

The net worth of the business as per the balance sheet of 31st March, 2010 is ₹ 6,00,000 backed by 10,000 fully paid equity shares of ₹ 10 each. Reserves and surplus constitute the balance net worth. Yogesh Ltd. has not declared any dividend till date.

You are asked to value equity shares on:

- (a) Yield basis as on 31.3.2015, assuming:
  - (i) 40% rate of tax
  - (ii) anticipated after tax yield of 20%.
  - (iii) differential weightage of 1 to 5 being given for the five years starting on 1.4.2010 for the actual profits of the respective years.
- (b) Net asset basis as per corrected balance sheets for each of the six years ended 31.3.2015.

Looking to the performance of the company over the 5 years period, would you invest in the company?

**Valuation of Business**

19. Shobhit Garments Ltd. produces and sells to retailers a certain range of fashion clothings.

- (a) They have made the following estimates of potential cash flows for the next 10 years.

| Year                    | 1     | 2     | 3     | 4     | 5     | 6     | 7     | 8     | 9      | 10     |
|-------------------------|-------|-------|-------|-------|-------|-------|-------|-------|--------|--------|
| Cash Flows (₹ in lakhs) | 30,00 | 34,00 | 40,00 | 50,00 | 60,00 | 68,00 | 76,00 | 90,00 | 100,00 | 120,00 |

- (b) Style Ltd. is a company which owns a series of boutiques in a certain locality. The boutiques buy clothes from various suppliers and retail them. Each boutique has a manager and an assistant but all purchasing and policy decisions are taken centrally. Independent cash flow estimates of Style Ltd. were as follows:

| Year                    | 1   | 2   | 3   | 4   | 5   | 6   | 7    | 8    | 9    | 10   |
|-------------------------|-----|-----|-----|-----|-----|-----|------|------|------|------|
| Cash flows (₹ in lakhs) | 240 | 320 | 400 | 560 | 680 | 920 | 1040 | 1200 | 1320 | 1600 |

- (c) Shobhit Garments Ltd. is interested in acquiring Style Ltd. in order to get some additional retail outlets. They make the following cost-benefit calculations:

- (i) Net value of assets of Style Ltd.

|   | ₹ in lakhs   |
|---|--------------|
| Tangible Fixed Assets                                 | 1600         |
| Investments   | 400          |
| Stock & Receivables                                   | <u>800</u>   |
|   | 2,800        |
| Less: Current Liabilities                             | <u>(800)</u> |
| Net Assets represented by Equity Shares of ₹ 100 each | <u>2,000</u> |

- (ii) Tangible Fixed Assets amounting to ₹ 100 lakhs cannot be used and their net realisable value is ₹ 90 lakhs.
- (iii) Stock & Receivables can be realised immediately at ₹ 940 lakhs.
- (iv) Investment can be disposed off for ₹ 424 lakhs.

- (v) Some workers of Style Ltd. are to be retrenched for which estimated compensation is ₹ 260 lakhs.
- (vi) Current Liabilities are to be discharged immediately.
- (vii) ₹ 14.10 lakhs are payable on account of a compensation claim awarded against Style Ltd., which has been treated as a Contingent Liability in the accounts on which 20% was provided for.
- (viii) Shobhit Garments Ltd. will invest ₹ 50 lakhs for renovating the building of Style Ltd. immediately on takeover and will invest further ₹ 50 lakhs at the end of second year.
- (ix) Expected cash flows of the combined business will be as follows:

| Year                     | 1     | 2     | 3     | 4     | 5     | 6     | 7     | 8      | 9      | 10     |
|--------------------------|-------|-------|-------|-------|-------|-------|-------|--------|--------|--------|
| Cash flow<br>(₹ in lacs) | 36,00 | 38,00 | 46,00 | 59,00 | 70,00 | 80,00 | 90,00 | 106,00 | 116,00 | 138,00 |

- (x) Shobhit Garments Ltd. estimates that its Goodwill in the industry will increase by a minimum of ₹ 300 lakhs consequent the acquisition.

Calculate the maximum price per share of Style Ltd. which Shobhit Garments Ltd. can quote. Use 20% as discount factor.

#### Value Added Statement

20. (a) From the following Profit & Loss Account of Brightex Co. Ltd., prepare a gross value added statement for the year ended 31.12.2014:

Show also the reconciliation between gross value added and profit before taxation.

#### Profit and Loss Account for the year ended 31.12.2014

|                                     | Notes | (₹ '000) | (₹ '000)  |
|-------------------------------------|-------|----------|-----------|
| Income:                             |       |          |           |
| Sales                               |       |          | 6,240     |
| Other Income                        |       |          | <u>55</u> |
|                                     |       |          | 6,295     |
| Expenditure:                        |       |          |           |
| Production and operational expenses | 1     | 4,320    |           |
| Administration expenses (Factory)   | 2     | 180      |           |
| Interest & Other charges            | 3     | 624      |           |

|   |  |            |                |
|---|--|------------|----------------|
| Depreciation                                    |  | <u>16</u>  | <u>(5,140)</u> |
| Profit before tax                               |  |            | 1,155          |
| Provision for tax                               |  |            | <u>(55)</u>    |
|   |  |            | 1,100          |
| Balance as per last Balance Sheet               |  |            | <u>60</u>      |
|   |  |            | 1,160          |
| Transferred to fixed assets replacement reserve |  | 400        |                |
| Dividend paid                                   |  | <u>160</u> | <u>(560)</u>   |
| Surplus carried to Balance Sheet                |  |            | <u>600</u>     |

Notes:

1. Production & Operation expenses:

|                                  |              |
|----------------------------------|--------------|
| Consumption of raw materials     | 3,210        |
| Consumption of stores            | 40           |
| Local tax                        | 8            |
| Salaries to administrative staff | 620          |
| Other manufacturing expenses     | <u>442</u>   |
|                                  | <u>4,320</u> |

2. Administration expenses include salaries and commission to directors.

3. Interest on other charges include:

|   |     |
|---|-----|
| (a) Interest on bank overdraft (Overdraft is of temporary nature)                                   | 109 |
| (b) Fixed loan from I.C.I.C.I.  | 51  |
| (c) Working capital loan from I.F.C.I.  | 20  |
| (d) Excise duties amount to one-tenth of total value added by manufacturing and trading activities. |     |

**Economic Value Added**

(b) Prosperous Ltd. provides you the following data to calculate Economic Value Added (EVA):

|   |     |
|---|-----|
| 30 crores Equity Shares of ₹ 10 each          |     |
| 1 crores, 15% Preference Shares of ₹ 100 each |     |
| 8 crores, 15% Debentures of ₹ 100 each        |     |
| Tax Rate                                      | 30% |

|   |              |
|---|--------------|
| Beta Factor                             | 1.5          |
| Market Rate of Return                   | 15.5%        |
| Equity Market Risk Premium              | 9%           |
| Financial Leverage                      | 1.5 times    |
| Immovable Property (held as Investment) | ₹ 100 crores |

### SUGGESTED ANSWERS / HINTS

1. (a) As per para 9 of AS 2 'Valuation of Inventories', for inclusion in the cost of inventory, allocation of fixed production overheads is based on the normal capacity of the production facilities.

In this, case finished stock has been valued at a standard cost of ₹ 1.8 lakhs per computer which incidentally synchronizes with the value computed on the basis of absorption costing as under:

|                               |              | (₹ in lakhs) |
|-------------------------------|--------------|--------------|
| Materials                     |              | 400          |
| Direct Labour                 |              | 250          |
| Variable production overheads |              | 150          |
| Fixed production overheads    | 290          |              |
| Less: Interest                | <u>(100)</u> | <u>190</u>   |
| Total cost                    |              | <u>990</u>   |

Number of computers produced = 550 computers (Assumed to be normal production)

Cost per computer ₹ 990 lakhs/550 computers = ₹ 1.80 lakhs

Policy of the company to value closing stock on the basis of standard costing is not as per AS 2. As per para 18 of AS 2, the techniques of standard cost method may be used for convenience if the result approximates to the actual cost. However, standard cost should be regularly reviewed, if necessary, and be revised in the light of the current conditions. In the instant case, the cost of inventory can be conveniently calculated as per absorption costing. Therefore, there is no reason to adopt standard costing method.

- (b) As per para 15 of AS 3 "Cash Flow Statements", cash payment for acquisition of shares, warrant or debt instruments shall be shown under investing activities if they are not qualified as cash equivalent.

As per para 6 of AS 3, an investment shall be qualified as cash equivalent if it is readily convertible to a known amount of cash i.e. it has short maturity of say three months or less from the date of acquisition.

It is given in the question that the Commercial Papers purchased by Finance House Ltd. has a ready market for its sale/purchase. Therefore, it should be considered as cash equivalent & not to be shown under Investing Activity.

2. (a) Losses on long-lived assets to be disposed of are neither unusual nor infrequent occurrences. Hence, it cannot be considered as an extraordinary item. Therefore, Answer (a) is incorrect. Answer (c) is incorrect because these losses are not part of selling or general and administrative expenses and they are not disclosed net of tax. Answer (d) is incorrect, because discontinued operations result from disposal of a business and not from the disposal of long-lived assets held for resale. As per AS 5 "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies" losses associated with long-lived assets, which are to be disposed of, are to be reported as a component of income from continuing operations before income-taxes for entities preparing income statements and are disclosed separately. Therefore, answer (b) is correct.

(b) (i) Depreciation to be charged in the Profit and Loss Account

|  | ₹               |
|--|-----------------|
| Depreciation on old Machinery<br>[20% on ₹ 6,32,000 for 3 months (01.4.14 to 30.6.14)]                             | 31,600          |
| <i>Add:</i> Depreciation machinery acquired on 01.06.2014<br>(₹ 1,20,000 x 20% x 10/12)                            | 20,000          |
| Depreciation on Machinery after adjustment of Exchange<br>[20% of ₹ (6,32,000 - 1,89,000 + 2,56,000) for 9 months] | <u>1,04,850</u> |
| Total Depreciation to be charged in Profit and Loss A/c  | <u>1,56,450</u> |

(ii) Book Value of Plant and Machinery as on 31.03.2015

|   | ₹               | ₹                 |
|---|-----------------|-------------------|
| Balance as per books on 01.04.2014                    |                 | 6,32,000          |
| <i>Add:</i> Included in purchases on 01.06.2014       | 1,20,000        |                   |
| <i>Add:</i> Purchase on 30.06.2014                    | <u>2,56,000</u> | <u>3,76,000</u>   |
|   |                 | 10,08,000         |
| <i>Less:</i> Book value of Machine sold on 30.06.2014 |                 | <u>(1,89,000)</u> |
|   |                 | 8,19,000          |

|  |                   |
|--|-------------------|
| Less: Depreciation on machinery in use<br>(1,56,450-9,450) | <u>(1,47,000)</u> |
| Book value as on 31.03.2015                                | <u>6,72,000</u>   |

## (iii) Loss on exchange of Machinery

|  | ₹                 |
|--|-------------------|
| Book value of machinery as on 01.04.2014 | 1,89,000          |
| Less: Depreciation for 3 months          | <u>(9,450)</u>    |
| WDV as on 30.06.2014                     | 1,79,550          |
| Less: Exchange value                     | <u>(1,75,000)</u> |
| Loss on exchange of machinery            | <u>4,550</u>      |

## 3. (a) Statement showing analysis of the contract details

|     |   | (₹ in crores)        |   |                       |
|-----|---|----------------------|---|-----------------------|
|     |   | Year I               | Year II   | Year III              |
| (a) | Initial revenue agreed                            | 900                  | 900   | 900                   |
| (b) | Increase in contract revenue                      | -                    | 20  | 20                    |
| (c) | Total Contract Value                              | 900                  | 920   | 920                   |
| (d) | Contract cost incurred upto the date of reporting | 161                  | 574<br>(excluding ₹ 10 crores of material stored) | 820                   |
| (e) | Estimated cost to complete                        | 644                  | 246   | -                     |
| (f) | Total estimated contract                          | 805                  | 820   | 820                   |
| (g) | Stage of Completion<br>(d/f 100)                  | 20%<br>(161/805x100) | 70%<br>(574/820x100)                              | 100%<br>(820/820x100) |

## Statement showing amount of revenue, expenses and profit to be recognized in the Statement of Profit and Loss in three years (₹ in crores)

|                        | Upto reporting date | Recognised in the prior year | Recognized in the current year |
|------------------------|---------------------|------------------------------|--------------------------------|
| Year I                 |                     |                              |                                |
| Revenue (900 x 20/100) | 180                 | -                            | 180                            |

|                         |            |            |            |
|-------------------------|------------|------------|------------|
| Expenses                | <u>161</u> | <u>-</u>   | <u>161</u> |
| Profit                  | <u>19</u>  | <u>-</u>   | <u>19</u>  |
| <b>Year II</b>          |            |            |            |
| Revenue (920 x 70/100)  | 644        | 180        | 464        |
| Expenses (820 x 70/100) | <u>574</u> | <u>161</u> | <u>413</u> |
| Profit                  | <u>70</u>  | <u>19</u>  | <u>51</u>  |
| <b>Year III</b>         |            |            |            |
| Revenue                 | 920        | 644        | 276        |
| Expenses                | <u>820</u> | <u>574</u> | <u>246</u> |
| Profit                  | <u>100</u> | <u>70</u>  | <u>30</u>  |

- (b) The Accounting Standard Board of ICAI has come up with an announcement in the earlier years wherein it clarified that the inter-divisional transfers / sales are not revenue as per AS 9 "Revenue Recognition". According to it, in case of inter-divisional transfers, risks and rewards remain within the enterprise and also there is no consideration from the point of view of the enterprise as a whole. Therefore, the recognition criteria for revenue recognition are also not fulfilled in respect of inter-divisional transfers. Hence, no revenue is recognized in the case of inter-divisional transfers.
- (c) As per AS 9 'Revenue Recognition', in a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method as the service is performed, whichever relates the revenue to the work accomplished.

In the given case, income accrues when the related advertisement appears before public. The advertisement service would be considered as performed on the day the advertisement is published and hence revenue is recognized on that date. In this case, 15.03.2015 is the date of publication of the magazine.

Hence, ₹ 3,00,000 (₹ 2,40,000 + ₹ 60,000) is recognized as income in March, 2015. The terms of payment are not relevant for considering the date on which revenue is to be recognized. Since, the revenue of ₹ 3,00,000 will be recognised in the March, 2015, ₹ 60,000 will be treated as amount due from advertisers as on 31.03.2015 and ₹ 2,40,000 will be treated as payment received against the sale.

However, if the publication is delayed till 02.04.2015 revenue recognition will also be delayed till the advertisements get published in the magazine. In that case revenue of ₹ 3,00,000 will be recognized in the year ended 31.03.2016 after the magazine is published on 02.04.2015. The amount received from sale of advertising space on 10.03.2015 of ₹ 2,40,000 will be considered as an advance from advertisers as on 31.03.2015.

4. (a) As per para 32 of AS 10 'Accounting for Fixed Assets', on disposal of a previously revalued item of fixed assets, the difference between net disposal proceeds and the net book value is normally charged or credited to the profit and loss statement except that to the extent such a loss is related to an increase which was previously recorded as a credit to revaluation reserve and which has not been subsequently reversed or utilized, it is charged directly to that account.

Accordingly, the amount standing in revaluation reserve account following the retirement or disposal of an asset, which relates to that asset, may be transferred to general reserve. Hence, the following journal entries are to be passed to reverse the effect already given in the books of Orbit Ltd.:

|                                |     | (₹ in lakhs) |     |
|--------------------------------|-----|--------------|-----|
| Profit on sale of property A/c | Dr. | 200          |     |
| To Cost of goods sold A/c      |     |              | 150 |
| To General reserve A/c         |     |              | 50  |

- (b) Exchange differences arising on restatement or repayment of liabilities incurred for the purpose of acquiring fixed assets should be adjusted in the carrying amount of the respective fixed assets as Path Ltd. has exercised the option and it is long term foreign currency monetary item.

Thus, the entire exchange loss due to variation of ₹ 20 lakhs on 31.03.2015 on payment of US \$ 10 lakhs, should be added to the carrying amount of fixed assets and not to the cost of goods sold. Further, depreciation on the unamortized depreciable amount should also be provided, in accordance with AS 6 "Depreciation Accounting".

**Calculation of Exchange loss:**

Foreign currency loan (in ₹) = (50 lakhs \$ x ₹ 60) = ₹ 3,000 lakhs

Exchange loss on outstanding loan on 31.03.2015 = ₹ 40 lakhs US \$ x (62.00-60.00) = ₹ 80 lakhs.

So, ₹ 80 lakhs should also be added to cost of fixed asset with corresponding credit to outstanding loan in addition to ₹ 20 lakhs on account of exchange loss on payment of instalment. The total cost of fixed asset to be increased by ₹ 100 lakhs.

Total depreciation to be provided for the year 2014-15 = 20% of (₹ 3,000 lakhs + 100 lakhs) = ₹ 620 lakhs.

5. (a) (i) Whether a subsidy applied is to be classified as prior period item as per AS 5, depends upon whether the company has committed an error in 2013-14 by not recognising the subsidy? The answer is in para 13 of AS 12 "Accounting for Government Grants" which permits recognition of grant only when there is reasonable assurance that (i) the enterprise will comply with the conditions

attached to them and (ii) the subsidy will be received. Mere making of an application does not provide the reasonable assurance that the subsidy will be received. Letter of sanction from IREDA is required to provide this assurance. Since, the subsidy was granted in June, 2014 after approval of accounts, non-recognition of grant in 2013-14 will not be considered as an error. Hence, this is not a prior period item. Therefore, the company was right in not recognizing the grant.

Further, AS 4 requires adjustment of events occurring after the balance sheet date only upto the date of approval of accounts by the Board of Directors. In view of this, the company is correct in not adjusting the same in the accounts in the year 2013-14.

- (ii) The subsidy should be deducted from the cost of the generator. The revised unamortised amount of generator should be written off over the remaining useful life.

Alternatively, the same may be treated as Deferred Income and allocated over the remaining useful life in the proportion in which depreciation is charged.

- (iii) Here in this case, the opinion given in (i) and (ii) above would change. AS 4 requires the value of assets and liabilities to be adjusted for events occurring after the balance sheet date which occur upto the date of approval of accounts by the Board of Directors if they confirm the conditions existing at the balance sheet date. Since, in this case books of account have not been approved, grant of subsidy will be considered as an adjusting event. Hence, the accounts should be adjusted for the subsidy in 2013-14. The subsidy should be credited to the cost of the generator.

Alternatively, the subsidy may be treated as deferred income to be written off over the useful life in proportion in which depreciation is written off.

- (iv) As per the past experience of the company wherein similar applications were made and subsidy was granted on all occasion, one can conclude that the reasonable assurance that subsidy will be received, as envisaged in Para 13, is there in the form of past record. If there are no changes in the subsidy scheme and the application is submitted in the same manner as in the past, then subsidy should have been accounted in 2013-14 itself. The opinion in (i) and (ii) would change. The opinion in (iii) above will hold good in this case also.
- (b) (i) The accounting treatment 'at cost' under the head 'Long Term Investment' in the separate financial statements of the company without providing for any diminution in value is correct and is in accordance with the provisions of AS 13 provided that there is no decline, other than temporary, in the value of investment.

- (ii) If the decline in the value of investment is not other than temporary compared to the time when the shares were purchased, no provision is required to be made. The reduction in market value should not be considered in isolation to determine the decline, other than temporary. The amount of the provision for diminution in the value of investment may be ascertained considering the factors indicated in paragraph 17 of AS 13.
  - (ii) The provision for diminution in the value of investment should be a charge to the profit and loss statement. As per the requirements of AS 13, the diminution in the value of investment can neither be accounted for as deferred revenue expenditure nor it can be written off in the statement of profit and loss.
  - (iii) The long-term investments should be carried at cost as per the requirements of AS 13. The amount paid over and above the market price should be treated as cost and cannot be accounted for separately.
6. (a) ICAI has opined that investments other than investment properties are not qualifying assets as per AS 16 "Borrowing Costs". Therefore, interest cost of holding such investments cannot be capitalized. Further, even interest in respect of investment properties can only be capitalized if such properties meet the definition of qualifying asset, namely, that it necessarily takes a substantial period of time to get ready for its intended use or sale. Even where the investment properties meet the definition of 'qualifying asset', for the capitalisation of borrowing costs the other requirements of the standard such as that borrowing cost should be directly attributable to the acquisition or construction of the investment property and suspension of capitalization as per paragraphs 17 and 18 of AS 16 have to be complied with.
- (b) The interest expense relating to overdrafts and other operating liabilities identified to a particular segment should not be included as a part of the segment expense unless the operations of the segment are primarily of a financial nature or unless the interest is included as a part of the cost of inventories.
- In case interest is included as part of the cost of inventories where it is so required as per AS 16 "Borrowing Costs", read with AS 2 "Valuation of Inventories", and those inventories are part of segment assets of a particular segment, such interest should be considered as a segment expense.
- In this case, the amount of such interest and the fact that the segment result has been arrived at after considering such interest should be disclosed by way of a note to the segment result.
7. (a) P Ltd. has direct economic interest in R Ltd. to the extent of 14%, and through Q Ltd. (in which it is the majority shareholders) it has further control of 12% in R Ltd. (60% of Q Ltd.'s 20%). These two taken together (14% + 12%) make the total control of 26%.

AS 18 'Related Party Disclosures', defines 'related party' as one that has at any time during the reporting period, the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Since, P Ltd. has total control of 26% (directly and indirectly by Q Ltd.) in R Ltd. which is less than half of the voting power of R Ltd., P Ltd. is said to have significant influence over R Ltd. Also it is given in the question that R Ltd. is a listed company and regularly supplies goods to P Ltd. Therefore, related party disclosure, as per AS 18, is required by R Ltd. in its financial statements, in respect of goods supplied to P Ltd.

**(b) (i) Determination of nature of lease**

Fair value of asset = ₹ 7,00,000

Unguaranteed residual value = ₹ 70,000

Present value of residual value at the end of 4<sup>th</sup> year = ₹ 70,000 x 0.683  
= ₹ 47,810

Present value of lease payment recoverable = ₹ 7,00,000 - ₹ 47,810  
= ₹ 6,52,190

The percentage of present value of lease payment to fair value of the asset is  
= (₹ 6,52,190/₹ 7,00,000)x100  
= 93.17%

Since, it substantially covers the major portion of lease payment and life of the asset, the lease constitutes a finance lease.

**(ii) Calculation of Unearned Finance Income**

Annual lease payment = ₹ 6,52,190 / 3.169  
= ₹ 2,05,803 (approx.)

Gross investment in the lease = Total minimum lease payment + unguaranteed residual value  
= (₹ 2,05,803 x 4) + ₹ 70,000  
= ₹ 8,23,212 + ₹ 70,000  
= ₹ 8,93,212

Unearned finance income = Gross investment – Present value of minimum lease payment and unguaranteed residual value.  
= ₹ 8,93,212 – ₹ 7,00,000 (₹ 6,52,190 + ₹ 47,810)  
= ₹ 1,93,212.

8. (a) The following dates should be considered for consideration of weights for calculation of weighted average number of shares in the given situations:
- (i) Equity Shares issued in exchange of cash - Date of Cash receivable
  - (ii) Equity Shares issued as a result of conversion of a debt instrument - Date of conversion
  - (iii) Equity Shares issued in exchange for the settlement of a liability of the enterprise - Date on which settlement becomes effective
  - (iv) Equity Shares issued for rendering of services to the enterprise - When the services are rendered
  - (v) Equity Shares issued in lieu of interest and/or principal of another financial instrument - Date when interest ceases to accrue
  - (vi) Equity Shares issued as consideration for the acquisition of an asset other than in cash - Date on which the acquisition is recognised.

A Potential Equity Share is a financial instrument or other contract that entitles, or may entitle its holder to equity shares.

- (b) Mere gradual phasing out is not considered as discontinuing operation as defined under para 3 of AS 24, 'Discontinuing Operations'.

Examples of activities that do not necessarily satisfy criterion of the definition, but that might do so in combination with other circumstances, include:

- (1) Gradual or evolutionary phasing out of a product line or class of service;
- (2) Discontinuing, even if relatively abruptly, several products within an ongoing line of business;
- (3) Shifting of some production or marketing activities for a particular line of business from one location to another; and
- (4) Closing of a facility to achieve productivity improvements or other cost savings.

A Reportable business segment or geographical segment as defined in AS 17, would normally satisfy criteria (b) of the definition.

In view of the above the answers are:

- (i) No, the companies' strategic plan has no final approval from the board through a resolution and there is no specific time bound activities like shifting of assets and employees. Above all, the new segment i.e. commercial vehicle production line in a new factory has not started.
- (ii) No, the resolution is salient about stoppage of the Car segment in definite time period. Though, sale of some assets and some transfer proposal were passed through a resolution to the new factory, closure road map and new segment starting roadmap are missing. Hence, AS 24 will not be applicable.

(iii) Yes, phased and time bound programme resolved in the board clearly indicates the closure of the passenger car segment in a definite time frame and will constitute a clear roadmap. Hence, this action will attract compliance of AS 24.

9. (a) Para 28 of AS 25 "Interim Financial Reporting" states that revenues and gains should be recognised in interim reports on the same basis as used in annual reports. As at September 30, 2014, X Ltd. would report the entire ₹ 3,00,000 loss on the disposal of its business segment since the loss was incurred during the interim period.

A cost charged as an expense in an annual period should be allocated among the interim periods, which are clearly benefited from the expense, through the use of accruals and/or deferrals. Since ₹ 80,000 property tax payment relates to the entire 2014 calendar year, only ₹ 40,000 of the payment would be reported as an expense at September 30, 2014, while out of the remaining ₹ 40,000, ₹ 20,000 for January, 2014 to March, 2014 would be shown as payment of the outstanding amount of previous year and another ₹ 20,000 related to quarter October, 2014 to December, 2014, would be reported as a prepaid expense.

- (b) Case 1: As per para 68 of AS 28 "Impairment of Assets" if an active market exists for the output produced by an asset or a group of assets, this asset or group of assets should be identified as a separate cash-generating unit, even if some or all of the output is used internally.

X could sell its products in an active market and, so, generate cash inflows from continuing use that would be largely independent of the cash inflows from Y. Therefore, it is likely that X is a separate cash-generating unit, although part of its production is used by Y.

It is likely that Y is also a separate cash-generating unit. Y sells 80% of its products to customers outside the reporting enterprise. Therefore, its cash inflows from continuing use can be considered to be largely independent.

Internal transfer prices do not reflect market prices for X's output. Therefore, in determining value in use of both X and Y, the enterprise adjusts financial budgets/forecasts to reflect management's best estimate of future market prices for those of X's products that are used internally.

Case 2: It is likely that the recoverable amount of each plant cannot be assessed independently from the recoverable amount of the other plant because:

- (a) the majority of X's production is used internally and could not be sold in an active market. So, cash inflows of X depend on demand for Y's products. Therefore, X cannot be considered to generate cash inflows that are largely independent from those of Y; and
- (b) the two plants are managed together.

As a consequence, it is likely that X and Y together is the smallest group of assets that generates cash inflows from continuing use that are largely independent.

10. (a) As per AS 29 'Provisions, Contingent Liabilities and Contingent Assets', a provision should be recognised when:
- (i) An enterprise has a present obligation as a result of past event;
  - (ii) It is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
  - (iii) A reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision should be recognised.

A contingent liability is disclosed, unless the possibility of an outflow of resources embodying economic benefits is remote. The possibility of an outflow of resources embodying economic benefits is remote in the given situation, since the directors of WZW Ltd. are of the opinion that the claim can be successfully resisted by the company. Therefore, the company shall not disclose the same as contingent liability. However, following note in this regard may be given in annual accounts:

"Litigation is in process against the company relating to a dispute with a competitor who alleges that the company has infringed patents and is seeking damages of ₹ 1,000 lakhs. However, the directors are of the opinion that the claim can be successfully resisted by the company".

- (b) Note 6 (B) given under Part I of Schedule III to the Companies Act, 2013 provides that debit balance of Statement of Profit and Loss (after all allocations and appropriations) shall be shown as a negative figure under the head 'Surplus'. Similarly, the balance of 'Reserves and Surplus', after adjusting negative balance of surplus, shall be shown under the head 'Reserves and Surplus' even if the resulting figure is in the negative.

In this case, the debit balance of profit and loss i.e. ₹ 250 lakhs exceeds the total of all the reserves i.e. ₹ 230 lakhs. Therefore, balance of 'Reserves and Surplus' after adjusting debit balance of profit and loss is negative by ₹ 20 lakhs, which should be disclosed on the face of the balance sheet as the sub-heading 'Reserves & Surplus' under the heading 'Shareholders' fund'. Thus, the treatment done by the company is incorrect.

11. (a)

|  | <i>Existing Accounting Standards</i>  | <i>IFRS</i>   |
|--|---|---|
| <b>Consolidated Financial Statements</b> | The accounting standard does not mandate an enterprise to present consolidated financial statements; but, if the enterprise | Under IFRS 10, if an entity is a parent, then it is mandatory to prepare consolidated financial statements (CFS). |

|  |   |  |
|--|---|--|
|  | presents consolidated financial statements for complying with the requirements of any statute or otherwise, it should prepare and present consolidated financial statements in accordance with AS 21. |  |
|  | As per AS 21, subsidiary is excluded from consolidation<br>(a) when control is intended to be temporary or<br>(b) when subsidiary operates under severe long term restrictions.                       | As per IFRS 10, an entity that is a parent shall be excluded to present consolidated financial statements when<br>(i) it is a wholly or partially owned subsidiary of another entity and all its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting consolidated financial statements;<br>(ii) its debt or equity instruments are not traded in a public market;<br>(iii) it did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; and<br>(iv) its ultimate or any intermediate parent produces consolidated financial statements that are available for public use and comply with IFRSs. |
|  | A mere ownership of more than 50% of equity shares is sufficient to constitute control under AS 21  | Control specifies that an investor has control over an investee if and only if it has  |

|   |   |
|---|---|
| or control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise so as to obtain economic benefits from its activities.   | power over the investee, exposure, or rights, to variable returns from its involvement with the investee and the ability to use its power over the investee to affect the amount of the investor's returns.   |
| In case an entity is controlled by two entities (one controls by virtue of ownership of majority of the voting power of that enterprise and other controls, by virtue of an agreement or otherwise, the composition of the board of directors so as to obtain economic benefit from its activities), an enterprise is controlled by two enterprises as per the definition of 'control', the enterprise will be considered as subsidiary of both the controlling enterprises and, therefore, both the enterprises need to consolidate the financial statements of that enterprise. | When two or more investors collectively control an investee, in such a case no investor can direct the activities without the co-operation of the others or no investor individually controls the investee.<br>Each investor would account for its interest in the investee in accordance with IFRS 11 "Joint Arrangements", IAS 28 "Investments in Associates and Joint Ventures" or IFRS 9 "Financial Instruments". |
| For considering share ownership, potential voting rights of the investee held by investor are not taken into account as per AS 21.  | As per IFRS 10, effects of potential voting rights are considered when assessing whether an entity has control over the subsidiary.   |
| AS 21 permits the use of financial statements of the subsidiaries drawn upto a date different from the date of financial statements of the parent after making adjustments regarding effects of significant transactions. The difference between the reporting dates should not be more than six months.  | As per IFRS 10, the length of difference in the reporting dates of the parent and the subsidiary should not be more than three months.  |
| As per AS 21, no deferred tax is recognised on elimination of   | IFRS 10 states that IAS 12 applies to temporary   |

|                    |  |   |
|--------------------|--|---|
|                    | intra-group transactions.  | differences that arise from the elimination of profits and losses resulting from intra-group transactions.  |
| Joint Arrangements | AS 27 recognises three forms of joint venture namely:<br>a) jointly controlled operations;<br>b) jointly controlled assets; and<br>c) jointly controlled entities. | As per IFRS 11 a joint arrangement is either a joint operation or a joint venture. Such classification of joint arrangement depends upon the rights and obligations of the parties to the arrangement and disregards the legal structure. |
|                    | AS 27 prescribes the use of proportionate consolidation method only.   | IFRS 11 provides that a venturer should recognise its interest in joint venture using only equity method.   |
|                    | AS 27 requires application of the proportionate consolidation method only when the entity has subsidiaries and prepares Consolidated Financial Statements.         | IFRS 11 requires application of equity method in financial statements other than separate financial statements in case of a joint venture, even if the venturer does not have any subsidiary in the financial statements.                 |

(b) There are many beneficiaries of convergence with IFRSs such as-

**The Economy:** When the markets expand globally the need for convergence increases since the convergence benefits the economy by increasing growth of its international business. It facilitates maintenance of orderly and efficient capital markets and also helps to increase the capital formation and thereby economic growth. It encourages international investing and thereby leads to more foreign capital flows to the country.

**Investors:** A strong case for convergence can be made from the viewpoint of the investors who wish to invest outside their own country. Investors want the information that is more relevant, reliable, timely and comparable across the jurisdictions. Financial statements prepared using a common set of accounting standards help investors better understand investment opportunities as opposed to financial statements prepared using a different set of national accounting standards. Investors' confidence is strong when accounting standards used are globally

accepted. Convergence with IFRSs contributes to investors' understanding and confidence in high quality financial statements.

*The industry:* A major force in the movement towards convergence has been the interest of the industry. The industry is able to raise capital from foreign markets at lower cost if it can create confidence in the minds of foreign investors that their financial statements comply with globally accepted accounting standards. With the diversity in accounting standards from country to country, enterprises which operate in different countries face a multitude of accounting requirements prevailing in the countries. The burden of financial reporting is lessened with convergence of accounting standards because it simplifies the process of preparing the individual and group financial statements and thereby reduces the costs of preparing the financial statements using different sets of accounting standards.

- (c) The listed companies in India are governed by one single regulator that is SEBI. SEBI is the regulator for the securities market in India. SEBI gets statutory powers through the SEBI Act, 1992 for protecting the interests of investors, developing, promoting and regulating the securities market in India.

SEBI majorly covers the following under its jurisdiction:

- Corporates in the issuance of capital and transfer of securities; and Intermediaries;
- Persons associated with securities market.

The Listing Agreement is a charter, issued by SEBI for all the listed companies and other entities which are covered through SEBI Act, 1992. This charter dictates the terms and conditions for the listed entities, which are to be mandatorily followed by them. In case, the said terms are not followed, these entities will be subject to the penal provisions, as laid down under the SEBI Act, 1992. The Listing Agreement gets amended from time to time, depending upon market and other economic conditions and to keep pace with other regulations in India.

Apart from the requirements with respect to registration and other compliance, SEBI emphasises much on the disclosures to be made by the listed entities to make the results of these entities transparent to the investors. SEBI has imposed a number of mandatory disclosures and other requirements on the listed entities in India. Some of these are:

1. Clause 32
  - (i) Sending Annual Report
    - Soft copies of full annual report are required to be sent to all those shareholder(s) who have registered their email address for this purpose.
    - Hard copy of statement containing the salient features of all the

prescribed documents is sent to those shareholder(s) who have not registered.

- Hard copy of full annual report is sent to those shareholders, who request for the same.

(ii) Disclosures in compliance with AS 18 on "Related Party Transactions" in its Annual Report.

2. Clause 40B

Compliance with Takeover Code

3. Clause 41

- Interim unaudited financial results are required to be disclosed and published.
- If the name of the company is changed due to any new line of business, separate disclosure of net sales or income, expenditure and net profit or loss after tax figures pertaining to the said new line of business is required in the financial statements. This separate disclosure shall continue for the three years succeeding the date of change in the name.

4. Clause 49

Compliance of Corporate governance explanation

5. Clause 53

(i) Companies are required to notify to stock exchange(s) and put on their website on immediately entering into agreement(s) with media companies, with respect to the following information:

- Disclosure regarding the shareholding (if any) of such media companies/associates in the company, nominee of such media company/companies/associates on the board of the company, etc
- Disclosures regarding any other back to back treaties/ contracts/ agreements/MoUs or similar instruments entered into by the company with media companies and/ or their associates for the purpose of advertising, publicity, etc

12. (a) Projected Profit and Loss Account of EF Ltd. for the period ending 31<sup>st</sup> March, 2015

| <i>Particulars</i>                | <i>₹</i> |
|-----------------------------------|----------|
| Total Revenue                     |          |
| Dividend Income [50,000 + 17,600] | 67,600   |
| Interest Income                   | 11,250   |

|  |          |
|--|----------|
|  | 78,850   |
| Less: Expenses   |          |
| Finance Costs (Interest on Bank Overdraft)   | (1,600)  |
| Other Expenses [Directors Fee (7,500) + Administrative Expenses (16,000) + Preliminary expenses (8,000)] | (31,500) |
| Profit before tax  | 45,750   |

(b) **Projected Balance Sheet of EF Ltd. as on 31st March, 2015**

|     | Particulars                           | Note No. | (₹)              |
|-----|---------------------------------------|----------|------------------|
| I.  | Equity and Liabilities                |          |                  |
|     | (1) Shareholders' Funds               |          |                  |
|     | (a) Share Capital                     | 1        | 15,70,000        |
|     | (b) Reserves and Surplus              | 2        | 3,49,450         |
|     | (2) Non-Current Liabilities           |          |                  |
|     | (3) Current Liabilities               |          |                  |
|     | (a) Other Current Liabilities         | 3        | <u>23,500</u>    |
|     | Total                                 |          | <u>19,42,950</u> |
| II. | Assets                                |          |                  |
|     | (1) Non-Current Assets                |          |                  |
|     | Non-Current Investments               | 4        | 14,34,000        |
|     | (2) Current Assets                    |          |                  |
|     | (a) Cash and Cash Equivalents (W.N.1) |          | 58,950           |
|     | (b) Other Current Assets              |          | <u>4,50,000</u>  |
|     | Total                                 |          | <u>19,42,950</u> |

**Notes to Accounts:**

|    | Particulars  | (₹)              |
|----|--|------------------|
| 1. | Share Capital  |                  |
|    | Authorised share capital   |                  |
|    | 4,00,000 Equity shares of ₹ 10 each  | <u>40,00,000</u> |
|    | Issued share capital   |                  |
|    | 1,57,000 Equity Shares of ₹ 10 each  | 15,70,000        |
|    | (Of the above 1,19,500 shares were issued for consideration other than cash) |                  |

|    |  |                 |                 |
|----|--|-----------------|-----------------|
| 2. | Reserves and Surplus                     |                 |                 |
|    | Securities Premium [2,39,000 + 1,12,500] |                 | 3,51,500        |
|    | Profit & Loss Account                    | 45,750          |                 |
|    | Less: Interim dividend (₹ 95,000 x 4%)   | <u>(47,800)</u> | <u>(2,050)</u>  |
|    |  |                 | <u>3,49,450</u> |
| 3. | Other Current Liabilities                |                 |                 |
|    | Bank Overdraft                           | 16,000          |                 |
|    | Directors Fee                            | <u>7,500</u>    | 23,500          |
| 4. | Non-current investment                   |                 |                 |
|    | Investment in shares of AB Ltd. @ ₹ 12   | 10,50,000       |                 |
|    | Investment in shares of CD Ltd. @ ₹ 12   | <u>3,84,000</u> | 14,34,000       |

## (c) Computation of Number of Shares to be issued to former shareholders

| Particulars   | AB Ltd.           | CD Ltd.         |
|---|-------------------|-----------------|
|   | ₹                 | ₹               |
| Future Maintainable EBIT  | 2,30,000          | 1,12,000        |
| Less: Interest on Debentures  | <u>(20,000)</u>   | -               |
|   | 2,10,000          | 1,12,000        |
| Less: Income tax @ 50%  | <u>(1,05,000)</u> | <u>(56,000)</u> |
| Profit after tax  | 1,05,000          | 56,000          |
| Less: Preference Dividend   | -                 | <u>(8,000)</u>  |
| Profit to Equity Shareholders   | <u>1,05,000</u>   | <u>48,000</u>   |
| PE Ratio  | 10                | 8               |
| Capitalised Earning   | 10,50,000         | 3,84,000        |
| Number of shares to be exchanged in EF Ltd.<br>@ ₹ 12 (including Premium of ₹ 2 each) | 87,500            | 32,000          |

## Working Note:

## Bank Account

| Particulars                 | ₹        | Particulars                      | ₹        |
|-----------------------------|----------|----------------------------------|----------|
| To Equity Share Capital A/c | 3,75,000 | By Preliminary Expenses          | 8,000    |
| To Securities Premium A/c   | 1,12,500 | By Interest on Bank<br>Overdraft | 1,600    |
| To Dividends from AB Ltd.   | 50,000   | By Advance to AB Ltd.            | 2,50,000 |

|                           |                 |                            |                 |
|---------------------------|-----------------|----------------------------|-----------------|
| To Dividends from CD Ltd. | 17,600          | By Advance to CD Ltd.      | 2,00,000        |
| To Interest Income        | 11,250          | By Interim Dividend        | 47,800          |
|                           |                 | By Balance c/d (Bal. fig.) | <u>58,950</u>   |
|                           | <u>5,66,350</u> |                            | <u>5,66,350</u> |

13. As per para 26 of AS 21 "Consolidated Financial Statements", the losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. The excess, and any further losses applicable to the minority, are adjusted against the majority interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses. If the subsidiary subsequently reports profits, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered. Accordingly,

| Year                               | Profit/(Loss)                         | Minority Interest (30%)                          | Additional Consolidated P & L (Dr.) Cr. | Minority's Share of losses borne by A Ltd. |         | Cost of Control |
|------------------------------------|---------------------------------------|--|---|--|---------|-----------------|
|                                    |                                       |  |   | ₹  | Balance |                 |
| At the time of acquisition in 2008 |                                       | 3,24,000 (W.N.)                                  | -                                       |  |         |                 |
| 2008-09                            | (2,50,000)                            | <u>(75,000)</u>                                  | (1,75,000)                              |  |         | 2,44,000 (W.N.) |
| 2009-10                            | (4,00,000)                            | 2,49,000<br><u>(1,20,000)</u>                    | (2,80,000)                              |  |         | 2,44,000        |
| 2010-11                            | -<br>(5,00,000)                       | 1,29,000<br><u>(1,50,000)</u>                    | (3,50,000)                              |  |         | 2,44,000        |
|                                    | Loss of minority borne by Holding Co. | <u>21,000</u>                                    | <u>(21,000)</u>                         | 21,000                                     | 21,000  |                 |
| 2011-12                            | (1,20,000)                            | Nil<br>-<br>(on application of para 26 of AS 21) | <u>(3,71,000)</u><br>(1,20,000)         | 36,000                                     | 57,000  | 2,44,000        |
| 2012-13                            | 50,000                                | Nil<br>-<br>(on                                  | 50,000                                  | (15,000)                                   | 42,000  | 2,44,000        |

|         |          |  |                                       |          |        |          |
|---------|----------|--|---------------------------------------|----------|--------|----------|
| 2013-14 | 1,00,000 | application of para 26 of AS 21)<br>Nil<br>-<br>(on application of para 26 of AS 21) | 1,00,000                              | (30,000) | 12,000 | 2,44,000 |
| 2014-15 | 1,50,000 | Nil<br>45,000<br><u>(12,000)</u><br>(application of para 26)<br>33,000               | 1,05,000<br><u>12,000</u><br>1,17,000 | (12,000) | Nil    | 2,44,000 |

**Working Note:**

Calculation of Minority interest and Cost of control on 1.1.2008

|                                 |           | <i>Share of Holding Co.</i> | <i>Minority Interest</i> |
|---------------------------------|-----------|-----------------------------|--------------------------|
|                                 | 100%      | 70%                         | 30%                      |
|                                 | (₹)       | (₹)                         | (₹)                      |
| Share Capital                   | 10,00,000 | 7,00,000                    | 3,00,000                 |
| Reserve                         | 80,000    | <u>56,000</u>               | <u>24,000</u>            |
|                                 |           | 7,56,000                    | <u>3,24,000</u>          |
| <i>Less: Cost of investment</i> |           | <u>(10,00,000)</u>          |                          |
| Goodwill                        |           | <u>2,44,000</u>             |                          |

14.

**Consolidated Balance Sheet as on 31.3.2015**

| <i>Particulars</i>           | <i>Note No.</i> | ₹        |
|------------------------------|-----------------|----------|
| I. Equity and Liabilities    |                 |          |
| (1) Shareholder's Funds      |                 |          |
| (a) Share Capital            | 1               | 1,00,000 |
| (b) Reserves and Surplus     | 2               | 1,20,700 |
| (2) Minority Interest (W.N.) |                 | 20,000   |
| (3) Current Liabilities      |                 |          |
| (a) Trade Receivables        | 3               | 23,000   |

|     |                               |   |          |
|-----|-------------------------------|---|----------|
|     | (b) Short Term Provisions     | 4 | 12,500   |
|     | (c) Other Current Liabilities | 5 | 10,000   |
|     | Total                         |   | 2,86,200 |
| II. | Assets                        |   |          |
|     | (1) Non-current assets        |   |          |
|     | (a) Fixed assets              | 6 | 2,15,500 |
|     | (b) Non-current investment    | 7 | 17,200   |
|     | (2) Current assets            | 8 | 53,500   |
|     | Total                         |   | 2,86,200 |

## Notes to Accounts

|    |                                     |                | ₹        |
|----|-------------------------------------|----------------|----------|
| 1. | Share Capital                       |                |          |
|    | Called up equity shares of ₹ 1 each |                | 1,00,000 |
| 2. | Reserves and Surplus                |                |          |
|    | General Reserve                     | 40,000         |          |
|    | Profit and Loss A/c (W.N.3)         | <u>80,700</u>  | 1,20,700 |
| 3. | Trade Receivables                   |                |          |
|    | Holding & Subsidiary                | 20,000         |          |
|    | Joint Venture (50%)                 | <u>3,000</u>   | 23,000   |
| 4. | Short term provisions               |                |          |
|    | Provisions for Tax                  |                |          |
|    | Holding & Subsidiary                | 9,000          |          |
|    | Joint Venture (50%)                 | <u>3,500</u>   | 12,500   |
| 5. | Other Current Liabilities           |                |          |
|    | Proposed Dividend                   |                |          |
|    | Holding & Subsidiary                | 10,000         |          |
|    | Joint Venture (50%)                 | <u>2,000</u>   |          |
|    |                                     | 12,000         |          |
|    | Less: Mutual owings                 | <u>(2,000)</u> | 10,000   |
| 6. | Fixed Assets                        |                |          |
|    | Holding & Subsidiary                | 1,95,000       |          |
|    | Joint Venture (50%)                 | <u>20,500</u>  | 2,15,500 |

|    |  |                |        |
|----|--|----------------|--------|
| 7. | Non-current investment   |                |        |
|    | Investment in Associate (W.N.4)  |                | 17,200 |
| 8. | Current Asset  |                |        |
|    | Holding & Subsidiary   | 21,000         |        |
|    | Joint Venture  | <u>34,500</u>  |        |
|    |  | 55,500         |        |
|    | Less: Mutual Owings (Dividend Receivable from Joint Venture included in Current Asset) | <u>(2,000)</u> | 53,500 |

**Working Notes:****1. Analysis of Profit & Loss of Associate / Joint Venture**

|  | <i>Pre-acquisition</i> | <i>Post-acquisition</i> |
|--|------------------------|-------------------------|
|  | ₹                      | ₹                       |
| Profit as on 31.3.2015                       | 27,000                 |                         |
|  | <u>16,000</u>          | <u>11,000</u>           |
| Share of Associate company (20%)             | <u>3,200</u>           | <u>2,200</u>            |
| Analysis of Profit and Loss of Joint Venture | Nil                    | <u>83,000</u>           |
| Share of Joint Venture (50%)                 |                        | <u>41,500</u>           |

**2. Calculation of Goodwill/Capital Reserve**

|                     | <i>Associate</i> |                 | <i>Joint Venture</i> |                |
|---------------------|------------------|-----------------|----------------------|----------------|
|                     | ₹                |                 | ₹                    |                |
| Investment          |                  | 15,000          |                      | 5,000          |
| Less: Nominal Value | 8,000            |                 | 5,000                |                |
| Capital Profit      | <u>3,200</u>     | <u>(11,200)</u> | —                    | <u>(5,000)</u> |
| Goodwill            |                  | <u>3,800</u>    |                      | <u>Nil</u>     |

**3. Calculation of Consolidated Profit and Loss Account**

|   | ₹             |
|---|---------------|
| Profit and Loss Account of Holding & Subsidiary | 37,000        |
| Add: Share of Associate                         | 2,200         |
| Joint Venture                                   | <u>41,500</u> |
|   | <u>80,700</u> |

## 4. Calculation of Investment in Associate

|                                     | ₹             |
|-------------------------------------|---------------|
| Goodwill (W.N.2)                    | 3,800         |
| Net worth                           | <u>11,200</u> |
| Cost                                | 15,000        |
| <i>Add:</i> Share of Revenue Profit | <u>2,200</u>  |
|                                     | <u>17,200</u> |

## Notes:

- Dividend income is booked without the receipt. This meant that income was on receivable stage appearing on the asset side.
- JCE was formed, by the Venturers two years ago. All the reserves as on the date of consolidation are to be treated as revenue.
- Out of ₹ 17,000 existed at the time of acquisition, only ₹ 16,000 (Opening Balance) is continuing in the books of the associate. Therefore, ₹ 16,000 is taken as capital profit assuming that it is a part of that ₹ 17,000 existed at the time of acquisition.

## 15. (i) Calculation of initial recognition amount of loan to employees

| Year end                    | Cash Inflow |               | Total     | P.V. factor<br>@10% | Present<br>value |
|-----------------------------|-------------|---------------|-----------|---------------------|------------------|
|                             | Principal   | Interest @ 4% |           |                     |                  |
|                             | ₹           | ₹             | ₹         |                     | ₹                |
| 2014                        | 20,00,000   | 4,00,000      | 24,00,000 | 0.9090              | 21,81,600        |
| 2015                        | 20,00,000   | 3,20,000      | 23,20,000 | 0.8263              | 19,17,016        |
| 2016                        | 20,00,000   | 2,40,000      | 22,40,000 | 0.7512              | 16,82,688        |
| 2017                        | 20,00,000   | 1,60,000      | 21,60,000 | 0.6829              | 14,75,064        |
| 2018                        | 20,00,000   | 80,000        | 20,80,000 | 0.6208              | <u>12,91,264</u> |
| Present value or Fair value |             |               |           |                     | <u>85,47,632</u> |

## (ii) Calculation of amortised cost of loan to employees

| Year | Amortised cost<br>(Opening balance)<br>[1] | Interest to be<br>recognised@10%<br>[2] | Repayment<br>(including interest)<br>[3] | Amortised Cost<br>(Closing balance)<br>[4]=[1]+ [2] - [3] |
|------|--|---|--|---|
|      | ₹  | ₹                                       | ₹  | ₹   |
| 2014 | 85,47,632                                  | 8,54,763                                | 24,00,000                                | 70,02,395   |
| 2015 | 70,02,395                                  | 7,00,240                                | 23,20,000                                | 53,82,635   |

|      |           |           |           |           |
|------|-----------|-----------|-----------|-----------|
| 2016 | 53,82,635 | 5,38,264  | 22,40,000 | 36,80,899 |
| 2017 | 36,80,899 | 3,68,090  | 21,60,000 | 18,88,989 |
| 2018 | 18,88,989 | 1,91,011* | 20,80,000 | Nil       |

(iii) **Journal Entries in the books of Friendly Ltd.**  
for the year ended 31<sup>st</sup> December, 2014 (regarding loan to employees)

|   |     | <i>Dr.</i><br><i>Amount (₹)</i> | <i>Cr.</i><br><i>Amount (₹)</i> |
|---|-----|---------------------------------|---------------------------------|
| Staff loan A/c  | Dr. | 1,00,00,000                     |                                 |
| To Bank A/c   |     |                                 | 1,00,00,000                     |
| (Being the disbursement of loans to staff)  |     |                                 |                                 |
| Staff cost A/c ₹ (1,00,00,000–85,47,632) [Refer part (ii)]  | Dr. | 14,52,368                       |                                 |
| To Staff loan A/c*  |     |                                 | 14,52,368                       |
| (Being the write off of excess of loan balance over present value thereof in order to reflect the loan at its present value of ₹ 85,47,632) |     |                                 |                                 |
| Staff loan A/c  | Dr. | 8,54,763                        |                                 |
| To Interest on staff loan A/c   |     |                                 | 8,54,763                        |
| (Being the charge of interest @ market rate of 10% on the loan)   |     |                                 |                                 |
| Bank A/c  | Dr. | 24,00,000                       |                                 |
| To Staff loan A/c   |     |                                 | 24,00,000                       |
| (Being the repayment of first instalment with interest for the year)  |     |                                 |                                 |
| Interest on staff loan A/c  | Dr. | 8,54,763                        |                                 |
| To Profit and loss A/c  |     |                                 | 8,54,763                        |
| (Being transfer of balance of staff loan Interest account to profit and loss account)   |     |                                 |                                 |
| Profit and loss A/c   | Dr. | 14,52,368                       |                                 |
| To Staff cost A/c   |     |                                 | 14,52,368                       |
| (Being transfer of balance of staff cost account to profit and loss account)  |     |                                 |                                 |

\* The difference of ₹ 2,112 (₹ 1,91,011 – ₹ 1,88,899) is due to approximation in computations.

\* Loans and receivables should be measured at amortized cost using the effective rate of interest method as per AS 30 'Financial Instruments: Recognition and Measurement'.

16. (a) **Employees Compensation Account**

| Year    |                                     | ₹               | Year    |                      | ₹               |
|---------|-------------------------------------|-----------------|---------|----------------------|-----------------|
| 2010-11 | To Provision for Liability (W.N. 3) | <u>1,27,200</u> | 2010-11 | By Profit & Loss A/c | <u>1,27,200</u> |
| 2011-12 | To Provision for Liability (W.N. 3) | <u>1,52,633</u> | 2011-12 | By Profit & Loss A/c | <u>1,52,633</u> |
| 2012-13 | To Provision for Liability (W.N. 3) | <u>2,02,867</u> | 2012-13 | By Profit & Loss A/c | <u>2,02,867</u> |

**Provision for Liability Component Account**

| Year    |                | ₹               | Year    |                               | ₹               |
|---------|----------------|-----------------|---------|-------------------------------|-----------------|
| 2010-11 | To Balance c/d | <u>1,27,200</u> | 2010-11 | By Employees Compensation A/c | <u>1,27,200</u> |
| 2011-12 | To Balance c/d | 2,79,833        | 2011-12 | By Balance b/d                | 1,27,200        |
|         |                | <u>2,79,833</u> |         | By Employees Compensation A/c | <u>1,52,633</u> |
| 2012-13 | To Balance c/d | 4,82,700        | 2012-13 | By Balance b/d                | 2,79,833        |
|         |                | <u>4,82,700</u> |         | By Employees Compensation A/c | <u>2,02,867</u> |
|         |                |                 |         |                               | <u>4,82,700</u> |

If Employee opts for Cash settlement

**Provision for Liability Component Account**

| Year    | Particulars              | ₹        | Year    | Particulars    | ₹        |
|---------|--------------------------|----------|---------|----------------|----------|
| 2013-14 | To Bank (5000 x ₹ 96.54) | 4,82,700 | 2013-14 | By Balance c/d | 4,82,700 |

If employee opts for Equity Settlement

**Provision for Liability Component Account**

| Year    | Particulars             | ₹        | Year    | Particulars    | ₹        |
|---------|-------------------------|----------|---------|----------------|----------|
| 2013-14 | To ESOP outstanding A/c | 4,82,700 | 2013-14 | By Balance c/d | 4,82,700 |

**ESOP Outstanding Account**

| Year    |                         | ₹      | Year    |                            | ₹        |
|---------|-------------------------|--------|---------|----------------------------|----------|
| 2013-14 | To Equity Share Capital | 60,000 | 2013-14 | By Provision for Liability | 4,82,700 |

|  |                           |           |  |                         |           |
|--|---------------------------|-----------|--|-------------------------|-----------|
|  | A/c (6000 x ₹ 10)         |           |  | Component A/c           |           |
|  | To Securities Premium A/c | 12,86,700 |  | By Bank (6,000 x ₹ 144) | 8,64,000  |
|  |                           | 13,46,700 |  |                         | 13,46,700 |

**Working Notes:****1. Computation of Fair Values**

|  |         |
|--|---------|
| Fair value of shares subject to lock in as on 1 <sup>st</sup> April, 2010              | ₹ 60    |
| % of increase in fair value of shares not subjected to lock in                         | 20%     |
| Fair value as on 1 <sup>st</sup> April, 2010 of shares not subject to lock in (60+20%) | ₹ 72    |
| % increase over previous value in respect of fair value on 31.03.2011                  | 6%      |
| Fair value of shares not subject to lock in restriction on 31.03.2011 (72 + 6%)        | ₹ 76.32 |
| % increase over previous value in respect of fair value on 31.03.2012                  | 10%     |
| Fair value of shares not subject to lock in restriction on 31.03.2012 (76.32 + 10%)    | ₹ 83.95 |
| % increase over previous value in respect of fair value on 31.03.2013                  | 15%     |
| Fair value of shares not subject to lock in restriction on 31.03.2013 (83.95 + 15%)    | ₹ 96.54 |

**2. Expense to be recognized in respect of Equity Component**

|  |          |
|--|----------|
| Fair value under Equity Settlement Option (6,000 x ₹ 60 )                          | 3,60,000 |
| Less: Fair value under cash settlement (liability component) option (5,000 x ₹ 72) | 3,60,000 |
| Equity component   | Nil      |
| Expenses to be recognized each year for equity component                           | Nil      |

**3. Expenses to be recognized for Liability Component**

|  | 2010-11 | 2011-12 | 2012-13 |
|--|---------|---------|---------|
| Number of shares (A)                   | 5000    | 5000    | 5000    |
| Fair value at the end of each year (B) | 76.32   | 83.95   | 96.54   |

|   |                 |                 |                 |
|---|-----------------|-----------------|-----------------|
| Fair value of liability component (A x B) | <u>3,81,600</u> | <u>4,19,750</u> | <u>4,82,700</u> |
| Expenses to be recognized*                | <u>1,27,200</u> | <u>1,52,633</u> | <u>2,02,867</u> |

\*Expenses to be recognized each year has been calculated on the basis:

$$\frac{\text{Fair Value} \times \text{No. of years Expired}}{\text{Vesting Period}} - \text{Expenditure recognised till previous year}$$

17. (a)

| Allocation of Earnings  | Old Unit Holders               | New Unit Holders              | Total            |
|---|--------------------------------|-------------------------------|------------------|
|   | [18 lakhs units]<br>₹ in lakhs | [2 lakhs units]<br>₹ in lakhs | ₹ in lakhs       |
| First half year (₹ 5 per unit)                                  | 90.00                          | Nil                           | 90.00            |
| Second half year (₹ 3.60 per unit)                              | <u>64.80</u>                   | <u>7.20</u>                   | <u>72.00</u>     |
|   | 154.80                         | 7.20                          | 162.00           |
| Add: Equalization payment recovered                             | -                              | -                             | <u>10.00</u>     |
| Total amount available for distribution                         |                                |                               | <u>172.00</u>    |
| Equalization Payment: (₹ 90 lakhs ÷ 18 lakhs)<br>= ₹ 5 per unit |                                |                               |                  |
|   |                                | Old Unit Holders              | New Unit Holders |
|   |                                | ₹                             | ₹                |
| Dividend distributed  |                                | 8.60                          | 8.60             |
| Less: Equalization payment                                      |                                | <u>-</u>                      | <u>(5.00)</u>    |
|   |                                | <u>8.60</u>                   | <u>3.60</u>      |

#### Journal Entries

| (₹ in lakhs) |  |     |        |
|--------------|--|-----|--------|
| 30.9.2014    | Bank A/c   | Dr. | 150.00 |
|              | To Unit Capital A/c  |     | 20.00  |
|              | To Reserve A/c   |     | 120.00 |
|              | To Dividend Equalization A/c   |     | 10.00  |
|              | (Being the amount received on sale of 2 lakhs units at a NAV of ₹ 70 per unit) |     |        |
| 31.3.2015    | Dividend Equalization A/c  | Dr. | 10.00  |
|              | To Revenue A/c   |     | 10.00  |

|           |  |        |        |
|-----------|--|--------|--------|
|           | (Being the amount transferred to Revenue Account)  |        |        |
| 30.9.2015 | Revenue A/c Dr.<br>To Bank A/c<br>(Being the amount distributed among 20 lakhs unit holders @ ₹ 8.60 per unit) | 172.00 | 172.00 |

## (b) Calculation of Provision required on Advances as on 31st March, 2015

|                                     | Amount<br>₹ in lakhs | Percentage<br>of provision | Provision<br>₹ in lakhs |
|-------------------------------------|----------------------|----------------------------|-------------------------|
| Standard assets                     | 16,800               | 0.25                       | 42                      |
| Sub-standard assets                 | 1,340                | 10                         | 134                     |
| Secured portion of doubtful debts   |                      |                            |                         |
| – upto one year                     | 320                  | 20                         | 64                      |
| – one year to three years           | 90                   | 30                         | 27                      |
| – more than three years             | 30                   | 50                         | 15                      |
| Unsecured portion of doubtful debts | 97                   | 100                        | 97                      |
| Loss assets                         | 48                   | 100                        | <u>48</u>               |
|                                     |                      |                            | <u>427</u>              |

**Note:** Prudential norms of NBFCs have been revised in November, 2014. According to it, provisioning rates of various Performing and Non-performing Assets have been changed. However, the changed rates are not applicable for the financial year 2014-15 and is also not applicable for May, 2015 examination.

18. (a) Valuation of Shares on Yield basis  
as on 31st March, 2015

| Year ended<br>31st March | Profits<br>as given | Adjustments |          | Revised<br>Profits | Tax<br>Provision | After tax<br>Profits | Weight | Weighted<br>profits |
|--------------------------|---------------------|-------------|----------|--------------------|------------------|----------------------|--------|---------------------|
|                          |                     | Increase    | Decrease |                    |                  |                      |        |                     |
|                          | ₹                   | ₹           | ₹        | ₹                  | ₹                | ₹                    |        | ₹                   |
| 2011                     | 4,00,000            | 1,00,000    | 1,25,000 | 3,75,000           | 1,50,000         | 2,25,000             | 1      | 2,25,000            |
| 2012                     | 3,50,000            | 2,50,000    | 1,00,000 | 4,75,000           | 1,90,000         | 2,85,000             | 2      | 5,70,000            |
|                          |                     | 1,50,000    | 1,75,000 |                    |                  |                      |        |                     |
| 2013                     | 6,50,000            | Nil         | 1,50,000 | 5,00,000           | 2,00,000         | 3,00,000             | 3      | 9,00,000            |
| 2014                     | 5,50,000            | 1,75,000    | Nil      | 7,50,000           | 3,00,000         | 4,50,000             | 4      | 18,00,000           |

|      |          |          |        |          |          |          |           |                  |
|------|----------|----------|--------|----------|----------|----------|-----------|------------------|
|      |          | 25,000   |        |          |          |          |           |                  |
| 2015 | 6,00,000 | 1,00,000 | 25,000 | 6,75,000 | 2,70,000 | 4,05,000 | <u>5</u>  | <u>20,25,000</u> |
|      |          |          |        |          |          |          | <u>15</u> | <u>55,20,000</u> |

$$\text{Weighted average profit (after tax)} = \frac{\text{₹ } 55,20,000}{15} = \text{₹ } 3,68,000$$

$$\text{Value of business} = \frac{\text{₹ } 3,68,000}{20\%} = \text{₹ } 18,40,000$$

$$\text{Value of equity share} = \frac{\text{₹ } 18,40,000}{10,000} = \text{₹ } 184$$

(b) Valuation of Shares on Net Asset Basis

| (i)  | Revised net worth as on 31st March, 2010  | ₹               | ₹                 |
|------|---|-----------------|-------------------|
|      | Net worth                                 |                 | 6,00,000          |
|      | Less: Adjustments relating to             |                 |                   |
|      | 2010-11                                   | 1,00,000        |                   |
|      | 2011-12                                   | <u>1,25,000</u> |                   |
|      |   | 2,25,000        |                   |
|      | Less: Relief from tax @ 40%               | <u>(90,000)</u> | <u>(1,35,000)</u> |
|      |   |                 | <u>4,65,000</u>   |
| (ii) | Net asset value (No. of shares = 10,000)  |                 |                   |
|      | As on 31st March                          | ₹               | ₹                 |
|      | 2010: Revised net worth                   | 4,65,000        |                   |
|      | Value per share                           |                 | 46.50             |
|      | 2011: Revised net worth as on 31.3.2010   | 4,65,000        |                   |
|      | Add: After tax revised profits of 2010-11 | <u>2,25,000</u> |                   |
|      | Net worth as on 31.3.2011                 | <u>6,90,000</u> |                   |
|      | Value per share                           |                 | 69.00             |
|      | 2012: Revised net worth as on 31.3.2011   | 6,90,000        |                   |
|      | Add: After tax revised profits of 2011-12 | <u>2,85,000</u> |                   |
|      | Net worth as on 31.3.2012                 | <u>9,75,000</u> |                   |
|      | Value per share                           |                 | 97.50             |
|      | 2013: Revised net worth as on 31.3.2012   | 9,75,000        |                   |
|      | Add: After tax revised profits of 2012-13 | <u>3,00,000</u> |                   |

|       |  |                  |        |
|-------|--|------------------|--------|
|       | Net worth as on 31.3.2013                        | <u>12,75,000</u> |        |
|       | Value per share                                  |                  | 127.50 |
| 2014: | Revised net worth as on 31.3.2013                | 12,75,000        |        |
|       | <i>Add:</i> After tax revised profits of 2013-14 | <u>4,50,000</u>  |        |
|       | Net worth as on 31.3.2014                        | <u>17,25,000</u> |        |
|       | Value per share                                  |                  | 172.50 |
| 2015: | Revised net worth as on 31.3.2014                | 17,25,000        |        |
|       | <i>Add:</i> After tax revised profits of 2014-15 | <u>4,05,000</u>  |        |
|       | Net worth as on 31.3.2015                        | <u>21,30,000</u> |        |
|       | Value per share                                  |                  | 213.00 |

### Performance Appraisal

| <i>Revised net worth as on 31st March</i> |           | <i>Profit during the year ended 31st March</i> |          | <i>Return on net worth</i> |
|---|-----------|--|----------|----------------------------|
|   | ₹         |  | ₹        | %                          |
| 2010                                      | 4,65,000  | 2011   | 2,25,000 | 48.39                      |
| 2011                                      | 6,90,000  | 2012   | 2,85,000 | 41.30                      |
| 2012                                      | 9,75,000  | 2013   | 3,00,000 | 30.77                      |
| 2013                                      | 12,75,000 | 2014   | 4,50,000 | 35.29                      |
| 2014                                      | 17,25,000 | 2015   | 4,05,000 | 23.48                      |

The company's return has fallen from 48.39% to 23.48%. This may be perhaps due to the fact that the company has been ploughing back its profits without having adequate reinvestment opportunities. Unless the company has profitable investment opportunities, it may not be advisable to invest in the company.

**Note:** Return on net worth may also be calculated on the basis of average net worth during the relevant year.

### 19. Maximum Value that can be quoted by Shobhit Garments Ltd.

|   | ₹ in lakhs | ₹ in lakhs     |
|---|------------|----------------|
| Present Value of Incremental Cash Flows (W.N.)                      |            | 3726.49        |
| <i>Add:</i> Cash to be collected immediately by disposal of assets: |            |                |
| Tangible Fixed Assets   | 90         |                |
| Investments   | 424        |                |
| Stock & Receivables   | <u>940</u> | <u>1454.00</u> |

|  |              |                |
|--|--------------|----------------|
|  |              | 5180.49        |
| Less: Current Liabilities [including 20% of 14.10] | 800          |                |
| Contingent Liability [14.10 x 80%]                 | 11.28        |                |
| Retrenchment Compensation                          | 260          |                |
| Renovation of Plant [50 + (50 x 0.6944)]           | <u>84.72</u> | (1156.00)      |
| Goodwill   |              | <u>300.00</u>  |
| Maximum Value that can be quoted                   |              | <u>4324.49</u> |
| Maximum Price per Share [4324.49/20 lakh shares]   |              | 216.22         |

**Working Note:****Calculation of Present Value of Incremental Cash Flows**

| Year | Cash Flows before takeover | Cash Flows after takeover | Incremental Cash Flows | Discount Factor | Discounted Cash Flow |
|------|----------------------------|---------------------------|------------------------|-----------------|----------------------|
|      |                            |                           | $D=C-B$                | @ 20%           | $F = D \times E$     |
| A    | B                          | C                         |                        | E               |                      |
| 1    | 3000                       | 3600                      | 600                    | 0.8333          | 499.98               |
| 2    | 3400                       | 3800                      | 400                    | 0.6944          | 277.76               |
| 3    | 4000                       | 4600                      | 600                    | 0.5787          | 347.22               |
| 4    | 5000                       | 5900                      | 900                    | 0.4823          | 434.07               |
| 5    | 6000                       | 7000                      | 1000                   | 0.4019          | 401.90               |
| 6    | 6800                       | 8000                      | 1200                   | 0.3349          | 401.88               |
| 7    | 7600                       | 9000                      | 1400                   | 0.2791          | 390.74               |
| 8    | 9000                       | 10600                     | 1600                   | 0.2326          | 372.16               |
| 9    | 10000                      | 11600                     | 1600                   | 0.1938          | 310.08               |
| 10   | 12000                      | 13800                     | 1800                   | 0.1615          | <u>290.70</u>        |
|      |                            |                           |                        |                 | <u>3726.49</u>       |

20. (a)

**Brightex Co. Ltd****Value Added Statement**

for the year ended 31st December, 2014

|  | (₹ in thousands) | (₹ in thousands) | % thousands |
|--|------------------|------------------|-------------|
| Sales  |                  | 6,240            |             |
| Less: Cost of bought in material and services: |                  |                  |             |
| Production and operational                     |                  |                  |             |

|  |            |                |               |
|--|------------|----------------|---------------|
| expenses<br>₹ (4,320 – 8 - 620)                          | 3,692      |                |               |
| Administration expenses ₹ (180 - 5)                      | 175        |                |               |
| Interest on bank overdraft                               | 109        |                |               |
| Interest on working capital loan                         | 20         |                |               |
| Excise duties (Refer to working note)                    | 180        |                |               |
| Other/miscellaneous charges ₹ (444 - 180)                | <u>264</u> | <u>(4,440)</u> |               |
| Value added by manufacturing and trading activities      |            | 1,800          |               |
| Add: Other income  |            | <u>55</u>      |               |
| Total Value Added  |            | <u>1,855</u>   |               |
| <b>Application of Value Added:</b>                       |            |                |               |
| To Pay Employees :                                       |            |                |               |
| Salaries to Administrative staff                         |            | 620            | 33.42         |
| To Pay Directors:  |            |                |               |
| Salaries and Commission                                  |            | 5              | 0.27          |
| To Pay Government:                                       |            |                |               |
| Local Tax  | 8          |                |               |
| Income Tax   | <u>55</u>  | 63             | 3.40          |
| To Pay Providers of Capital :                            |            |                |               |
| Interest on Fixed Loan                                   | 51         |                |               |
| Dividend   | <u>160</u> | 211            | 11.37         |
| To Provide For Maintenance and Expansion of the Company: |            |                |               |
| Depreciation   | 16         |                |               |
| Fixed Assets Replacement Reserve                         | 400        |                |               |
| Retained Profit ₹ (600 - 60)                             | <u>540</u> | <u>956</u>     | <u>51.54</u>  |
|  |            | <u>1,855</u>   | <u>100.00</u> |

**Reconciliation between Total Value Added and Profit Before Taxation:**

|                   | (₹ in thousands) | (₹ in thousands) |
|-------------------|------------------|------------------|
| Profit before Tax |                  | 1,155            |
| Add back:         |                  |                  |

|                                  |          |              |
|----------------------------------|----------|--------------|
| Depreciation                     | 16       |              |
| Salaries to Administrative Staff | 620      |              |
| Director's Remuneration          | 5        |              |
| Interest on Fixed Loan           | 51       |              |
| Local Tax                        | <u>8</u> | <u>700</u>   |
| Total Value Added                |          | <u>1,855</u> |

**Working Note:***Calculation of Excise Duty*

|   |           | (₹ in thousands) |
|---|-----------|------------------|
| Interest and other charges                    |           | 624              |
| Less : Interest on bank overdraft             | 109       |                  |
| Interest on loan from ICICI                   | 51        |                  |
| Interest on loan from IFCL                    | <u>20</u> | <u>(180)</u>     |
| Excise duties and other/miscellaneous charges |           | <u>444</u>       |

Assuming that these miscellaneous charges have to be taken for arriving at Value Added (In the first part of Value Added Statement), the excise duty will be computed as follows.

Let excise duty be  $x$ ; thus miscellaneous/ other charges = ₹ 444 -  $x$

Thus  $x = 1/10 \times [\text{₹ } 6,240 - \{\text{₹ } 3692 + \text{₹ } 175 + \text{₹ } 109 + \text{₹ } 20 + x + (\text{₹ } 444 - x)\}]$

$$= 1/10 \times [\text{₹ } 6240 - \text{₹ } 4440] = \text{₹ } 180$$

Other/ miscellaneous charges = ₹ 444 - ₹ 180 = ₹ 264

The above solution is given accordingly.

However, if other/miscellaneous charges are taken as any type of application of Value Added (i.e, to be taken in the application part), then excise duty ( $x$ ) will be computed as follows:

$$x = 1/10 \times [\text{₹ } 6240 - \text{₹ } (3692 + 175 + 109 + 20 + x)]$$

$$x = 1/10 \times [\text{₹ } 2244 - x]$$

$$11x = \text{₹ } 2244$$

$$x = \text{₹ } 204$$

And thus total value added will be ₹ 2040 + ₹ 55 (other income) = ₹ 2095

And accordingly, application part will be prepared, taking miscellaneous charges.

₹ ('000) 240 [i.e, ₹ 444 - ₹ 204] as the application of value added.

## (b) Computation of EVA

| <i>Particulars</i>  | <i>₹ in crores</i> |
|---|--------------------|
| Net Operating Profit after Tax (NOPAT)                              | 252.00             |
| Less: Cost of Operating Capital Employed (COCE) [13.25% of ₹ 1,100] | <u>(145.75)</u>    |
| Economic Value Added (EVA)  | <u>106.25</u>      |

**Working Notes:**

1. Cost of Debt = Interest Rate (1 – Tax Rate) = 15% (1 - 30) = 10.50%
2. Cost of Preference Share = 15%
3. Cost of Equity = Risk Free Rate + (Beta x Equity Market Risk Premium)  
= (15.5% - 9%) + (1.5 x 9) = 20%
4. Total Capital Employed = 800 + 100 + 300 = 1,200 crores
5. WACC =  $\left(\frac{800}{1,200} \times 10.50\%\right) + \left(\frac{100}{1,200} \times 15\%\right) + \left(\frac{300}{1,200} \times 20\%\right)$   
= 7% + 1.25% + 5% = 13.25%
6. Financial Leverage =  $\frac{\text{EBIT}}{\text{EBIT} - \text{Interest}} = \frac{\text{EBIT}}{\text{EBIT} - 120} = 1.5$   
EBIT = (120 x 1.5)/0.5 = 360
7. Net Operating Profit after Tax = 360 - 30% of 360 = 252
8. Operating Capital Employed = Total Capital Employed - Non-Operating Capital Employed  
= 1,200 - 100 = 1,100 crores