Question Paper
Financial Statement Analysis (CFA560): January 2009

- **Answer all 70 questions.**
- **Marks are indicated against each question.**

Total Marks : 100

1. SFAC 6 issued by Financial Accounting Standards Board (FASB) deals with <Answer>

   (a) Objectives of financial reporting by business enterprises
   (b) Qualitative characteristics of accounting information
   (c) Elements of financial statements
   (d) Recognition and measurement in financial statements of enterprises
   (e) Using cash flow information and present value in accounting measurements. **(1 mark)**

2. Decrease in net assets from peripheral transactions of an entity and from all other transactions and other events and circumstances affecting the entity except those that result from expenses or distribution to owners is known as <Answer>

   (a) Assets
   (b) Liabilities
   (c) Revenues
   (d) Losses
   (e) Expenses. **(1 mark)**

3. Liabilities that are incurred and which are known or estimated and payable at future dates are generally reported at their <Answer>

   (a) Net settlement values
   (b) Gross realizable values
   (c) Book values
   (d) Current market values
   (e) Present values. **(1 mark)**

4. Which of the following statements is **false**? <Answer>

   (a) Going concern concept assumes that business will be carried on for a definite period
   (b) The actual receipts or payments are not taken as the base under the accrual system
   (c) The revenues/expenses are recognized if they belong to the relevant accounting period, irrespective of whether cash or cash equivalent is received/paid or not
   (d) Inventories are valued at lower of cost or market value in recognition of conservatism concept
   (e) The financial statements provide information of not only the amount of cash payments or receipts during the reporting period, but also the cash payable or receivable in the reporting period. **(1 mark)**

5. Which of the following concepts states that the performance can be measured only if revenues and related costs are accounted for during the same time period? <Answer>

   (a) Going concern concept
   (b) Accrual concept
   (c) Consistency concept
   (d) Matching concept
   (e) Realization concept. **(1 mark)**

6. Which of the following statements is **false** with reference to statement of comprehensive income? <Answer>

   (a) It arises as a result of exchange transactions between the entity and its owners
   (b) It arises as a result of professional services
   (c) It arises as a result of lending and insurance activities
   (d) It arises as a result of environmental activities
   (e) It arises as a result of price changes. **(1 mark)**

7. Significant worldwide accounting diversities are observed in the following areas **except** in <Answer>

(a) Inventory valuation
(b) Accounting for lease
(c) Accounting for research and development costs
(d) Accounting for joint ventures
(e) Treatment of ordinary items. **(1 mark)**

8. Who among the following is **not** considered as an internal user of Financial Statements? <Answer>

(a) Board of Directors
(b) Partners
(c) Prospective Investors
(d) Managers
(e) Officers. **(1 mark)**

9. In the Consolidated Balance Sheet of a holding company, the value of minority interest does **not** consist of a proportionate share of minority shareholders in the <Answer>

(a) Nominal value of share capital of subsidiary company
(b) Reserves and profits of the subsidiary company at the time of acquisition by the holding company
(c) Income of the subsidiary company after its acquisition by the holding company
(d) Subsidiary company's losses or decrease in the value of assets of subsidiary company
(e) Reserves of the holding company. **(1 mark)**

10. The following estimated data was extracted from the books of Ram Ltd., for the year 2008-09: <Answer>

Particulars	Rs.
Sale price per unit	92
Total variable production cost per unit	51
Fixed production overhead	4,85,500
Fixed administrative and selling overhead	3,08,300

If commission on sales is estimated to be 5%, the number of units to be sold by the company in order to earn a profit of Rs.1,16,200 for the year 2008-09 is

(a) 25,000
(b) 19,361
(c) 21,808
(d) 22,195
(e) 14,675. **(2marks)**

11. Margin of safety will **not** be increased by <Answer>

(a) Increasing the level of production
(b) Reducing the fixed cost
(c) Reducing the selling price
(d) Reducing the variable cost
(e) Substituting the existing unprofitable product with profitable ones. **(1 mark)**

12. An increase in variable costs where selling price and fixed cost remain constant will result in <Answer>

(a) An increase in net profit
(b) No change in net profit
(c) A fall in the sales level at which break even point will occur
(d) A rise in the sales level at which break even point will occur
(e) No change in the sales level at which break even point will occur. **(1 mark)**

13. Which of the following statements is **false** with reference to translation of financial statements of non-integral foreign operations? <Answer>

(a) All monetary assets and liabilities are translated using the closing rate
(b) Items of income are translated using exchange rates of the date of the transaction
(c) All non-monetary assets and liabilities are translated using opening rate
(d) All resulting exchanges differences are to be accumulated in a foreign currency translation reserve until the net investment is disposed off
(e) Tax effects arising from such a translation is to be accounted as per AS-22. **(1 mark)**

14. Under univariate analysis which of the following ratios is **not** considered to predict corporate bankruptcy? <Answer>

(a) Cash flow to total assets
(b) Sales to inventory
(c) Total debt to total assets
(d) Net assets to total assets
(e) Current assets to current liabilities. **(1 mark)**

15. A firm has combined leverage of 1.7 and financial leverage of 1.04. If the firm's sales amounts to be Rs.5,00,000 p.a. and its EBIT is equal to Rs.2,32,500, what will be the variable cost of the firm? <Answer>

(a) Rs.1,21,000
(b) Rs.1,22,000
(c) Rs.1,24,000
(d) Rs.1,26,000
(e) Rs.1,28,000. **(2marks)**

16. 'X' Ltd. has 50,000 equity shares at the rate of Rs.10 per share, fully paid-up and its retained earnings are half the equity share capital. The fixed and current assets are in the ratio of 3:1. The fixed assets are Rs.14,06,250. The outside liabilities of the company are <Answer>

(a) Rs.10,60,000
(b) Rs.11,50,000
(c) Rs.18,75,000
(d) Rs.17,50,000
(e) Rs.11,25,000. **(2marks)**

17. The following information is pertaining to Alpha Pneumatic Ltd.: <Answer>

Current ratio	4.0
Acid-test ratio	2.80
Current liabilities	Rs.15.50 lakh

The value of Inventory is

(a) Rs. 62.0 lakh
(b) Rs. 43.0 lakh
(c) Rs. 18.6 lakh
(d) Rs.105.4 lakh
(e) Rs. 12.4 lakh. **(2marks)**

18. The total capital employed by Venus Ltd., is Rs.36,00,000. The firm has debt-equity ratio of 5:4. The ratio of owner's equity to fixed assets is 8:15. The amount of fixed assets in the company is <Answer>

(a) Rs.30,00,000
(b) Rs.36,00,000
(c) Rs.40,00,000
(d) Rs.42,00,000
(e) Rs.50,00,000. **(2marks)**

19. The following information is extracted from the books of Jeet Ltd.: <Answer>

Particulars	Debit (Rs.)	Credit (Rs.)
Opening stock (1/4/2007)	1,86,420	
Purchases and sales	7,18,210	11,69,900
Returns	12,680	9,850
Manufacturing wages	1,09,740	
Carriage inwards	4,910	
Sundry Manufacturing Expenses	19,240	

On March 31, 2008, outstanding manufacturing wages stood at Rs.1,890. On the same date, stock was valued at Rs.1,24,840.

The Gross Profit ratio for the year is

(a) 21.73%
(b) 22.58%
(c) 20.42%
(d) 18.25%
(e) 19.00%. **(2marks)**

20. Jupon Ltd., has furnished the following data for the year ended March 31, 2008: <Answer>

Particulars	Rs.
Sales	30,00,000
Opening inventory	6,00,000
Closing inventory	4,00,000

If inventory turnover ratio is 3.6 times, gross profit of Jupon Ltd., for the year ended March 31, 2008 was

(a) Rs.42,00,000
(b) Rs. 6,00,000
(c) Rs.18,00,000
(d) Rs.12,00,000
(e) Rs. 8,75,000. **(2marks)**

21. Swara Corp., had 12,00,000 shares of common stock outstanding on January 01, 2008 and December 31, 2008. In connection with the acquisition of a subsidiary company in June 2007, Swara Corp., is required to issue 50,000 additional shares of its common stock on July 1, 2009, to the former owners of the subsidiary. Swara Corp., paid Rs.2,00,000 in preferred stock dividends in 2008 and reported net income of Rs.34,00,000 for the year. Diluted EPS of Swara Corp., for the year 2008 should be <Answer>

(a) Rs.2.83
(b) Rs.2.72
(c) Rs.2.67
(d) Rs.2.56
(e) Rs.2.00. **(2marks)**

22. In the preparation of cash flow statements as per AS-3, payments for future contracts are classified as <Answer>

(a) Marketing activities
(b) Financing activities
(c) Operating activities
(d) Investment activities
(e) Non-cash activities. **(1 mark)**

<Answer>

23. The following data was extracted from the books of Legend Ltd., for the year 2008:

Particulars	Units	Per Unit LC	Exchange rate at that time 1 LC= Rs.
Opening stock	240	1.00	1.00
Purchases	400	1.20	0.80
Units sold	460		

If exchange rate at the end of the year is 1 Local Currency (LC) = Rs.1.10, the translated value of closing stock under current method (use FIFO method) is

(a) Rs.180.00
(b) Rs.198.00
(c) Rs.216.00
(d) Rs.237.60
(e) Rs.231.80. **(1 mark)**

<Answer>

24. The major areas where manipulation of financial data is generally **not** possible can be

(a) Income from continuing operations
(b) Treatment of recurring income items
(c) Changes in accounting estimates
(d) Adjustments for changes in accounting policies
(e) Extraordinary items. **(1 mark)**

<Answer>

25. The following data was furnished by Rahul Ltd., for the year 2008:

Particulars	Rs.
Operating cash flow	5,00,000
Total capital expenditure	1,50,000
After tax proceeds from sale of assets	50,000

The amount of free cash flow of Rahul Ltd., for the year 2008 was

(a) Rs.5,00,000
(b) Rs.3,50,000
(c) Rs.4,00,000
(d) Rs.4,50,000
(e) Rs.3,00,000. **(2marks)**

<Answer>

26. Long lived assets classified as 'held for sale' are reported at

(a) Net fair value
(b) Carrying value
(c) Net fair value or carrying value, whichever is lower
(d) Net fair value or carrying value, whichever is higher
(e) Cost value. **(1 mark)**

<Answer>

27. Which of the following is **not** a method of revenue recognition?

(a) Sales basis method
(b) Percentage of completion method
(c) Completed contract method
(d) Specific identification method
(e) Cost recovery method. **(1 mark)**

<Answer>

28. In a revenue manipulation, vendor financing occurs when a company

(a) Loans money to a customer to purchase goods from the company
(b) Sells goods to customer by providing loan through a bank
(c) Sells goods to customer by cash
(d) Loans money to a customer to purchase goods from another company
(e) Loans money to a customer to purchase goods from competitor. **(1 mark)**

<Answer>

29. Expense manipulation can be done by

(a) Understating the allowance for uncollectible accounts
(b) Trade loading
(c) Channel stuffing
(d) Capitalizing revenue cost
(e) Not recognizing discounts. **(1 mark)**

<Answer>

30. The difference between the treatment of expenditures on the tax return and for financial reporting is known as

(a) Taxable temporary difference
(b) Timing difference
(c) Permanent difference
(d) Unrecognized tax benefits
(e) Income difference. **(1 mark)**

<Answer>

31. Which of the following is **not** a permanent difference under US GAAP?

(a) Interest received from investments in bonds issued by the State Government
(b) Investment expense incurred to obtain tax-exempt income
(c) Revenues reported for financial reporting purposes before being reported for tax purposes
(d) Expenses due to violation of law
(e) Life insurance proceeds on the death of an insured executive. **(1 mark)**

<Answer>

32. The following data was extracted from the books of Ram Ltd., for the year 2008:

Particulars	Rs.
Pre tax profit	3,60,000
Non taxable interest received on municipal securities	11,250
Long term loss accrual in excess of deductible amount	22,500
Depreciation as per financial records	1,50,000
Depreciation as per income tax provisions	2,06,250

If tax rate is 40%, the amount of deferred tax liability reported in the balance sheet as on December 31, 2008 was

(a) Rs.13,500
(b) Rs.22,500
(c) Rs. 9,000
(d) Rs.31,500
(e) Rs.27,000. **(2marks)**

<Answer>

33. Rosy Ltd., began operations on April 1, 2005. It recognizes incomes from long term construction contracts under percentage of completion method in its financial statements and under the completed contract method for income tax reporting. Income computed under each method is as follows:

Year	Completed contract method (Rs.)	Percentage of completion method (Rs.)
2005-06	Nil	6,00,000
2006-07	7,50,000	10,50,000
2007-08	12,00,000	14,25,000

The income tax rate for the years 2005-06 to 2007-08 was 30%. However, from 2008-09, the income tax rate is 25%. Provided there are no temporary differences, the total deferred tax liability reported should be

(a) Rs.7,68,750
(b) Rs.4,87,500
(c) Rs.2,81,250
(d) Rs.3,00,000
(e) Rs.3,56,250. **(2marks)**

<Answer>

34. Roman Ltd., has furnished the following data for the year ended December 31, 2008:

Particulars	Rs.
Pre tax income	4,80,000
Gain on involuntary conversion	2,10,000
Depreciation as per income tax provisions	1,20,000
Depreciation charged in financial records	90,000
Tax payments for the year 2008	42,000

If tax rate is 30%, the net current tax payable for the year 2008 was

(a) Rs.66,000
(b) Rs.30,000
(c) Rs.93,000
(d) Rs.42,000
(e) Rs.75,000. **(2marks)**

<Answer>

35. Max Ltd., maintains its accounts on calendar year basis. It reports the following operating income (loss) before income tax for its first three years of operations:

Year	Rs.
2006	4,00,000
2007	(8,00,000)
2008	16,00,000

There are no permanent or temporary differences between the operating income (loss) for financial and income tax reporting purposes. When filing its 2007 tax return, Max Ltd., did not elect to forego the carry back of its loss for 2007. Assuming a tax rate of 40% for all the years, the income tax liability of Max Ltd., as on December 31, 2008 was

(a) Rs.6,40,000
(b) Rs.5,60,000
(c) Rs.4,80,000
(d) Rs.8,00,000
(e) Rs.3,20,000. **(2marks)**

<Answer>

36. As per ARB-43, which of the following liabilities is treated under the category of 'amount and payee known'?

(a) Taxes payable
(b) Bonus payable
(c) Compensated absences
(d) Product warranties
(e) Unearned revenues. **(1 mark)**

<Answer>

37. SK Ltd., grants two weeks of paid vacation to all its employees for each year of employment. Unused vacation can be accumulated and carried forward to succeeding years. Unused vacation is paid by SK Ltd., on the basis of salaries in effect when vacations are taken or when employment is terminated. There was no employee turnover in 2008. Additional information for the year ended December 31, 2008, was as follows:

Particulars	Rs.
Liability for accumulated vacations at December 31, 2007	70,000
Pre-2008 accrued vacations taken from January 1, 2008 to September 30, 2008 (the authorized period for vacations)	40,000
Vacations earned for work in 2008 (adjusted to current rates)	60,000

On October 1, 2008, SK Ltd., granted annual salary increase of 10% to all its employees. The vacation pay expense reported by SK Ltd., for the year ended December 31, 2008 was

(a) Rs.90,000
(b) Rs.67,000
(c) Rs.63,000
(d) Rs.60,000
(e) Rs.40,000. **(2marks)**

38. On January 1, 2008, Alekya Ltd., issued Rs.8,40,000 of 12% Bonds. The interest on bonds is payable semi annually on June 30 and December 31. The maturity period of bonds is three years. If market yield for bonds of similar risk and maturity is 10%, the price of the bonds at present value is <Answer>

(a) Rs.8,82,640
(b) Rs.2,55,815
(c) Rs.6,26,825
(d) Rs.7,35,333
(e) Rs.5,22,354. **(2marks)**

39. Amar Ltd., issued a 3 year 5% annual coupon bond with a face value of Rs.4,00,000 on December 31, 2005. If the bond was issued at a market rate of interest of 4% and the present value of bond on December 31, 2005 was Rs.4,11,100, the amount of premium amortized at the end of the year 2008 was <Answer>

(a) Rs.3,556
(b) Rs.3,846
(c) Rs.3,698
(d) Rs.3,772
(e) Rs.3,896. **(2marks)**

40. On January 1, 2003, Amol Ltd., issued 1,200 of its 10% Rs.1,000 Bonds for Rs.12,48,000. These bonds were to mature on January 1, 2013 but were callable at 101% any time after December 31, 2006. Interest is paid semi annually on June 30 and December 31. On July 1, 2008, Amol Ltd., called off all of the bonds and retired them. If bond premium was amortized on a straight line basis, pre tax gain or loss in the year 2008 on this early retirement of debt was <Answer>

(a) Rs.48,000
(b) Rs.21,600
(c) Rs.26,400
(d) Rs. 9,600
(e) Rs.14,400. **(2marks)**

41. During the period of a lease, usually the non-refundable security deposit received from the lessee is recorded in the books of lessor as <Answer>

(a) Unearned Revenue
(b) Loss
(c) Reserve
(d) Asset
(e) Prepaid rent. **(1 mark)**

42. Which of the following statements is **false** with reference to leveraged lease? <Answer>

(a) The lease must meet the definitions of a direct financing lease
(b) The lease involves three parties – lessor, lessee and a long-term creditor
(c) The lease is ‘leveraged’ because the lessor borrows to finance the transaction
(d) The lessor’s net investment is reduced in the early years and increases in the later years until it is eliminated
(e) The lease will affect the lessee’s accounting treatment. **(1 mark)**

43. On April 1, 2008, Siri Ltd., leased three cars from Rohit Automobiles for five years for an equal annual rent of Rs.1,00,000 per car to be paid on April 1, each year. Siri Ltd., guaranteed Rs.40,000 as a residual value to Rohit Automobiles at the end of the lease period. The lease fulfills all criteria as capital lease and the implicit interest rate in the lease is considered as 9%. Present values of 9% for different periods are <Answer>

For an annuity due with 5 payments	4.240
For an ordinary annuity with 5 payments	3.890
Present value of Re.1 for 5^{th} period	0.650

If the first annual payment is made on April 1, 2008, Siri Ltd.,’s recorded capital lease liability immediately after the first required payment is

(a) Rs.4,50,000
(b) Rs.4,15,000
(c) Rs.4,05,000
(d) Rs.3,75,000
(e) Rs.3,50,000. **(2marks)**

44. Maytas Ltd., is engaged in the business of leasing computers under direct finance lease. These computers have no residual value at the end of the lease period of five years and lessee has no bargain purchase option. Maytas Ltd., wants to earn 8% return on investment with a fair value of Rs.3,44,960. Total amount of interest revenue earned by Maytas Ltd., over the life of the lease will be <Answer>

(Assume that the present value on a 5 year lease @ 8% of an annuity of Re.1 is 4.312)

(a) Rs.1,39,450
(b) Rs.1,29,360
(c) Rs. 80,000
(d) Rs. 55,040
(e) Rs. 50,000. **(2marks)**

45. Akash Ltd., entered into a five year operating lease agreement with Anuradha Enterprises at a monthly rental of Rs.1,000. Akash Ltd., granted first nine months as free of rent as an inducement for Anuradha Enterprises to enter into the contract. The lease and rental commenced from June 1, 2007 and March 1, 2008 respectively. The rent expense of Anuradha Enterprises to be reported in the financial statements for the year ended March 31, 2008 was <Answer>

(a) Rs. 1,000
(b) Rs. 9,000
(c) Rs.10,200
(d) Rs.10,500
(e) Rs.10,000. **(2marks)**

46. When payments are made as part of a capital lease agreement, the amount to be debited to the account "obligation under capital leases" by the lessee is equal to the <Answer>

(a) Lease payment
(b) Difference between the lease payment and the principal amount
(c) Amortization of the leased asset
(d) Difference between the lease payment and the interest expense
(e) Interest expense only. **(1 mark)**

47. The actuarial present value of benefits attributed during the current period is known as <Answer>

(a) Service cost
(b) Interest cost
(c) Actual return on plan assets
(d) Actuarial Gain or loss
(e) Prior service cost. **(1 mark)**

48. Which of the following items is always to be deducted from service cost to arrive at net pension cost? <Answer>

(a) Interest cost
(b) Decrease in expected return on plan assets
(c) Amortization of un recognized prior service cost
(d) Amortization of transactional assets
(e) Increase in expected return on plan assets. **(1 mark)**

49. The following data is pertaining to pension plan of Sun Ltd., for the year 2008: <Answer>

Particulars	Rs.
Actuarial estimates of Projected Benefit Obligation (PBO) at the beginning of the year	90,000
Service cost	21,600
Interest cost	9,000
Pension benefits paid	18,000

If no change occurred in actuarial estimates measured during the year 2008, the company's Projected Benefit Obligation as on December 31, 2008 was

(a) Rs. 77,040
(b) Rs. 90,000
(c) Rs.1,02,600
(d) Rs. 95,040
(e) Rs.1,38,600. **(2marks)**

50. Run Ltd., has furnished the following data pertaining to its pension benefit plan for the year 2008: <u><Answer></u>

Particulars	Rs.
Service cost	2,16,000
Actual gain on plan assets	54,000
Unexpected loss on asset related to disposal of a subsidiary in the year 2008	60,000
Amortization of unrecognized prior service cost	18,000
Annual interest on pension obligation	72,000

The net pension expense to be reported in the income statement of 2008 was

(a) Rs.2,16,000
(b) Rs.2,88,000
(c) Rs.3,06,000
(d) Rs.2,52,000
(e) Rs.3,12,000. **(2marks)**

51. The method of accounting for investments in which recognition of percentage share of income or loss, dividends and any changes in the investment percentage in an investee by an investor is considered is called <u><Answer></u>

(a) Equity method
(b) Cost method
(c) Market method
(d) Cost adjusted fair value method
(e) Consolidation method. **(1 mark)**

52. On June 1, 2008, Adarsh Ltd., bought 9% Gilt securities (face value Rs.4,80,000) for Rs.4,76,400 which includes an accrued interest of Rs.10,800. The maturity date for these securities is September 1, 2009 and a semi-annual interest is paid on April 1 and October 31 every year. If Adarsh Ltd., uses straight line method of amortization and intends to hold these securities till their maturity, the carrying amount of this investment in its balance sheet as on December 31, 2008 was <u><Answer></u>

(a) Rs.4,76,400
(b) Rs.4,72,320
(c) Rs.4,65,600
(d) Rs.4,80,480
(e) Rs.4,72,800. **(2marks)**

53. If cost of the acquired enterprise is in excess of the sum of the amounts assigned to net identifiable assets acquired, such excess is known as <u><Answer></u>

(a) Capital reserve
(b) Net worth
(c) Goodwill
(d) Equity
(e) Outside liabilities. **(1 mark)**

54. Telex Ltd., has the following investments in marketable securities: <u><Answer></u>

Type of security	Cost (Rs.)	Market value as on	
		March 31, 2008 (Rs.)	March 31, 2007 (Rs.)
Trading	1,50,000	1,55,000	1,00,000
Available-for-sale	1,50,000	1,30,000	1,20,000

The amount to be reported by Telex Ltd., as unrealized holding gains in its 2007-08 income statement was

(a) Rs.65,000
(b) Rs.55,000
(c) Rs.50,000
(d) Rs.20,000
(e) Rs.10,000. **(2marks)**

55. The existence of significant influence by an investor is **not** usually evidenced by <Answer>

(a) Representation of the board of directors of the investor
(b) Participation in policy making processes
(c) Material transactions between the investor and the investee
(d) Interchange of managerial personnel
(e) Provision for essential technical information. **(1 mark)**

56. On October 01, 2007, Sky Ltd., acquired 60% shares in Star Ltd., at a cost of Rs.37,50,000. On October 01, 2007 the Profit and Loss account and Capital reserve of Star Ltd., showed credit balances of Rs.5,00,000 and Rs.9,00,000 respectively. Following is the Balance Sheet of Star Ltd., as on March 31, 2008: <Answer>

Liabilities	Rs.	Assets	Rs.
Share capital	40,00,000	Land and building	31,50,000
(4,00,000 shares of Rs.10 each)		Machinery	14,70,000
Capital reserve	12,00,000	Furniture and fittings	10,80,000
Profit and Loss account	8,00,000	Sundry debtors	3,90,000
Short term loan	4,00,000	Closing inventory	2,40,000
Sundry creditors	60,000	Cash on hand	70,000
		Cash at bank	60,000
	64,60,000		64,60,000

On November 15, 2007 Star Ltd., declared a dividend of 10% out of its pre-acquisition profits. Amount of goodwill that is to be shown in the Consolidated Balance Sheet as on March 31, 2008 was

(a) Rs.5,10,000
(b) Rs.5,70,000
(c) Rs.3,50,000
(d) Rs.7,50,000
(e) Rs.2,70,000. **(2marks)**

57. Hari Ltd., acquired 60% shares of Siva Ltd., on November 01, 2007. The Profit and Loss account of Siva Ltd., showed a debit balance of Rs.1,80,000 on April 01, 2007 and a credit balance of Rs.3,00,000 on March 31, 2008. The share of Hari Ltd., in the capital profit/loss of Siva Ltd., to be considered to find out cost of control as on March 31, 2008 was <Answer>

(a) Rs.1,00,000 (Capital loss)
(b) Rs. 84,000 (Capital loss)
(c) Rs.1,68,000 (Capital profit)
(d) Rs.1,05,000 (Capital profit)
(e) Rs. 60,000 (Capital profit). **(2marks)**

58. On March 31, 2008, Omkar Ltd., acquired 80% equity shares of Om Ltd. Consider the following data: <Answer>

- Share of Omkar Ltd., in the capital profits of Om Ltd., was Rs.5,88,000.
  The post acquisition profits of Om Ltd., were Rs.1,39,500.
  The unrealized profit on account of inter company sales was Rs.30,000.
  The Profit and Loss account of Omkar Ltd., showed a credit balance of Rs.12,00,000 as on April 01, 2007 and the company made a profit of Rs. 4,80,000 during the year 2007-08.

In the Consolidated Balance Sheet as on March 31, 2008, the Profit and Loss account of Omkar Ltd., was

(a) Rs.17,67,600
(b) Rs.17,61,600
(c) Rs.10,47,600
(d) Rs.18,15,600
(e) Rs.10,71,600. **(2marks)**

59. On July 01, 2007, Shure Ltd., acquired 14,000 equity shares of Pure Ltd., for a consideration of Rs.16,00,000. The share capital of Pure Ltd., consists of 20,000 equity shares of Rs.100 each. **<Answer>**

The balances of General reserve and Profit and Loss account of Pure Ltd., are as under:

Particulars	As on July 01, 2007 (Rs.)	As on March 31, 2008 (Rs.)
General reserve	3,40,000	4,00,000
Profit and Loss account	3,00,000	3,50,000

The amount of minority interest shown in the Consolidated Balance Sheet as on March 31, 2008 was

(a) Rs.9,15,000
(b) Rs.7,20,000
(c) Rs.6,15,000
(d) Rs.8,10,000
(e) Rs.8,25,000. **(2marks)**

60. The three basic elements in a balance sheet of a company are **<Answer>**

(a) Assets, liabilities and preference share capital
(b) Assets, liabilities and capital reserve
(c) Assets, liabilities and shareholders' equity
(d) Assets, liabilities and revenues
(e) Assets, liabilities and unclaimed dividends. **(1 mark)**

61. In the process of translation of the financial statements of a foreign entity, which of the following methods will retain the relationship between various items of the income statement and balance sheet? **<Answer>**

(a) Monetary method
(b) Non-monetary method
(c) Temporal method
(d) Remeasurement method
(e) Current rate method. **(1 mark)**

62. Sea Ltd., acquired 55% shares of River Ltd., on February 01, 2007. Sea Ltd., sells goods at cost plus 20%. During the year 2007-08, it supplied goods worth Rs.1,80,000 to River Ltd., out of which, 60% were still in stock of River Ltd., as on March 31, 2008. If the value of closing stocks of Sea Ltd., and River Ltd., were Rs.2,70,000 and Rs.2,40,000 respectively, the value of closing stock in the Consolidated Balance Sheet as on March 31, 2008 was **<Answer>**

(a) Rs.5,10,000
(b) Rs.3,30,000
(c) Rs.4,92,000
(d) Rs.4,32,000
(e) Rs.4,02,000. **(2marks)**

63. On April 01, 2007 Gold Ltd., purchased 80% equity shares of Silver Ltd. As on that date Silver Ltd., had Rs.22,500 in General Reserve and Rs.67,500 (debit) in Profit and Loss account. On the date of purchase, the fixed assets of Silver Ltd., were considered to be worth Rs.90,000 as against a book value of Rs.75,000. **<Answer>**

The Investments of Gold Ltd., showed a book value of Rs.2,10,000 and the company has no other investments than shares of Silver Ltd.
The Share capital of Silver Ltd., consists of 30,000 shares of Rs.10 each.
The cost of control shown in the Consolidated Balance Sheet as on March 31, 2008 was

(a) Rs.30,000 (Goodwill)
(b) Rs. 6,000 (Capital Reserve)
(c) Rs.54,000 (Capital Reserve)
(d) Rs. 6,000 (Goodwill)
(e) Rs.24,000 (Goodwill). **(2marks)**

64. The process of translation of local currency transactions into functional currency is known as <Answer>

(a) Translation
(b) Remeasurement
(c) Foreign currency translation
(d) Current exchange
(e) Future exchange. **(1 mark)**

65. Which of the following statements is **false** with reference to temporal method used for conversion? <Answer>

(a) Fixed assets are translated at historical rate as of the date of purchase
(b) Monetary assets and liabilities are translated using the current rate
(c) Non-monetary assets and liabilities are translated at the historical rate
(d) Revenues are translated at the average rate
(e) Expenses are translated at the historical rate. **(1 mark)**

66. As per US GAAP, cash flows in the reporting currency must replicate the cash flows in the <Answer>

(a) Foreign currency
(b) Functional currency
(c) Local currency
(d) Reporting currency
(e) Authorized currency. **(1 mark)**

67. Which of the following ratios is same under both translation and remeasurement process? <Answer>

(a) Receivables turnover ratio
(b) Fixed turnover ratio
(c) Current asset turnover ratio
(d) Return on equity ratio
(e) Return on capital employed ratio. **(1 mark)**

68. The amount of proposed dividend out of pre-acquisition profits of the subsidiary company belonging to the holding company is <Answer>

(a) Debited to Profit and Loss Appropriation account of holding company
(b) Debited to Profit and Loss account of holding company
(c) Shown under ‘proposed dividend in the consolidated balance sheet
(d) Credited to the investment account of the holding company
(e) Credited to the consolidated profit and loss account. **(1 mark)**

69. The information about the financial distress **cannot** be obtained from sources like <Answer>

(a) Cash flow analysis for current period
(b) Cash flow analysis for future periods
(c) Analysis of financial statements of the firm
(d) Corporate strategy analysis
(e) Break-even analysis. **(1 mark)**

70. Under the purview of GAAP, which of the following is generally considered as a mis-classification of financing and operating cash flows? <Answer>

(a) Cash held for specific purpose
(b) Asset held for sale
(c) Capitalization of operating expenses
(d) Insurance settlements
(e) Loans procured from shareholders. **(1 mark)**

END OF QUESTION PAPER

Suggested Answers
Financial Statement Analysis (CFA560): January 2009

Answer **Reason**

1. C SFAC 6 issued by Financial Accounting Standards Board (FASB) deals with elements of financial statements.

2. D Decrease in net assets from peripheral transactions of an entity and from all other transactions and other events and circumstances affecting the entity except those that result from expenses or distribution to owners is known as losses.

3. A Liabilities that are incurred and which are known or estimated and payable at future dates are generally reported at their net settlement values.

4. A The going concern concept assumes that the enterprise has neither the intention nor the necessity to liquidate or curtail materially the scale of operation of its business venture in the foreseeable future. The statements in other alternatives (b) The actual receipts or payments are not taken as the base under the accrual system, (c) The revenues/expenses are recognized if they belong to the relevant accounting period irrespective of cash or cash equivalent received/paid or not, (d) Securities are valued at lower of cost or market value in recognition of conservatism concept (e) The financial statements provide information not only the amount cash payments or receipts during the reporting period, but also the cash payable or receivable in the reporting period are true statements. Thus, the correct answer is (a).

5. D Matching concept (matching principle) states that the performance can be measured only if revenues and related costs are accounted for during the same time period.

6. A Comprehensive income statement arises as a result of

- Exchange transactions between the entity and entities other than the owners

Professional services
Lending and insurance
Environmental activities
Price changes.

Hence, (a) is false statement.

7. E Significant world wide accounting diversities are observed in the following areas:

- Inventory valuation

Accounting for lease
Accounting for research and development costs
Accounting for joint ventures
Treatment of extra-ordinary items.

Hence, (e) is correct answer.

8. C Prospective Investors are not considered as an internal user of financial statements. Board of Directors, partners, managers and officers are internal users of financial statements. <

9. E In the Consolidated Balance Sheet of a Holding Company, the value of minority interest consists of the proportionate share of minority shareholders in the <

1. Nominal value of share capital of subsidiary company
2. Reserves and profits of the subsidiary company at the time of acquisition by the holding company
3. Income of the subsidiary company after its acquisition by the holding company
4. Subsidiary company's losses or decreases in the value of assets of subsidiary company.

The value of minority interest does not consists of the proportionate share of minority shareholders in the reserves of the holding company. Hence, (e) is the correct answer.

10. A <

Particulars	Rs.	Rs.
Sale price per unit		92.00
Total variable production cost per unit	51.00	
Variable selling expenses (5% on Rs.92)	4.60	55.60
Contribution per unit		36.40
Fixed production overhead	4,85,500	
Fixed administration and selling overheads	3,08,300	
Estimated profit	1,16,200	
Total contribution		9,10,000
Number of units to be sold = $\frac{\text{Total Contribution}}{\text{Contribution per unit}}$	$\frac{\text{Rs.}9{,}10{,}000}{\text{Rs.}36.40}$	25,000 units

11. C Margin of safety will be increased <

- By increasing the level of production

By reducing the fixed cost

By increasing the selling price

By reducing the variable cost

By substituting the existing unprofitable product with profitable ones.

Hence, (c) is correct answer.

12. D If variable cost increases, contribution per unit decreases, break-even point will be increased, provided sales price per unit and fixed cost remain same. Other options given in (a), (b), (c) and (e) are not correct. <

13. C Accounts of non-integral foreign operations are translated using the following principles: ≤

- Assets and liabilities are both translated using the closing rate, whether they are monetary or non-monetary.

Items of income and expenses are translated using exchange rates of the date of the transaction.

All resulting exchange differences are to be accumulated in a foreign currency translation reserve until the net investments is disposed off.

Tax effects arising from such a translation is to be accounted as per AS-22.

Hence option (c) is correct answer.

14. B The following ratios are considered to predict corporate bankruptcy: ≤

- Cash flow to total assets.

Net assets to total assets.

Total debt to total assets.

Working capital to total assets.

Current asset to current liabilities.

Hence, sales to inventory is not considered to predict corporate bankruptcy.

15. E ≤

$$\text{TL} = \text{OL} \times \text{FL}$$

$$\text{or OL} = \frac{\text{TL}}{\text{FL}} = \frac{1.7}{1.04} = 1.6$$

$$\text{OL} = \frac{\text{Contribution}}{\text{EBIT}}$$

$$\text{or OL} = \frac{(\text{S} - \text{VC})}{\text{EBIT}}$$

$$\text{or VC} = \text{S} - (\text{OL} \times \text{EBIT})$$

$$\text{or VC} = \text{Rs.}5,00,000 - (1.6 \times \text{Rs.}2,32,500) = \text{Rs.}1,28,000$$

16. E Since the fixed assets and current assets are in the ratio of 3:1. ≤

Fixed assets	=	Rs. 14,06,250	
Current assets	=	Rs. 14,06,250 × 1/3 = Rs.4,68,750	
Total assets	=	Rs. 18,75,000	
As total assets	= total liabilities =		Rs.18,75,000
Less: Equity share capital	= 50,000 x Rs.10 =	Rs. 5,00,000	
Less: Retained earnings	= 50% of capital	Rs. 2,50,000	
			Rs. 7,50,000
Outside liabilities			Rs.11,25,000.

17. C Current ratio = CA/CL = 4. Or CA = 4CL = 4 x 15.5= Rs. 62 lakh. ≤

Acid test ratio = (CA - Inventory)/CL = 2.80

Or CA -Inventory = 2.80 × Rs.15.5 = Rs.43.4 lakh. Inventory = Rs.62 – Rs.43.4 = Rs.18.6 lakh.

18. A Debt equity ratio = 5:4 ≤

Equity = 4/9 × 36,00,000 = Rs.16,00,000.

Computation of fixed assets:

It is given that ratio of owner's equity to fixed assets is 8:15.

Rs.16,00,000/Fixed Assets =8/15

Fixed assets = Rs.16,00,000 × 15/8 = Rs.30,00,000.

19. A Trading account of Jeet Ltd., for the year ended March 31, 2008 ≤

Particulars	Rs.	Rs.	Particulars	Rs.	Rs.
To Opening stock (1/4/07)		1,86,420	By Sales	11,69,900	
			Less : returns	12,680	
To Purchases	7,18,210				11,57,220
Less returns	9,850	7,08,360	By Closing stock		1,24,840
To Wages	1,09,740				
+ Outstanding	1,890	1,11,630			
To Carriage inwards		4,910			
To Sundry Manufacturing expenses		19,240			
To Gross Profit		2,51,500			
		12,82,060			12,82,060

Gross profit ratio = Gross profit / Net Sales × 100

= Rs.2,51,500 / Rs.11,57,220 × 100 = 21.73%

20. D Inventory turnover = Cost of goods sold/ Average inventory ≤

= cost of goods sold / Rs.5,00,000 = 3.6 times.

Cost of goods sold = Rs.5,00,000 × 3.6 = Rs.18,00,000

Gross profit = Sales – Cost of goods sold

= Rs.30,00,000 – Rs.18,00,000 = Rs.12,00,000.

21. D The requirement is to compute the diluted EPS for 2008. Therefore, all potential common shares that reduce current EPS must be included in the computation. The formula for diluted EPS is ≤

$$\frac{\text{Net income available to common shareholders}}{\text{Weighted} - \text{average common shares outstanding}}$$

The net income available to common shareholders is Rs.32,00,000. This is after deducting Rs.2,00,000 of preferred stock dividends. The weighted-average common shares outstanding is 12,50,000. This is computed as the actual common shares outstanding for the full year of 12,00,000 plus the contingent common shares of 50,000 that were outstanding for the full year because the contingency was incurred in the year 2007. Thus,

Diluted EPS = Rs.32,00,000/12,50,000 = Rs.2.56.

22. C Payments for future contracts are an operating activity of a concern. ≤

23. D ≤

Particulars	Units
Opening stock	240
Add: Purchases	400
Less: Units sold	460
Closing stock	180

Value of closing stock in LC (under LIFO) = 180 × LC 1.20 = LC 216.

Translated value of closing stock = LC 216 ×1.10 = Rs.237.60.

24. B The major areas where manipulations of financial data are possible can be classified as ≤

- Income from continuing operations

Treatment of non-recurring income items

Changes in accounting estimates

Adjustments for changes in accounting policies

Extraordinary items.

Hence, (b) is correct answer.

25. C ≤

Particulars	Rs.	Rs.
Operating cash flow		5,00,000
Total capital expenditure	1,50,000	
After tax proceeds from sale of assets	50,000	1,00,000
Free cash flow of Rahul Ltd.		4,00,000

26. C Long lived assets classified as 'held for sale' are reported at net fair value or carrying value whichever is lower. ≤

27. D The specific identification method is not the method of revenue recognition. The methods mentioned in other options are methods of revenue recognition. ≤

28. A In a revenue manipulation, vendor financing occurs when a company loans money to a customer to purchase goods from the company. ≤

29. D Expense manipulation can be done by capitalizing revenue cost. ≤

30. B The difference between the treatment of expenditures on the tax return and for financial reporting is known as timing difference. ≤

31. C Revenues reported for financial reporting purposes before being reported for tax purposes is not a permanent difference as it is an example of temporary difference under the US GAAP. <

32. A <

Particulars	Rs.	Rs.
Non taxable interest received on municipal securities (permanent difference)		-
Long term loss accrual in excess of deductible amount (Rs.22,500× .40)		9,000
Depreciation as per income tax purpose	2,06,250	
Depreciation as per financial records	1,50,000	
Depreciastion in excess of financial statement amount	56,250	
Deffred tax liability (Rs.56,250 × .40)		22,500
Net deffered tax liability		13,500

33. C <

Particulars	Rs.
Total accounting income as per percentage of completion method	30,75,000
Total accounting income as per completed contract method	19,50,000
The amount of accounting income not recognized for tax purpose	11,25,000
Total deferred tax liability (Rs.11,25,000 × 25%)	2,81,250

34. B <

Particulars	Rs.	Rs.
Pre tax income		4,80,000
Gain on involuntary conversion	2,10,000	
Excess tax depreication	30,000	2,40,000
Taxabale income		2,40,000
Total tax liability (Rs.2,40,000 x .30)		72,000
Tax payments for the year 2008		42,000
Net current tax payable for the year 2008		30,000

35. C Max Ltd., did not elect to forego the loss carry back so Rs.4,00,000 of the Rs.8,00,000 loss will be carried back to offset 2006 income, resulting in a tax refund of Rs.1,60,000 (40% × Rs.4,00,000). The remaining Rs.4,00,000 of the 2007 loss will be carried forward to offset part of 2006 income. Thus the income tax liability at December 31, 2008 will be Rs.4,80,000 [40% × (Rs.16,00,000 – Rs.4,00,000)]. <

36. E <

- The liability which is treated under the category of 'amount and payee known' is unearned revenues.

Taxes payable is treated under the category of 'payee known but amount may have to be estimated'.

Bonus payable is treated under the category of 'payee known but amount may have to be estimated'

Compensated absences is treated under the category of 'payee known but amount may have to be estimated'

Product warranties is treated under the category of 'payee unknown and the amount may have to be estimated.

37. C As per SFAS 43, an employer is required to accrue a liability for employees' rights to receive compensation for future absences, such as vacations, when certain conditions are met. The Statement does not, however, specify how such liabilities are to be measured. Since vacation time is paid by SK Ltd., at the salaries in effect when vacations are taken or when employment is terminated. SK Ltd., adjusts its vacation liability and expense to current salary levels. SK Ltd.,'s 2008 vacation pay expense consists of vacations earned for work in 2008 (adjusted to current rates) of Rs.60,000 plus the amount necessary to adjust its pre-2008 vacation liability for the 10% salary increase. The adjustment is equal to 10% of the pre-existing liability balance, at December 31, 2008 [(Rs.70,000 – Rs.40,000) × 10%= Rs.3,000]. Therefore, total vacation pay expense for the period is equal to Rs.63,000 (Rs.60,000 + Rs.3,000). ≤

38. A As interest payable semi annually, ≤

the amount of interest for every six months is Rs.8,40,000 × 12% × 6/12 = Rs. 50,400

Present value of interest for 3 years = 50,400 × *5.0757 = Rs.2,55,815

Present value of principal amount of bond = Rs.8,40,000 × **.74622 = Rs.6,26,825

Present value of bond = Rs.8,82,640

*Present value of annuity for interest payable semi annually i.e., for Re.1; N = 6; I = 5%.

**Present value of principal payable at the end of 3rd year i.e. for Re.1; N = 6; I = 5%.

39. B ≤

Year	Present value at the beginning (Rs.)	Interest expense @4% (Rs.)	Coupon interest at 5% (Rs.)	Present value at the end (Rs.)
2006	4,11,100	16,444	20,000	4,07,544
2007	4,07,544	16,302	20,000	4,03,846
2008	4,03,846	16,154	20,000	4,00,000

The premium amortized at the end of the year 2008 was Rs.20,000 – Rs.16,154 = Rs.3,846

40. D ≤

Particulars	Rs.
Issue value of the bonds	12,48,000
Less: Face value of the bond (1,200 × Rs.1,000)	12,00,000
Balance in premium account	48,000
The amount of premium amortized (Rs.48,000 × *11/20)	26,400
Unamortized premium	21,600
Add: Face value of the bonds	12,00,000
The book value of the bonds	12,21,600
Value of retired bonds (Rs.12,00,000 × 101%)	12,12,000
Gain on early retirement of the bonds	9,600

On July 1, 2008, the premium has been amortized for five and half years or eleven six months periods (January 1, 2003 to July 1, 2008). Since the bond term was 10 years or 20 six months periods, the amount of Premium amortized by 11/20.

41. A A non-refundable security deposit is recorded usually as Unearned Revenue in the books of lessor. ≤

42. E As per SFAS-13 defines leveraged lease as a lease which satisfies the following prerequisites: ≤

- The lease must meet the definitions of a direct financing lease.
  The lease involves three parties – lessor, lessee and a long-term creditor.
  The lease is 'leveraged' because the lessor borrows to finance the transaction.
  The lessor's net investment is reduced in the early years and increases in the later years until it is eliminated.
  The lease does not affect the lessee's accounting treatment.

Hence, (e) is correct answer.

43. E Before the payment was made on 1st April 2008, the initial lease liability will be the present value of the five years lease rental together with the present value of the residual value i.e. Rs.(1,00,000 × 4.240 + 40,000 × 0.6500) = Rs.4,50,000. The payment made on 1st April 2008 should be excluded from this value and the capital leased liability will be Rs.(4,50,000 – 1,00,000) = Rs.3,50,000. ≤

44. D The annual lease payment is Rs.80,000 (Rs.3,44,960 /4.312). Maytas Company will receive 5 x Rs.80,000 = Rs.4,00,000 over the five years. Thus the interest revenue will be the excess of lease payment over the present value of the asset i.e. Rs.(4,00,000 – 3,44,960) = Rs.55,040. ≤

45. C According to SFAS 13, rent expense of operating leases is to be amortized on a straight-line basis if no other better-suited method is available. In the given case, Anuradha Enterprises should pay monthly rental for 5 years i.e. (60-9) = 51 months. The total rental amount of Rs.51,000 i.e. 51 x Rs.1,000 will be amortized over 5 years. Thus Rs.51,000/5 = Rs.10,200 to be shown as rent expense in Anuradha Enterprises' financial statement for the year ended March 31, 2008. ≤

46. D The debit to the "Obligation under capital lease" account is the principal payment on the lease. It is the difference between the total lease payment (excluding executory costs) and the interest expense, which is the lease obligation balance times the discount rate. ≤

47. A Service cost is the actuarial present value of benefits attributed during the current period. ≤

48. E Increase in expected return on plan assets is to be deducted from service cost to arrive at net pension cost. ≤

49. C Calculation of PBO at the end of the year ≤

Particulars	Rs.	Rs.
PBO at the beginning		90,000
Add: Service cost	21,600	
Add: Interest cost	9,000	30,600
		1,20,600
Less: benefits paid		18,000
PBO at the end of the year		1,02,600

50. D ≤

Particulars	Rs.	Rs.
Service cost		2,16,000
Interest cost	72,000	
Amortization of unrecognized prior service cost	18,000	90,000
		3,06,000
Less: Actual or expected gain on assets		54,000
Pension expense		2,52,000

The unexpected loss on assets related to disposal of a subsidiary Rs.60,000 is not considered for the computation of net pension cost.

51. A Under equity method of accounting, investments in which recognition of percentage share of income or loss, dividends and any changes in the investment percentage in an investee by an investor is considered. <

52. B Held-to maturity securities are to be carried at amortized cost. <

Particulars	Rs.
Acquisition cost of securities	4,76,400
Less: Accrued interest	10,800
Cost of securities	4,65,600
Add: amortized discount (Rs.4,80,000-Rs.4,65,600) x 7/15	6,720
Carrying amount of securities	4,72,320

53. C If cost of the acquired enterprise is in excess of the sum of the amounts assigned to net identifiable assets acquired, such excess is known as goodwill. <

54. B Trading securities are reported at fair value with unrealized gain or loss included in earnings. In the year 2007-08, the company should report an unrealized gain of Rs.55,000 (Rs.1,55,000 – Rs.1,00,000). <

55. A The existence of significant influence by an investor is usually evidenced by <

- Representation of the board of directors of the investee

Participation in policy making processes

Material transactions between the investor and the investee

Interchange of managerial personnel

Provision for essential technical information.

Representation of the board directors of the investee, not investor, evidences the existence of significant influence by an investor. Hence, option (a) is correct answer.

56. A <

Capital Profits	(Rs.)
Pre-acquisition reserve	9,00,000
Pre-acquisition profits	5,00,000
	14,00,000
Less: Dividend (40,00,000 × 10%)	4,00,000
	10,00,000

Particulars	(Rs.)	(Rs.)
Cost of investments		37,50,000
Face value of investments (Rs.40,00,000 × 60%)	24,00,000	
Capital profits (Rs.10,00,000 × 60%)	6,00,000	
Dividend out of pre-acquisition profits Rs.(4,00,000 × 60%)	2,40,000	32,40,000
Goodwill		5,10,000

57. E Profit made during the year 2007-08 = Rs.3,00,000 + Rs.1,80,000 = Rs.4,80,000 ≤

Profit made for the period from April 01, 2007 to November 01, 2007

= Rs.4,80,000 × 7/12 = Rs.2,80,000

The credit balance in Profit and Loss account as on November 01, 2007 was

= Rs.2,80,000 – Rs.1,80,000 = Rs.1,00,000

Hence capital profit = Rs.1,00,000

Share of Hari Ltd., in the capital profit = Rs.1,00,000 × 60% = Rs.60,000.

58. B Degree of control in Om Ltd: 80% ≤

Particulars	Rs.
Profit & Loss account on 1-4-2007	12,00,000
Profit for the year 2007-08	4,80,000
Share of Revenue Profit in Om Ltd. 80% of 1,39,500	1,11,600
	17,91,600
Less: Unrealised Profit	30,000
	17,61,600

Share in capital profit will be considered for the calculation of the cost of control and not added to the Profit and Loss account of Omkar Ltd.

59. E ≤

Particulars	Rs.
Nominal value of 6,000 shares @ Rs.100 per share	6,00,000
Share of capital Profit (3,40,000 + 3,00,000) × 30%	1,92,000
Share of Revenue Profit Rs.[(4,00,000 – 3,40,000) + (3,50,000 – 3,00,000)] × 30%	33,000
Minority interest	8,25,000

60. C The three basic elements in a balance sheet of a company are Assets, liabilities and shareholders equity. ≤

61. E In the process of translation of the financial statements of a foreign entity, current rate method will retain the relationship between various items of the income statement and balance sheet ≤

62. C Value of goods in stock = Rs.1,80,000 × 60% = Rs.1,08,000 ≤

Profit included in the goods = Rs.1,08,000 × 20 / 120 = Rs.18,000

Unrealized stock to be adjusted = Rs.18,000.

Particulars	Rs.
Stock of Sea Ltd.,	2,70,000
Stock of River Ltd.,	2,40,000
	5,10,000
Less: Unrealized profit	18,000
Value of closing stock in the Consolidated Balance Sheet	4,92,000

63. B Degree of control 80% ≤

Capital Profit/loss:	Rs.	Rs.
Pre-acquisition Profit and loss account (Dr.)		67,500
Pre-acquisition reserve	22,500	
Revaluation profit (Rs.90,000-Rs.75,000)	15,000	37,500
Capital loss		30,000
The share of Gold Ltd. (80%of Rs.30,000)		24,000
Cost of control:		
Cost of investments		2,10,000
Face value of shares held	2,40,000	
Less: Capital Loss share	24,000	2,16,000
Capital reserve		6,000

64. B The process of translation of local currency transactions into functional currency is known as remeasurement. ≤

65. E Under temporal method: ≤

- Monetary assets and liabilities i.e., cash, accounts receivables, accounts payable, short term debt, and long term debt are translated using the current rate.

Non-monetary assets and liabilities i.e., all assets and liabilities except above mentioned, are translated at the historical rate.

Revenues and expenses are translated at the average rate.

Purchase of inventory and fixed assets are re-measured at the historical rate as of the date of purchase. Therefore, depreciation and cost of goods sold are re-measured based on the historical rates prevailing at the time of purchase.

The translation gain or loss is shown in the income statement.

66. C As per US GAAP, cash flows in the reporting currency must replicate the cash flows in the local currency. ≤

67. A There is confusion between remeasurement process and translation. As per US GAAP remeasurement refers to the process of converting local currency translations into the functional currency with a foreign subsidiary. Translation refers to conversion of the functional currency data of a foreign subsidiary into the reporting currency. ≤

Functional currency affects both the income statement and balance sheet. Thus, many financial ratios effect with the choice of functional currency. Another important issue is the ratios are different under translation and remeasurement and ratios under translation are different from those in the local currency.

Receivables and sales are translated at the same rate in both translation and remeasurement and thus, the receivables turnover ratio is same under both the conditions. But all other asset turnover ratios differ under translation and remeasurement. Hence, option (a) is correct answer.

68. D The amount of proposed dividend out of pre-acquisition profits of the subsidiary company belonging to the holding company is credited to the investment account of the holding company. Therefore option (d) is the correct answer. ≤

69. E Financial distress means severe liquidity problems that covers, both the difficulty a firm has in meeting its debt obligations and the consequences of these difficulties, which may take the form of restrictions imposed by creditors on a company’s behavior (for example, a company may find it impossible to raise new funds). <

The information about the financial distress can be obtained from sources like cash flow analysis for current and future periods, corporate strategy analysis, analysis of financial statements of the firm and those of a comparison set of firms and external variables such as security returns and bond ratings.

Hence, option (e) is correct answer.

70. E Mis-classification of Financing and Operating Cash Flows: <

- Stock options
- Loans procured from shareholders
- Payment of dividends:
- Bank overdrafts:
- Advance payment by customers:
- Financing of Accounts receivables:

The other options are instances of mis-classification of investing cash flows and operating cash flows.

Hence, option (e) is correct answer.

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