Gurukripa's Guideline Answers to Nov 2012 Exam Questions Final Group I – Financial Reporting

Question 1 is compulsory **(4 × 5 = 20 Marks)**
Answer **any five** questions from the **remaining six** questions **(16 × 5 = 80 Marks).** [Answer any 4 out of 5 in Q.7]

Question 1(a): AS 19 – Leases – Unearned Finance Income N 12 (5 Marks)

Prakash Limited leased a Machine to Badal Limited on the following terms –

	(₹ in Lakhs)
(i) Fair Value of the Machine	48.00
(ii) Lease Term	5 years
(iii) Lease Rental per annum	8.00
(iv) Guaranteed Residual Value	1.60
(v) Expected Residual Value	3.00
(vi) Internal Rate of Return	15%

Discounted rates for 1st year to 5th year are 0.8696, 0.7561, 0.6575, 0.5718 and 0.4972 respectively.
Ascertain Unearned Financial Income.

Solution:

Unearned Finance Income = Gross Investment – [PV of aggregate of minimum lease payment + PV of unguarantee and residual value]
Gross Investment = Aggregate of MLP + Guaranteed Residual Value + Any unguaranteed Residual value.
Gross Investment = (8,00,000 × 5) + 1,60,000 + 1,40,000 = ₹ **43,00,000**

Year	Amount	Discounting Factor at 15%	Discounted Amount
1	8,00,000	0.8696	6,95,680
2	8,00,000	0.7561	6,04,880
3	8,00,000	0.6575	5,26,000
4	8,00,000	0.5718	4,57,440
5	8,00,000	0.4972	3,97,760
5	1,60,000	0.4972	79,552
5	1,40,000	0.4972	69,608
Total	**43,00,000**		**28,30,920**

Unearned Finance Income = 43,00,000 – 28,30,920 = ₹ **14,69,080**

Question 1(b): AS – 22 – Deferred Taxes N 12 (5 Marks)

Goodwill Limited is a full tax–free Enterprise for the 1st 12 years of its existence and is in third year of operations. Depreciation Timing Difference resulting in a deferred tax liability in 1st, 2nd and 3rd year is ₹ 200 Lakhs, ₹ 300 Lakhs and ₹ 400 Lakhs respectively. From the 4th year onwards, it is expected that the timing difference would reverse each year by ₹ 10 Lakhs. Assuming tax rate at 35%, find out the deferred tax liability at the end of 3rd year and any charge to the Profit and Loss Account.

Solution: Similar to Q.No.42 / Page 22.18 of Padhuka's Students' Referencer on Accounting Standards, F(A/c) M 10

Particulars	Year 1	Year 2	Year 3
Originating Timing Difference	200	300	400
Less: Reversing during Tax Holiday period	(10 × 9) 90	–	–
Reversing after Tax Holiday Period	110	300	400
Cumulative Timing Difference as at year end	110	410	810
DTL to be created at 35% (Current Year) by debit to P&L	38.50 (110 × 35%)	105 (300 × 35%)	140 (400 × 35%)
Cumulative Balance in Deferred Tax Liability A/c	**38.50**	**143.50**	**283.50**

Question 1(c): Computation of Value of Closing Stock N 12 (5 Marks)

In a manufacturing proves of Vijoy Limited, one by–product BP emerges besides two main products MP1 and MP2 apart from scrap. Details of cost of production process is here under –

Item	Unit	Amount (₹)	Output (Unit)	Closing Stock as on 31–03–2012
Raw–Material	15000	1,60,000	MP1–6250	800
Wages	–	82,000	MP2–5000	200
Fixed Overhead	–	58,000	BP–1600	–
Variable Overhead	–	40,000	–	–

Average Market Price of MP1 and MP2 is ₹ 80 per unit and ₹ 50 per unit respectively, by–product is sold at ₹ 25 per unit. There is a Profit of ₹ 5,000 on sale of by–product after incurring separate processing charges of ₹ 4,000 and packing charges of ₹ 6,000. ₹ 6,000 was realized from sale of scrap. Calculate the value of Closing Stock of MP1 and MP2 as on 31–03–2012.

Solution:

Joint Cost = ₹ 1,60,000 + ₹ 8,200 + ₹ 58,000 + ₹ 40,000 = ₹ 3,40,000

NRV of By–product = Sale Price 40,000 (1,600 × 25) – Further Cost 10,000 = ₹ 30,000

NRV of By–product and Scrap = ₹ 30,000 + ₹ 6,000 = ₹ 36,000

Net Joint Cost = ₹ 3,40,000 – ₹ 36,000 = ₹ 3,04,000.

Particulars	**MP1**	**MP2**	**Total**
Production Quantity	6,250	5,000	11,250
Apportionment Joint Cost based on sale value (80 × 6,250) : (50 × 5,000) or 2:1	2,02,667	1,01,333	3,04,000
Average Joint Cost	32.43	20.27	–
Closing Stock Units	800	200	–
Value	**25,944**	**4,054**	**29,998**

Note: It is assumed that Net Realisable Value is more than Cost. The Profit on by–product is irrelevant, since only Net Realisable Value has to be considered.

Question 1(d): AS – 25 – Interim Financial Reporting N 12 (5 Marks)

Antarbarti Limited reported a Profit Before Tax (PBT) of ₹ 4 Lakhs for the third quarter ending 30th September 2011. On enquiry you observe the following. Give the treatment required under AS–25.

(i) Dividend Income of ₹ 4 Lakhs received during the quarter has been recognised to the extent of ₹ 1 Lakh only.

(ii) 80% of Sales Promotion Expenses ₹ 15 Lakhs incurred in the third quarter has been deferred to the fourth quarter as the Sales in the last quarter is high.

(iii) In the third quarter, the Company changed depreciation method from WDV to SLM, which resulted in excess depreciation of depreciation of ₹ 12 Lakhs. The entire amount has been debited in the third quarter, though the share of the third is only ₹ 3 Lakhs.

(iv) ₹ 2 Lakhs Extraordinary Gain received in third quarter was allocated equally to the third and fourth quarter.

(v) Cumulative loss resulting from change in method of Inventory Valuation was recognized in the third quarter of ₹ 3 Lakhs. Out of this loss ₹ 1 Lakh relates to previous quarters.

(vi) Sale of investment in the first quarter resulted in a gain of ₹ 20 Lakhs. The Company had apportioned this equally to the four quarters.

Prepare the adjusted Profit Before Tax for the third quarter.

Solution: Similar to Q.No.27 / Page 25.9 of Padhuka's Students' Referencer on Accounting Standards

	Particulars	**₹**
	PBT as reported	4,00,000
Add:	Dividend Income (Balance Dividend Income to be recognized) (4,00,000 – 1,00,000)	3,00,000
	Difference due to change in method of Depreciation (12,00,000 – 3,00,000)	9,00,000
	Extraordinary Gain allocated to fourth quarter (2,00,000 – 1,00,000)	1,00,000
	Loss on Change in the method of Inventory Valuation relating to previous quarters	1,00,000
Less:	Sales Promotion Expenses relating to this quarter (15,00,000 × 80%)	(12,00,000)
	Apportioned Gain on Sale of Investments in first quarter to be reversed (20,00,000 ÷ 4)	(5,00,000)
	Adjusted PBT for the Third Quarter	**1,00,000**

Note: The Company should also re–state the results of the previous quarters based on the above adjustments.

Question 2: Consolidated Financial Statements N 12 (16 Marks)

War Limited purchased 48,000 Shares in Peace Limited on 31st March 2010, at 50% premium over Face Value by issue of 8% Debentures at 20% premium. The Balance Sheets of War Limited and Peace Limited as on 31.03.2010, i.e., on the date of purchase were as under –

Equity & Liabilities	War Ltd	Peace Ltd	Assets	War Ltd	Peace Ltd
Share Capital of ₹ 10 each	10,50,000	6,00,000	Fixed Assets	6,50,000	2,00,000
General Reserve	1,20,000	40,000	Stock–in–Trade	3,00,000	1,80,000
Profit and Loss A/c	80,000	–	Sundry Debtors	3,20,000	2,00,000
Sundry Creditors	1,00,000	60,000	Cash in Hand	60,000	30,000
			Preliminary Expenses	20,000	10,000
			Profit and Loss A/c	–	80,000
	13,50,000	7,00,000		13,50,000	7,00,000

1. Particulars of War Limited:
   (a) Profits made: 2010–11 ₹ 1,60,000
   2011–12 ₹ 2,00,000
   (b) The above profit was made after charging depreciation of ₹ 60,000 and ₹ 40,000 respectively.
   (c) Out of profit shown above, every year ₹ 20,000 had been transferred to General Reserve.
   (d) 10% Dividend had been paid in both the years
   (e) It has been decided to write down Investment to Face Value of Shares in 10 years and to provide fro share of loss to Subsidiary.

2. Particulars of Peace Limited:
   The Company incurred losses of ₹ 40,000 and ₹ 60,000 in 2010–2011 and 2011–2012 after charging depreciation of 10% p.a. on the Book Value of Fixed Assets as on 01.04.2010.

   Prepare Consolidated Balance Sheet of War Limited and its subsidiary as at 31st March 2012 as per requirement of Revised Schedule VI.

Solution: **Similar to Page 3.30, Q.No.14**

A. PREPARATION OF B/S OF WAR LIMITED AND PEACE LIMITED AS AT 31.03.2012

1. General Reserve & Profit & Loss Account as at 31.03.2012

Particulars	**War Ltd**		**Peace Ltd**	
	Gen. Res.	**P&L A/c**	**Gen. Res.**	**P&L A/c**
Balance as on 31.03.2010	1,20,000	80,000	40,000	(80,000)
Add/Less: Profits (Losses) for 2010–2011 & 2011–2012 (War = 1,60,000 + 2,00,000; Peace = 40,000 + 60,000)	–	3,60,000	–	(1,00,000)
Add/ Less: Transfer to General Reserve (20,000 × 2 Yrs)	40,000	(40,000)	–	–
Less: Dividends Paid (10,50,000 × 10% × 2 years)	–	(2,10,000)	–	–
Less: Provision for Losses in Subsidiary (1,00,000 × 80%)	–	(80,000)	–	–
Less: Premium on acquisition of Shares written off **(WN 6)**	–	(48,000)		
Balance as on 31.03.2012	**1,60,000**	**62,000**	**40,000**	**(1,80,000)**

2. Debentures issued for acquisition of Shares

	Particulars	**₹**
	Cost of Acquisition of Shares (48,000 Shares × ₹ 15 per Share)	7,20,000
	Therefore, Value of 8% Debentures issued	7,20,000
Less:	Amount of Debenture Premium at 20% (20 ÷ 120 × 7,20,000)	(1,20,000)
	Face Value Debentures Issued	**6,00,000**

3. Fixed Assets balances on 31.03.2012

	Particulars	War	Peace
	Balance as on 31.03.2010	6,50,000	2,00,000
Less:	Depreciation for 2010–2011	(60,000)	(20,000)
Less:	Depreciation for 2011–2012	(40,000)	(20,000)
	Balance as on 31.03.2012	**5,50,000**	**1,60,000**

4. Stock, Debtors & Creditors: Assuming that the Company maintains the same level of Stock, Debtors and Creditor, balance as on 31.03.2012 is the same as on 31.03.2010 (as given in the question).

Particulars	War	Peace
Stock in Trade	3,00,000	1,80,000
Sundry Debtors	3,20,000	2,00,000
Sundry Creditors	1,00,000	60,000

5. Cash & Bank balances on 31.03.2012

	Particulars	War	Peace
	Balance as on 31.03.2010	60,000	30,000
Add / Less:	Profit / Loss for 2010–2011	1,60,000	(40,000)
Add / Less:	Profit / Loss for 2011–2012	2,00,000	(60,000)
Add:	Depreciation for 2010–2011 and 2011–2012	1,00,000	40,000
Less:	Cash Dividend (10,50,000 × 10% × 2 years)	(2,10,000)	–
	Balance as on 31.03.2012	**3,10,000**	**(30,000)**

6. Investment in Peace Ltd as per books on 31.03.2012

	Particulars	₹
	Cost of Investment	7,20,000
Less:	Premium on Acquisition W/Off (₹ 5 per Share × 48,000 Shares × 2 Years / 10 Years)	(48,000)
	Balance as on 31.03.2012	**6,72,000**

7. Balance Sheet as at 31.03.2012

Liabilities	War	Peace	Assets	War	Peace
Share Capital (₹ 10)	10,50,000	6,00,000	Fixed Assets **(WN 3)**	5,50,000	1,60,000
Securities Premium **(WN 2)**	1,20,000	–	Stock–in–Trade **(WN 4)**	3,00,000	1,80,000
General Reserve **(WN 1)**	1,60,000	40,000	Sundry Debtors **(WN 4)**	3,20,000	2,00,000
P&L A/c **(WN 1)**	62,000	–	Cash & Bank **(WN 5)**	3,10,000	(30,000)
8% Debentures **(WN 2)**	6,00,000	–	Investment in Peace Ltd **(WN 6)**	6,72,000	–
Provision for Loss of Subsidiary	80,000	–	Preliminary Expenses	20,000	10,000
Sundry Creditors **(WN 4)**	1,00,000	60,000	P&L A/c **(WN 1)**	–	1,80,000
Total	**21,72,000**	**7,00,000**	**Total**	**21,72,000**	**7,00,000**

B. PREPARATION OF CONSOLIDATED BALANCE SHEET AS AT 31.03.2012

1. Basic Information

Company Status	Dates	Holding Status
Holding Company = War Ltd	Acquisition: 31.03.2010	Holding Company = 80%
Subsidiary Company = Peace Ltd	Consolidation: 31.03.2012	Minority Interest = 20%

2. Analysis of Reserves & Surplus of Peace Ltd

(a) General Reserve

Balance as on 31.03.2012 ₹ 40,000

On date of acquisition **₹ 40,000** — **Capital Profit**

Date of Acquisition to Date of Consolidation **NIL** — **Revenue Reserve**

(b) Profit & Loss Account

Balance as on 31.03.2012 ₹ (1,80,000)

On date of acquisition ₹ **(80,000)** **Capital**

Date of Acquisition to Date of Consolidation ₹ **(1,00,000)** **Revenue**

(c) Preliminary Expenses (₹ 10,000) – **Capital Profit**

3. Consolidation of Balances

Particulars	**Total**	**Minority Interest**	**Pre–Acqn.**	**Post Acquistion**		
(Holding – 80%, Minority – 20%)				**Gen. Res.**	**P&L A/c**	**Prel. Exp.**
Equity Capital	6,00,000	1,20,000	4,80,000	–	–	–
General Reserve	40,000	8,000	32,000	–		–
Profit and Loss A/c	(1,80,000)	(36,000)	(64,000)	–	(80,000)	–
Preliminary Expenses	(10,000)	(2,000)	(8,000)	–	–	–
Minority Interest		**90,000**				
Total [Cr]			**4,40,000**		**(80,000)**	
Cost of Investment [Dr]			**(6,72,000)**			
Parent's Balances				1,60,000	62,000	
Provision for Loss					80,000	
For Consolidated Balance Sheet		**90,000**	**(2,32,000) (Goodwill)**	**1,60,000**	**62,000**	**–**

4. Consolidated Balance Sheet of War Ltd and its Subsidiary Peace Ltd as on 31.03.2012

	Particulars as at 31st December	**Note**	**This Year**	**Prev. Year**
I	**EQUITY AND LIABILITIES:**			
(1)	**Shareholders' Funds:**			
	(a) Share Capital	**1**	10,50,000	
	(b) Reserves and Surplus	**2**	3,22,000	
(2)	**Minority Interest**		90,000	
(3)	**Non–Current Liabilities:**			
	Long Term Borrowings – 8% Debentures		6,00,000	
(4)	**Current Liabilities** – Trade Payables (1,00,000 + 60,000)		1,60,000	
	Total		**22,22,000**	
II	**ASSETS**			
(1)	**Non–Current Assets**			
	(a) Fixed Assets: Tangible Assets		7,10,000	
	Intangible Assets – Goodwill		2,32,000	
(2)	**Current Assets:**			
	(a) Inventories (3,00,000 + 1,80,000)		4,80,000	
	(b) Trade Receivables (3,00,000 + 2,20,000)		5,20,000	
	(c) Cash and Cash Equivalents (3,10,000 – 30,000)		2,80,000	
	Total		**22,22,000**	

Note 1: Share Capital

Particulars		**This Year**	**Prev. Year**
Authorised:	.... Equity Shares of ₹ 10 each	XXXX	
Issued, Subscribed & Paid up:	1,05,000 Equity Shares of ₹ 10 each	10,50,000	
Total		**10,50,000**	

Note 2: Reserves and Surplus

Particulars	This Year	Prev. Year
Securities Premium	1,20,000	
Other Reserves – General Reserve	1,60,000	
Surplus (P&L A/c) (Opening 62,000 – Preliminary Expenses Writen Off 20,000)	42,000	
Total	**3,22,000**	

Question 3: External Reconstruction — N 12 (16 Marks)

The Abridged Balance Sheet (Draft) of V Ltd as on 31st March 2012 is as under –

Equity & Liabilities	₹	Assets	₹
24,000, Equity Shares of ₹ 10 each	2,40,000	Goodwill	5,000
5000, 8% Cumulative Preference Shares of ₹ 10 each	50,000	Fixed Assets	2,57,000
8% Debentures	1,00,000	Stock	50,000
Interest Accrued on Debentures	8,000	Debtors	60,000
Creditors	1,00,000	Bank	1,000
		Preliminary Expenses	15,000
		Profit & Loss Account	1,10,000
Total	4,98,000	Total	4,98,000

The following scheme is passed and sanctioned by the Court –

(i) A New Company P Ltd is formed with ₹ 3,00,000, divided into 30,000 Equity shares of ₹ 10 each.

(ii) The New Company will acquire the Assets and Liabilities of V Ltd on the following terms:

   (a) Old Company's Debentures are paid by similar Debentures in New Company and for Outstanding Accrued Interest, Shares of equal amount are issued at par.

   (b) The Creditors are paid for every ₹ 100, ₹ 16 in cash and 10 Shares issued at par.

   (c) Preference Shareholders are to get equal number of Equity Shares at par. For Arrears of Dividend amounting to ₹ 12,000, 5 Shares are issued at par for each ₹ 100 in full satisfaction.

   (d) Equity Shareholders are issued one Share at par for every three Shares held.

   (e) Expenses of ₹8,000 are to be borne by the New company.

(iii) Current Assets are to be taken at book value (except Stock, which is to be reduced by ₹ 3,000). Goodwill is to be eliminated, balance of Purchase Consideration being attributed to Fixed Assets.

(iv) Remaining Shares of the New Company are issued to public at par and are fully paid.

You are required to show:

(a) In the Old Company's books –

   (i) Realisation and Reconstruction (combined) Account

   (ii) Equity Shareholder's Account

(b) In the New Company's books –

   (i) Bank Account

   (ii) Summarised Balance Sheet as per requirement of Revised Schedule VI.

Solution: **Similar to Page 2.125, Q.No.59, M 90**

1. Computation of Purchase Consideration

Particulars	Mode	Computation	₹
Equity Shareholders	1 Equity Share of P Ltd of ₹ 10 each issued at par for every 3 Shares	24,000 Shares × 1/3 × ₹ 10	80,000
Pref. Shareholders			
(a) For Share Capital	1 Equity Share of P Ltd of ₹ 10 each issued at par for every 1 Share	5,000 Shares × ₹ 10	50,000
(b) For Arrears of Dividend	5 Equity Shares of P Ltd of ₹ 10 each issued at par for every ₹ 100 arrears of Dividend	$\frac{₹12{,}000}{₹100}$ × 5 Shares × ₹ 10	6,000
Total Purchase Consideration			**1,36,000**

2. In the Books of V Ltd

A. Realisation & Reconstruction A/c

Particulars	₹	Particulars	₹
To Goodwill A/c	5,000	By P Ltd A/c	1,36,000
To Fixed Assets	2,57,000	By Creditors A/c	1,00,000
To Stock	50,000	By 8% Debentures	1,00,000
To Debtors	60,000	By Accrued Interest on debentures	8,000
To Bank	1,000	By Preference Shareholders A/c	6,000
To Preference Shareholders A/c (Dividend)	12,000	By Equity Shareholder A/c – Loss **(b/f)**	**35,000**
Total	**3,85,000**	**Total**	3,85,000

B. Equity Shareholders A/c

Particulars	₹	Particulars	₹
To Preliminary Expenses A/c	15,000	By Equity Share Capital A/c	2,40,000
To P & L A/c	1,10,000		
To Equity Shares in P Ltd A/c	80,000		
To Realisation A/c	35,000		
Total	**2,40,000**	**Total**	**2,40,000**

C. Preference Shareholders A/c

Particulars	₹	Particulars	₹
To Equity Shares in P Ltd	56,000	By Preference Share Capital A/c	50,000
To Realisation A/c **(balancing figure)**	**6,000**	By Realisation Arrears of Dividend A/c	12,000
Total	**62,000**	**Total**	**62,000**

3. In the Books of P Ltd

A. Bank A/c

Particulars	₹	Particulars	₹
To balance taken over on acquisition	1,000	By Expenses on Acquisition	8,000
To Share Capital **(WN 1)** (5,600 Shares × ₹ 10)	56,000	By Creditors (1,00,000 × $\frac{16}{100}$)	16,000
		By balance c/d **(balancing figure)**	**33,000**
Total	**57,000**	**Total**	**57,000**

Working Notes:

1. Computation of Shares to be issued to Public

	Particulars	No. of Shares
	Total No. of Equity Shares	30,000
Less:	Allotment by way of purchase consideration	(13,600)
Less:	Settlement of accrued interest on debentures (₹ 8,000 ÷ ₹ 10)	(800)
Less:	Settlement of Creditors ($\frac{₹\ 1,00,000}{₹\ 100}$ × 10 Shares)	(10,000)
	No. of Shares issued to Public at par	**5,600**

2. Value of Fixed Assets Taken over

	Particulars	₹	₹
	Purchase Consideration		1,36,000
Add:	**Liabilities taken over**		
	(i) 8% debentures	1,00,000	
	(ii) Interest accrued on debentures	8,000	
	(iii) Creditors [16,000 + (10,000 Shares × ₹ 10 each)	1,16,000	2,24,000

Particulars		₹	₹
Less:	**Assets taken over**		
	(i) Stock (50,000 – 3,000)	47,000	
	(ii) Debtors	60,000	
	(iii) Bank	1,000	(1,08,000)
Add:	Expenses on acquisition		8,000
Value of Fixed Assets			**2,60,000**

4. Consolidated Balance Sheet of War Ltd and its Subsidiary Peace Ltd as on 31.03.2012

	Particulars as at 31st December	Note	This Year	Prev. Year
I	**EQUITY AND LIABILITIES:**			
(1)	**Shareholders' Funds** – Share Capital	**1**	3,00,000	
(2)	**Non–Current Liabilities:**			
	Long Term Borrowings – 8% Debentures		1,00,000	
	Total		**4,00,000**	
II	**ASSETS**			
(1)	**Non–Current Assets**			
	Fixed Assets –Tangible Assets **(WN 2)**		2,60,000	
(2)	**Current Assets:**			
	(a) Inventories		47,000	
	(b) Trade Receivables		60,000	
	(c) Cash and Cash Equivalents – Balances with Banks		33,000	
	Total		**4,00,000**	

Note 1: Share Capital

Particulars		This Year	Prev. Year
Authorised:	30,000 Equity Shares of ₹ 10 each	**3,00,000**	
Issued, Subscribed & Paid up:	30,000 Equity Shares of ₹ 10 each (Of the above 24,400 Equity Shares are issued for non–cash consideration)	3,00,000	
Total		**3,00,000**	

Question 4(a): Non–Banking Finance Company N 12 (10 Marks)

Samvedan Limited is a Non–Banking Finance Company. It accepts Public Deposit and also deals in hire purchase business. It provides you with the following information regarding major hire purchase deals as on 31.03.2010. Few machines were sold on hire purchase basis. The hire purchase price was set as ₹ 100 Lakhs as against the Cash Price of ₹ 80 Lakhs. The amount was payable as ₹ 20 Lakhs down payment and balance in 5 equal instalments. The Hire Vendor collected First Instalment as on 31.03.2011, but could not collect the Second Instalment which was due on 31.03.2012. The Company was finalising accounts for the year ending 31.03.2012. Till 15.05.2012, the date on which the Board of Directors signed the accounts, the second instalment was not collected. Presume IRR to be 10.42%.

Required:

(i) What should be the principal outstanding on 01.04.2011? Should the Company recognise finance charge for the year 2011–12 as income?

(ii) What should be the Net Book value of Assets on 31.03.2012 so far Samvedan Ltd. is concerned as per NBFC prudential norms requirement for provisioning?

(iii) What should be the amount of provision to be made as per prudential norms for NBFC laid down by RBI?

Solution:

Particulars	₹ in Lakhs
(a) HP Price	100
(b) Down Payment	20
(c) Balance amount payable (a) – (b)	80
(d) Amount payable in each instalment (80 Lakhs ÷ 5 instalments)	16
(e) AF at 10.42% for 5 Years	3.7505
(f) PV of the instalments (d) × (e)	60
(g) Interest Component (c) – (f)	20

Loan Repayment Schedule

Year	Opening Principal	Instalment Amount	Interest	Principal Repaid	Closing Principal
(1)	**(2)**	**(3)**	**(4) = (2) × 10.42%**	**(5) = (3) – (4)**	**(6) = (2) – (5)**
1	60	16	6.252	9.748	50.252
2	50.252	16	5.236	10.764	39.488
3	39.488	16	4.115	11.885	27.603
4	27.603	16	2.876	13.124	14.479
5	14.479	16	1.521	14.479	Nil
	Total	**80**	**20**	**60**	

Principal outstanding as on 01.04.2011 = **₹ 50.252 Lakhs**. Finance Charges for the year 2011–12 can be recognized as income since the instalments are overdue for a period less than 12 months. Since as at Balance Sheet it is **not** yet Non Performing Asset.

Computation of Net Book Value Assets

Particulars	₹ in Lakhs
(a) Aggregate of Overdue and Future Instalments Receivable (₹ 16 Lakhs × 4)	64
(b) Balance of Unmatured Finance Charges (4.115 + 2.876 + 1.521)	8.512
(c) Provision for Non–Performing Assets **(Note)**	7.488
(d) Net Book Value of the Asset	**48**

Note:

Particulars	₹ in Lakhs
(a) Aggregate of Overdue and Future Instalments Receivable	64
(b) Balance of Unmatured Finance Charges	8.512
(c) Depreciated Value of the Asset [₹ 80 Lakhs – (80 Lakhs × 20% × 2 years)]	48
(d) Provision to be created **(a) – (b) – (c)** (shown as reduction on Liabilities Side in Balance Sheet)	**7.488**
(e) Provision on Standard Assets at 0.25% of ₹ 48,00,000	**0.12**
(f) **Total Provision to be created (d) + (e)**	**7.608**

Question 4(b): Valuation of Goodwill –Leverage Effect on Goodwill N 12 (6 Marks)

Find out Leverage effect on Goodwill in the following case:

(i)	Current cost of capital employed	₹ 10,40,000
(ii)	Profit earned after current cost adjustments	₹ 1,72,000
(iii)	10% Long Term Loan	₹ 4,50,000
(iv)	Normal Rate of Return :	
	On Equity Capital Employed	15.6%
	On Long Term Capital Employed	13.5%

Solution: **Similar to Page 1.48, Q No. 17 Pt 5 & 6, M 10**

1. Computation of Goodwill using different approaches

Particulars	Owners Funds	Total
(a) Future Maintainable Profits	1,72,000	1,72,000 + (10% × 4,50,000) = 2,17,000
(b) Normal Rate of Return	15.6%	13.5%
(c) Capitalised Value of Future Maintainable Profits (a) ÷ (b)	11,02,564	16,07,407
(d) Capital Employed	10,40,000	14,90,000
(e) Goodwill (c) – (d)	**62,564**	**1,17,407**

2. Leverage Effect on Goodwill

- Goodwill computed using Equity Fund Concept (₹62,564), is low when compared to the Goodwill as computed using Total Long Term Funds Concept (₹ 1,17,407)
- Leverage Effect on Goodwill = ₹ 1,17,407 – ₹ 62,564 = ₹ **54,843**

Question 5(a): Valuation of Shares – Different Types of Share & Paid Up Values N 12 (10 Marks)

The Balance Sheet of Mulyan Ltd, as on 31st December, 2010 is as follows –

Equity & Liabilities		₹	Assets	₹
Share Capital			Goodwill	50,000
Equity Shares of ₹ 10 each	5,00,000		Fixed Assets	
Less: Calls in Arrear (₹ 2 for final call)	(10,000)	4,90,000	Machinery	2,30,000
8% Preference Shares of ₹ 10 each fully paid		2,00,000	Factory shed	3,00,000
Reserve and Surplus			Vehicles	60,000
General Reserve		2,00,000	Furniture	25,000
Profit & Loss A/c		1,40,000	Investments	1,00,000
Current Liabilities			Current Assets	
Sundry Creditors		2,70,000	Stock–in–Trade	2,10,000
Bank Loan		1,00,000	Sundry Debtors	3,50,000
			Cash at Bank	50,000
			Preliminary Expenses	25,000
Total		14,00,000	Total	14,00,000

Additional Information:

(i) Fixed Assets are worth 20% above their actual Book Value, Depreciation on appreciated portion of Fixed Assets is to be ignored for valuation of Goodwill.

(ii) Of the Investment, 80% is Non–Trading and the Balance is Trading. All Trade Investments are to be valued at 20% below cost. A uniform rate of dividend of 10% is earned on all Investments.

(iii) For the purpose of valuation of Shares, Goodwill is to be considered on the basis of 6 year's purchase of the Super Profits based on Simple Average Profit of the last 3 years. Profits after tax at 50%, are as follows – Year 2008 – 1,90,000, Year 2009 – 2,00,000 and Year 2010 – 2,50,000

In a similar business, Return on Capital Employed is 20%. In 2008, a new Furniture costing ₹ 10,000 was purchased but wrongly charged to revenue. No effect has yet been give for rectifying the same. Depreciation is charged on Furniture at 10% p.a. (Diminishing Balance Method).

Find out the value of each fully paid and partly paid Equity Shares.

Solution: **Similar to Page 1.104, Q.No.29, N 83 (Adapted), N 10**

1. Computation of Value per Share

Particulars	₹
Capital Employed **(WN 2)**	10,01,393
Add: (a) Calls in Arrears	10,000
(b) Non Trade Investments	80,000
(c) Goodwill **(WN 2)**	37,614
Sub total	**11,29,007**
Less: Preference Share Capital	2,00,000
Net Capital Employed belonging to Equity Shareholders	9,29,007
No. of Shares (5,00,000 ÷ 10)	50,000
Value of ₹ 10 Paid–up Share (Face Value ₹ 10 per Share)	**18.58**
Value of ₹ 8 Paid–up Share (Face Value ₹ 10 per Share) (₹ 18.58 – ₹ 2.00)	**16.58**

2. Computation of Closing Capital Employed

Particulars	Computation	₹
(A) Assets		
1. Machinery	2,30,000 + 20%	2,76,000
2. Factory Shed	3,00,000 + 20%	3,60,000
3. Vehicle	60,000 + 20%	72,000
4. Furniture **(Note)**	32,290 + 20%	38,784
5. Investments	1,00,000 × 20% trading × 80% (i.e. 20% below cost)	16,000
6. Stock–in–Trade		2,10,000
7. Sundry Debtors		3,50,000
8. Cash at Bank		50,000
Sub Total (A)		**13,72,748**
(B) Liabilities		
1. Bank Loan		1,00,000
2. Sundry Creditors		2,70,000
3. Provision for Tax	**(WN 3)**	(1,355)
Sub Total (B)		**3,71,355**
Capital Employed [(A) – (B)]		**10,01,393**

3. Computation of Future Maintainable Profits

Particulars	2008	2009	2010
Profit after tax before adjustment	1,90,000	2,00,000	2,50,000
Add: Furniture wromgly recorded as revenue (after tax effect)	5,000	–	–
Less: Adjustment for Depreciation (after tax effect)	(500)	(450)	(405)
Less: Income from Non–Trade Investments (assumed tax free dividends)	(8,000)	(8,000)	(8,000)
Future Maintainable Profits	1,86,500	1,91,550	2,41,595
Average Profits	₹ 2,06,548		
Normal Rate of Return × Capital Employed (20% × 10,01,393)	₹ 2,00,279		
Super Profits (₹ 2,06,548 – ₹ 2,00,279)	₹ 6,269		
Goodwill (₹ 6,269 × 6 Years of Purchase)	**₹ 37,614**		

4. Computation of Provision for Tax

Adjustment	Gross Amount (₹)	Tax Effect at 50% (₹)
Furniture Wrongly expensed – rectified	10,000	5,000
Depreciation on Furniture now capitalized		
(a) Year 2008	(10,000 × 10%) 1,000	(500)
(b) Year 2009	(9,000 × 10%) 900	(450)
(c) Year 2010	(8,100 × 10%) 810	(405)
Income from Non–Trade Investments	8,000	Nil (assumed tax free dividend)
Total (Savings in Income Tax)		**(1,355)**

Note: Numbers in brackets indicate savings in Income Tax.
Net WDV of Furniture on 31.12.2012 = 10,000 – 1,000 – 900 – 810 = 7,290

Question 5(b): Mutual Funds — N 12 (6 Marks)

Ramesh Goyal has invested in three mutual funds. From the details given below, find out effective yield on per annum basis in respect of each of the schemes to Ramesh Goyal upto 31.03.2012.

Mutual Fund	X	Y	Z
Date of Investment	01.12.2011	01.01.2012	01.03.2012
Amount of investment (₹)	1,00,000	2,00,000	1,00,000
NAV at the date of investment (₹)	10.50	10.00	10.00
Dividend receipt upto 31.03.2012 (₹)	1,900	3,000	Nil
NAV as on 31.03.2012 (₹)	10.40	10.10	9.80

Solution:

1. Computation of Net Value Added during the year ended 31.03.2012

Schemes	Opening NAV (₹)	NAV as at entry date	Units (No.)	NAV as at 31.03.2012 (₹)	Total NAV (₹)	Net NAV
(1)	**(2)**	**(3)**	**(4) = (2) ÷ (3)**	**(5)**	**(6) = (4) × (5)**	**(7) = (2) – (6)**
MF X	1,00,000	10.50	9,523.81	10.40	99,047.62	(–)952.38
MF Y	2,00,000	10.00	20,000	10.10	2,02,000	(+)2,000
MF Z	1,00,000	10.00	10,000	9.80	98,000	(–)2,000

2. Effective yield in %

- Total Yield = Net NAV + Dividend
- Effective Yield in % = $\frac{\text{Total Yield}}{\text{Opening NAV}} \times \frac{365}{\text{No. of days of holding}}$

Schemes	Dividend Received (₹)	Net NAV (₹)	Total Yield	No. of Days	Effective Yield % p.a.
MF X	1,900	(–)952.38	947.62	122	2.84%
MF Y	3,000	(+)2,000	5,000	91	10.03%
MF Z	Nil	(–)2,000	(–) 2,000	31	(23.55)%

Question 6(a): Capital Restructuring – Buy Back N 12 (8 Marks)

Kharid Ltd has the following Capital Structures as on 31.03.2011 –

Particulars	(₹ in Crores)	
Equity Share Capital (Shares of ₹ 10 each, fully paid)		660
Reserve and Surplus		
General Reserve	480	
Securities Premium Account	180	
Profit and Loss Account	180	
Infrastructure Development Reserve	360	1,200
Loan Funds		3,600

The Shareholders of Kharid Ltd have on the recommendation of their Board of Directors approved on 12.09.2011, a proposal to buy–back maximum permissible number of Equity Shares, considering the large surplus funds available at the disposal of the Company.

The prevailing Market Value of the Company's Shares is ₹ 25 per Share and in order to induce the existing Shareholders to offer their Shares for buy–back, it was decided to offer a price 20% over Market Value.

You are also informed that the Infrastructure Development Reserve is created to satisfy Income Tax requirements.

You are required to compute the Maximum Number of Shares that can be bought back in the light of the above information and also under a situation where the loan funds of the Company were either ₹ 2,400 Crores or ₹ 3,000 Crores.

Assuming that the entire buy–back is completed by 09.12.2011, show the Accounting Entries with full narrations in the Company's Books in each situation.

Solution: **Similar to Page 2.110, Q.No. 51, M 10**

1. Analysis of Companies Act Provisions

Rule 1: Percentage of Shares Bought Back = 25% of Shares Outstanding

- Since the buyback is approved by the Shareholders in their General Meeting, the maximum permissible percentage of Shares is 25% of the total shares outstanding i.e. 25% of 66 Crore Shares = **16.5 Crore Shares.**
- If the Buyback is as per Board Resolution only and not authorised by the Shareholders, the maximum buyback can be only 10%.

Rule 2: Distributable Assets = 25% of Assets representing Capital and Free Reserves

- Cash Available with the Co. = 25% of Paid Up Capital and Free Reserves including Securities Premium = 25% × (660 + 480 + 180 + 180) = 25% of 1,500 = ₹ 375 Crores.
- Offer Price for buyback = Market Price + 20% = ₹ 25 + 20% thereon = ₹ 30 per Share.
- Maximum Permissible Buyback = ₹ 375 Crores ÷ ₹ 30 per share = **12.5 Crore Shares.**

Rule 3: Debt Equity Ratio to be 2:1

Situation	I	II	III
(a) Desired Debt Equity Ratio after buy back	2:1	2:1	2:1
(b) Debt (given in the question)	3,600	2,400	3,000
(c) Equity to be maintained after Buyback = (b) ÷ 2	1,800	1,200	1,500
(d) Existing Equity (Share Capital + Free Reserves + Securities Premium)	1,500	1,500	1,500
(e) Permissible Dilution in Equity = (c) – (d)	Nil	300	Nil
(f) Buyback price as calculated above	30	30	30
(g) Maximum Permissible Buyback in Crores of Shares = (e) ÷ [(f) + FV]	Nil	300 ÷ [30 + 10] = 7.5	Nil

2. Summary of above for determining the Maximum Number of Shares that can be bought back

Particulars (in Crore Shares)	Situation I	Situation II	Situation III
(a) Rule 1: Percentage of Shares Bought Back	16.50	16.50	16.50
(b) Rule 2: Cash Availability	12.50	12.50	12.50
(c) Rule 3: Debt Equity Ratio to be 2:1	Nil	7.50	Nil
(d) **Maximum Permissible Buyback = Least of a, b, c**	Nil	7.50	Nil

3. Journal Entries in respect of Situation II is given below (₹ in Crores)

S.No	Particulars		Dr.	Cr.
1.	Equity Share Capital A/c (7.5 Crore Shares × ₹ 10)	Dr.	75.00	
	Securities Premium A/c	Dr.	150.00	
	To Equity Shareholders A/c			225.00
	(Being amount made due for share buy back vide resolution dated……, Share Capital cancelled and excess payment adjusted against Securities Premium)			
2.	Equity Shareholders A/c	Dr.	225.00	
	To Bank A/c			225.00
	(Being payment of amounts due under a scheme of buy back)			
3.	Securities Premium A/c	Dr.	30.00	
	General Reserve A/c	Dr.	45.00	
	To Capital Redemption Reserve A/c			75.00
	(Being transfer to Capital Redemption Reserve on account of Equity Shares being bought back)			

Question 6(b): Human Resource Accounting – Lev and Schwartz Model — N 12 (4 Marks)

From the following details, compute according to Lev and Schwartz (1971) Model, the value of Human Resources of Skilled Employees Group.

(i)	Annual Average Earning of an Employee till the retirement age	₹ 1,00,000
(ii)	Age of Retirement	65 years
(iii)	Discount Rate	15%
(iv)	No. of Employees in the group	20
(v)	Average Age	62 years

Solution:

Particulars	
(a) Average Annual Earning till retirement	₹ 1,00,000
(b) Annuity Factor for 3 years at 15%	2.2832
(c) No. of Employees	20
(d) Value of Human Resource of Skilled Employees group (a) × (b) × (c)	₹ 45,66,400

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

Question 6(c): N 12 (4 Marks)

H Ltd, engaged in the business of manufacturing Lotus Wine. The process of manufacturing this wine takes around 18 months. Due to this reason H Ltd, has prepared its Financial Statements considering its Operating Cycle as 18 months and accordingly classified the Raw Material purchased and held in stock for less than 18 months as Current Asset. Comment on the accuracy of the decision and the treatment of Asset by H Ltd as per Revised Schedule VI.

Solution:

1. **Definition of Operating Cycle as per Revised Schedule VI:** An Operating Cycle is the time difference between the acquisition of asset for processing and their realisation in cash and cash equivalents. Where the normal operating cycle cannot be defined, it is assumed to have duration of 12 months.
2. Operating Cycle should not be considered for each component i.e, Inventory or Debtors separately, but only for each business lines separately.
3. H Ltd has classified Raw Material as a Current Asset after ascertaining the Operating Cycle as 18 months.
4. In computation of Operating Cycle, only the processing time of Raw Material to Finished Goods has been considered.
5. Since the Operating Cycle computed by H Ltd does not consider Debtors Credit Period and the Credit period given by the Creditors, it is **not** in accordance with the Revised Schedule VI.

Question 7(a): Employee Share Based Payment N 12 (4 Marks)

Goodluck Limited grants 180 Share Options to each of its 690 employees. Each grant containing condition on the employees working for Goodluck Ltd over the next 4 years. Goodluck Ltd has estimated that the Fair Value Option is ₹ 15. Goodluck Ltd also estimated that 30% of employees will leave during four year period and hence forfeit their rights to the Share Option. If the above expectations are correct, what amount of expenses to be recognized during vesting period?

Solution:

Vesting Period	4 years
Total Number of Options Granted (Employees 690 × Options per Employee 180)	1,24,200
Fair Value per Option (Given)	₹ 15
Forfeiture Expected over the Vesting Period	30%
Total Number of Options Expected to Vest [1,24,200 × 70%]	86,940 Shares
Value of Options Expected to Vest at the end of Vesting Period = Fair Value [Options Expected to Vest × air Value per Option]	₹ 13,04,100
Amount to be expensed in Year 1 = 1/4th of Total Value of Options	₹ 3,26,025

Question 7(b): AS – 18 – Related Party Disclosures N 12 (4 Marks)

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?

Solution: Similar to Q No.17/Page 18.7 of Padhuka's Students' Referencer on Accounting Standards P(A/c)–N07

1. **Holding:** As per the holding structure given above, P Ltd has an economic interest of 26% in R Ltd. (Total Holding = Direct Holding of 14% + Indirect Holding through Q Ltd, i.e. 60% of 20% = 12%)
2. **Substantial Interest and Significant Influence:**
   (a) An Enterprise / Individual is considered to have a **substantial interest** in another enterprise, if that Enterprise / individual owns, directly or indirectly, 20% or more interest in the voting power of the enterprise.
   (b) When an investing party holds, directly or indirectly through intermediaries, 20% or more of the voting power, it is **presumed** that there is a **significant influence**, unless otherwise proved.
3. **Analysis:**
   (a) P Ltd is a majority Shareholder (60%) in Q Ltd. Thus P Ltd has control over Q Ltd.
   (b) Q Ltd holds 20% of Shares in R Ltd. So, Q Ltd has significant influence over R Ltd. [As per Point 2(a) and (b) above].
   (c) P Ltd and Q Ltd, together hold 14% + 20% = 34% of the Shares in R Ltd. So, P Ltd has **significant influence** over R Ltd. [As per Point 2(a) and (b) above].
4. **Conclusion:** P Ltd, Q Ltd and R Ltd are Related Parties. Hence, the disclosure requirements of AS – 18 are applicable in the above case.

Question 7(c): AS – 29 – Provisions, Contingent Liabilities & Contingent Assets N 12 (4 Marks)

An Oil Company has been contaminating Land for several years. It does not clean up because there is no legislation requiring cleaning up. At 31st March 2012, it is virtually certain that a law requiring a clean–up of land already contaminated will be enacted shortly after the year end. Is provisioning presently necessary?

Solution: Similar to Situation 5 / Page 29.19, of Padhuka's Students' Referencer on Accounting Standards

Analysis	Conclusion and Treatment
• **Present Obligation:** Obligating Event is the contamination of the land because of the virtual certainty of legislation requiring cleaning up. • **Outflow of Resources:** Probable. • **Estimate:** Best Estimate of the liability can be made.	Provision is recognised for the best estimate of the costs of the clean up (Para 14 and 21).

Question 7(d): Change in Accounting Policy N 12 (4 Marks)

Vijaya Ltd had to pay delayed Cotton Clearing Charges over and above the negotiated price for taking delayed delivery of cotton from the Supplier's Godown. Upto 2010–11, the Company has regularly included such charges in the valuation of Closing Stock. This charge, being in the nature of interest, the Company has decided to exclude it from Closing Stock valuation. This would result in decrease of Profit by ₹ 8.60 Lakhs.

What is the treatment in the Final Statement of Accounts for the year ended 31–03–2012? Also draft a suitable note for disclosure.

Solution: Similar to Q.No.20/Page 5.7, of Padhuka's Students' Referencer on Accounting Standards–F (A/c) M 95

1. **Principle:** Exclusion of interest in Stock Valuation is in line with AS – 2 and would result in more appropriate preparation of Financial Statements. Hence, change in accounting policy is permissible under AS – 5.

2. **Conclusion:** As per AS–2, the accounting policy adopted for valuation of inventories including the cost formulae used should be **disclosed** in the Financial Statements.

3. **Draft Disclosure Note:** Appropriate disclosure of the change and the amount by which any item in the Financial Statements is affected by such change, is necessary as per AS–1, AS–2 and AS – 5. Therefore, the under–mentioned note should be given in the Annual Accounts.

   "In compliance with the Accounting Standards issued by the ICAI, delayed Cotton Clearing Charges which are in the nature of interest have been excluded from the valuation of Closing Stock unlike preceding years. Had the Company continued the accounting practice followed earlier, the value of Closing Stock as well as Profit before Tax for the year would have been higher by ₹ 8.60 Lakhs".

   Alternative Disclosure Note: "To be in conformity with the Accounting Standard – 2 on Valuation of Inventories issued by ICAI, interest has been excluded from the valuation of Closing Stock unlike preceding years. Had the same principle of previous years been followed, Profit for the year and year–end Net Assets would have been higher by ₹ 8,60,000."

Question 7(e): Market Value Added N 12 (4 Marks)

Write short notes on "Market Value Added."

Solution: **Refer Page 5.27, Q.No.6**