

FINAL EXAMINATION

GROUP IV

(SYLLABUS 2008)

SUGGESTED ANSWERS TO QUESTIONS

JUNE 2011

Paper- 16 : ADVANCED FINANCIAL ACCOUNTING & REPORTING

Part A questions are compulsory. Attempt all of them.

Part B has seven questions. Attempt any five of them.

PART A (25 Marks)

Q.1. (a) In each of the cases given below, one out of four alternatives is correct. Indicate the correct answer (= 1 mark) and give your workings/reasons briefly (= 1 mark) :

(i) PRARTHANA LTD, a firm of contractors provides the following details for the year ended 31st March, 2011 :

Total Contract Price Rs. 1,000 lakhs, Work Certified Rs. 500 lakhs, Work not Certified Rs. 105 lakhs, Estimated further Cost to Completion Rs. 495 lakhs, Progress Payment : Received Rs. 400 lakhs, To be Received Rs. 140 lakhs.

Amount due to customers as per AS-7 will be :

- A. Rs. 100 lakhs
- B. Rs. 550 lakhs
- C. Rs. 35 lakhs
- D. None of these

- (ii) RAJASTHALI & CO. purchased fixed assets costing Rs. 3,000 lakhs on 1.4.2010 and the same was fully financed by foreign currency loan (U.S. Dollars) payable in three annual equal instalments. Exchange rates were 1 Dollar = Rs. 40.00 and Rs. 42.50 as on 1.4.2010 and 31.03.2011 respectively. First instalment was paid on 31.03.2011. As per AS-11 (Revised)
- Exchange Difference of Rs. 187.50 lakhs should be charged to P&L A/c.
 - Exchange Difference of Rs. 125 lakhs should be charged to P&L A/c.
 - Exchange Difference of Rs. 187.5 lakhs should be added to Fixed Assets A/c.
 - Exchange Difference of Rs. 125 lakhs should be added to Fixed Assets A/c.

- (iii) Mr. RAKESH BEHARI bought a forward contract for three months of US\$ 1,00,000 on 1st December at 1 US\$ = Rs. 47.10 when exchange rate was US\$ 1 = Rs. 47.11. On 31st December when he closed his books, exchange rate was US\$ 1 = Rs. 47.15. On 31st January, he decided to sell the contract at Rs. 47.18 per dollar. The profits from contract to be recognized in the P&L/c will be :

- A. Rs. 1,000
B. Rs. 5,000
C. Rs. 8,000
D. None of these

- (iv) BHARAT & TUSHAR LTD. obtained a loan from a bank for Rs. 50 lakhs on 30.04.2010. It was utilized as follows :

utilized as follows :

Construction of a shed Rs. 50 lakhs, Purchase of a machinery Rs. 40 lakhs, Working Capital Rs. 20 lakhs, Advance for purchase of truck Rs. 10 lakhs, Construction of shed was completed in March 2011. The machinery was installed on the same date. Delivery truck was not received. Total interest charged by the bank for the year ending 31.03.2011 was Rs. 18 lakhs. Interest to be debited to Profit & Loss Account will be :

- A. Rs. 18 lakhs
B. Rs. 10.5 lakhs
C. Rs. 4.5 lakhs
D. None of these

- (v) The Chief Accountant of PELF FIN STOCK Ltd. gives the following data regarding its six segments :

The Chief Accountant of PELF FIN STOCK Ltd. gives the following details:							
	Rs. in lakhs						
Particulars	M	N	O	P	Q	R	Total
Segment Assets	50	25	10	5	5	5	100
Segment Results	-50	-140	80	10	-10	10	-100
Segment Revenue	200	320	200	90	90	100	1000

Reportable Segments As per AS-17 are :

- A. M, N, O, P, Q, R
B. M, N, O, P, Q only
C. M, N, O, P only
D. M, N, O, R only

- (vi) X Ltd. holds 51% of Y Ltd., Y Ltd. holds 51% of W Ltd., Z Ltd. holds 49% of W Ltd.

Related Parties as per AS-18 are :

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

- (vii) S. S. SECURITIES LTD. provides the following information :

Net Profit for the current year Rs. 1,00,00,000, No. of equity shares outstanding 50,00,000, Basic earnings per share Rs. 2.00, No. of 12% convertible debentures of Rs. 100 each 1,00,000. Each debenture is convertible into 10 equity shares, Interest expense for the current year Rs. 12,00,000, Tax relating to interest expense (30%) Rs. 3,60,000. Diluted Earnings per share is :

- A. Rs. 1.67
- B. Rs. 1.87
- C. Rs. 1.81
- D. None of these

- (viii) M.S. GOYAL & A. JINDAL LTD. provides the following information:

Accounting Profit Rs. 6,00,000, Book Profit as per MAT Rs. 3,50,000, Profit as per Income Tax Act Rs. 60,000, Tax Rate 20%, MAT Rate 7.50%. Deferred Tax Asset/Liability as per AS-22 will be:

- A. Rs. 1,20,000 (DTL)
- B. Rs. 1,08,000 (DTL)
- C. Rs. 1,20,000 (DTA)
- D. Rs. 1,08,000 (DTA)

- (ix) A Ltd. had acquired 80% share in the B Ltd. for Rs. 25 lacs. The net assets of B Ltd. on the day are Rs. 22 lacs.

During the year A Ltd. sold the investment for Rs. 30 lacs and net assets of B Ltd. on the date of disposal was Rs. 35 lacs. The Profit or Loss on disposal of this investment to be recognised in consolidated financial statement is:

- A. Profit Rs. 5,00,000
- B. Profit Rs. 2,00,000
- C. Loss Rs. 9,40,000
- D. Loss Rs. 5,40,000

- (x) Accountants of NAVEEN ND Ltd. show a net profit of Rs. 7,20,000 for the third quarter of 2011 after incorporating the following :

- (i) Bad debts of Rs. 40,000 incurred during the quarter. 50% of the bad debts have been deferred to the next quarter.
- (ii) Extra ordinary loss of Rs. 35,000 incurred during the quarter has been fully recognized in this quarter.

(iii) Additional depreciation of Rs. 45,000 resulting from the change in the method of charge of depreciation.

The Correct Quarterly Income as per AS-25 is:

- A. Rs. 7,00,000
- B. Rs. 6,85,000
- C. Rs. 6,65,000
- D. None of these

[2×10=20]

[1×5=5]

(b) State any five Indian Accounting Standards which make use of Fair Value.

Answer 1. (a)

(i) C.
Amount due from/to customers = Contract costs + Recognised profit – Recognised losses – (Progress payments received + Progress payments to be received)

$$= [605 + \text{Nil} - 100 - (400 + 140)] \text{ Rs. in lakhs}$$

Amount due to customers = Rs. 35 lakhs

(ii) A.

$$\text{Foreign currency loan} = \frac{\text{Rs. 3,000 lakhs}}{\text{Rs. 40}} = 75 \text{ lakhs US Dollars}$$

$$\text{Exchange difference} = 75 \text{ lakhs US Dollars} \times (42.50 - 40.00) = \text{Rs. 187.50 lakhs}$$

(Including exchange Loss on payment of first instalment). To be charged to Profit & Loss account for the year.

(iii) C.

Sale Rate

Rs. 47.18

Less : Contract Rate

Rs. 47.10

Premium on Contract

Rs. 0.08

Contract Amount

US\$ 1,00,000

Total Profit (1,00,000 × 0.08)

Rs. 8,000

(iv) B.

Qualifying Asset as per AS-16 = Rs. 50 lakhs (construction of a shed)

Borrowing cost to be capitalized = $18 \times 50/120 = \text{Rs. 7.5 lakhs}$

Interest to be debited to Profit or Loss account = Rs. (18 – 7.5) lakhs = Rs. 10.5 lakhs

(v) D.

As per para 27 of AS-17 'Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if :

- (i) Its revenue from sales to external customers and from other transactions with other segments is 10% or more of the total revenue—external and internal of all segments; or
- M, N, O, R have at least 10% of Total Segment Revenue.

(ii) Its segment result whether profit or loss is 10% or more of :

(1) The combined result of all segments in profit; or

(2) The combined result of all segments in loss,
whichever is greater in absolute amount; or

M, N, O have at least 10% of Total Segment Result, (i.e. Rs. 200 lakhs)

(iii) Its segment assets are 10% or more of the total assets of all segments.

M, N, O have at least 10% of Total Segment Assets.

(vi) A.

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

(vii) C.

Adjusted net profit for the current year $(1,00,00,000 + 12,00,000 - 3,60,000) = \text{Rs. } 1,08,40,000$

No. of equity shares resulting from conversion of debentures : 10,00,000 Shares

No. of equity shares used to compute diluted EPS : $(50,00,000 + 10,00,000) = 60,00,000$ Shares

Diluted earnings per share : $(1,08,40,000 / 60,00,000) = \text{Rs. } 1.81$

(viii) B.

Tax as per accounting profit

$$6,00,000 \times 20\% = 1,20,000$$

Tax as per Income-tax Profit

$$60,000 \times 20\% = 12,000$$

Therefore, Deferred Tax liability as on 31-03-2011

$$= 1,20,000 - 12,000 = 1,08,000$$

(ix) D.

Proceeds from the sale of Investment

30,00,000

Less : A Ltd.'s share in net assets (35 lacs $\times$ 80%)

28,00,000

2,00,000

Less : Goodwill in the Consolidated Financial Statement

Cost of Investment

25,00,000

Less : A Ltd.'s Share in net asset on the date (22 lacs $\times$ 80%)

17,60,000

7,40,000

Loss on sale of Investment

5,40,000

(x) A.

Bad debts of Rs. 40,000 incurred during current quarter but deferred 50% (i.e. Rs. 20,000) to the next quarter should be deducted from Rs. 7,20,000.

Answer 1. (b)

AS-2, 10, 13, 15, 26, 28, 30, 31, 32 [Any Five]

PART B (75 Marks)

[5+5+5=15]

Q. 2. Answer any three of the following :

- (a) HEAVEN & HELL Ltd. is developing a new production process. During the financial year 31st March 2010, the total expenditure on this process was Rs. 40 lakhs. The production process met the criteria for recognition as an intangible asset on 1st Dec. 2009. Expenditure incurred till this date was Rs. 16 lakhs.

Further expenditure incurred on the process for the financial year ending 31st March 2011, was Rs. 70 lakhs. As at 31-3-2011, the recoverable amount of know-how embodied in the process is estimated to be Rs. 62 lakhs. This includes estimates of future cash outflows as well as inflows. You are required to work out :

- (i) What is the expenditure to be charged to the profit and loss account for the financial year ended 31 st March 2010? (Ignore depreciation for this purpose)
- (ii) What is the carrying amount of the intangible asset as at 31st March 2010?
- (iii) What is the expenditure to be charged to the profit and loss account for the financial year ended 31st March 2011? (Ignore depreciation for this purpose)
- (iv) What is the carrying amount of the intangible asset as at 31st March 2011?

- (b) LOVE & SACRIFICE LTD. gives the following estimates of cash flows relating to fixed asset on 31-12-2010.

The discount rate is 15%.

Year	2011	2012	2013	2014	2015
Cash Flow (Rs. in lakhs)	4000	6000	6000	8000	4000
Present Value Factors @ 15%	0.870	0.756	0.658	0.572	0.497

Residual value at the end of 2015 Rs. 1000 lakhs, Fixed Asset purchased on 1-1-2008 Rs. 40,000 lakhs, Useful life 8 years, Net selling price on 31-12-2010 Rs. 20,000 lakhs.

Calculate on 31-12-2010 :

- (a) Value in use on 31-12-2010
- (b) Carrying amount at the end of 2010
- (c) Recoverable amount on 31-12-2010
- (d) Impairment loss to be recognized for the year ended 31-12-2010
- (e) Revised carrying amount
- (f) Depreciation charge for 2011

- (c) At the end of the financial year ending on 31st March 2011, COUNSLE & CLIENT LTD. finds that there are twenty law suits outstanding which have not been settled till the date of approval of accounts by the Board of Directors. The possible outcome as estimated by the Board is as follows :

	Probability	Loss (Rs.)
In respect of five cases (Win)	100%	—
Next ten cases (Win)	60%	—
Lose (Low damages)	30%	1,20,000
Lose (High damages)	10%	2,00,000
Remaining five cases		
Win	50%	—
Lose (Low damages)	30%	1,00,000
Lose (High damages)	20%	2,10,000

Outcome of each case is to be taken as a separate entity. Ascertain the amount of contingent loss and the accounting treatment in respect thereof.

- (d) J Ltd. purchased machinery from K Ltd. on 30.09.2010. The price was Rs. 370.44 lakhs after charging 8% Sales-tax and giving a trade discount of 2% on the quoted price. Transport charges were 0.25% on the quoted price and installation charges come to 1 % on the quoted price. A loan of Rs. 300 lakhs was taken from the bank on which interest at 15% per annum was to be paid. Expenditure incurred on the trial run was Materials Rs. 35,000, Wages Rs. 25,000 and Overheads Rs. 15,000. Machinery was ready for use on 1.12.2010. However, it was actually put to use only on 1.5.2011. Find out the cost of the machine and suggest the accounting treatment for the expenses incurred in the interval between the dates 1.12.2010 to 1.5.2011. The entire loan amount remained unpaid on 1.5.2011.

- (e) FIRE & WATER LTD. provides the following information :

Net profit for the year 2009-2010	Rs. 11,00,000
Net profit for the year 2010-2011	Rs. 15,00,000
No. of shares outstanding prior to rights issue	5,00,000 shares
Rights Issue price	Rs.15.00
Last date to exercise rights	1st March 2011

Rights issue is one new share for each five outstanding (i.e. 1,00,000 new shares)

Fair value of one equity share immediately prior to exercise of rights on 1st March 2011 was Rs. 21.00. Compute Basic Earnings Per Share.

Answer 2. (a)

- (i) Rs. 16 lakhs
- (ii) Carrying amount as on 31-3-2010 will be expenditure incurred after 1-12-2009 = Rs. 24 lakhs
- (iii) Book cost of intangible asset as on 31-3-2011 is as follows
 Total Book cost = Rs. (70 + 24) lakhs = Rs. 94 lakhs
 Recoverable amount as estimated = Rs. 62 lakhs.
 Difference to be charged to Profit and Loss account = Rs. 32 lakhs
- (iv) Rs. 62 lakhs

Answer 2. (b)**(a) Calculation of value in use**

Year	Cash Flow	Discount as per 15%	Discounted cash flow
2011	4000	0.870	3480
2012	6000	0.756	4536
2013	6000	0.658	3948
2014	8000	0.572	4576
2015	4000	0.497	1988
2015	1000 (Residual Value)	0.497	497
		Value in use	19,025

- (b) Carrying Amount on 31-12-2010 = [Original cost – Depreciation till date]
 = Rs. 40,000 – [(40,000 – 1000) × 3/8] = Rs. 25,375
- (c) Recoverable Amount (being Higher of Value in use and Net Selling Price) = Rs. 20,000 lakhs
- (d) Impairment Loss [Carrying Amount – Recoverable Amount] = Rs. (25,375 – 20,000) = Rs. 5,375 lakhs
- (e) Revised carrying amount = Rs. (25,375 – 5,375) lakhs = Rs. 20,000 lakhs
- (f) Depreciation Charge for 2011 = (20,000 – 1000)/5 = Rs. 3,800

Answer 2. (c)

According to AS 29 'Provisions, Contingent Liabilities and Contingent Assets', contingent liability should be disclosed in the financial statements if following conditions are satisfied :

- (i) There is a present obligation arising out of past events but not recognized as provision.
- (ii) It is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation.
- (iii) The possibility of an outflow of resources embodying economic benefits is also remote.
- (iv) The amount of the obligation cannot be measured with sufficient reliability to be recognized as provision.

In this case, the probability of winning of first five cases is 100% and hence, question of providing for contingent loss does not arise. The probability of winning of next ten cases is 60% and for remaining five cases is 50%. As per AS 29, we make a provision if the loss is probable. As the loss does not appear to be probable and the possibility of an outflow of resources embodying economic benefits is not remote rather there is reasonable possibility of loss, therefore disclosure by way of note should be made. For the purpose of the disclosure of contingent liability by way of note, amount may be calculated as under :

Expected loss in next ten cases = 30% of Rs. 1,20,000 + 10% of Rs. 2,00,000 = Rs. 56,000.

Expected loss in remaining five cases = 30% of Rs. 1,00,000 + 20% of Rs. 2,10,000 = Rs. 72,000

To disclose contingent liability on the basis of maximum loss will be highly unrealistic. Therefore, the better approach will be to disclose the overall expected loss of Rs. 9,20,000 (Rs. 56,000 × 10 + Rs. 72,000 × 5) as contingent liability.

Answer 2. (d)

	Rs. (In lakhs)	Rs. (In lakhs)
Quoted price (refer to working note)	350.00	
Less : 2% Trade Discount	7.00	
	<u>343.00</u>	
Add : 8% Sales tax (8% × Rs. 343 lakhs)	27.44	370.44
Transport charges (0.25% × Rs. 350 lakhs)		0.88 (approx.)
Installation charges (1% × Rs. 350 lakhs)		3.50
Financing cost for the period from 30.9.2010 to 1.12.2010 (Rs. 300 lakhs × 15% × 2/12)		7.50
Trial Run Expenses :		
Material	0.35	
Wages	0.25	
Overheads	0.15	0.75
Total cost		<u>383.07</u>

Interest on loan for the period 1.12.2010 to 1.05.2011 = Rs. 300 lakhs × $\frac{15}{100} \times \frac{5}{12}$ = Rs. 18.75 lakhs

The expenditure may be charged to Profit and Loss Account or deferred for amortization between say three to five years. It has been assumed that no other expenses are incurred on the machine during this period.

Working Note :

Let the quoted price 'X'

Less : Trade Discount 0.02X.

Actual Price = 0.98X.

Sales Tax @ 8% = 1.08 × 0.98 X

or $X = \frac{\text{Rs. 370.44 lakhs}}{1.08 \times 0.98} = \text{Rs. 350 lakhs.}$

Answer 2. (e)

$$\frac{\text{Fair value of shares immediately prior to exercise of rights} + \text{Total amount received from exercise}}{\text{Number of shares outstanding prior to exercise} + \text{Number of shares issued in the exercise}}$$

$$\frac{(\text{Rs. } 21.00 \times 5,00,000 \text{ shares}) + (\text{Rs. } 15.00 \times 1,00,000 \text{ Shares})}{5,00,000 \text{ Shares} + 1,00,000 \text{ Shares}}$$

Theoretical ex-rights fair value per share = Rs. 20.00

Computation of adjustment factor :

$$\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex-rights value per share}}$$

$$\frac{\text{Rs. } 21.00}{\text{Rs. } 20.00} = 1.05$$

Computation of earnings per share :

EPS for the year 2009-2010 as originally reported : Rs. 11,00,000/5,00,000 shares = Rs. 2.20

EPS for the year 2009-2010 restated for rights issue : Rs. 11,00,000/(5,00,000 shares × 1.05) = Rs. 2.10

EPS for the year 2010-11 including effects of rights issue :

$$(5,00,000 \times 1.05 \times 2/12) + (6,00,000 \times 10/12) = 5,87,500 \text{ shares}$$

$$\text{EPS} = 15,00,000/5,87,500 = \text{Rs. } 2.55$$

Q. 3. (a) On 24th January 2011 NAVEEN JOSHI of Delhi sold goods to PEARSON of New York, U.S.A. for an invoice price of \$ 40,000 when the spot market rate was Rs. 44.20 per US \$. Payment was to be received after three months on 24th April 2011. To mitigate the risk of loss from decline in the exchange rate on the date of receipt of payment, NAVEEN JOSHI immediately acquired a forward contract to sell on 24th April 2011 US \$ 40,000 @ Rs. 43.70. NAVEEN JOSHI closed his books of account on 31st March 2011 when the spot rate was Rs. 43.20 per US \$. On 24th April 2011, the date of receipt of money by NAVEEN JOSHI, the spot rate was Rs. 42.70 per US \$.

Pass journal entries in the books of NAVEEN JOSHI to record the effect of all the above mentioned effects.

Or,

The following are the Balance Sheets of C Ltd. and D Ltd. as at 31st March, 2011 :

Liabilities	C Ltd. Rs.	D Ltd. Rs.	Assets	C Ltd. Rs.	D Ltd. Rs.
Equity Shares of Rs. 100 each fully paid	45,00,000	15,00,000	Fixed Assets	30,00,000	1,50,000
General Reserve	4,00,000	3,00,000	Investments		
Profit and Loss A/c	7,34,000	30,000	3,000 Shares in D Ltd.	4,50,000	
Current Liabilities	6,00,000	11,70,000	9,000 Shares in C Ltd.	—	15,00,000
			Current Assets	27,84,000	13,50,000
	62,34,000	30,00,000		62,34,000	30,00,000

C Ltd. absorbs D Ltd. on the basis of the intrinsic value of the shares of both companies as on 31st March 2011. Before absorption C Ltd. has declared a dividend of 12%. Dividend tax is 10%. Show the Calculation of Purchase consideration and the working for the number of shares issued.

- (b) SUN & MOON LTD. has its share capital divided into shares of Rs. 10 each. On 1st April 2009 it granted 10,000 employees' stock options at Rs. 40, when the market price was Rs. 130. The options were to be exercised between 16th December 2010 and 15th March 2011. The employees exercised their options for 9,500 shares only; the remaining options lapsed. The company closes its books on 31st March every year. Show Journal Entries. [10+5=15]

Answer 3. (a)

Journal Entries in the books of NAVEEN JOSHI

2011		Dr. (Rs.)	Cr. (Rs.)
Jan. 24	Pearson Account Dr.	17,68,000	
	To Sales Account (Credit sales made to Pearson, USA for \$40,000 recorded at spot market rate of Rs. 44.20 per US \$)		17,68,000
	Forward (Rs.) Contract Receivable Account Dr. Deferred Discount Account Dr. To Forward (\$) Contract Payable (Forward contract acquired to sell on 24th April, US \$ 40,000 @ Rs. 43.70)	17,48,000 20,000	17,68,000
March 31	Exchange Loss Account Dr. To Pearson Account (Record of exchange loss @ Re. 1 per \$ due to market rate becoming Rs. 43.20 per US \$ rather than Rs. 44.20 per US \$)	40,000	40,000
	Forward (\$) Contract Payable Dr. To Exchange Gain Account (Decrease in liability on forward contract due to fall in exchange rate)	40,000	40,000
	Discount Account Dr. To Deffered Discount Account (Record of proportionate discount expense for 66 days out of 90 days)	14,667	14,667
April 24	Bank Account Dr. Exchange Loss Account Dr. To Pearson Account (Receipt of \$40,000 from Pearson, USA customer @ Rs. 42.70 per US \$; exchange loss being Rs. 20,000)	17,08,000 20,000	17,28,000

Forward (\$) Contract Payable Account To Exchange Gain Account To Bank Account (Settlement of forward contract by payment of \$ 40,000)	Dr.	17,28,000	20,000 17,08,00
Bank Account To Forward (Rs.) Contract Receivable (Receipt of cash in settlement of forward contract receivable)	Dr.	17,48,000	17,48,000
Discount Account To Deferred Discount Account (Recording of discount expenses for 24 days : $\text{Rs. } 20,000 \times \frac{24 \text{ days}}{90 \text{ days}} = \text{Rs. } 5,333$)	Dr.	5,333	5,333

Or

(i) Computation of Net Assets excluding Inter-Company Investments

	C Ltd. Rs.	D Ltd. Rs.
A Total Assets		
Tangible Assets	57,84,000	15,00,000
Dividend Receivable	—	1,08,000
	<u>57,84,000</u>	<u>16,08,000</u>
B. External Liabilities		
Current Liabilities	6,00,000	2,70,000
Proposed Dividend	5,40,000	—
Dividend Tax	54,000	—
14% Debentures	—	9,00,000
	<u>11,94,000</u>	<u>11,70,000</u>
C. Net Assets (A – B)	<u>45,90,000</u>	<u>4,38,000</u>

(ii) Intrinsic value of equity shares.

Assume 'a' is the intrinsic value (net assets including inter company investments) of equity shares of C Ltd. and 'b' is the intrinsic value of equity shares of D Ltd.

$$a = \text{Rs. } 45,90,000 + \frac{1}{5} b \quad \dots (1)$$

$$b = \text{Rs. } 4,38,000 + \frac{1}{5} a \quad \dots (2)$$

$$\text{or, } b = \text{Rs. } 4,38,000 + \frac{1}{5} (45,90,000 + \frac{1}{5} \times b)$$

$$\text{or, } b = \text{Rs. } 4,38,000 + 9,18,000 + \frac{b}{25}$$

$$\text{or, } \frac{24}{25} \times b = \text{Rs. } 13,56,000$$

$$\text{or, } b = \text{Rs. } 13,56,000 \times \frac{25}{24} = \text{Rs. } 14,12,500$$

Putting the value of b in equation (1) we get,

$$a = \text{Rs. } 45,90,000 + (\text{Rs. } 14,12,500 \times \frac{1}{5}) = \text{Rs. } 48,72,500$$

Intrinsic value of share of C Ltd. = Rs. 48,72,500 / 45,000 = Rs. 108.278 App.

Intrinsic value of share of C Ltd. = Rs. 14,12,500 / 15,000 = Rs. 94.167 App.

(iii) Calculation of Purchase consideration

Value of shares held by outside shareholders in D Ltd. = Rs. 14,12,500 × 12,000 / 15,000 = Rs. 11,30,000

Shares to be issued by C Ltd. on the basis of intrinsic value
of shares = Rs. 11,30,000 × 45,000 / 48,72,500 =

Less : Shares held by D Ltd.

Number of shares to be issued

10,436.12

9,000.00

1,436.12

Total Purchase Price for outside shareholders

Additional shares in C Ltd. (1,436 × Rs. 108.278)

Cash for fractional shares (0.12 × Rs. 108.278)

Value of 3000 shares held by C Ltd.

Rs.

1,55,487*

13*

2,82,500

4,38,000

Answer 3. (b)

Journal Entries in the books of NAVEEN JOSHI

2009	Particulars	Dr. (Rs.)	Cr. (Rs.)
April 1	Employee Compensation Expense A/c Dr. To Employee Stock Options Outstanding A/c (Being grant of 10,000 stock options to employees at Rs. 40 when market price is Rs. 130)	9,00,000	9,00,000
2010 16th Dec. to 15th March	Bank A/c Dr. Employee stock options outstanding A/c Dr. To Equity share capital A/c To Securities premium A/c (Being allotment to employees of 9,500 equity share of Rs. 10 each at a premium of Rs. 120 per share in exercise of stock options by employees)	3,80,000 8,55,000	95,000 11,40,000
March 16	Employees stock option outstanding A/c Dr. To Employee compensation expenses A/c (Being entry for lapse of stock options for 500 shares)	45,000	45,000
March 31	Profit and Loss A/c Dr. To Employee compensation expenses A/c (Being transfer of employee compensation expenses to profit and loss account)	8,55,000	8,55,000

Q. 4. (a) Calculate the Minority Interest and Cost of Control from the following Balance Sheets of A Ltd. and B Ltd. as at 31st March 2011 :

Liabilities	A Ltd. Rs.	B Ltd. Rs.	Assets	A Ltd. Rs.	B Ltd. Rs.
Share Capital : (Rs. 100 each)	5,00,000	2,00,000	Investment : 1,600 shares in B Ltd.	2,20,000	—
Profits :			1,000 shares in A Ltd.	—	1,50,000
Capital profit	1,00,000	80,000	Sundry Assets	8,30,000	2,40,000
Revenue profit	3,00,000	50,000			
Creditors	1,50,000	60,000			
	10,50,000	3,90,000		10,50,000	3,90,000

(b) A Ltd. purchased 40% stake of B Ltd. for Rs. 12 per share. After two years A Ltd. decided to purchase another 40% share in B Ltd. B Ltd. has 1,00,00,000 equity shares of Rs. 10 each as fully paid up shares. The purchase deal was finalised on the following terms:

- Purchase price per share to be calculated on the basis of average profit of last three years capitalised at 7.5%. Profits for last three years are Rs. 35 lacs, Rs. 65 lacs and Rs. 89 lacs.
- Total assets of B Ltd. of Rs. 11,50,00,000. Assets to be appreciated by Rs. 40,00,000.
- Of the External Creditors for Rs. 2,50,00,000 one creditor to whom Rs. 10,00,000 was due has expired and nothing is to be paid to settle this liability.
- B Ltd. will declare dividend @ 15%.

Calculate the Goodwill or Capital Reserve for A Ltd. in Consolidated Financial Statement.

[9+6=15]

Answer 4. (a)

Suppose :

A = Revenue Profits of A Ltd., and

B = Revenue Profits of B Ltd.

Then,

$$A = 3,00,000 + \frac{4}{5} B$$

$$B = 50,000 + \frac{1}{5} A$$

$$B = 50,000 + \frac{1}{5} (3,00,000 + \frac{4}{5} B) \text{ [Substituting for A]}$$

$$B = 50,000 + 60,000 + \frac{4}{25} B$$

$$B = 1,10,000 + \frac{4}{25} B$$

$$25B = 27,50,000 + 4B$$

$$21B = 27,50,000$$

$$B = 1,30,952$$

Minority Interest in Revenue profits is $\frac{1}{5}$ of Rs. 1,30,952 or Rs. 26,190. Total revenue profit being Rs. 3,50,000 for A Ltd. and B Ltd. together, Rs. 3,23,810 remains for the group.

Capital Profits :

$$A = 1,00,000 + \frac{4}{5} B$$

$$B = 80,000 + \frac{1}{5} A$$

$$B = 80,000 + \frac{1}{5} (1,00,000 + \frac{4}{5} B)$$

$$B = 80,000 + 20,000 + \frac{4}{25} B$$

$$B = 1,00,000 + \frac{4}{25} B$$

$$25B = 25,00,000 + 4B$$

$$21B = 25,00,000$$

$$B = 1,19,048$$

Total Minority Interest :

	Rs.
Shares held by outsiders	40,000
Revenue Profit	26,190
Capital	<u>23,810</u>
	<u>90,000</u>

Cost of control :

Amount paid by both companies

3,70,000

Less : Face Value :

Rs.

Shares in B Ltd.

1,60,000

Shares in A Ltd.

1,00,000

Capital Profits (Rs. 1,19,048 – 23,810)

95,2383,55,23814,762

Cost of Control

Answer 4. (b)

Calculation of Purchase Consideration

Particulars	Rs.
Profits for Last 3 years : First	8,900,000
Second	6,500,000
Third	3,500,000
	<u>18,900,000</u>
Total profits for last 3 years	6,300,000
Average Profits (1,89,00,000/3)	84,000,000
Total value of B Ltd. (63,00,000/7.5%)	10,00,000
Number of Shares in B Ltd.	8.40
Value per Share	33,600,000
Purchase Consideration (1,00,00,000 × 40%) × 8.4	

Calculation of Goodwill/Capital Reserve

Particulars	Rs.	Rs.
Fixed Assets	115,000,000	
Add : Appreciation in value of the asset	4,000,000	119,000,000
Less : Creditors	25,000,000	
Less : Amount to be written off	1,000,000	24,000,000
Net Assets		95,000,000
Share in Net Assets (9,50,00,000 × 80%)		76,000,000
Less : Cost of Investment : Purchase Consideration	33,600,000	
Less : Dividend Received (10,00,00,000 × 40% × 15%)	6,000,000	
	27,600,000	
Add : Investment (1,00,00,000 × 40% × 12)	48,000,000	75,600,000
Capital Reserve		400,000

Q. 5. (a) A Ltd. acquired 25% of shares in B Ltd. as on 31.3.2010 for Rs. 3 lakhs. The Balance Sheet of B Ltd. as on 31.3.2010 is given below :

	Rs.
Share Capital	5,00,000
Reserves and Surplus	5,00,000
	10,00,000
Fixed Assets	5,00,000
Investments	2,00,000
Current Assets	3,00,000
	10,00,000

During the year ended 31.3.2011 the following are additional information available :

- A Ltd. received dividend from B Ltd., for the year ended 31.3.2011 at 40% from the Reserves.
- B Ltd., made a profit after tax of Rs. 7 lakhs for the year ended 31.3.2011.
- B Ltd., declared a dividend @ 50% for the year ended 31.3.2011 on 30.4.2011.

A Ltd. is preparing Consolidated Financial Statements in accordance with AS-21 for its various subsidiaries.

Calculate :

- Goodwill if any on acquisition of B Ltd.'s shares.
- How A Ltd., will reflect the value of investment in B Ltd., in the Consolidated Financial Statements?
- How the dividend received from B Ltd. will be shown in the Consolidated Financial Statements?

- (b) A Ltd. entered into a joint venture with B Ltd. on 1 : 1 basis and a new company C Ltd. was formed for the same purpose and following are the balance sheets of all the three companies as at 31st March 2011 :

Particulars	A Ltd	B Ltd	C Ltd
Share Capital	10,00,000	7,50,000	5,00,000
Reserve & Surplus	18,00,000	16,00,000	12,00,000
Loans	3,00,000	4,00,000	2,00,000
Current Liabilities	4,00,000	2,50,000	1,00,000
Fixed Assets	30,50,000	26,25,000	19,50,000
Investment in JV	2,50,000	2,50,000	—
Current Assets	2,00,000	125,000	50,000

Prepare the Balance Sheet of A Ltd., B Ltd. and C Ltd. under proportionate consolidation method.
[9+6=15]

Answer 5. (a)

In terms of AS 23 B Ltd. will be considered as an associate company of A Ltd. as shares acquired represent to more than 20%.

- (i) Calculation of Goodwill

Cost of Investment

Rs. in lakhs

3.00

Less : Share in the value of Equity of B. Ltd.

as at the date of investment

[25% of Rs. 10 lakhs (Rs. 5 lakhs + Rs. 5 lakhs)]

2.50

Goodwill

0.50

- (ii) A Ltd.

Consolidated Profit and Loss Account for the year ended 31st March, 2011

Rs. in lakhs

	By Share of profits in B Ltd.	1.75
	By Dividend received from B Ltd.	0.50
	Transfer to investment A/c	<u>0.50</u>
		Nil

- (iii) A Ltd.

Consolidated Balance Sheet as on 31.3.2011

Rs. in lakhs

	Investment in B Ltd.	
	Share in B Ltd.'s Equity	2.50
	Less : Dividend received	<u>0.50</u>
		2.00
	Share of Profit for year 2010-11	<u>1.75</u>
		3.75
	Add : Goodwill	<u>0.50</u>
		4.25

Working Notes :

1. Dividend received from B Ltd. amounting to Rs. 0.50 lakhs will be reduced from investment value in the books of A Ltd. However goodwill will not change.
2. B Ltd. made a profit of Rs. 7 lakhs for the year ended 31st March, 2011. A Ltd.'s share in the profits of Rs. 7 lakhs is Rs. 1.75 lakhs. Investment in B Ltd. will be increased by Rs. 1.75 lakhs and consolidated profit and loss account of A Ltd. will be credited with Rs. 1.75 lakhs in the consolidated financial statement of A Ltd.
3. Dividend declared on 30th April, 2011 will not be recognised in the consolidated financial statement of A Ltd.

Answer 5. (b)

Balance Sheet of A Ltd. as at 31st March, 2011 :

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
Share Capital :		1,000,000	Fixed Assets :		
Reserve & Surplus :			A Ltd.	3,050,000	
A Ltd.	1,800,000		C Ltd.	975,000	4,025,000
C Ltd.	600,000	2,400,000			
Loans :			Current Assets :		
A Ltd.	300,000		A Ltd.	200,000	
C Ltd.	100,000	400,000	C Ltd.	25,000	225,000
Current Liabilities :					
A Ltd.	400,000				
C Ltd.	50,000	450,000			
		4,250,000			4,250,000

Balance Sheet of B Ltd. as at 31st March, 2011 :

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
Share Capital :		750,000	Fixed Assets :		
Reserve & Surplus :			B Ltd.	2,625,000	
B Ltd.	1,600,000		C Ltd.	975,000	3,600,000
C Ltd.	600,000	2,200,000			
Loans :			Current Assets :		
B Ltd.	400,000		B Ltd.	125,000	
C Ltd.	100,000	500,000	C Ltd.	25,000	150,000
Current Liabilities :					
B Ltd.	250,000				
C Ltd.	50,000	300,000			
		3,750,000			3,750,000

[5+5+5=15]

Q. 6. Answer any three of the following :

- (a) At the beginning of year 1, DONOR & BEGGER LTD. issued 20,000 Convertible Debentures with face value Rs. 100 per debenture, at par. The debentures have six-year term. The interest at annual rate of 9% is paid half-yearly. The bondholders have an option to convert half of the face value of debentures into 2 ordinary shares at the end of year 3. The bondholders not exercising the conversion option will be repaid at par to the extent of Rs. 50 per debenture at the end of year 3. The non-convertible portion will be repaid at 10% premium at the end of year 6. At the time of issue, the prevailing market interest rate for similar debt without conversion option was 10%.

Compute the Value of Embedded Derivative.

Years	1-3	3-6	1-6	7-12
Annuity Factors @ 10%	2.487	1.868	4.355	2.459
Annuity Factors @ 5%	2.723	2.353	5.076	3.787

Present Value Factors @ 10%/5% at the end of 6th year and 12th year respectively are 0.564 and 0.557.

- (b) RICH & POOR LTD. issued certain callable convertible debentures at Rs. 60. The value of similar debentures without call or equity conversion option is Rs. 57. The value of call as determined using Black and Scholes model for option pricing is Rs. 2. Determine values of liability and equity component.
- (c) On April 1, 2010, BORROWER LTD. borrowed Rs. 10 lakh at annual fixed interest rate of 7% payable half-yearly. The life of the loan is 4 years with no pre-payment permitted. The company expected the interest rate to fall and on the same day, it entered into an interest rate swap arrangement, whereby the company would pay 6 month LIBOR and would receive annual fixed interest of 7% every half-year. The swap effectively converted the company's fixed rate obligation to floating rate obligation.

The following value of swap and debt are available :

	Value of swap Rs. lakh	Value of debt Rs. lakh
April 1, 2010	+ 0.2	10.2
March 31, 2011	- 0.1	9.9

Six-month LIBOR on April 1, 2010 was 6% and that on October 1, 2011 was 8%.

Show important accounting entries in respect of the swap arrangement.

- (d) As on 1st April 2010 the fair value of plan assets was Rs. 1,00,000 in respect of a pension plan of BHC out benefits of Rs. 19,000 and received inward contributions of Rs. 49,000. On 31st March 2011 the fair value of the defined benefit obligation was Rs. 1,47,920. Actuarial losses on the obligations for the year 2010-11 were :

On 1st April 2010 the company made the following estimates, based on its market studies, understanding and prevailing prices.

	%
Interest and dividend income, after tax payable by the fund	9.25
Realized and unrealized gains on plan assets (after tax)	2.00
Fund administrative costs	(1.00)
Expected Rate of Return	10.25

You are required to find the Expected and Actual Returns on Plan Assets and Actuarial Gain/Loss for the year 2010-11.

Answer 6. (a)

Half-year	Cash Flow Rs. 000	DF (5%)	PV Rs. 000
1 - 6	90	5.076	456.84
7 - 12	45	3.787	170.41
12	1,100	0.557	612.70
Value of host (Liability component)			1,239.95
Value of embedded derivative (Equity component) (Balancing Figure)			760.05
Issue proceeds			2,000.00

Answer 6. (b)

A callable bond is one that gives the issuer a right to buy the bond from the bondholders at a specified price. This feature in effect is a call option written by the bondholder. The option premium (value of call) is payable by the issuer.

Liability component (disregarding the call) = Rs. 57

Value of call payable by issuer = Rs. 2

Liability component = Rs. 57 – Rs. 2 = Rs. 55

Equity component = Rs. 60 – Rs. 55 = Rs. 5

used to hedge fair value of fixed-rate debt. This is a case of fair value hedge.

Books of BORROWER LTD

	Dr. (Rs. lakhs)	Cr. (Rs. lakhs)	
Interest A/c To Cash A/c (Interest on fund borrowed for first half-year 2010-11)	0.35	0.35	$[10 \times 7\% \times 6/12]$
Loss on valuation of debt A/c To Loan A/c (Increase in value of debt recognised)	0.20	0.20	$[10.2 - 10]$
Swap Hedge A/c To Gain on Swap Hedge A/c (Increase in value of swap recognised)	0.20	0.20	
Cash A/c To Interest A/c (Swap settlement received for first half-year 2010-11)	0.05	0.05	$[10 (7\% - 6\%) \times 6/12]$
Interest A/c To Cash A/c (Interest on fund borrowed for second half-year 2010-11)	0.35	0.35	$[10 \times 7\% \times 6/12]$
Loan A/c To Gain on valuation of debt A/c (Decrease in value of debt recognised)	0.30	0.30	$[10.2 - 9.9]$
Loss on Swap Hedge A/c To Swap Hedge A/c (Cumulative loss on swap recognised)	0.30	0.30	$[0.2 - (-0.1)]$
Interest A/c To Cash A/c (Swap settlement paid for second half-year 2010-11)	0.05	0.05	$[10 (8\% - 7\%) \times 6/12]$

Answer 6. (d)

	Rs.
A. Closing Balance of Fair Value of Plan Assets	1,50,000
B. Add : Benefits Paid	19,000
C. Less : Contributions Received	(49,000)
D. Less : Opening Balance of Fair Value of Plan Assets	(1,00,000)
E. Actual Return on Plan Assets	20,000

A. Return on Opening Balance of Fair Value of Plan Assets [Rs. 1,00,000 × 10.25% × 12/12]	Rs. 10,250
B. Return on Net Contributions Received [Contributions - Benefits Paid] [(Rs. 49,000 - Rs. 19,000) × 5%]	Rs. 1,500
C. Expected Return on Plan Assets	Rs. 11,750

Note : Equivalent Half Yearly Compounding Interest Rate = $\sqrt{(1 + \text{EXPECTED RATE OF RETURN})} - 1$
 $= \sqrt{(1 + .1025)} - 1 = .05 \text{ or } 5\%$

Acturial Gain = Actual Return on Plan Assets - Expected Return on Plan Assets
 = Rs. 20,000 - Rs. 11,750 = Rs. 8,250

Q. 7. (a) A Ltd. Leased a machinery to B Ltd. on the following terms :

Fair value of the machinery Rs. 20 lakhs, Lease term 5 years, Lease Rental per annum Rs. 5 lakhs, Guaranteed Residual value Rs. 1 lakh, Expected Residual value Rs. 2 lakhs, Internal Rate of Return 15%.

Depreciation is provided on straight line method @ 10% per annum. Ascertain unearned financial income and necessary entries may be passed in the books of the Lessee in the First year.

Or,

The Balance Sheet of HARD LUCK Ltd. on 31st March, 2011 is as under :

Liabilities	Rs.	Assets	Rs.
Authorised, Issued Equity Share Capital 20,000 shares of Rs. 100 each	20,00,000	Goodwill	2,00,000
10,000, 7% Preference Shares of 100 each	10,00,000	Plant and Machinery	18,00,000
Sundry Creditors	7,00,000	Stock	3,00,000
Bank Overdraft	3,00,000	Debtors	7,50,000
		Preliminary Expenses	1,00,000
		Cash	1,50,000
		Profit and Loss Account	7,00,000
	40,00,000		40,00,000

The dividends are in arrears. The company had bad time during the last two years or better business in future, earning profit and paying dividend provided the dividends are reduced.

A reconstruction scheme as follows was agreed to by all concerned :

Debtors agreed to forego 50% of the claim.

Preference shareholders withdrew arrear dividend claim. They also agreed to lower their capital claim by 20% by reducing nominal value in consideration of 9% dividend effective after reorganization in case equity shareholders' loss exceed 50% on the application of the scheme.

- (iii) Bank agreed to convert overdraft into term loan to the extent required for making current ratio equal to 2 : 1.
- (iv) Revalued figure for plant and machinery was accepted as Rs. 15,00,000.
- (v) Debtors to the extent of Rs. 4,00,000 were considered goods.
- (vi) Equity shares shall be exchanged for the same number of equity shares at a revised denomination as required after the reorganisation.

Show :

- (a) Total loss to be borne by the equity and preference shareholders for the reorganization;
- (b) Share of loss to the individual classes of shareholders;
- (c) New structure of share capital after reorganization;
- (d) Working capital of the reorganized Company.

- (b) Prepare a Gross Value Added Statement from the following Profit and Loss Account of STRONG and WEEK Ltd. Show also the reconciliation between Gross Value Added and Profit before Taxation :

Profit and Loss Account for the year ended 31st March 2011

Income	Notes	Amount	
		(Rs. in lakhs)	(Rs. in lakhs)
Sales		610	
Other Income		<u>25</u>	
			635
Expenditure			
Production and Operational Expenses	1	465	
Administration Expenses	2	19	
Interest and Other Charges	3	27	
Depreciation		<u>14</u>	<u>525</u>
Profit before Taxes			110
Provision for Taxes			<u>16</u>
			94
Balance as per Last Balance Sheet			<u>7</u>
			<u>101</u>

Transferred to :

General Reserve	60	
Proposed Dividend	<u>11</u>	71
Surplus Carried to Balance Sheet		<u>30</u>
		<u>101</u>

Notes :

1. Production and Operational Expenses	(Rs. in lakhs)
Increase in Stock	112
Consumption of Raw Materials	185
Consumps of Stores	22
Salaries, Wages, Bonus and Other Benefits	41
Cess and Local Taxes	11
Other Manufacturing Expenses	<u>94</u>
	<u>465</u>
2. Administration expenses include <i>inter-alia</i> audit fees of Rs. 4.8 lakhs, salaries and commission to directors Rs. 5 lakhs and provisions for doubtful debts Rs. 5.20 lakhs.	
	(Rs. in lakhs)
3. Interest and Other Charges :	
On Working Capital Loans from Bank	8
On Fixed Loans from IDBI	12
Debentures	<u>7</u>
	<u>27</u>
	[9+6=15]

Answer 7. (a)

Computation of Unearned Finance Income

As per AS 19 on Leases, *unearned finance income* is the difference between (a) the *gross investment* in the lease and (b) the present value of minimum lease payments under a finance lease from the standpoint of the lessor; and any unguaranteed residual value accruing to the lessor, at the interest rate implicit in the lease.

where :

- (a) **Gross Investment** in the lease is the aggregate of (i) minimum lease payments from the stand point of the lessor and (ii) any unguaranteed residual value accruing to the lessor.

Gross Investment = Minimum lease payment + Unguaranteed residual value

= (Total lease rent + Guaranteed residual value) + Unguaranteed residual value

= [(Rs. 5,00,000 × 5 years) + Rs. 1,00,000] + Rs. 1,00,000

= Rs. 27,00,000 (a)

ent value of (i) Minimum lease payments (MLP) and (ii) Unguaranteed residual

	MLP inclusive of URV Rs.	Internal rate of return (Discount factor 15%)	Present Value Rs.	
1	5,00,000	0.8696	4,34,800	
2	5,00,000	0.7561	3,78,050	
3	5,00,000	0.6575	3,28,750	
4	5,00,000	0.5718	2,85,900	
5	5,00,000	0.4972	2,48,600	
	1,00,000	0.4972	49,720	
	(guaranteed residual value)		17,25,820	(i)
	1,00,000	0.4972	49,720	(ii)
	(unguaranteed residual value)	(i) + (ii)	17,75,540	(b)

$$\begin{aligned}
 \text{Unearned Finance Income} &= (a) - (b) \\
 &= \text{Rs. } 27,00,000 - \text{Rs. } 17,75,540 \\
 &= \text{Rs. } 9,24,460
 \end{aligned}$$

Journal Entries in the books of B Ltd.

		Rs.	Rs.
At the inception of lease			
Machinery account	Dr.	17,25,820*	
To A Ltd.'s account			17,25,820*
(Being lease of machinery recorded at present value of MLP)			
At the end of the first year of lease			
Finance charges account (Refer Working Note)	Dr.	2,58,873	
To A Ltd.'s account			2,58,873
(Being the finance charges for first year due)			
A Ltd.'s account	Dr.	5,00,000	
To Bank account			5,00,000
(Being the lease rent paid to the lessor which includes outstanding liability of Rs. 2,41,127 and finance charge of Rs. 2,58,873)			

Depreciation account To Machinery account (Being the depreciation provided @ 10% p.a. on straight line method)	Dr.	1,72,582	1,72,582
Profit and loss account To Depreciation account To Finance charges account (Being the depreciation and finance charges transferred to profit and loss account)	Dr.	4,31,455	1,72,582 2,58,873

Working Note :

Table showing apportionment of lease payments by B. Ltd. between the finance charges and the reduction of outstanding liability.

Year	Outstanding liability (opening balance)	Lease rent	Finance charge	Reduction in outstanding liability	Outstanding liability (closing balance)
	Rs.	Rs.	Rs.	Rs.	Rs.
1	17,25,820	5,00,000	2,58,873	2,41,127	14,84,693
2	14,84,693	5,00,000	2,22,704	2,77,296	12,07,397
3	12,07,397	5,00,000	1,81,110	3,18,890	8,88,507
4	8,88,507	5,00,000	1,33,276	3,66,724	5,21,783
5	5,21,783	5,00,000	78,267	5,21,783	1,00,050*
			<u>8,74,230</u>	<u>17,25,820</u>	

- * The difference between this figure and guaranteed residual value (Rs. 1,00,000) is due to approximation in computing the interest rate implicit in the lease.

Answer 7. (a) Or

(a) Loss to be born by Equity and Preference Shareholders	
Profit and loss account (debit balance)	7,00,000
Preliminary expenses	1,00,000
Goodwill	2,00,000
Plant and machinery (Rs. 18,00,000 – Rs. 15,00,000)	3,00,000
Debtors (Rs. 7,50,000 – Rs. 4,00,000)	<u>3,50,000</u>
Amount to be written off	16,50,000
Less : 50% of sundry creditors	<u>3,50,000</u>
Total loss to be borne by the equity and preference shareholders	<u>13,00,000</u>

Note : Two years' preference dividend (arrears) have been ignored in the computation of loss to be borne by equity and preference shareholders.

(b) Share of loss to preference shareholders and equity shareholders

Total loss of Rs. 13,00,000 being more than 50% of equity share capital i.e. Rs. 10,00,000.

Preference shareholders' share of loss = 20% of Rs. 10,00,000 = Rs. 2,00,000

Equity shareholders' share of loss (Rs. 13,00,000 – Rs. 2,00,000) = Rs. 11,00,000

Total loss = Rs. 13,00,000

(c) New structure of share capital after reorganisation

Equity shares :

20,000 equity shares of Rs. 45 each, fully paid up

(Rs. 20,00,000 – Rs. 11,00,000)

Preference shares :

10,000, 9% preference shares of Rs. 80 each, fully paid up

(Rs. 10,00,000 – Rs. 2,00,000)

Rs.

9,00,000

8,00,000

17,00,000

Rs.

Rs.

(d) Working capital of the reorganized company

Current Assets :

Stock

Debtors

Cash

3,00,000

4,00,000

1,50,000

8,50,000

Less : Current Liabilities :

Creditors

Bank overdraft**

Working capital

3,50,000

75,000

4,25,000

4,25,000

Note : Current ratio shall be 2 : 1, i.e. total current liabilities shall be 50% of Rs. 8,50,000 (i.e. Rs. 3,00,000 + 4,00,000 + 1,50,000) = Rs. 4,25,000. Therefore, Bank overdraft = Rs. 75,000 (Rs. 4,25,000 less creditors Rs. 3,50,000).

Answer 7. (b)

STRONG & WEEK LTD.**Value Added Statement for the year ended 31st March, 2011**

	Rs. in lakhs	Rs. in lakhs	%
Sales		610	
Less : Cost of bought-in material and services :	413		
Production and operational expenses	14		
Administration expenses	8	435	
Interest on working capital loans		175	
Value added by manufacturing and trading activities		25	
Add : Other income		200	
Total Value Added			

Application of Value Added :

To Pay Employees :			
Salaries, Wages, Bonus and Other Benefits		41	20.50
To Pay Directors :			
Salaries and Commission		5	2.50
To Pay Government :			
Cess and Local Taxes	11		
Income Tax	<u>16</u>		
		27	13.50
To Pay Providers of Capital :			
Interest on Debentures	7		
Interest on Fixed Loans	<u>12</u>		
Dividend	<u>11</u>		
		30	15.00
To Provide for Maintenance and Expansion of the Company :			
Depreciation	14		
General Reserve	<u>60</u>		
Retained Profit (30 – 7)	<u>23</u>		
		<u>97</u>	<u>48.50</u>
		<u>200</u>	<u>100.00</u>

Reconciliation Between Total Value Added And Profit Before Taxation :

	Rs. in lakhs	Rs. in lakhs
Profit before Tax		110
Add back :		
Depreciation	14	
Salaries, Wages, Bonus and other Benefits	41	
Directors' Remuneration	5	
Cess and Local Taxes	11	
Interest on Debentures	7	
Interest on Fixed Loans	<u>12</u>	
Total Value Added		<u>90</u>
		<u>200</u>

Q. 8. Answer any three of the following :

[3×5=15]

- (a) State the criteria of Reportable Segment as per AS-17.
- (b) Briefly describe the Role of Public Accounts Committee.
- (c) Write a short note on Environmental Accounting.
- (d) Write a short note on Human Resource Accounting.
- (e) Compare the following items as per Indian AS and IFRS :
 - (i) Impairment of Assets
 - (ii) Business Combination.

Answer 8. (a)

As per para 27 of AS 17 'Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if :

- (i) Its revenue from sales to external customers and from other transactions with other segments is 10% or more of the total revenue-external and internal of all segments; or
- (ii) Its segment result whether profit or loss is 10% or more of;
 - (1) The combined result of all segments in profit; or
 - (2) The combined result of all segments in loss, whichever is greater in absolute amount; or
- (iii) Its segment assets are 10% or more of the total assets of all segments.

If the total external revenue attributable to reportable segments constitutes less than 75% of total enterprise revenue, additional segments should be identified as reportable segments even if they do not meet the 10% thresholds until at least 75% of total enterprise revenue is included in reportable segments.

Answer 8. (b)**Role of Public Accounts Committee :**

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

1. Examining the Government financial documents; and
2. Considering the reports of the Auditor-General.

A significant amount of the Committee's Work involves following up matter raised in the reports to Parliament by the Auditor-General. This ensures that public sector financial issues are securities for the benefit of Parliament and the public. While scrutinising the Appropriation Accounts of the Government of India and the Reports of the Controller and Auditor General thereon, it is the duty of the Committee to satisfy itself ;

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

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

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

Answer 8. (c)

The term 'environment' includes everything in all its manifest forms, on the earth, beneath the earth and above the earth. A business enterprise takes support of social and ecological system in order to maximize wealth. Economic activity, social welfare and a diverse environment, all are linked and ultimately depend on each other. The functioning of an enterprise may have some favourable and some adverse effects on the environment. Hence, it is felt that there is a need for maintaining accounts of the effects of activities of business entity on the environment. Environmental accounting can be defined as a system (methodology) for measuring environmental performance and communicating the results of these measurements to users. It helps in presenting the utilization of natural resources by an enterprise, the costs incurred to use them and the income earned therefrom in a transparent manner. Environmental accounting, entirely a new concept, is a faithful attempt to identify the resources exhausted and the costs rendered reciprocally to the enterprise by a business corporation. Thus environmental accounting stands for recording and documenting environmental performance to facilitate effectiveness of environmental management system with reference to compliance, safety and quality control. It provides a data base for taking corrective steps and future action for developing organisation's environmental strategy and for identifying environmentally based opportunities for gaining an edge over one's competitors. If proper environmental accounting system is established, the enterprise will be able to anticipate environmental damage and therefore can prevent it from happening.

Of course environmental accounting is still in an early stage of evolution and it is being groomed under the voluntary leadership of a variety of enterprises around the world. Recognising the importance of protecting and preserving the environment, a number of laws have been enacted throughout the world.

Answer 8. (d)

Human Resources Accounting (HRA) is an attempt to identify, quantify and report investment made in human resources of an organization. Leading public sector units like OIL, BHEL, NTPC and SAIL etc. have started reporting human resources in their annual reports as additional information. Although human being are considered as the prime mover for achieving productivity, and are placed above technology, equipment and money, the conventional accounting practice does not assign significance to the human resource. Human resources are not thus recognized as 'assets' in the Balance Sheet. While investments in human resources are not considered as assets and not amortised over the economic service life, the result is that the income and expenditure statement comprising current revenue and expenditure gives a distorted picture of the real affairs of the organization.

Accountants have been severely criticized by the Behavioural Scientists for their failure to value human resources, as this has come out as a handicap for effective management.

Human resource accounting provides scope for planning and decision making in relation to proper manpower planning. Also, such accounting can bring out the effect of various new rules, procedures and incentives relating to work force, and in turn, can act as an eye opener for modifications of existing statutes and laws.

Answer 8. (e)

	Indian AS	IFRS
(i) Impairment of Assets	Assets are impaired if Recoverable Amount is less than the carrying Amount. Recoverable Amount will be calculated as higher of net selling price and value in used based on discounted cashflows. Impairment test is to be conducted every year and if there is upward increase in the value of asset, then reversal of impairment losses is required in certain circumstances. Assets are not separately classified or disclosed as held for sale on the face of the balance sheet.	Similar to Indian AS However, assets are classified and disclosed separately on the face of the balance sheet as held for sale or disposal.
(ii) Business Combinations	No particular standard has been issued by ICAI till date. However, all business acquisitions are business combinations except pooling of interest method for certain amalgamations.	All business acquisitions are business combinations as per IFRS 3.