Test Series : February, 2012

MOCK TEST PAPER – 1

FINAL COURSE: GROUP – I

PAPER – 1: FINANCIAL REPORTING

Question No. 1 is compulsory.

Attempt any ***five*** *questions from the remaining* ***six*** *Questions.*

Working notes should form part of the answer.

Wherever necessary, suitable assumptions may be made by the candidates.

Time Allowed – 3 Hours — Maximum Marks – 100

1. (a) VX Limited began construction of a new plant on 1st April, 2010 and obtained a special loan of ₹ 4,00,000 to finance the construction of the plant. The rate of interest on loan was 10%.

The expenditure that was made on the project of plant is as follows:

	₹
1st April, 2010	5,00,000
1st August, 2010	12,00,000
1st January, 2011	2,00,000

The company's other outstanding non-specific loan was ₹ 23,00,000 at an interest rate of 12%. The construction of the plant completed on 31st March, 2011. You are required to calculate the amount of interest to be capitalized as per the provisions of AS-16 "Borrowing Cost".

(b) A limited company created a provision for bad and doubtful debts at 2.5% on debtors in preparing the financial statements for the year 2011-2012.

Subsequently on a review of the credit period allowed and financial capacity of the customers, the company decided to increase the provision to 8% on debtors as on 31.3.2012. The accounts were not approved by the Board of Directors till the date of decision. While applying the relevant accounting standard can this revision be considered as an extraordinary item or prior-period item?

(c) Shyam Ltd. based in India has branches in London. The Vice-President (Accounts) is of the opinion that the net exchange difference of ₹ 20 lakhs on the translation of items in financial statements of London Branches should be credited to the Profit and Loss Account of the company. The details regarding exchange differences are given below:

Favourable exchange differences on items other than Fixed Assets	₹ 50 lakhs

Less: Unfavourable exchange difference on account of increase in term liability on purchase of Fixed Assets (₹ 30 lakhs)

Net Exchange Difference transferred to Profit and Loss Account ₹ 20 lakhs

Do you agree with the Vice-President (Accounts)? Give reasons.

(d) X Ltd. acquired 100% shares of Y Ltd. prior to 31st March, 2011. During 2011-2012 the individual companies included in their financial statements the following items:

	X Ltd.	Y Ltd.
Officer's salary	1,17,500	32,340
Officer's expenses	99,000	10,000
Loans to Officers	7,25,000	3,67,000
Inter-company sales to Y Ltd.	16,43,420	

The CEO and Finance Directors of the Company are unable to decide, whether the amount of ₹ 16,43,420 being sales from X Ltd. to Y Ltd. should get reported as related-party disclosure in the notes to accounts of consolidated financial statements, for the accounting period ended on 31st March, 2012. Advise.

(4 x 5 = 20 Marks)

2. The following are the Balance Sheets of P Ltd. and Q Ltd. as on 30th September, 2011:

Liabilities	*P Ltd.*	*Q Ltd.*	*Assets*	*P Ltd.*	*Q Ltd.*
	₹	₹		₹	₹
Share Capital:			Fixed assets:		
Equity shares of ₹100 each	5,00,000	2,00,000	Goodwill	60,000	40,000
			Machinery	1,00,000	60,000
12% Preference shares of ₹ 10 each	1,00,000	50,000	Vehicle	1,80,000	70,000
			Furniture	50,000	30,000
Reserves and surplus:			Shares in Q Ltd. at cost	3,80,000	
General reserve	1,00,000	60,000	Current assets:		
Profit & loss account	1,50,000	90,000	Stock	70,000	1,40,000
Current liabilities and provisions:			Debtors	1,00,000	1,65,000
			Bank Balance	40,000	25,000
Creditors	60,000	70,000			
Income Tax	70,000	60,000			
	9,80,000	5,30,000		9,80,000	5,30,000

The following further information are furnished:

(1) P Ltd. acquired 1,200 equity shares and 4,000 preference shares on 1st October, 2010 at the cost of ₹ 2,80,000 and ₹ 1,00,000 respectively.

(2) The profit and loss account of Q Ltd. had a credit balance of ₹ 30,000 as on 1st October, 2010 and that of General Reserve on that date was ₹ 50,000.

(3) On 1st December, 2010 Q Ltd. declared a dividend out of its pre-acquisition profits of 12% on its share capital. P Ltd. credited the receipt of dividend to its Profit and Loss Account.

(4) On 1st April, 2011, Q Ltd. issued one equity share for every three shares held as bonus shares at a face value of ₹ 100 each per share out of its General Reserve. No entry was made in the books of P Ltd. for receipt of bonus shares.

(5) Q Ltd. owned ₹ 20,000 for purchase of stock from P Ltd. The entire stock is held by Q Ltd. as on 30th September, 2011. P Ltd. made a profit of 25% on cost.

Prepare a Consolidated Balance Sheet of P Ltd. and Q Ltd as on 30th September, 2011.

(16 Marks)

3. The following abridged Balance Sheet as at 31st March, 2011 pertains to Rohan Ltd.:

Liabilities	₹ in lakhs	Assets	₹ in lakhs
Share Capital:		Goodwill, at cost	420
180 lakhs Equity shares of ₹ 10 each, fully paid up	1,800	Other Fixed Assets	11,166
		Current Assets	2,910
90 lakhs Equity shares of ₹ 10 each, ₹ 8 paid up	720	Loans and Advances	933
		Miscellaneous Expenditure	171
150 lakhs Equity shares of ₹ 5 each, fully paid-up	750		
Reserves and Surplus	5,628		
Secured Loans	4,500		
Current Liabilities	1,242		
Provisions	960		
	15,600		15,600

You are required to calculate the following for each one of the three categories of equity shares appearing in the above mentioned Balance Sheet:

(i) Intrinsic value on the basis of book values of Assets and Liabilities including goodwill;

(ii) Value per share on the basis of dividend yield.

Normal rate of dividend in the concerned industry is 15%, whereas Rohan Ltd. has been paying 20% dividend for the last four years and is expected to maintain it in the next few years; and

(iii) Value per share on the basis of EPS.

For the year ended 31st March, 2011 the company has earned ₹ 1,371 lakhs as profit after tax, which can be considered to be normal for the company. Average EPS for a fully paid share of ₹ 10 of a Company in the same industry is ₹ 2. *(16 Marks)*

4. Following are the Balance Sheets of companies as at 31.12.2011:

Liabilities	*H Ltd.*	*S Ltd.*	*Assets*	*H Ltd.*	*S Ltd.*
	₹	₹		₹	₹
Equity share capital (₹ 100)	8,00,000	6,00,000	Goodwill	6,00,000	–
			Fixed Assets	5,00,000	8,00,000
General Reserve	4,00,000	3,00,000	Investments	2,00,000	4,00,000
Investment Allowance			Current Assets	4,00,000	3,00,000
Reserve	–	4,00,000			
Sundry Creditors	5,00,000	2,00,000			
	17,00,000	15,00,000		17,00,000	15,00,000

H Ltd. took over S Ltd. on the basis of the respective shares' value, adjusting wherever necessary, the book values of assets and liabilities on the basis of the following information:

(i) Investment Allowance Reserve was in respect of addition made to fixed assets by S Ltd. in the year 2009-2010 on which income tax relief has been obtained. In terms of the Income Tax Act, 1961, the company has to carry forward till 2014 reserve of ₹ 2,00,000 for utilization.

(ii) Investments of S Ltd. included 1,000 shares in H Ltd. acquired at cost of ₹ 150 per share. The other investments of S Ltd. have a market value of ₹ 1,92,500.

(iii) The market value of investments of H Ltd. are to be taken at ₹ 1,00,000.

(iv) Goodwill of H Ltd. and S Ltd. are to be taken at ₹ 5,00,000 and ₹ 1,00,000 respectively.

(v) Fixed assets of H Ltd. and S Ltd. are valued at ₹ 6,00,000 and ₹ 8,50,000 respectively.

(vi) Current assets of H Ltd. included ₹ 80,000 of stock in trade received from S Ltd. at cost plus 25%.

The above scheme has been duly adopted. Pass necessary Journal Entries in the books of H Ltd. and prepare Balance Sheet of H Ltd. after taking over the business of S Ltd. Fractional share to be settled in cash, rest in shares of H Ltd. Calculation shall be made to the nearest multiple of a rupee. *(16 Marks)*

5. (a) ABC Commercial Bank has a criteria that it will give loan to companies that have an economic value added greater than zero for the past three years on average. The bank is considering lending money to a small company that has the economic value characteristics shown below. Does that company meet the bank's criteria for a positive economic value added? The data relating to the company is as follows:

   (i) Average operating income after tax equals ₹ 25,00,000 per year for the last three years.

   (ii) The average total assets of company over the past three years equals ₹ 75,00,000.

   (iii) The weighted average cost of capital appropriate for the company equals 10% which is applicable to all three years.

   (iv) The company's average current liabilities over the past three year equals ₹ 15,00,000.

   (b) Sampark Mutual Fund is registered with SEBI and having its registered office at Pune. The fund is in the process of finalizing the annual statement of accounts of one of its Open ended Mutual Fund Scheme. From the information furnished below you are required to prepare a statement showing the movement of unit holders' funds for the financial year ended 31st March, 2012.

Opening Balance of net assets	12,00,000
Net Income for the year (Audited)	85,000
8,50,200 units issued during 2011-12	96,500
7,52,300 units redeemed during 2011-12	71,320
The par value per unit is ₹ 100	
Note : Figures given above are in ₹ '000.	

(8+8= 16 Marks)

6. (a) On April 1, 2011, Om Ltd. borrowed ₹ 10 lakhs 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	*Value of debt*
	₹ in lakh	*₹ in lakh*
April 1, 2011	+ 0.2	10.2
March 31, 2012	– 0.1	9.9

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

Show important accounting entries in respect of the swap arrangement.

(b) ABC Ltd. grants 1,000 employees stock options on 1.4.2008 at ₹ 40, when the market price is ₹ 160. The vesting period is 2½ years and the maximum exercise period is one year. 300 unvested options lapse on 1.5.2010. 600 options are exercised on 30.6.2011. 100 vested options lapse at the end of the exercise period.

Pass Journal Entries giving suitable narrations. *(8+8=16 Marks)*

7. Answer any **four** parts of the question:

(a) PQR Ltd., has a capital base of ₹ 5,00,000 and it earned profits of ₹ 50,000. The return on investment of the same group of firms is 12%. If the services of a particular Engineer, Mr. P is acquired, it is expected that the profits will raise by ₹ 30,000 over and above the target profit. Determine the amount of maximum bid price for that particular engineer.

(b) Kotak Finance Ltd. is a non-banking finance company. The extracts of its balance sheet are given below:

Liabilities	*Amount*	*Assets*	*Amount*
Paid up equity share capital	100	Leased out Assets Investment:	800
Free Reserves	500	In shares of subsidiaries and	
Loans	400	group companies	100
Deposits	400	In debentures of subsidiaries and	
		group companies	100
		Cash and Bank balances	200
		Deferred Expenditure	200
	1,400		1,400

You are required to compute Tier – I Capital of Mahindra Finance Ltd. according to NBFC Prudential Norms (RBI) Directions.

(c) P Limited has recognized ₹ 10 lakhs on accrual basis income from dividend on units of mutual funds of the face value of ₹ 50 lakhs held by it as at the end of the financial year 31st March, 2011. The dividends on mutual funds were declared at the rate of 20% on 15th June, 2011. The dividend was proposed on 10th April, 2011 by the declaring company. Whether the treatment is as per the relevant Accounting Standard? You are asked to answer with reference to provisions of Accounting Standard.

(d) Explain significant differences and similarities between Existing Indian Accounting Standards, IFRS and US GAAPs on the issues of:

(i) Impairment of assets

(ii) Earnings per share- diluted.

(e) A Ltd. had 6,00,000 equity shares on April 1, 2010. The company earned a profit of ₹ 15,00,000 during the year 2010-11. The average fair value per share during 2010-11 was ₹ 25. The company has given share option to its employees of 1,00,000 equity shares at option price of ₹ 15. Calculate basic EPS and diluted EPS. *(4 x 4 = 16 Marks)*