

PAPER – 1 : FINANCIAL REPORTING

PART – I : RELEVANT AMENDMENTS, NOTIFICATIONS AND ANNOUNCEMENTS

A. Applicable for November, 2013 examination

(i) Securities and Exchange Board of India Mutual Funds (Amendment) Regulations, 2013

In exercise of the powers conferred by section 30 of the Securities and Exchange Board of India Act, 1992 (15 of 1992), the Board vide notification No. LAD-NRO/GN/2013-14/03/5652 dated April 16, 2013 had made amendment to the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996. These Regulations may be called as the Securities and Exchange Board of India (Mutual Funds) (Amendment) Regulations, 2013. The SEBI (Mutual Funds) (Amendment) Regulations, 2013 can be downloaded from the link http://www.sebi.gov.in/cms/sebi_data/attachdocs/1366172455558.pdf

(ii) Securities and Exchange Board of India (Stock Brokers And Sub-Brokers) (Amendment) Regulations, 2013

In exercise of the powers conferred by section 30 of the Securities and Exchange Board of India Act, 1992 (15 of 1992), the Board vide notification No. LAD-NRO/GN/2013-14/01/8129 dated April 5, 2013 had made amendment to the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996. These Regulations may be called as the Securities and Exchange Board of India (Stock Brokers and Sub-brokers) (Amendment) Regulations, 2013. The SEBI (Stock Brokers and Sub-brokers) (Amendment) Regulations, 2013 can be downloaded from the link http://www.sebi.gov.in/cms/sebi_data/attachdocs/1365161667044.pdf

(iii) Presentation of Foreign Currency Monetary Item Translation Difference Account (FCMITDA)

In the Revised Schedule VI format, no line item has been specified for the presentation of "Foreign Currency Monetary Item Translation Difference Account (FCMITDA)". Therefore, the Council of the Institute at its 324th meeting held on March 24-26, 2013 at New Delhi, decided that debit or credit balance in FCMITDA should be shown on the "Equity and Liabilities" side of the balance sheet under the head 'Reserves and Surplus' as a separate line item.

(iv) Criteria for Classification of Entities and Applicability of Accounting Standards

Due to recent changes in the enhancement of tax audit limit, the Council of the ICAI has recently decided to change the 1st criteria of Level II Non-Corporate Entities i.e. determination of SME on turnover basis **from ₹ 40 lakhs to ₹ 1 Crore** vide announcement "Revision in the Criteria for classifying Level II Non-Corporate Entities" issued by ICAI on 7th March, 2013. This revision is applicable with effect from the accounting year commencing on or after April 1, 2012.

(v) **Amendments to SEBI (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999 and Equity Listing Agreement**

SEBI has noticed that some listed entities have been framing their own employees benefit schemes wherein Trusts have been set up to deal in their own securities in the secondary market. It is apprehended that some entities may frame such schemes with the purpose of dealing in its own securities with the object of inflating, depressing, maintaining or causing fluctuation in the price of the securities by engaging in fraudulent and unfair trade practices.

In order to address the concerns over acquisition of shares by employee welfare Trusts from the secondary market, it has been decided to prohibit the listed entities from framing any employee benefit schemes involving acquisition of own securities from the secondary market. To implement this decision, some amendments (applicable with immediate effect) are being made in the SEBI (ESOS and ESPS) Guidelines 1999 and Equity Listing Agreement vide circular no CIR/CFD/DIL/3/2013 dated January 17, 2013.

Equity Listing Agreement

Certain listing conditions are hereby specified by way of inserting Clause 35C in the Equity Listing Agreement as given below:

- “(i) The issuer agrees that all the employee benefit schemes involving the securities of the company shall be in compliance with SEBI (ESOS and ESPS) Guidelines, 1999 and any other guidelines, regulations etc. framed by SEBI in this regard.
- (ii) The issuer further agrees that all the employee benefit schemes already framed and implemented by the company involving dealing in the securities of the company, before the insertion of this clause shall be aligned with and made to conform to SEBI (ESOS and ESPS) Guidelines, 1999 by June 30, 2013.”

SEBI (ESOS and ESPS) Guidelines, 1999

In respect of those companies, which have already framed and implemented before the date of this circular any employee benefit schemes involving dealing in the securities of the company, which are not in accordance with SEBI (ESOS and ESPS) Guidelines, it has been decided that:-

- (i) such companies will be required to inform the details of their schemes to the Stock Exchanges within 30 days from date of this circular, in the prescribed format provided.
- (ii) such companies shall align any existing employee benefit schemes with SEBI (ESOS and ESPS) Guidelines on or before June 30, 2013.

A new clause 22B has also been inserted after clause 22A in the SEBI (ESOS and ESPS) Guidelines 1999 as given below:

“Prohibition on acquisition of securities from secondary market: No ESOS/ESPS shall involve acquisition of securities from the secondary market”.

(vi) Requirement of Base Minimum Capital for Stock Trading Member

The BMC (Base Minimum Capital) deposit requirement for stock brokers trading on stock exchange has been prescribed by SEBI to be commensurate with the risks (other than market risk), that the broker may bring to the system. The various technological changes and the increased speeds of trading have brought to fore the greater quantum of risks arising during the course of execution of transactions. In light of this, based on deliberations at various forums, it has been decided to realign the BMC requirements with the risk profiles of the stock brokers / trading members in cash / derivative segment of the stock exchange vide circular no. CIR/MRD/DRMNP/ 36 /2012 dated December 19, 2012 which shall be implemented by March 31, 2013. This circular is being issued in exercise of powers conferred under Section 11(1) of the Securities and Exchange Board of India Act, 1992 to protect the interests of investors in securities and to promote the development of, and to regulate the securities market.

Accordingly, the requirement of BMC would be implemented in the following manner:

- (i) It shall be enhanced for members holding registration as “stock-broker” in cash segment.
- (ii) BMC shall be introduced for members holding registration as “trading member” in any derivative segment.
- (iii) Stock brokers / trading members shall maintain the prescribed BMC based on their profiles –

Categories	BMC Deposit
Deposit Only Proprietary trading without Algorithmic trading (Algo)	₹ 10 Lacs
Trading only on behalf of Client (without proprietary trading) and without Algo	₹15 Lacs
Proprietary trading and trading on behalf of Client without Algo	₹ 25 Lacs
All Trading Members/Brokers with Algo	₹ 50 Lacs

Explanation: The profiling of members may be explained with the following example – A scenario may arise, wherein, a member has registration as a “stock broker” as well as a “trading member” and is engaged as a principal doing proprietary trading on cash segment and is also engaged as an agent and transacting only on behalf of the clients in the derivatives segment.

Further, the member may not have availed facility for algorithmic trading. In such a case, the profile of such a member shall be assessed as “Proprietary trading and trading on

behalf of client without Algo". The applicable BMC deposit for such a member shall be ₹ 25 Lacs.

This BMC deposit requirement stipulated in the above table, is applicable to all stock brokers / trading members of exchanges having nation-wide trading terminals.

- (iv) For stock brokers / trading members of exchanges not having nation-wide trading terminals, the deposit requirement shall be 40% of the above said BMC deposit requirements.
- (v) The BMC deposit shall be maintained for meeting contingencies in any segment of the exchange. For members having registration for more than one segment of the same exchange, the BMC deposit requirement shall not be additive for such number of segments and shall be the highest applicable BMC deposit, across various segment.
- (v) No exposure shall be granted against such BMC deposit. The Stock Exchanges shall be permitted to prescribe suitable deposit requirements, over and above the SEBI prescribed norms, based on their perception and evaluation of risks involved.
- (vi) Minimum 50% of the deposit shall be in the form of cash and cash equivalents. The existing guidelines on collateral composition shall continue to remain applicable.

The relevant SEBI circular no SMD/SED/RCG/270/96 dated January 19, 1996 and circular no MRD/DoP/SE/Cir-07/2005 dated February 23, 2005, stand modified suitably. All other relevant provisions shall continue to remain applicable.

(vii) Schedule VI revised by the Ministry of Corporate Affairs

The Ministry of Corporate Affairs (MCA) has revised Schedule VI to the Companies Act 1956 on the 28th February, 2011 pertaining to the preparation of Balance Sheet and Profit and Loss Account under the Companies Act, 1956. This revised Schedule VI has been framed as per the existing non-converged Indian Accounting Standards notified under the Companies (Accounting Standards), Rules, 2006. The Revised Schedule VI shall come into force for the Balance Sheet and Profit and Loss Account to be prepared for the financial year commencing on or after 1.4.2011.

(viii) Amendment to para 46 of Accounting Standard 11 of the Companies (Accounting Standards) Rules, 2006

Ministry of Corporate Affairs vide its notification number G.S.R 913(E), dated 29th December, 2011, has amended the para 46 of AS 11 of the Companies (Accounting Standards) Amendment Rules, 2011. Through this notification, the MCA has extended the option (for the enterprises) to capitalize the exchange differences arising on reporting of long term foreign currency monetary items till 31st March, 2020 instead of 31st March, 2012.

(ix) **Insertion of para 46A in Accounting Standard 11 of the Companies (Accounting Standards) Rules, 2006**

Ministry of Corporate Affairs vide its notification number G.S.R 914(E), dated 29th December, 2011, inserted under-mentioned para 46A in AS 11 of the Companies (Accounting Standards) Rules, 2006.

"46A. (1) In respect of accounting periods commencing on or after the 1st April, 2011, for an enterprise which had earlier exercised the option under paragraph 46 and at the option of any other enterprise (such option to be irrevocable and to be applied to all such foreign currency monetary items), the exchange differences arising on reporting of long-term foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, in so far as they relate to the acquisition of a depreciable capital assets, can be added to or deducted from the cost of the assets and shall be depreciated over the balance life of the assets, and in other cases, can be accumulated in a "Foreign Currency Monetary Item Translation Difference Account" in the enterprise's financial statements and amortized over the balance period of such long term assets or liability, by recognition as income or expense in each of such periods, with the exception of exchange differences dealt with in accordance with the provisions of paragraph 15 of the said rules.

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

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

Note: The principal regulations were published in the Gazette of India Extraordinary, Part II, Section 3, Sub Section (i) vide G.S.R 739(E), dated the 7th December, 2006 and amended vide notification number G.S.R. 212(E), dated the 27th March, 2008 and subsequently amended by No. G.S.R. 225(E) dated 31st March, 2009 and No. G.S.R. 378(E), dated 11th May, 2011.

(x) **Clarification on Para 46A of notification number G.S.R. 914(E) dated 29.12.2011 on Accounting Standard 11 relating to "The effects of Changes in Foreign Exchange Rates"**

The Ministry has received several representations from industry associations that Para 6 of AS 11 and Para 4(e) of AS 16 are posing problems in proper implementation of Para 46A of AS 11 inserted vide notification 914(E) dated 29.12.2011. In order to resolve the problems faced by industry, MCA had further clarified vide Circular No. 25/2012 dated

09.08.2012 that Para 6 of AS 11 and Para 4(e) of the AS 16 shall not apply to a company which is applying clause Para 46A of AS 11.

(xi) Application of AS 30, Financial Instruments: Recognition and Measurement, for the accounting periods ending on or before 31st March 2011 and from 1st April, 2011 onwards

1. Accounting Standard Board of ICAI has issued a clarification regarding applicability of AS 30 (dated 11th February, 2011). It is clarified that in respect of the financial statements or other financial information for the accounting periods commencing on or after 1st April 2009 and ending on or before 31st March 2011, the status of AS 30 would be as below:
 - (i) To the extent of accounting treatments covered by any of the existing notified accounting standards (for eg. AS 11, AS 13 etc,) the existing accounting standards would continue to prevail over AS 30.
 - (ii) In cases where a relevant regulatory authority has prescribed specific regulatory requirements (eg. Loan impairment, investment classification or accounting for securitizations by the RBI, etc), the prescribed regulatory requirements would continue to prevail over AS 30.
 - (iii) The preparers of the financial statements are encouraged to follow the principles enunciated in the accounting treatments contained in AS 30. The aforesaid is, however, subject to (i) and (ii) above.
2. From 1st April 2011 onwards,
 - (i) the entities to which converged Indian accounting standards will be applied as per the roadmap issued by MCA, the Indian Accounting Standard (Ind AS) 39, *Financial Instruments: Recognition and Measurement*, will apply.
 - (ii) for entities other than those covered under paragraph 2(i) above, the status of AS 30 will continue as clarified in paragraph 1 above.
3. The abovementioned clarifications would also be relevant to the existing AS 31, *Financial Instruments: Presentation* and AS 32, *Financial Instruments: Disclosures* as well as for Ind AS 32, *Financial Instruments: Presentation* and Ind AS 107, *Financial Instruments: Disclosures*, after 1st April 2011 onwards.

Note: Ind AS, have not been notified till date. AS 30, 31 and 32 have also not been notified. Therefore, AS 30, 31 and 32 will presumed as encouraged to be followed by all the entities.

B. Not applicable for November, 2013 examination

(i) Ind ASs issued by the Ministry of Corporate Affairs

The Ministry of Corporate Affairs (MCA) has hosted 35 Converged Indian Accounting Standards (known as "Ind-AS"), without announcing the applicability date. The issuance

of Ind-AS is a significant step towards the implementation of converged standards in India. The MCA will intimate the implementation date later. However, Ind ASs are not made applicable for November, 2013 examination.

(ii) Inflation Accounting

As per the Council's decision, in its 306th meeting, the topic of 'Inflation Accounting' has been excluded from the syllabus of Financial Reporting. Therefore, the chapter on 'Inflation Accounting' is not applicable for November, 2013 examination.

PART – II : QUESTIONS AND ANSWERS

QUESTIONS

Applicability of Accounting Standards to various entities

1. M/s Omega & Co. (a partnership firm), had a turnover of ₹ 1.25 crores (excluding other income) and borrowings of ₹ 0.95 crores in the previous year. It wants to avail the exemptions available in application of Accounting Standards to non-corporate entities for the year ended 31.3.2013. Advise the management of M/s Omega & Co in respect of the exemptions of provisions of ASs, as per the directive issued by the ICAI.

AS 1

2. (a) X Limited has sold its building for ₹ 50 lakhs to the purchaser who has paid the full price. Company has given possession to the purchaser. The book value of the building is ₹ 35 lakhs. As at 31st March, 2013, documentation and legal formalities are pending. The company has not recorded the disposal. It has shown the amount received as advance. Do you agree with this accounting treatment done by X Ltd.? If not, then suggest the correct accounting treatment in this regard.

AS 2

- (b) From the following information, ascertain the value of stock as on 31st March, 2013:

	₹
Stock as on 01.04.2012	28,500
Purchases	1,52,500
Manufacturing Expenses	30,000
Selling Expenses	12,100
Administration Expenses	6,000
Financial Expenses	4,300
Sales	2,49,000

At the time of valuing stock as on 31st March, 2012 a sum of ₹ 3,500 was written off on a particular item, which was originally purchased for ₹ 10,000 and was sold

during the year for ₹ 9,000. Barring the transaction relating to this item, the gross profit earned during the year was 20% on sales.

AS 3

- (c) Financial information of Great Ltd. for the year ended 31st March, 2012 and 2013 are as follows:

Summarised Balance Sheets of Great Ltd.**as on 31st March, 2013 and 2012**

	2013	2012
	₹	₹
Assets		
Cash and cash equivalents	4,500	1,500
Trade receivables	7,500	3,750
Inventory	3,000	2,250
Intangible asset (net)	1,500	2,250
Due from associates	28,500	28,500
Property, plant and equipment at cost	18,000	33,750
Accumulated depreciation	(7,500)	(9,000)
Property, plant and equipment (net)	<u>10,500</u>	<u>24,750</u>
Total assets	<u>55,500</u>	<u>63,000</u>
Liabilities		
Accounts payable	7,500	18,750
Provision for taxation	<u>7,500</u>	<u>4,500</u>
Total liabilities (A)	<u>15,000</u>	<u>23,250</u>
Shareholders' equity		
Share capital	9,750	9,750
Retained earnings	<u>30,750</u>	<u>30,000</u>
Total shareholders' equity (B)	<u>40,500</u>	<u>39,750</u>
Total liabilities and shareholders' equity (A + B)	<u>55,500</u>	<u>63,000</u>

Summarised Statement of Profit and Loss of Great Ltd.**For the year ended 31st March, 2013**

	₹
Sales	45,000
Cost of sales	<u>(15,000)</u>
Gross operating profit	30,000
Administrative and selling expenses	<u>(3,000)</u>

Interest expenses	(3,000)
Depreciation of property, plant and equipment	(3,000)
Amortization of intangible asset	(750)
Investment income	<u>4,500</u>
Net profit before taxation	24,750
Taxes on profit	<u>(6,000)</u>
Net profit	<u>18,750</u>

Additional information:

1. All sales made by Great Ltd. are credit sales. All purchases are also credit purchases.
2. Interest expense for the year 2012-2013 was ₹ 3,000, which was fully paid during the year.
3. The company pays salaries and other employee dues before the end of each month. All administration and selling expenses incurred were paid before 31st March, 2013.
4. Investment income comprised dividend income from investments in shares of blue chip companies. This was received before 31st March, 2013.
5. Equipment with a net book value of ₹ 11,250 and original cost of ₹ 15,750 was sold for ₹ 11,250.
6. The company declared and paid dividends of ₹ 18,000 to its shareholders during 2012-2013.
7. Income tax expense for the year 2012-2013 was ₹ 6,000, against which the company paid ₹ 3,000 during 2012-2013 as an estimate.

Using all the given financial information of Great Ltd., prepare the cash flows statement as per AS 3 under indirect method.

AS 4

- (d) During the year 2012-2013, Raj Ltd. was sued by a competitor for ₹ 15 lakhs for infringement of a trademark. Based on the advice of the company's legal counsel, Raj Ltd. provided for a sum of ₹ 10 lakhs in its financial statements for the year ended 31st March, 2013. On 18th May, 2013, the Court decided in favour of the party alleging infringement of the trademark and ordered Raj Ltd. to pay the aggrieved party a sum of ₹ 14 lakhs. The financial statements were prepared by the company's management on 30th April, 2013, and approved by the board on 30th May, 2013.

Should Raj Ltd. adjust its financial statements for the year ended 31st March, 2013? What would be the treatment of the above, in case the court decision was held on 1st June, 2013.

AS 7

3. (a) Trustworthy Ltd. is a construction company, well known for its expertise in building flyovers and maintaining these structures. Impressed with Trustworthy Ltd.'s track record, the local municipal authorities have awarded them a contract for two years to build a super flyover in the heart of the city (the largest in the region) and another contract for maintenance of the flyover for ten years after completion of the construction. Payment for both the contracts is paid considering it as a single package.

Evaluate whether these two contracts should be segmented or combined into one contract for the purpose of AS 7.

AS 5 and AS 9

- (b) Sahara Ltd. is in regular business with Railways and dealings with them are shown in its financial statements as ordinary activities of the business. A claim was lodged by it, with the Railways in March, 2010 for loss of goods of ₹ 2,00,000. The claim had been passed for payment in March, 2013 for ₹ 1,50,000. No entry was passed in the books of the company, when the claim was lodged. Advise Sahara Ltd. about the treatment of the above in the final statement of accounts for the year ended on 31st March, 2013.

AS 6 and AS 10

- (c) Value Ltd. acquired a plant on 1.4.2004 for ₹ 100 lakhs. The company charges straight line depreciation on the basis of estimated useful life of the asset as 10 years and scrap value at the end as 2.5% of the cost. At the beginning of the 5th year, the asset was revalued upward by 40% of the written down value and the revaluation profit was transferred to Revaluation Reserve. While charging depreciation after revaluation, estimated remaining useful life was assumed to be 6 years and scrap realisation was expected to be 2.5% of the revalued figure. No additional depreciation was adjusted through Revaluation Reserve account. At the beginning of the 8th year the company found the asset useless and accordingly, decided to retire it. On the date of retirement the estimated realisable value of the asset is ₹ 3,80,000. Ascertain the loss on retirement of the asset to be charged to the Statement of Profit and Loss.

AS 12

4. (a) Yogya Ltd. received a specific grant of ₹ 300 lakhs for acquiring the plant of ₹ 1,500 lakhs during 2009-10 having useful life of 10 years. The grant received was credited to deferred income in the balance sheet. During 2012-13, due to non-compliance of conditions laid down for the grant of ₹ 300 lakhs, the company had to

refund the grant to the Government. Balance in the deferred income on that date was ₹ 210 lakhs and written down value of plant was ₹ 1,050 lakhs.

- (i) What should be the treatment of the refund of the grant and the effect on cost of the fixed asset and the amount of depreciation to be charged during the year 2012-13 in the Statement of Profit and Loss?
- (ii) What should be the treatment of the refund if grant was deducted from the cost of the plant during 2009-10?

Assume depreciation is charged on assets as per Straight Line Method.

AS 13

- (b) X Ltd. on 1-1-2012 had made an investment of ₹ 600 lakhs in the equity shares of Y Ltd. of which 50% is made in the long term category and the rest as temporary investment. The realizable value of all such investment on 31-3-2012 became ₹ 200 lakhs as Y Ltd. lost a case of copyright. From the given market conditions, it is apparent that the reduction in the value is permanent in nature. How will you recognize the reduction in financial statements for the year ended on 31-3-2012?

AS 11

- (c) Explain briefly the accounting treatment needed in the following cases as per AS 11 'The Effects of Changes in Foreign Exchange Rates'.
 - (i) Sundry Debtors include amount receivable from Ted ₹ 5,00,000 recorded at the prevailing exchange rate on the date of sales, transactions recorded at \$1 = ₹ 38.70
 - (ii) Long term loan taken from a U.S. Company, amounting to ₹ 60,00,000. It was recorded at \$1 = ₹ 35.60, taking exchange rate prevailing at the date of transactions.
 - (iii) Another long term loan was there in Pound Sterling for purchase of machinery amounting to ₹ 10,00,000. It was recorded at Pounds ₹ 62.80.
Exchange rates at the end of the year were as under:
 \$1 Receivable = ₹ 45.80
 Pounds = ₹ 72.30
 \$ 1 Payable = ₹ 45.90

AS 16

5. (a) X Limited began construction of a new plant on 1st April, 2012 and obtained a special loan of 8 lakhs to finance the construction of the plant. The rate of interest on loan was 10 per cent per annum.

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

	₹
1-4-2012	10,00,000

1-8-2012	24,00,000
1-1-2013	4,00,000

The Company's other outstanding non-specific loan was ₹ 46,00,000 at an interest of 12 percent per annum.

The construction of the plant was completed on 31-3-2013. You are required to calculate the total amount to be capitalised including amount of interest as per the provisions of AS 16 'Borrowing Cost'.

AS 17

- (b) Comment whether other income like (i) export incentives; and (ii) interest from customers should be considered/included as segment revenue or not as per AS 17.

AS 18

- (c) X Limited is a wholly owned subsidiary of Z Limited and a 50% co-venturer in joint venture XY. Whether transactions between joint venture XY and Z would require disclosures?

AS 19

6. (a) Classify the following into either operating or finance leases.
- Ownership of an asset gets vested to the lessee at the end of lease term
 - Lessee has option to purchase the asset at lower than fair value, at the end of lease term.
 - Economic life of the asset is 5 years, lease term is 4½ years, but asset is not acquired at the end of lease term.
 - PV of MLP = "X", Fair value of the asset is Y.
 - Economic life is 5 years, lease term is 2 years, but the asset is of a special nature, and has been procured only for use of lessee.

AS 20

- (b) From the information furnished you are required to compute the Basic and Diluted EPS for accounting year 01-04-2012 to 31-03-2013 and adjusted EPS for the year 01-04-2011 to 31-03-2012.

Net profit for year ended 31-03-2012	₹ 75,50,000
Net profit for year ended 31-03-2013	₹ 1,00,25,000
No. of equity shares as on 01-04-2012	50,00,250
Bonus issue on 01-01-2013	1 share for every 2 held

No. of 12% Convertible Debentures of ₹ 100 each issued on 01-01-2013	1,00,000
Conversion ratio of Debentures	10 shares per debenture
Tax rate	30 percent

AS 22

- (c) What is the tax effect of sale of fixed assets, considering the block of assets approach followed in the Income-tax Act, 1961?

Company X has a block of assets with a written down value of ₹ 1,00,000 on 1st April, 2011 for tax purposes. The book value of the assets for accounting purposes is also ₹ 1,00,000. The assets are depreciated on written down value basis at 25 per cent per annum for both accounting and tax purposes. Of the entire block, assets costing ₹ 5,000 on April 1, 2011, were sold for ₹ 10,000 on 31st March, 2013. Compute the deferred tax asset/liability assuming tax rate of 40 percent.

AS 23

7. (a) X Limited holds 6% shares of Y Limited. Z Limited holds 8% shares of Y Limited. Z Limited is a subsidiary of X Limited, which virtually participate in most of the policy making process of Y Limited. Does X Limited have significant influence over Y Ltd. Explain?

AS 24

- (b) A cosmetic items producing company provides the following information:

	<i>Fairness Cream</i>	<i>Vanishing Cream</i>
January, 2012 - September, 2012 per month	2,00,000	2,00,000
October, 2012 - December, 2012 per month	2,00,000	3,00,000
January, 2013 - March, 2013 per month	0	4,00,000

The company has enforced a gradual change in product-line on the basis of an overall plan. The Board of Directors of the Company has passed a resolution in March, 2012 to this effect. The company follows calendar year as its accounting year. Should this be treated as a discontinuing operation? Give reasons in support of your answer.

AS 25

8. (a) Antarbarti Limited reported a Profit Before Tax (PBT) of ₹ 4 lakhs for the third quarter ending 30-09-2012. 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 recognized 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 ₹ 12 lakhs. The entire amount has been debited in the third quarter, though the share of the third quarter is only ₹ 3 lakhs.
- (iv) ₹ 2 lakhs extra-ordinary 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.

AS 28

- (b) The following information is available as regards to the fixed asset of a company:
 - (i) Carrying amount of the asset shown in the balance sheet net of accumulated depreciation is ₹ 340 lakhs. Assets are 2 years old. The present market price of the asset is ₹ 300 lakhs. The company charges depreciation @10% on SLM assuming 10 years as its useful life.
 - (ii) At the beginning of the current year, on review, remaining useful life of the asset has been assessed as 5 years because of technological changes.
 - (iii) Market rate of interest has declined. Accordingly, there is decline in the discount factor from 16% to 15%.
 - (iv) Book value to market capitalisation ratio of the company is 0.80.

Is there an indication of impairment of asset? If yes, then how should it be adjusted?

AS 29

- 9. (a) Raja Ltd. had announced a Voluntary Retirement Scheme (VRS) for its employees on 1st January 2012. The scheme is scheduled to close on 30th June 2012. The scheme envisaged an initial lump-sum payment of maximum of ₹ 2 Lakhs and monthly payments over the balance period of service of employees coming under the plan. 200 employees opted for the scheme as on 31st March 2012. The total lump sum payment for these employees would be ₹ 250 Lakhs and the aggregate of future payments to them would amount to ₹ 1,500 Lakhs.

However no payment had been made to the employees under the scheme up to 31st March 2012. The Company had not made any provision in its accounts towards any liability under the scheme. Give your views on the above.

Accounting Standards (as applicable in India), IFRS and US GAAP

- (b) State the treatment of the following items with reference to Accounting Standards (as applicable in India), IFRS and US GAAP:
- (i) Property, Plant and Equipment
 - (ii) Purchase method – negative goodwill.

Corporate Financial Reporting - Schedule VI

10. The Balance Sheet of Appropriate Ltd. as at 31st March, 2013 is as follows:.

	Note No.	31 st March, 2013	31 st March, 2012
Equity & Liabilities			
Share Capital	1	XXX	XXX
Reserves and Surplus	2	0	0
Employee stock option outstanding	3	XXX	XXX
Share application money refundable	4	XXX	XXX
Non-Current Liabilities			
Deferred tax liability (Arising from Indian Income Tax)	5	XXX	XXX
Current Liabilities			
Trade Payables	6	<u>XXX</u>	<u>XXX</u>
Total		<u>XXXX</u>	<u>XXXX</u>
Assets			
Non-Current Assets			
Fixed Assets -Tangible	7	XXX	XXX
Capital Work in progress (including capital advances)	8	XXX	XXX
Current Assets			
Trade Receivables	9	XXX	XXX
Deferred Tax Asset (Arising from Indian Income Tax)	10	XXX	XXX
Profit and Loss (Debit balance)		<u>XXX</u>	<u>XXX</u>
Total		<u>XXXX</u>	<u>XXXX</u>

Comment on the presentation in terms of revised Schedule VI and Accounting Standards notified by the Central Government.

Corporate Restructuring –Amalgamation

11. Ram Limited and Shyam Limited carry on business of a similar nature and it is agreed that they should amalgamate. A new company, Ram and Shyam Limited, is to be formed to which the assets and liabilities of the existing companies, with certain exception, are to be transferred. On 31st March, 2013, the Balance Sheets of the two companies were as under:

Ram Limited**Balance Sheet as at 31st March, 2013**

<i>Liabilities</i>	₹	<i>Assets</i>	₹
Issued and Subscribed Share capital: 30,000 Equity shares of ₹ 10 each, fully paid	3,00,000	Freehold Property, at cost	2,10,000
General Reserve	1,60,000	Plant and Machinery, at cost less depreciation	50,000
Profit and Loss Account	40,000	Motor Vehicles, at cost less depreciation	20,000
Sundry Creditors	1,50,000	Stock	1,20,000
		Debtors	1,64,000
		Cash at Bank	86,000
	6,50,000		6,50,000

Shyam Limited**Balance Sheet as at 31st March, 2013**

<i>Liabilities</i>	₹	<i>Assets</i>	₹
Issued and Subscribed Share Capital: 16,000 Equity shares of ₹ 10 each, fully paid	1,60,000	Freehold Property, at cost	1,20,000
Profit and Loss Account	40,000	Plant and Machinery, at cost less depreciation	30,000
6% Debentures	1,20,000	Stock	1,56,000
Sundry Creditors	64,000	Debtors	42,000
		Cash at Bank	36,000
	3,84,000		3,84,000

Assets and Liabilities are to be taken at book-value, with the following exceptions:

- (a) Goodwill of Ram Limited and of Shyam Limited is to be valued at ₹ 1,60,000 and ₹ 60,000 respectively.

- (b) Motor Vehicles of Ram Limited are to be valued at ₹ 60,000.
- (c) The debentures of Shyam Limited are to be discharged by the issue of 6% Debentures of Ram and Shyam Limited at a premium of 5%.
- (d) The debtors of Shyam Ltd. realized fully and bank balance of Shyam Ltd, are to be retained by the liquidator and the sundry creditors of Shyam Ltd. are to be paid out of the proceeds thereof.

You are required to:

- (i) Compute the basis on which shares in Ram and Shyam Limited will be issued to the shareholders of the existing companies assuming that the nominal value of each share in Ram and Shyam Limited is ₹ 10.
- (ii) Draw up a Balance Sheet of Ram and Shyam Limited as of 1st April, 2013, the date of completion of amalgamation.
- (iii) Write up journal entries, including bank entries, for closing the books of Shyam Limited.

Consolidated Financial Statements – Chain Holdings

12. As on 31-3-2013, the summarized balance sheets of companies in a group showed the following position:

Assets	A	B	C
	₹	₹	₹
Fixed assets	1,35,000	60,000	70,000
Investments at cost	1,60,000	1,50,000	10,000
Stock	55,240	36,840	61,760
Debtors	1,10,070	69,120	93,880
Bank Balance	<u>1,31,290</u>	<u>16,540</u>	<u>52,610</u>
Total	<u>5,91,600</u>	<u>3,32,500</u>	<u>2,88,250</u>
Liabilities	₹	₹	₹
Equity shares of ₹ 10 each	2,00,000	1,50,000	80,000
Capital Reserve	50,000	-	23,000
Revenue Reserve	99,540	49,370	45,060
Creditors	1,12,060	73,130	78,190
Provision for Taxation	30,000	-	22,000
Proposed Dividends	<u>1,00,000</u>	<u>60,000</u>	<u>40,000</u>
Total	<u>5,91,600</u>	<u>3,32,500</u>	<u>2,88,250</u>

Additional information:

- (i) B Ltd. acquired 6,800 shares in C Ltd. at ₹ 22 per share in 2009 when the balance on capital reserve was ₹ 15,000 and revenue reserve was ₹ 30,500.
- (ii) A Ltd. purchased 8,000 shares in B Ltd. in 2009 when the balance in revenue reserve was ₹ 40,000. A Ltd. purchased further 4,000 shares in B Ltd. in 2010 when revenue reserve stood at ₹ 45,000. There was no other investment held by A Ltd. as on 31.3.2013.
- (iii) Parent companies included their share of proposed dividend in debtors account.

Prepare consolidated balance sheet of the group as on 31.3.2013 from the above informations.

Consolidated Financial Statements - Investment in Associates and Joint Ventures

13. H Ltd., which has an authorised and issued share capital of ₹ 10 crore equity shares of ₹ 10 each fully paid, has a balance of revenue reserve of ₹ 1,62,000 thousand on 31st March, 2011, after paying a dividend for the year ended on that date.

You are also given the following information:

- (1) On 1st April, 2011, H Ltd. purchased 90 lakh of the 4 crore issued equity shares of ₹ 10 each fully paid in A Ltd. for ₹ 1,42,500 thousand. The balance in revenue reserve of A Ltd. as on 31st March, 2011 was ₹ 3,45,000 thousand after paying dividend for the year.
- (2) For the year ended 31st March 2012, H Ltd. made a trading profit of ₹ 1,84,000 thousand and paid a dividend of 15% while Anoop Ltd. made a trading profit of ₹ 1,40,000 thousand and paid a dividend of 20%.
- (3) For the year ended 31st March, 2013, H Ltd. made a trading profit of ₹ 2,65,400 thousand and paid a dividend of 20% while A Ltd. incurred a trading loss of ₹ 1,41,000 thousand and no dividend was paid.
- (4) During the year ended 31st March, 2013, A Ltd. had manufactured and sold to H Ltd. an item of plant for ₹ 80,000 thousand which included 25% profit on selling price to A Ltd. The plant had been included in the fixed assets of H Ltd. and a full year's depreciation had been provided thereon at 20% on cost.

You are required to show the relevant Notes to Accounts for the Consolidated Balance Sheet of H Ltd. as on 31st March, 2013, together with the corresponding figures for the preceding year, assuming that H Ltd. has a subsidiary and it prepared consolidated financial statements on 31.3.2012 as well as 31.3.2013.

Accounting and Reporting of Financial Instruments (AS 30, 31 and 32)

14. A Ltd. holds an option to purchase equity shares in a listed company B Ltd. for ₹ 5 per share at the end of a 90 day period. State whether the option is a derivative financial asset or not with reasons.

Share Based Payments

15. On 1.1.2010, Happy Ltd. grants to its senior officer, a right to choose either 250 shares (with some post-vesting restrictions) or a cash payment equal to value of 200 shares, conditional upon remaining in service for 3 years.

Fair value of a share without considering post-vesting restrictions is ₹ 70 on 1.1.2010, ₹ 75 on 31.12.2010, ₹ 80 on 31.12.2011 and ₹ 85 on 31.12.2012. Fair value of a share after taking into account post-vesting restrictions is ₹ 68 on 1.1.2010. Face value per share is ₹ 10. Give the amounts to be recognised each year. Also, give the journal entries for settlement if (1) employee chooses cash payments (2) employee chooses shares.

Computation of Future Maintainable Profits

16. (a) ET Ltd. gives the following information – (All figures in ₹ '000s)

Particulars	2008	2009	2010	2011	2012
Net Profit after appropriation for Proposed Dividend at 20% on Equity Share Capital	19,10	18,50	22,40	20,15	25,25
Equity Share Capital	150,00	150,00	180,00	180,00	180,00
Advance Tax paid during the year	50,00	35,00	60,00	55,00	60,00
Provision for Taxation (A/c balance at end of the year)	3,20	2,00	3,00	2,00	1,00

The company made the following changes in its accounting policies:

- Switched over to FIFO basis of Stock Valuation after 2010.
- Switched over to WDV method of Depreciation after 2011.
- Earlier the company was recognizing the gain/loss on the basis of difference between collection rate & exchange rate. However, the company now decided to generate exchange gain on sundry debtors at the year-end.

Effects of stock valuation for different years were quantified as below:

Particulars for the year	2008	2009	2010
Stock Adjustments – LIFO	(Cr.) 1,21	(Cr.) 1,31	(Cr.) 1,42
Stock Adjustments – FIFO	(Dr.) 15	(Cr.) 21	(Cr.) 54

Amount of depreciation under two alternative methods were as below:

Particulars	2008	2009	2010	2011
Straight Line	7,12	8,10	8,25	8,40
WDV	8,10	8,95	9,25	9,30

Details of debtors in foreign exchange along with relevant exchange rates were as below:

Year ended	Debtors in Aus \$ in '000	Entry Rate	Year end Rate	Collection Rate
31.12.2008	5,000	49.10	49.25	49.35
31.12.2009	6,200	49.40	49.55	50.40
31.12.2010	6,300	50.35	52.40	51.95
31.12.2011	7,200	54.10	53.90	55.10
31.12.2012	8,200	57.10	56.95	57.15

Year end Debtors were collected in the next year. Before change in accounting policy, the entire Profit or Loss arising out of change in exchange rate was taken to Profit or Loss Account in the year of collection.

The following expenses and income were not charged in the year when they occurred. Instead they were charged in the next year as prior period adjustments:

Year	2008	2009	2010	2011
Expenses (₹ 000s)	87	14	25	54
Income (₹ 000s)	12	35	8	68

Ascertain future maintainable profit for the purpose of valuation of Goodwill, assuming future tax rate as 34%. Effect of changes in accounting policies on the tax liability of the previous years may be ignored.

Valuation of Shares

- (b) A Ltd. and its subsidiary B Ltd. get their supply of some essential raw materials from C Ltd. To co-ordinate their production on a more profitable basis, A Ltd. and C Ltd. agreed between themselves each to acquire a quarter of shares in the other's Authorized Capital by means of exchange of shares. The terms are as follows:
- A Ltd.'s shares are quoted at ₹ 14, but for the purpose of exchange the value is to be taken at the higher of the two values, e.g. (a) quoted and (b) on the basis of the Balance Sheet Valuation;
 - C Ltd.'s shares which are unquoted are to be taken at the higher of the value as on (a) yield basis and (b) the Balance sheet basis. The future profits are estimated as ₹ 1,05,000 subject to one-third to be retained for development purposes. Shares of similar companies yield 8%;
 - Tangible Fixed Assets of C Ltd. are to be taken at ₹ 8,70,000;
 - Balance due on settlement is to be treated as loan between two companies.

The summarised Balance Sheets of the companies at the relevant date stood as follows:

	<i>A Ltd.</i>	<i>B Ltd.</i>	<i>C Ltd.</i>
	₹	₹	₹
Authorised Share Capital	<u>12,00,000</u>	<u>5,00,000</u>	<u>10,00,000</u>
Equity Shares of ₹ 10 each issued and fully paid up	8,00,000	5,00,000	7,50,000
Securities Premium	80,000	-	-
7% Debentures	3,00,000	-	-
Profit and Loss A/c	2,40,000	2,20,000	2,10,000
Trade Payables	2,80,000	1,80,000	2,10,000
Bank Overdraft	1,00,000	50,000	-
	18,00,000	9,50,000	11,70,000
Tangible Fixed Assets	11,10,000	7,00,000	7,70,000
Investment (40,000 Shares in B Ltd.)	4,70,000	-	-
Current Assets	2,10,000	2,40,000	3,90,000
Underwriting Commission	10,000	10,000	10,000
	18,00,000	9,50,000	11,70,000

Compute the value of the shares according to the terms of the agreements and to present the final settlement, showing all the necessary workings.

Mutual Fund

17. (a) What is NAV of a Mutual Fund and how is it calculated? What is the significance of its calculation?
- (b) Calculate the year-end NAV of the Mutual Fund scheme on the basis of the information given below:
 - (i) UTI launched a new Fund scheme for ₹ 6,000 crore.
 - (ii) Underwriting Commission is 1% of the fund shared equally by SBI, PNB, Syndicate Bank and UTI Bank.
 - (iii) The Fund was launched on 1.4.2012 with a face value of ₹ 1000 per unit.
 - (iv) Underwriting Commission was paid in full.
 - (vi) Management Expense was allowed by SEBI @ 1% of the Fund raised. However, during the year management expense was of ₹ 45 crore only. The management decided to defer the payment of ₹ 5 crore to the next financial year.

- (vii) On 1.5.2012, the total fund received was invested after deduction of underwriting commission and ₹ 100 crore to meet the day to day management expenses. The investment fund received yielded 10% interest per annum. The interest was received for 3 quarters and the interest of last quarter is yet to receive. The interest realized in cash has been distributed to the unit holders @ 80%. The financial year runs from April to March. The quarter starts from the date of investment i.e. 1.5.2012.

Non – Banking Finance Companies

18. Forever Finance Ltd. is a non-banking finance company. It makes available to you the costs and market price of various investments held by it as on 31.3.2013:

(₹ in lakhs)

Scripts:		Cost	Market Price
A.	Equity Shares		
	A	60.00	61.20
	B	31.50	24.00
	C	60.00	36.00
	D	60.00	120.00
	E	90.00	105.00
	F	75.00	90.00
	G	30.00	6.00
B.	Mutual funds		
	MF-1	39.00	24.00
	MF-2	30.00	21.00
	MF-3	6.00	9.00
C.	Government securities		
	GV-1	60.00	66.00
	GV-2	75.00	72.00

- Can the company adjust depreciation of a particular item of investment within a category?
- What should be the value of investments as on 31.3.2013?
- Is it possible to off-set depreciation in investment in mutual funds against appreciation of the value of investment in equity shares and government securities?

Value Added Statement

19. Prepare a value added statement for the year ended on 31.3.2013 and reconciliation of total value added with profit before taxation, from the Profit and Loss Account of Addition Ltd. for the year ended on 31.3.2013:

		(₹ in '000)
Income:		
Sales	24,400	
Other Income	<u>508</u>	<u>24,908</u>
Expenditure:		
Operating cost	21,250	
Excise duty	1,110	
Interest on Bank Overdraft	75	
Interest on 9% Debenture	<u>1,200</u>	<u>23,635</u>

	(₹ in '000)
Profit before Depreciation	1,273
Depreciation	<u>(405)</u>
Profit before tax	868
Provision for tax	<u>(320)</u>
Profit after tax	548
Proposed Dividend	<u>(48)</u>
Retained Profit	<u>500</u>

The following additional information are given:

- (i) Sales represents net sales after adjusting discounts, returns and sales tax.
- (ii) Operating cost includes ₹ 82,50,000 as wages, salaries and other benefits to employees.
- (iii) Bank overdraft is temporary.

Economic Value Added

20. (a) Booming Ltd. provides you the following data:

No. of Equity Shares of ₹ 10 each	192 crores
No. of 10% Debentures of ₹ 100 each	?
Free Reserves	₹ 1440 crores
Capital Reserve	₹ 960 crores
Securities Premium	₹ 480 crores
Tax Rate	30%
Beta Factor	1.05
Market Rate of Return	14%

Risk Free Rate	10%
Debt-Equity Ratio	1 : 2

Compute the Economic Value Added where net operating profit after tax is ₹ 1848 crores.

Also explain the reason for the difference between the EVA and the MVA (Market Value Added).

Human Resource Accounting

- (b) From the following details, compute according to Lev and Schwartz (1971) model, the total value of human resources of the employee groups skilled and unskilled.

		Skilled	Unskilled
(i)	Annual average earning of an employee till the retirement age	₹ 50,000	₹ 30,000
(ii)	Age of retirement	65 years	62 years
(iii)	Discount rate	15%	15%
(iv)	No. of employees in the group	20	25
(v)	Average age	62 years	60 years

SUGGESTED ANSWERS / HINTS

- The question deals with the issue of Applicability of Accounting Standards to a non-corporate entity. For availment of the exemptions, first of all, it has to be seen that M/s Omega & Co. falls in which level of the non-corporate entities. Its classification will be done on the basis of the classification of non-corporate entities as prescribed by the ICAI. According to the ICAI, non-corporate entities can be classified under 3 levels viz Level I, Level II (SMEs) and Level III (SMEs).

If an entity whose turnover (excluding other income) exceeds rupees fifty crore in the immediately preceding accounting year, it does not fall under the category of Level I entities. Non-corporate entities which are not Level I entities but fall in any one or more of the following categories are classified as Level II entities:

- All commercial, industrial and business reporting entities, whose turnover (excluding other income) exceeds rupees one crore but does not exceed rupees fifty crore in the immediately preceding accounting year.
- All commercial, industrial and business reporting entities having borrowings (including public deposits) in excess of rupees one crore but not in excess of rupees ten crore at any time during the immediately preceding accounting year.

(iii) Holding and subsidiary entities of any one of the above.

As the turnover of M/s Omega & Co. is more than ₹ 1 crore, it falls under 1st criteria of Level II non-corporate entities as defined above. Even if its borrowings of ₹ 0.95 crores is less than ₹ 1 crores, it will be classified as Level II Entity. In this case, AS 3, AS 17, AS 21, AS 23, AS 27 will not be applicable to M/s Omega & Co. Relaxations from certain requirements in respect of AS 15, AS 19, AS 20, AS 25, AS 28 and AS 29 are also available to M/s Omega & Co.

2. (a) Although legal title has not been transferred, the economic reality and substance is that the rights and beneficial interest in the immovable property have been transferred. Therefore, recording of disposal by the transferor would in substance represent the transaction entered into.

In view of this, X Ltd. should record the sales and recognize the profit of ₹ 15 lakhs in its Statement of Profit & Loss. It should remove building account from its balance sheet. Further, in its 'Notes to Accounts', X Ltd. should disclose the following:

"Building has been sold and full consideration has been received and possession of the same has been handed over to the buyer. However, documentation and legal formalities are pending as on 31.3.2013."

(b) **Statement showing valuation of stock as on 31.3.2013**

	₹	₹
Stock as on 01.04.2012	28,500	
Less: Book value of abnormal stock (₹ 10,000 – ₹ 3,500)	<u>(6,500)</u>	22,000
Add: Purchases		1,52,500
Manufacturing Expenses		<u>30,000</u>
		2,04,500
Less: Cost of Sales:		
Sales as per Books	2,49,000	
Less: Sales of Abnormal item	<u>(9,000)</u>	
	2,40,000	
Less: G.P. @ 20%	<u>(48,000)</u>	<u>(1,92,000)</u>
Value of Stock as on 31 st March, 2013		<u>12,500</u>

(c) **Cash Flow Statement of Great Ltd.**

For the year ended 31st March, 2013

	₹	₹
Cash flows from operating activities		
Net profit before taxation	24,750	

Adjustments for:		
Depreciation of property, plant, and equipment	3,000	
Amortization of intangible assets	750	
Investment income	(4,500)	
Interest expense	<u>3,000</u>	
Operating profit before working capital changes	27,000	
Increase in accounts receivable	(3,750)	
Increase in inventories	(750)	
Decrease in accounts payable	<u>(11,250)</u>	
Cash provided by operations	11,250	
Income taxes paid	<u>(3,000)</u>	
Net cash from operating activities		8,250
Cash flows from investing activities		
Proceeds from sale of equipment	11,250	
Dividends received	<u>4,500</u>	
Net Cash from investing activities		15,750
Cash flows from financing activities		
Dividends paid	(18,000)	
Interest paid	<u>(3,000)</u>	
Net Cash used in financing activities		<u>(21,000)</u>
Net increase in cash and cash equivalents		3,000
Cash and cash equivalents at the beginning of the year		<u>1,500</u>
Cash and cash equivalents at the end of the year		<u>4,500</u>

- (d) As per para 8 of AS 4 "Contingencies and Events Occurring After the Balance Sheet Date, adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date.

In the given case, since Raj Ltd. was sued by a competitor for infringement of a trademark during the year 2012-13 for which the provision was also made by it, the decision of the Court on 18th May, 2013, for payment of the penalty will constitute as an adjusting event because it is an event occurred before approval of the financial statements. Therefore, Raj Ltd. should adjust the provision upward by ₹ 4 lakhs to reflect the award decreed by the Court to be paid by them to its competitor.

Had the judgment of the Court been delivered on 1st June, 2013, it would be considered as post reporting period i.e. event occurred after the approval of the financial statements. In that case, no adjustment in the financial statements of 2012-13 would have been required.

3. (a) As per para 8 of AS 7 'Construction Contracts', a group of contracts with a single customer, should be treated as a single construction contract when:
- (i) the group of contracts is negotiated as a single package;
 - (ii) the contracts are so closely interrelated that they are, in effect, part of a single project with an overall profit margin; and
 - (iii) the contracts are performed concurrently or in a continuous sequence.

Accordingly, in the given case, the two contracts should be combined and treated as a single contract since they meet all the three criteria stated above.

- (b) Para 9 of AS 9 'Revenue Recognition' states that where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, revenue recognition is postponed to the extent of uncertainty involved. Further it also states that when recognition of revenue is postponed due to effect of uncertainties, it is considered as revenue of the period in which it is properly recognized. In this case it may be assumed that liability of claim was not certain in the earlier periods i.e. in years 2009-10, 2010-11 and 2011-12. This is also evident from the fact that only ₹ 1,50,000 were collected against a claim of ₹ 2,00,000. So this transaction cannot be taken as a prior period item.

Since dealings with the Railways are an ordinary business activities for Sahara Ltd., it will not be treated as extraordinary item as per para 4.2 of AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies'. However, para 12 of AS 5 states that when items of income and expense within profit and loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of enterprises for the period, the nature and amount of such items should be disclosed separately. Accordingly, the nature and amount of this claim should be disclosed separately in the financial statements of Sahara Ltd. for the year ended 31st March, 2013.

- (c) Table showing computation of net loss on retirement of a revalued asset of Value Ltd.

Particulars	₹
Original cost	1,00,00,000
Less: SLM depreciation up to 4 th year	
$\left[\frac{1,00,00,000 - 2,50,000}{10} \right] \times 4$	<u>(39,00,000)</u>

Net book value at the end of 4th year or at the beginning of 5 th year	61,00,000
Add: Revaluation profit (credited to Revaluation Reserve)	<u>24,40,000</u>
Revised carrying amount	85,40,000
Revised residual value (2.5% of 85,40,000) = ₹ 2,13,500	
Less: Depreciation for 5 th , 6 th and 7 th years	
$\left(\frac{85,40,000 - 2,13,500}{6 \text{ years}} \right) \times 3 \text{ years}$	<u>(41,63,250)</u>
Net book value at the end of 7 th year or at the beginning of 8 th year	43,76,750
Net realizable value on date of retirement	<u>(3,80,000)</u>
Loss on retirement of plant	39,96,750
Less: Revaluation reserve	<u>(24,40,000)</u>
Net loss charged to Statement of Profit and Loss	<u>15,56,750</u>

4. (a) As per para 21 of AS 12, amount refundable in respect of a grant related to revenue should be applied first against any unamortised deferred credit remaining in respect of the grant. To the extent the amount refundable exceeds any such deferred credit, the amount should be charged to profit and loss statement.
- (i) In this case the grant refunded is ₹ 300 lakhs and balance in deferred income is ₹ 210 lakhs, therefore, ₹ 90 lakhs shall be charged to the profit and loss account for the year 2012-13. There will be no effect on the cost of the fixed asset and depreciation charge will be same as charged in the earlier years.
- (ii) As per para 21 of AS 12, the amount refundable in respect of grant which was related to specific fixed assets should be recorded by increasing the book value of the assets by the amount refundable. Where the book value of the asset is increased, depreciation on the revised book value should be provided prospectively over the residual useful life of the asset. Therefore, in this case the book value of the plant shall be increased by ₹ 300 lakhs. The increased cost of ₹ 300 lakhs of the plant should be amortised over 7 years (residual life). Depreciation charged during the year 2012-13 shall be $1200/10 + 300/7 = ₹ 162.86$ lakhs.
- (b) X Ltd. invested ₹ 600 lakhs in the equity shares of Y Ltd. Out of the same, the company intends to hold 50% shares for long term period i.e. ₹ 300 lakhs and remaining as temporary (current) investment i.e. ₹ 300 lakhs. Irrespective of the fact that investment has been held by X Ltd. only for 3 months (from 1.1.2012 to 31.3.2012), AS 13 lays emphasis on intention of the investor to classify the

investment as current or long term even though the long term investment may be readily marketable.

In the given situation, the realizable value of all such investments on 31.3.2012 became ₹ 200 lakhs i.e. ₹ 100 lakhs in respect of current investment and ₹ 100 lakhs in respect of long term investment.

As per AS 13, 'Accounting for Investment', the carrying amount for current investments is the lower of cost and fair value. In respect of current investments for which an active market exists, market value generally provides the best evidence of fair value.

Accordingly, the carrying value of investment held as temporary investment should be shown at realizable value i.e. at ₹ 100 lakhs. The reduction of ₹ 200 lakhs in the carrying value of current investment will be charged to the profit and loss account.

Standard further states that long-term investments are usually carried at cost. However, when there is a decline, other than temporary, in the value of long term investment, the carrying amount is reduced to recognise the decline.

Here, Y Ltd. lost a case of copyright which drastically reduced the realisable value of its shares to one third which is quite a substantial figure. Losing the case of copyright may affect the business and the performance of the company in long run. Accordingly, it will be appropriate to reduce the carrying amount of long term investment by ₹ 200 lakhs and show the investments at ₹ 100 lakhs, since the downfall in the value of shares is other than temporary. The reduction of ₹ 200 lakhs in the carrying value of long term investment will be charged to the Statement of profit and loss.

- (c) AS 11, The "Effects of Changes in Foreign Exchange Rates" provides that exchange differences attributable to monetary items should be taken to Profit and Loss account. In case the option under para 46A is exercised, the exchange differences arising on long-term foreign currency monetary items can be adjusted in the cost of the depreciable capital asset or in other cases parked in Foreign Currency Monetary Item Translation Difference Account and amortised.

Item 1. Sundry Debtors: This is a monetary item.

<i>Particulars</i>	<i>Foreign currency</i>	<i>Rate</i>	<i>Rupees</i>
Initial recognition	US \$12,919.90	38.70	5,00,000
Rate on B/S date		45.80	
Exchange Difference	US \$12,919.90	7.10	91,731
Gain or loss			Gain
Treatment			Credit P/L ₹ 91,731

Item 2. Long Term loan

Particulars	Foreign currency	Rate	Rupees
Initial recognition	US \$ 1,68,539.33	35.60	60,00,000
Rate on B/S date		45.90	
Exchange Difference	US \$ 1,68,539.33	10.30	17,35,955
Gain or loss			Loss
Treatment			Debit P/L ₹ 17,35,955 or transfer to FCMTD A/c and amortise

Item 3. Loan for acquisition of a depreciable capital asset

Particulars	Foreign currency	Rate	Rupees
Initial recognition	P.St. 15,923.57	62.80	10,00,000
Rate on B/S date		72.30	
Exchange Difference	P.St. 15,923.57	9.50	1,51,274
Gain or loss			Loss
Treatment			Debit P/L ₹ 1,51,274 or adjust in the cost of the asset and depreciate accordingly.

5. (a) (i) Computation of weighted average accumulated expenses

		₹
₹ 10,00,000 x 12 / 12	=	10,00,000
₹ 24,00,000 x 8 / 12	=	16,00,000
₹ 4,00,000 x 3 / 12	=	<u>1,00,000</u>
		<u>27,00,000</u>

(ii) Non-specific Borrowings

Non-specific Borrowings = Average accumulated capital expenses – Specific borrowings

$$= ₹ 27,00,000 - ₹ 8,00,000 = ₹ 19,00,000$$

(ii) Interest on average accumulated expenses

		₹
Specific borrowings ($\text{₹ } 8,00,000 \times 10\%$)	=	80,000
Non-specific borrowings ($\text{₹ } 19,00,000 \times 12\%$)	=	<u>2,28,000</u>
Amount of interest to be capitalized	=	<u>3,08,000</u>

(iii) Total expenses to be capitalized for Plant

		₹
Cost of plant ($10,00,000 + 24,00,000 + 4,00,000$)		38,00,000
Add: Amount of interest to be capitalised		<u>3,08,000</u>
Total cost of plant		<u>41,08,000</u>

- (b)** As per para 5 of AS 17 'Segment Reporting', enterprise revenue is revenue from sales to external customers as reported in the statement of profit and loss and segment revenue is the aggregate of:

- the portion of enterprise revenue that is directly attributable to a segment,
- the relevant portion of enterprise revenue that can be allocated on a reasonable basis to a segment, and
- revenue from transactions with other segments of the enterprise.

Further as per the definition segment revenue excludes:

- extraordinary items as defined in AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies;
- interest or dividend income, including interest earned on advances or loans to other segments unless the operations of the segment are primarily of a financial nature; and
- gains on sales of investments or on extinguishment of debt unless the operations of the segment are primarily of a financial nature.

Accordingly, other income should be included as part of the segment revenue if they do not fall under the exclusion definition and if it is essentially operating in nature. Other income will have to be analyzed into what is operating and non-operating, i.e. what belongs to be segment and what does not. Segment result is the difference between segment revenue and segment expenses and therefore includes income incidental to external turnover or the main activity of the segment. Export incentives are price subsidies for achieving exports in a fiercely competitive export market. Therefore they are indirectly a component of export turnover and should be included in segment revenue.

Non-operating interest should be excluded from segment revenue. However, interest received from customers due to delay in making payment is an operating income. Segment assets are those operating assets that are employed by a segment in its operating activities and that either are directly attributable to the segment or can be allocated to the segment on a reasonable basis. Since receivables are part of the segment asset. The related income should be included in segment revenue.

- (c) As per para 3(a) of AS 18 "Related Party Disclosures", enterprises that directly or indirectly through one or more intermediaries, control or are controlled by, or are under common control with the reporting enterprise are said to be in related party relationships.

Control is defined as to include substantial interest in voting power and the power to direct, by statute or agreement, the financial and/ or operating policies of the enterprise.

In the given case, Z Limited controls X Limited, due to holding subsidiary relationship. X Limited is a 50% co-venturer and accordingly Z Limited has the joint control over the joint venture XY through X Limited. Hence, transactions between Z Limited and the joint venture may be considered as related party transactions under AS 18.

6. (a) (i) Finance Lease.
 (ii) If it becomes certain at the inception of lease itself that the option will be exercised by the lessee it is a Finance Lease.
 (iii) It will still be classified as a finance lease, since substantial portion of the life of the asset is covered by the lease term.
 (iv) Where $X = Y$, or where X substantially equals Y , it is a finance lease.
 (v) Since the asset is procured only for the use of lessee, it is a finance lease.

(b) Number of Bonus shares issued as on 1.1.2013

On existing shares $(50,00,250 \times \frac{1}{2})$ 25,00,125 shares

On convertible debentures as per SEBI Guidelines on Bonus Issue

$(1,00,000 \text{ debentures} \times 10 \text{ shares} \times \frac{1}{2})$ 5,00,000 shares

Basic Earnings per share for the year 2012-13

$$\frac{\text{Net profit for the year ended 31.3.2013}}{\text{Weighted average number of equity share as on 31.3.2013}} = \frac{\text{₹ } 1,00,25,000}{(50,00,250 + 25,00,125 + 5,00,000)} = \text{₹ } 1.25$$

Adjusted earnings per share for the year 2011-12

$$= \frac{\text{₹ } 75,50,000}{(50,00,250 + 25,00,125 + 5,00,000)} = \text{₹ } 0.94$$

Diluted Earnings Per Share for the year 2012-13

Interest expense for the current year = ₹ 12,00,000

Tax relating to interest expense (30%) = ₹ 3,60,000

Adjusted net profit for the current year = [₹ 1,00,25,000 + {(12,00,000 - 3,60,000) × 3/12}]
= ₹ 1,02,35,000

Number of equity shares resulting from conversion of debentures

$$= 1,00,000 \times 10 \text{ shares} = 10,00,000$$

Number of equity shares used to compute diluted earnings per share

$$= 50,00,250 + 25,00,125 + 5,00,000 + (10,00,000 \times 3/12)$$

$$= 50,00,250 + 25,00,125 + 5,00,000 + 2,50,000$$

$$= 82,50,375 \text{ shares}$$

Diluted earnings per share = 1,02,35,000/82,50,375 = ₹ 1.24

Note: As per AS 20, bonus shares issued to existing shareholders and to convertible debenture holders (on conversion of debentures into shares) are an issue without consideration. Therefore, it is treated as if it had occurred prior to the beginning of the year 2011- 12, the earliest period reported.

(c) In the case of Company A, the following computations will be made:

2011-12

In this year, depreciation for both accounting and taxation purposes would be ₹ 25,000 (25 per cent of ₹ 1,00,000). Accordingly, no timing difference arises on this account.

2012-13

Depreciation for the year would ₹ 18,750 (25 per cent of ₹ 75,000) as per the books of account, while for tax purposes it would be ₹ 16,250 as sale proceeds of ₹ 10,000 would be reduced from the block of assets prior to the computation of depreciation. Accordingly, the following timing differences arise:

- (i) Depreciation for tax purposes is ₹ 16,250 and for accounting purposes ₹ 18,750 giving rise to a timing difference of ₹ 2,500.
- (ii) Profit on sale of fixed asset amounting to ₹ 7,188 (₹ 10,000 - ₹ 2,812 being the WDV of the asset as on 31st March, 2013) is recognized for accounting

purposes. However, for tax purposes this income is not considered. This will result in a timing difference of ₹ 7,188.

The net timing difference would be ₹ 4,688 by which the accounting income would exceed the taxable income, thus requiring creation of a deferred tax liability of ₹ 1,875 (4,688 X 0.4).

The difference of ₹ 4,688 would reverse in future years when depreciation for accounting purposes would be higher as compared to depreciation for tax purposes because depreciation for accounting purposes would be computed on higher carrying amount of fixed assets as compared to carrying amount of those block of assets for tax purposes. ₹ 4,688 is also the difference between the accounting book value and tax written down value of the assets as on 31st March, 2013 [i.e., assets for accounting purposes of ₹ 53,438 (75,000 – 18,750 – 2,812) less block of assets for tax purposes of ₹ 48,750 (75,000 - 10,000 - 16,250)].

7. (a) Yes. As per para 4 of AS 23 "Accounting for Investments in Associates in Consolidated Financial Statements", if the investor holds directly or indirectly through subsidiaries, 20% or more of voting power, he is said to have significant influence. In the given case, X Ltd., holds only 14% (directly and indirectly) of the shares of Y Ltd. Although it holds only 14%, it is said to have significant influence because its subsidiary Z Ltd. virtually participate in most of the policy making process of the company. As per para 5, significant influence can be evidenced by participating in policy decision making, therefore, X Ltd. has significant influence over Y Ltd.
- (b) Business enterprises frequently close facilities, abandon products or even product lines and reduce the size of their workforce in response to market forces. These kinds of terminations, generally, are not in themselves discontinuing operations unless they satisfy the definition criteria. By gradually reducing the size of operations in the product line of Fairness cream, as given in para 3 of AS 24 "Discontinuing Operations", the company has increased its scale of operations in vanishing cream. Such a change is a gradual or evolutionary, phasing out of a product line or class of services does not meet definition criteria in paragraph 3(a) of AS 24 namely, disposing of substantially in its entirety a component of the enterprise. Hence, this change over is not a discontinuing operation.
8. (a) As per para 36 of AS 25 "Interim Financial Reporting", revenues that are received seasonally or occasionally within a financial year should not be anticipated or deferred as of an interim date if anticipation or deferral would not be appropriate at the end of the enterprise's financial year. Therefore dividend income, extra-ordinary gain, and gain on sale of investment received during 3rd quarter should be recognised in the 3rd quarter only. Similarly, sales promotion expenses incurred in the 3rd quarter should also be charged in the 3rd quarter only.

Further, as per the standard, if there is change in the accounting policy within the current financial year, then such a change should be applied retrospectively by restating the financial statements of prior interim periods of the current financial year. The change in the method of depreciation or inventory valuation is a change in the accounting policy. Therefore, the prior interim periods' financial statements should be restated by applying the change in the method of valuation retrospectively.

Accordingly, the adjusted profit before tax for the 3rd quarter will be as follows:

Statement showing Adjusted Profit Before Tax for the third quarter

	(₹ in lakhs)
Profit before tax (as reported)	4
Add: Dividend income ₹ (4-1) lakhs	3
Excess depreciation charged in the 3 rd quarter, due to change in the method, should be applied retrospectively ₹ (12-3) lakhs	9
Extra ordinary gain ₹ (2-1) lakhs	1
Cumulative loss due to change in the method of inventory valuation should be applied retrospectively ₹ (3-2) lakhs	<u>1</u>
	18
Less: Sales promotion expenses (80% of ₹ 15 lakhs)	(12)
Gain on sale of investment (occasional gain should not be deferred)	<u>(5)</u>
Adjusted Profit before tax for the third quarter	<u>1</u>

- (b) Impairment loss is said to occur when the carrying amount is more than recoverable amount. Recoverable amount, in turn, is the higher of Net Selling Price and Value in Use. Based on this, the following determination is made. Para 8 of AS 28 'Impairment of Assets' states some minimum indications for assessing whether there can be any impairment of an asset. These are:
- (i) **Decline in Net Selling Price:** In the instant case, market price is indicated at ₹ 300 lakhs. This is lower than carrying amount i.e. ₹ 340 lakhs. Hence, there is an indication of impairment loss.
 - (ii) **Estimated remaining useful life of the asset:** Estimated remaining useful life of the asset has declined from 8 years to five years due to technological changes that have taken place. This change from eight to five years is considered as a "significant change in the useful life of asset". Therefore, there is an indication of impairment of assets
 - (iii) **Decline in market interest rates:** The decline in market interest rate from 16% to 15% does not indicate impairment.

(iv) **Higher carrying amount of the net assets to its market capitalization:**

Here, carrying amount of the asset to market capitalisation ratio is also favourable i.e. 0.80 (i.e., book value is 0.8, and market capitalisation is 1). Therefore, there is no indication of impairment.

Out of the above four parameters, two are unfavourable. More particularly, market price being lower by ₹ 40 lakhs is an important element. Hence, there is an indication of impairment of asset. It is advisable to review the adequacy of depreciation charge, and if this is readjusted to fall in line with the remaining useful life of five years, the impairment would be taken care automatically.

Where the useful life of a depreciable asset undergoes a change i.e. reduced, impairment is automatically taken care of since the unamortised amount is depreciated over the shorter remaining useful life resulting into higher depreciation amount. When higher depreciation amount is charged, the net book value of the asset shown in books is less.

In this case, annual depreciation charge would be ₹ 340 lakhs/5 = ₹ 68.00 lakhs and the revised net book value would be ₹ 272.00 lakhs (340-68). This is well below the market price, and the impairment is automatically taken care of.

9. (a) 1. Recognition- As per AS 29 a provision should be recognised if the following conditions are satisfied.

Condition -1	Condition -2	Condition -3
Present obligation is a result of past event	Outflow of the resources to settle the obligation is probable	Reliable estimate of the amount can be made.
VRS started in January 2012 and existed on the balance sheet date. As on the balance sheet date, nearly 200 employees had opted for the scheme evidencing the existence of a liability on the balance sheet date.	As and when the employees' applications are accepted, the outflow of resources to settle the obligation is probable. Also it is probable that the liability will increase, if more people opt for VRS.	Lumpsum payment is ₹ 250 lakhs and estimated payment is ₹ 1,500 lakhs (given).

2. **Treatment and Conclusion:** Since all the conditions for recognition of a Provision are satisfied, a Provision should be recognized for the year ending 31st March 2012. Hence, the treatment of the Company for not recognizing the provision violates AS 29 requirements.

(b) Table showing differences among AS (applicable in India), IFRS and US GAAP

<i>Topic</i>	<i>Accounting Standard</i>	<i>IFRS</i>	<i>US GAAP</i>
Property, plant and equipment	Historical cost is used. Revaluations are permitted, however, frequency of revaluation has not mentioned. On revaluation, an entire class of assets is revalued, or assets to be revalued are selected on systematic basis.	Historical cost or revalued amounts are used. On opting revaluation option, regular valuations of entire classes of assets are required.	Historical cost is used; revaluations are not permitted.
Purchase method-Capital Reserve	Negative goodwill is recorded in equity as capital reserve, which is not amortised to income. However, in case of an amalgamation, the fair value of intangible assets with no active market is reduced to the extent of capital reserve, if any, arising on the amalgamation.	The identification and measurement of acquiree's identifiable assets, liabilities and contingent liabilities are reassessed. Any excess remaining after reassessment is recognised in Income statement immediately.	Any remaining excess after reassessment is used to reduce proportionately the fair values assigned to non-current assets (with certain exceptions). Any excess is recognized in the income statement immediately as an extraordinary gain.

10. (1) 'Share Capital' and 'Reserves and Surplus' are required to be shown under the heading "Shareholders' funds", which have not been shown in the given balance sheet. Although it is a part of 'Equity and Liabilities' yet it must be shown under the head "Shareholders' Funds". The heading "Shareholders' Funds" is missing in the balance sheet given in the question.

- (2) Reserves & Surplus is showing zero balance, which is not correct since there is. Debit balance of Statement of Profit & Loss. This debit balance of Profit and Loss should be shown as a negative figure under the head 'Surplus'. The balance of 'Reserves and Surplus', after adjusting negative balance of surplus shall be shown under the head 'Reserves and Surplus' even if the resulting figure is in the negative. It should be noted that Profit and Loss Debit Balance is not a part of current assets rather debit balance of Statement of Profit and Loss shall be shown as a negative figure under the head 'Surplus' as per requirement of Revised Schedule VI.
- (3) As per Revised Schedule VI Employee Stock Option Outstanding A/c is part of Reserves and Surplus and should not be shown separately. Classification of Reserves and Surplus should be reflected in 'Notes to Accounts' for the same.
- (4) Share application money refundable shall be shown by way of note under the sub-heading "Other Current Liabilities". As this is refundable and not pending for allotment, hence it is not a part of equity.
- (5) Deferred Tax Liabilities has been correctly shown under Non-Current Liabilities. But Deferred tax assets and deferred tax liabilities, both, can not be shown in balance sheet because only the net balance of Deferred Tax Liabilities or Asset is to be shown as per para 29 of AS 22, Appropriate Ltd. should offset Deferred Tax Asset & Deferred Tax Liabilities and the break up of Deferred Tax Asset & Deferred Tax Liabilities into major components of the respective balance should be disclosed in 'Notes to Account'. Deferred Tax Asset shall be shown under Non-Current Asset. It should be the net balance of Deferred Tax Asset after adjusting the balance of deferred tax liability.
- (6) Under the main heading of Non-Current Assets, Fixed Assets are further classified as under:
 - (i) Tangible assets
 - (ii) Intangible assets
 - (iii) Capital work in Progress
 - (iv) Intangible assets under development.

Keeping in view the above, the Capital Work-in Progress shall be shown under Fixed Assets as Capital Work in Progress. The amount of Capital advances included in CWIP shall be disclosed under the sub-heading "Long term loans and advances" under the heading Non-Current Assets.

11. Calculation of Purchase consideration

	Ram Ltd.	Shyam Ltd.
<i>Purchase Consideration:</i>	₹	₹
Goodwill	1,60,000	60,000

Freehold property	2,10,000	1,20,000
Plant and Machinery	50,000	30,000
Motor vehicles	60,000	-
Stock	1,20,000	1,56,000
Debtors	1,64,000	-
Cash at Bank	<u>86,000</u>	<u>-</u>
	8,50,000	3,66,000
Less: Liabilities:		
6% Debentures (1,20,000 x 105%)	-	(1,26,000)
Sundry Creditors	<u>(1,50,000)</u>	<u>-</u>
Net Assets taken over	<u>7,00,000</u>	<u>2,40,000</u>
To be satisfied by issue of shares of Ram and Shyam Ltd. @ ₹10 each	70,000	24,000

Balance Sheet Ram & Shyam Ltd. as at 1st April, 2011

		Particulars	Note No.	Amount
				₹
		EQUITY AND LIABILITIES		
1		Shareholders' funds		
	(a)	Share capital	1	9,40,000
	(b)	Reserves and Surplus	2	6,000
2		Non-current liabilities		
	(a)	Long-term borrowings	3	1,20,000
3		Current liabilities		
	(a)	Trade payables		<u>1,50,000</u>
		Total		<u>12,16,000</u>
		ASSETS		
1		Non-current assets		
	(a)	Fixed assets		
	i	Tangible assets	4	4,70,000
	ii	Intangible assets	5	2,20,000
2		Current assets		
	(a)	Inventories (1,20,000+1,56,000)		2,76,000

(b)	Trade receivables		1,64,000
(c)	Cash and cash equivalents		<u>86,000</u>
	Total		<u>12,16,000</u>

Notes to accounts

		₹	₹
1. Share Capital			
Equity share capital			
94,000 shares of ₹10 each			9,40,000
2. Reserves and Surplus			
Securities Premium A/c (W.N.)			6,000
3. Long-term borrowings			
Secured			
6% Debentures			1,20,000
4. Tangible assets			
Freehold property			
Ram Ltd.	2,10,000		
Shyam Ltd.	<u>1,20,000</u>		3,30,000
Plant and Machinery			
Ram Ltd.	50,000		
Shyam Ltd.	<u>30,000</u>		80,000
Motor vehicles Ram Ltd.			<u>60,000</u>
			<u>4,70,000</u>
5. Intangible assets			
Goodwill			
Ram Ltd.	1,60,000		
Shyam Ltd.	<u>60,000</u>		2,20,000

In the books of Shyam Ltd.**Journal Entries**

		₹	₹
1.	Realisation A/c Dr. To Freehold Property	3,48,000	1,20,000

	To Plant and Machinery		30,000	
	To Stock		1,56,000	
	To Debtors		42,000	
	(Being all assets except cash transferred to Realisation Account)			
2.	6% Debentures A/c Dr.	1,20,000		
	Sundry Creditors A/c Dr.	64,000		
	To Realisation A/c		1,84,000	
	(Being all liabilities transferred to Realisation Account)			
3.	Equity Share Capital A/c Dr.	1,60,000		
	Profit and Loss A/c Dr.	40,000		
	To Realisation A/c		2,00,000	
	(Being equity transferred to equity shareholders account)			
4.	Ram and Shyam Ltd. Dr.	2,40,000		
	To Realisation A/c		2,40,000	
	(Being purchase consideration due)			
5.	Bank A/c Dr.	42,000		
	To Realisation A/c		42,000	
	(Being cash realized from debtors in full)			
6.	Realisation A/c Dr.	64,000		
	To Bank A/c		64,000	
	(Being payment made to creditors)			
7.	Shares in Ram and Shyam Ltd. Dr.	2,40,000		
	To Ram and Shyam Ltd.		2,40,000	
	(Being purchase consideration received in the form of shares of Ram and Shyam Ltd.)			
8.	Realisation A/c Dr.	54,000		
	To Equity shareholders A/c		54,000	
	(Being profit on Realisation account transferred to shareholders account)			
9.	Equity shareholders A/c Dr.	2,54,000		

To Shares in Ram and Shyam Ltd.	2,40,000
To Bank A/c	14,000
(Being final payment made to shareholders)	

Working Note:**Calculation of Securities Premium balance**

Debentures issued by Ram and Shyam Ltd. to Shyam Ltd. at 5% premium

Therefore, securities premium account will be credited with (₹ 1,20,000 x 5%) ₹ 6,000.

12. Consolidated Balance Sheet of A Ltd. and its subsidiaries as on 31.3.13

Particulars	Note No.	₹
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	2,00,000
(b) Reserves and Surplus	2	1,71,044
(2) Minority Interest [W.N.3]	3	65,918
(3) Current Liabilities		
(a) Trade payables	4	2,63,380
(b) Short term provisions	5	52,000
(c) Other current liabilities	6	1,18,000
Total		8,70,342
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
i. Tangible assets	7	2,65,000
ii. Intangible assets	8	49,592
(b) Non-current investments	9	10,400
(2) Current assets		
(a) Inventories	10	1,53,840
(b) Trade receivables	11	1,91,070
(c) Cash and cash equivalents	12	2,00,440
Total		8,70,342

Notes to Accounts

		₹	₹
1.	Share Capital		
	Equity Share Capital		2,00,000
2.	Reserves and surplus		
	Capital Reserve		
	A Ltd.	50,000	
	Add: Share of Capital Reserve (W.N.2B)	<u>5,440</u>	55,440
	Revenue Reserve		
	A Ltd.	99,540	
	Add: Share of Revenue Reserve (W.N.2B)	<u>16,064</u>	<u>1,15,604</u>
			<u>1,71,044</u>
3.	Minority Interest [W.N.3]		
	B Ltd.	43,709	
	C Ltd.	<u>22,209</u>	65,918
4.	Trade payables		
	A Ltd.	1,12,060	
	B Ltd.	73,130	
	C Ltd.	<u>78,190</u>	2,63,380
5.	Short term provisions		
	Provision for Taxation		
	A Ltd.	30,000	
	C Ltd.	<u>22,000</u>	52,000
6.	Other current liabilities		
	Proposed Dividend (W.N.5)		1,18,000
7.	Tangible assets		
	A Ltd.	1,35,000	
	B Ltd.	60,000	
	C Ltd.	<u>70,000</u>	2,65,000
8.	Intangible assets		
	Goodwill (W.N.4)		49,592
9.	Investments		
	A Ltd.	NIL	

	B Ltd. [1,50,000 – 1,49,600]	400	
	C Ltd.	<u>10,000</u>	10,400
10.	Inventories		
	A Ltd.	55,240	
	B Ltd.	36,840	
	C Ltd.	<u>61,760</u>	1,53,840
11.	Trade receivables (W.N.5)		1,91,070
12.	Cash and cash equivalents		
	A Ltd.	1,31,290	
	B Ltd.	16,540	
	C Ltd.	<u>52,610</u>	<u>2,00,440</u>

Working Notes:**1. Date and Percentage of holding**

	<i>A Ltd. in B Ltd.</i>	<i>B Ltd. in C Ltd.</i>
Date of acquisition 1	2009 (1)	2009
Date of acquisition 2	2010 (2)	
Date of Consolidation	31-3-2013	
% of Holding	$[(8,000 + 4,000)/15,000] = 80\%$	$[6,800/8,000] = 85\%$
Minority Interest	= 20%	= 15%

2. Analysis of Reserves & Surplus

	<i>Pre-acquisition</i>	<i>Post acquisition</i>	
		<i>Capital reserve</i>	<i>Revenue reserve</i>
	₹	₹	₹
A. Analysis of Reserves & Surplus of C Ltd.			
Capital Reserve	15,000	8,000	
Revenue Reserve	<u>30,500</u>	-	<u>14,560</u>
	<u>45,500</u>	<u>8,000</u>	<u>14,560</u>
Minority Interest (15%)	6,825	1,200	2,184
B Ltd. (85%)	38,675	6,800	12,376

B. Analysis of Reserves and Surplus of B Ltd.			
Revenue Reserve	40,000	-	9,370
Share of B Ltd. in C Ltd.	<u>-</u>	<u>6,800</u>	<u>12,376</u>
	40,000	6,800	21,746
Less: Minority Interest (20%)	<u>(8,000)</u>	<u>(1,360)</u>	<u>(4,349)</u>
	32,000	5,440	17,397
Capital portion in 2 nd acquisition (i.e. ₹ 5,000 x 4/15)	<u>1,333</u>	<u>-</u>	<u>(1,333)</u>
	<u>33,333</u>	<u>5,440</u>	<u>16,064</u>

(3) Minority Interest

	<i>B Ltd.</i>	<i>C Ltd</i>
	₹	₹
Share Capital	30,000	12,000
Pre-acquisition Capital Profit	8,000	6,825
Post acquisition Capital Reserve (Refer W.N.2)	1,360	1,200
Post acquisition Revenue Reserve	<u>4,349</u>	<u>2,184</u>
	<u>43,709</u>	<u>22,209</u>

(4) Cost of Control i.e. Goodwill/Capital Reserve

		₹
Investments:		
of B Ltd. in C Ltd. (6,800 x 22)	1,49,600	
of A Ltd. in B Ltd.	<u>1,60,000</u>	3,09,600
Less: Nominal Value of Equity Share Capital		
B Ltd.	1,20,000	
C Ltd.	68,000	
Capital Profit		
B Ltd. (W.N.2B)	33,333	
C Ltd. (W.N.2A)	<u>38,675</u>	<u>(2,60,008)</u>
Goodwill		<u>49,592</u>

(5) Elimination of Mutual Owings

		<i>Debtors</i> ₹	<i>Proposed Dividend</i> ₹
A Ltd.		1,10,070	1,00,000
B Ltd.		69,120	60,000
C Ltd.		<u>93,880</u>	<u>40,000</u>
		2,73,070	2,00,000
Less: Mutual Owings	60,000 x 80% = 48,000		
	40,000 x 85% = <u>34,000</u>	<u>(82,000)</u>	<u>(82,000)</u>
Balance in consolidated balance sheet		<u>1,91,070</u>	<u>1,18,000</u>

Note: The above solution has been done on the basis of direct approach.

13. Notes to Accounts for Consolidated Balance Sheet of H Ltd. as on 31st March, 2013 (An Extract)

		<i>As on 31st March, 2013</i>	<i>As on 31st March, 2012</i>
		₹ '000	₹ '000
1. Share Capital			
10 crore Equity Shares of ₹ 10 each fully paid up		10,00,000	10,00,000
2. Reserves and Surplus			
Profit & Loss A/c	2,43,175		
Less: Unrealised gain (W.N.5)	<u>(4,500)</u>	2,38,675	2,09,500
Investment Reserve A/c (9/40 of pre-acquisition profits)		<u>77,625</u>	<u>77,625</u>
		<u>3,16,300</u>	<u>2,87,125</u>
3 Non-current Investment			
In A Ltd. (Associate) at cost (including capital reserve ₹ 25,125)		1,42,500	1,42,500
Share of Profit / (loss)			
Post-acquisition		(18,225)	13,500
Pre-acquisition profits		<u>77,625</u>	<u>77,625</u>
		<u>2,01,900</u>	<u>2,33,625</u>

Working Notes:**1. Profit and Loss Account Balances**

	<i>H Ltd.</i>	<i>A Ltd.</i>
	₹ '000	₹ '000
Balance as on April 1, 2011	1,62,000	3,45,000
Add: Profit for 2011-12	<u>1,84,000</u>	<u>1,40,000</u>
	3,46,000	4,85,000
Less: Dividend, 15% and 20% respectively	<u>(1,50,000)</u>	<u>80,000</u>
Balances as on April 1, 2012	1,96,000	4,05,000
Add: Profit (Loss) for 2012-13	<u>2,65,400</u>	<u>(1,41,000)</u>
	4,61,400	2,64,000
Less: Dividend for 2012-13	<u>(2,00,000)</u>	<u>-</u>
Balance as on 31 st March, 2013	2,61,400	<u>2,64,000</u>
Less: Share of Net loss (W.N.2)	<u>(18,225)</u>	
	<u>2,43,175</u>	

2. Share of Profit/Loss of H Ltd. in A Ltd. (22.5%)

	31.3.12	31.2.13
	₹ '000	₹ '000
Post acquisition Profit/loss	1,40,000	(1,41,000)
Less: Dividend	(80,000)	-
	60,000	(1,41,000)
Share of H Ltd.	13,500	(31,725)
Adjustment of post acquisition profit of 2011-12 in 2012-13	-	13,500
	13,500	(18,225)

3. Goodwill / Capital Reserve on acquisition of shares of A Ltd.

	₹ '000
Investment	1,42,500
Less: Share capital	(90,000)
Pre-acquisition profit (3,45,000 x 22.5%)	(77,625)
Capital Reserve	25,125

4. Profit or Loss of H Ltd. after including share of profit of A Ltd. as on 31.3.2012

	₹'000
Balance as on 31.3.12	1,96,000
Add: Share of profit of A Ltd. (W.N.2)	13,500
	2,09,500

5. Unrealised gain on sale of plant

	₹'000
Profit on sale ₹ 80,000 thousand x 25%	20,000
Share of H Ltd. i.e. 22.5%	4,500

14. The above call option gives A Ltd. a contractual right to exchange cash of ₹ 5 for an equity share in another entity and will be exercised if the market value of the share exceeds ₹ 5 at the end of the 90 day period because it will be favourable to A Ltd., if it exercises the call option. Since A Ltd. stands to gain if the call option is exercised, the exchange is potentially favourable to the company. Therefore, the option is a derivative financial asset from the time the company becomes a party to the option contract.

15. Fair value under equity settlement = 250 shares x ₹ 68 = ₹ 17,000

Fair value under cash settlement = 200 shares x ₹ 70 = ₹ 14,000

So, fair value of equity component = ₹ 17,000 - ₹ 14,000 = ₹ 3,000

Fair value of liability component = ₹ 14,000

Fair value of liability component should be accounted for as per cash-settled employee share-based plan. Fair value of equity component should be accounted for as per equity-settled employee share-based payment plan.

Amounts to be recognised for liability component:

	Particulars	31.12.10	31.12.11	31.12.12
A	Fair value of share without restrictions	75	80	85
B	Closing provision required	5,000 [200 x 75 x 1 / 3]	10,667 [200 x 80 x 2 / 3]	17,000 [200 x 85 x 3 / 3]
C	Opening provision	0	5,000	10,667
D	Expense for the year (B - C)	5,000	5,667	6,333

Amounts to be recognised for equity component:

	Particulars	31.12.10	31.12.11	31.12.12
E	Cumulative expense to be	1,000	2,000	3,000

	recognised till date	[3,000 x 1/3]	[3,000 x 2/3]	[3,000 x 3/3]
F	Cumulative expense already recognised	0	1,000	2,000
G	Expense for the year (E - F)	1,000	1,000	1,000

Particulars	Debit (₹)	Credit (₹)
Year 31.12.10		
Employee compensation expense A/c Dr.	5,000	
To Provision for liability component of employee share-based payment plan A/c		5,000
(Being expense recognised in respect of liability component of the plan with cash alternative)		
Year 31.12.10		
Employee compensation expense A/c Dr.	1,000	
To Stock options outstanding A/c		1,000
(Being expense recognised in respect of equity component of the plan with cash alternative)		
Year 31.12.11		
Employee compensation expense A/c Dr.	5,667	
To Provision for liability component of employee share-based payment plan A/c		5,667
(Being expense recognised in respect of liability component of the plan with cash alternative)		
Year 31.12.11		
Employee compensation expense A/c Dr.	1,000	
To Stock options outstanding A/c		1,000
(Being expense recognised in respect of equity component of the plan with cash alternative)		
Year 31.12.12		
Employee compensation expense A/c Dr.	6,333	
To Provision for liability component of employee share-based payment plan A/c		6,333
(Being expense recognised in respect of liability component of the plan with cash alternative)		
Year 31.12.12		
Employee compensation expense A/c Dr.	1,000	

To Stock options outstanding A/c (Being expense recognised in respect of equity component of the plan with cash alternative)		1,000
Case (1) - When cash settlement is made:		
Provision for liability component of employee share-based payment plan A/c To Bank A/c (Being cash paid under the plan with cash alternative)	Dr. 17,000	17,000
Stock options outstanding A/c To General reserve A/c (Being balance in the equity account transferred to general reserve)	Dr. 3,000	3,000
Case (2) - When equity settlement is made:		
Stock options outstanding A/c Provision for liability component of employee share-based payment plan A/c To Share capital A/c To Securities premium A/c (Being shares issued under the plan on exercise of equity alternative)	Dr. 3,000 Dr. 17,000	2,500 17,500

16. (a) 1. Effect of foreign Exchange Rate Differences in Debtors (₹ '000s)

Year	2008	2009	2010	2011	2012
(a) Gain to be correctly considered					
(i) On restatement [Debtors × (Year end Rate – Entry Rate)]	750	930	12,915	(1,440)	(1,230)
(ii) On collection of proceeds [Debtors × (Year end Rate – Collection Rate)]	-	500	5,270	(2,835)	8,640
Total Profit to be considered (i) + (ii)	750	1,430	18,185	(4,275)	7,410
(b) Less: Gain wrongly considered [Debtors × (Collection rate – Entry rate)]	Nil	(1,250)	(6,200)	(10,080)	(7,200)
(c) Effect on Profit i.e. Increase/(Decrease)	750	180	11,985	(14,355)	210

2. Effect of differences in treatment of expenses and incomes (₹ 000s)

Year	2008	2009	2010	2011	2012
(a) Expenses: To be considered	87	14	25	54	
Actually considered		87	14	25	54
Net Effect on Profit i.e. Increase/(Decrease)	(87)	73	(11)	(29)	54
(b) Income: To be considered	12	35	8	68	
Actually considered		12	35	8	68
Net Effect on Profit i.e. Increase/(Decrease)	12	23	(27)	60	(68)
(c) Net Effect of the above on Profits (a) – (b)	(75)	96	(38)	31	(14)

3. Computation of Adjusted profits of past years (₹ '000s)

Year	2008	2009	2010	2011	2012
Net Profit after appropriation of dividend	19,10	18,50	22,40	20,15	25,25
Add: Proposed dividend at 20% of Capital	30,00	30,00	36,00	36,00	36,00
Tax expense for the year (See note below)	53,20	37,00	63,00	57,00	61,00
Net Profit before taxes	1,02,30	85,50	1,21,40	1,13,15	1,22,25
Adjust: Effect of change in Stock Valuation i.e. Reversal of LIFO basis	(1,21)	(1,31)	(1,42)	-	-
Implementation of FIFO basis	(15)	21	54		
Effect of change in method of depreciation i.e. WDV less SLM	(98)	(85)	(100)	(90)	-
Effect of Exchange Gain/Loss adjusted in Debtors (W.N.1)	7,50	1,80	11,985	(14,355)	210
Effect of adjustment of expenses and incomes (W.N. 2)	(75)	96	(38)	31	(14)
Adjusted Profits Before Tax	1,06,71	86,31	2,38,99	(30,99)	1,24,21

4. Computation of Future Maintainable Profits (₹ '000s)

a. Simple Average of past 5 years adjusted profits before tax = FMP before tax = $[(1,06,71 + 86,31 + 2,38,99 - 30,99 + 1,24,21) \div 5]$	1,05,04.60
b. Less: Tax Expense @ 34%	<u>(3,571.56)</u>
c. Future Maintainable Profit after tax for the purpose of valuation of goodwill	<u>6,933.04</u>

(b) Statement showing the Valuation of Shares on Balance Sheet basis

<i>Particulars</i>	<i>A Ltd.</i> ₹	<i>B Ltd.</i> ₹	<i>C Ltd.</i> ₹
A. Total Assets i.e. at Current Values:			
Tangible Fixed Assets	11,10,000	7,00,000	8,70,000
Investment in B Ltd. (4/5 of Net Assets i.e. ₹ 7,10,000)	5,68,000	-	-
Current Assets	2,10,000	2,40,000	3,90,000
	18,88,000	9,40,000	12,60,000
B. Outside liabilities:			
7% Debentures	3,00,000		
Trade Payables	2,80,000	1,80,000	2,10,000
Bank overdraft	1,00,000	50,000	-
	6,80,000	2,30,000	2,10,000
C. Net Assets [A - B]	12,08,000	7,10,000	10,50,000
D. No. of Shares	80,000	50,000	75,000
E. Book Value per share	15.10	14.20	14.00

Valuation of C Ltd.'s shares on yield basis

Estimated annual future profits	1,05,000
Less: 1/3 retained for Development	(35,000)
Distributable Profits	70,000
Earning Rate [(₹ 70,000 / ₹ 7,50,000) × 100]	9.33%
Normal Rate of Yield	8%

$$\text{Value per share} = \left[\frac{\text{Earning Rate}}{\text{Normal Rate}} \times \text{Paid up Value} \right] = \frac{9.33\%}{8\%} \times 10 = ₹ 11.67$$

Value taken as per agreement for exchange of shares between A Ltd. and C Ltd.

A Ltd.:

₹ 15.10 per share, being the amount of Balance Sheet value, higher than the quoted value of ₹ 14.00 per share.

C Ltd.:

₹ 14.00 per share being the amount of Balance Sheet value, higher than the yield value of ₹ 11.67 per share.

Statement of Settlement

	₹
Shares issued by A Ltd. to C Ltd. - 30,000 shares @ ₹ 15.10 per share	4,53,000
Shares issued by C Ltd. to A Ltd. - 25,000 shares @ ₹ 14.00 per share	<u>3,50,000</u>
Loan by A Ltd. to C Ltd.	<u>1,03,000</u>

17. (a) The net asset value of a mutual fund scheme is basically the Per Unit Market value of all the assets of the scheme.

Formula:

NAV = (Market Value of All Securities Held by Fund + Cash and Cash Equivalent Holdings by a fund – Fund Liabilities) / Total outstanding units of a Fund.

Net assets value is like a stock price which measures the value of single unit of a fund. At the time of investment in a particular scheme of mutual fund, it gives investors a factor to compare a fund's performance with market or industry benchmarks. However, once an investor invests in a fund at a particular NAV, that initial NAV becomes a sinking cost. Therefore, later on what matters is the change in NAV over a period i.e. if NAV increases with time then it implies that your investment is giving a higher or good return and you will earn at the time of selling that investment; reverse is the case in the vice versa situation.

(b) Calculation of Net Asset Value of a fund

	₹ in crores	
Total Assets:		
Investment (6,000 - 60 - 100)	5,840.00	
Add: Closing Cash Balance (Refer W.N.)	147.60	
Add: Interest for two months due to be received	<u>97.33</u>	6,084.93
$(5,840 \times 10\% \times \frac{2}{12})$		
Less: Outstanding Management Expenses		<u>(5.00)</u>
Total value of the fund		<u>6,079.93</u>

$$\text{No. of Units} = \frac{\text{₹ 6,000 crore}}{1,000} = 6 \text{ crore units}$$

$$\text{NAV per unit} = \frac{\text{₹ 6079.93 crore}}{6 \text{ crore}} = \text{₹ 1,013.32 per unit}$$

Working Note:**Calculation of year-end cash/bank balance of the fund**

	₹ in crores
Cash received during the year for the fund	
Sale of units	6,000
Add: Interest for 3 quarters on investment (5,840 x 10% x $\frac{9}{12}$)	<u>438</u>
	6,438
Less: Underwriting commission	60
Management expenses paid in cash	40
Investment	5,840
Dividend paid (438 x 80%)	350.40 (6,290.40)
	<u>147.60</u>

18. (i) Quoted current investments for each category shall be valued at cost or market value, whichever is lower. For this purpose, the investments in each category shall be considered scrip-wise and the cost and market value aggregated for all investments in each category. If the aggregate market value for the category is less than the aggregate cost for that category, the net depreciation shall be provided for or charged to the profit and loss account. If the aggregate market value for the category exceeds the aggregate cost for the category, the net appreciation shall be ignored. Therefore, depreciation of a particular item of investments can be adjusted within the same category of investments.

- (ii) Value of Investments as on 31.3.2013

Type of Investment	Valuation Principle	Value ₹ in lakhs
Equity Shares (Aggregated)	Lower of cost or market Value	406.50
Mutual Funds	NAV (Market value, assumed)	54.00
Government securities	Cost	135.00
		<u>595.50</u>

As per para 14 of AS 13 "Accounting for Investments", the carrying amount for current investments is the lower of cost and market price. Sometimes, the concern of an enterprise may be with the value of a category of related current investments and not with each individual investment, and accordingly, the investments may be computed at the lower of cost and market value computed category-wise.

- (iii) Inter category adjustments of appreciation and depreciation in values of investments cannot be done. It is not possible to offset depreciation in investment in

mutual funds against appreciation of the value of investments in equity shares and Government securities.

19. Value Added Statement of Addition Ltd.

	₹ in '000		%
Sales		24,400	
Less: Operating cost - Cost of bought in material & services (₹ 21,250 – ₹ 8,250)	13,000		
Excise duty	1,110		
Interest on bank overdraft	75	(14,185)	
Value added by trading and manufacturing activities		10,215	
Add: Other income		508	
Total value added		10,723	
Application of value added			
<i>To pay Employees:</i>			
Wages, salaries and other benefits		8,250	76.94
<i>To pay Government :</i>			
Corporate tax		320	2.98
<i>To pay Providers of capital:</i>			
Interest on 9% debentures	1,200		
Dividends	48	1,248	11.64
<i>To provide for Maintenance and expansion of the company:</i>			
Depreciation	405		
Retained profit	500	905	8.44
		10,723	100.00
Reconciliation			
Profit before tax		868	
Depreciation		405	
Wages, salaries and other benefits		8,250	
Debenture interest		1,200	
		10,723	

20. (a) Computation of Economic Value Added

Particulars	₹ in crores
Net Operating Profit After Tax (NOPAT)	1,848.00
Less: Cost of Operating Capital employed (COCE) (11.8% of ₹ 7,200 crores)	(849.60)
Economic Value Added	998.40

Working Notes:

- Cost of Equity = Risk Free Rate + Beta factor x (Market Rate - Risk Free Rate)
 $= 10 + 1.05 (14 - 10) = 14.2\%$
- Debt-Equity Ratio = Long-term Debt/Equity
 $0.5 = \text{Long-term Debt} / (1,920 + 1,440 + 960 + 480)$
Long-term Debt = $4,800 \times 0.5 = 2,400$
- Cost of Debt = Interest Rate (1 - Tax Rate) = $10\% (1 - .30) = 7\%$
- Capital Employed = (Share Capital + Reserve and Surplus) + Long-term Debt
 $= (1,920 + 1,440 + 960 + 480) + 2,400 = 7,200$
- $$WACC = \left[\left(\frac{4,800}{7,200} \times 14.2 \right) + \left(\frac{2,400}{7,200} \times 7 \right) \right] = 11.80\%$$

Reason for the difference between EVA and Market Value Added

- The Market Value of a firm reflects not only the Expected EVA of Assets in place but also the Expected EVA from Future Projects.
 - MVA of a company is the Net Present Value (NPV) of all its future EVAs.
 - EVA reflects only the current earning efficiency of the company.
- (b) According to Lev and Schwartz, the value of human capital embodied in a person of age is the present value of his remaining future earnings from employment. Their valuation model for a discrete income stream is given by the following formula:

$$V = \sum_{t=\tau}^t \frac{I(t)}{(1+r)^{t-\tau}}$$

Where,

$V_{\square}$ = the human capital value of a person $\square$ years old.

$I(t)$ = the person's annual earnings up to retirement.

r = a discount rate specific to the person.

t = retirement age.

Value of skilled employees:

$$= \frac{50,000}{(1+0.15)^{(65-62)}} + \frac{50,000}{(1+0.15)^{(65-63)}} + \frac{50,000}{(1+0.15)^{(65-64)}}$$

$$₹ 32,875.81 + ₹ 37,807.18 + ₹ 43,478.26 = ₹ 1, 14,161.25$$

Total value of skilled employees is ₹ 1, 14,161.25 × 20 = ₹ 22,83,225.

Value of unskilled employees

$$= \frac{30,000}{(1+0.15)^{(62-60)}} + \frac{30,000}{(1+0.15)^{(62-61)}} = \frac{30,000}{(1+0.15)^2} + \frac{30,000}{(1+0.15)}$$

$$= ₹ 22,684.31 + ₹ 26,086.96 = ₹ 48,771.27$$

Total value of the unskilled employees = ₹ 48,771.27 × 25 = ₹ 12,19,282

Total value of human resources (skilled and unskilled) = ₹ 22,83,225 + ₹ 12,19,282
= ₹ 35,02,507.