Test Series: March, 2018

MOCK TEST PAPER

FINAL (OLD): GROUP – I

PAPER – 1: FINANCIAL REPORTING

*Question No. **1** is compulsory.*

*Answer any **five** questions from the remaining **six** questions.*

Wherever necessary suitable assumptions may be made and disclosed by way of a note.

Working Notes should form part of the answer.

(Time allowed: 3 hours) **(Maximum Marks: 100)**

1. (a) Top-notch Equity Investments Ltd., wants to re-classify its investments in accordance with AS 13.

(i) Long term investments in Company A, costing ₹ 17 lakhs are to be re-classified as current. The company had reduced the value of these investments to ₹13 lakhs to recognize a permanent decline in value. The fair value on date of transfer is ₹13.6 lakhs.

(ii) Long term investments in Company B, costing ₹ 14 lakhs are to be re-classified as current. The fair value on date of transfer is ₹ 16 lakhs and book value is ₹ 14 lakhs.

(iii) Current investment in Company C, costing ₹ 20 lakhs are to be re-classified as long term as the company wants to retain them. The market value on date of transfer is ₹ 24 lakhs.

(iv) Current investment in Company D, costing ₹ 30 lakhs are to be re-classified as long term. The market value on date of transfer is ₹ 28 lakhs.

Advise the company, as per the guidance given in the standard, on reclassification of its investment and the amount at which the same has to be recognized.

(b) Mobility Ltd. is in the business of manufacture of Passenger cars and commercial vehicles. The company is working on a strategic plan to shift from the Passenger car segment over the coming 5 years. However, no specific plans have been drawn up for sale of neither the division nor its assets. As part of its plan, it will reduce the production of passenger cars by 20% annually. It also plans to commence another new factory for the manufacture of commercial vehicles and transfer its excess employees in a phased manner.

(i) You are required to comment if mere gradual phasing out in itself can be considered as a 'Discontinuing Operation' within the meaning of AS 24.

(ii) If the company passes a resolution to sell some of the assets in the passenger car division and also to transfer few other assets of the passenger car division to the new factory, does this trigger the application of AS 24?

(iii) Would your answer to the above be different if the company resolves to sell the assets of the Passenger Car Division in a phased but time bound manner?

(c) Saheli Publications publishes a monthly magazine on the 15^{th} of every month. It sells advertising space in the magazine to advertisers on the terms of 80% sale value payable in advance and the balance within 30 days of the release of the publication. The sale of space for the March, 2018 issue was made in February, 2018. The magazine was published on its scheduled date. It received ₹2,40,000 on 10.3.2018 and ₹60,000 on 10.4.2018 for the March 2018 issue.

Discuss in the context of AS 9 the amount of revenue to be recognized and the treatment of the amount received from advertisers for the year ending 31.3.2018. What will be the treatment if the publication is delayed till 2.4.2018?

(d) An equipment is leased for 3 years and its useful life is 5 years. Both the cost and the fair value of the equipment are ₹ 3,00,000. The amount will be paid in 3 instalments and at the termination of lease lessor will get back the equipment. The unguaranteed residual value at the end of 3 years is ₹ 40,000. The (internal rate of return) IRR of the investment is 10%. The present value of annuity factor of Re. 1 due at the end of 3rd year at 10% IRR is 2.4868. The present value of Re. 1 due at the end of 3rd year at 10% rate of interest is 0.7513.

(i) State with reason whether the lease constitutes finance lease.

(ii) Calculate unearned finance income. ***(4 x 5 = 20 Marks)***

2. AB Ltd. and CD Ltd. two private companies, decide to amalgamate their business into a new holding company EF Ltd., which was incorporated on 1st August, 2017 with an authorised capital of ₹ 40,00,000 in equity shares of ₹ 10 each. The new company plans to commence operations on 1st October, 2017.

From the information given below, and assuming that all transactions are completed by 31st March, 2018, you are required to:

(a) Prepare Projected Statement of Profit & Loss of EF Ltd. for the six months ending 31st March, 2018.

(b) Prepare Projected Balance Sheet of EF Ltd. as on 31st March, 2018.

(c) Show the computation of number of shares to be issued to the former shareholders of AB Ltd. and CD Ltd.

Information

(1) EF Ltd. will acquire the whole of the Equity share capital of AB Ltd. and CD Ltd. by issuing its fully paid own shares.

(2) The number of shares to be issued is to be calculated by multiplying the future annual maintainable profits available to the Equity shareholders in each of the two companies by agreed price earnings ratios.

The following information is relevant:

	AB Ltd. (₹)	*CD Ltd. (₹)*
Equity Shares of ₹ 10 each fully paid	10,00,000	4,00,000
8% Cumulative Preference shares		1,00,000
10% Debentures	2,00,000	
Future annual maintainable pre tax profits (before interest/dividend)	2,30,000	1,12,000
Price Earnings Ratio	10 times	8 times

(3) Shares in the holding company are to be issued to the shareholders in subsidiary companies at a premium of 20% and thereafter these shares will be marketed on the stock exchange.

(4) It is expected that the Group profits of the new company in 2017-18 will be at least ₹ 4,50,000 but that will be required as additional working capital to facilitate expansion. Accordingly, it is planned to make a further issue of 37,500 Equity shares to the public for cash at a premium of 30% on 1st February, 2018. The new shares will not rank for interest/dividend to be paid on 31st March, 2018.

(5) Out of the proceeds of the right issue EF Ltd. will advance ₹ 2,50,000 to AB Ltd. and ₹ 2,00,000 to CD Ltd. on 1st February, 2018 for working capital. These advances will carry interest @ 15% p.a. to be paid monthly.

(6) Preliminary Expenses are estimated at ₹ 8,000 and Administrative Expenses for the half-year ended 31st March, 2018 at ₹ 16,000 but this expenditure will be covered by temporary overdraft facility. It is estimated that Interest on Bank Overdraft cost will be ₹ 1,600 in the first six months.

(7) A provision for ₹ 7,500 should be made for Directors Fee for the half-year.

(8) On 31st March, 2018, Interim Dividends on Equity Shares, will be paid by AB Ltd. @ 5%, by CD Ltd. @ 4.4% and by EF Ltd. @ 4%.

(9) Income tax is to be taken @ 50% for calculation of number of shares. However, ignore tax effect while preparing Projected Statement of Profit and Loss. ***(16 Marks)***

3. Following are the summarized Balance Sheets of A Ltd., B. Ltd. & C Ltd., as on 31.3.2018:

Liabilities	*A Ltd.*	*B Ltd.*	*C Ltd.*	*Assets*	*A Ltd.*	*B Ltd.*	*C Ltd.*
	₹	₹	₹		₹	₹	₹
Share capital of ₹ 10 each	5,00,000	3,00,000	2,00,000	Fixed Assets Investment	2,00,000	1,50,000	1,20,000
General Reserves	80,000	60,000	50,000	24,000 Shares in			
Profit & Loss A/c	1,00,000	80,000	60,000	B Ltd.	2,50,000		
Sundry Creditors B Ltd. Balance	70,000	20,000	30,000 40,000	6,000 Shares in C Ltd.	80,000		
C Ltd. Balance	1,20,000			12,000 shares in C Ltd.		1,60,000	
				Stock in trade	1,00,000	60,000	60,000
				Debtors	1,50,000	40,000	80,000
				C Ltd. Balance		30,000	
				A Ltd. Balance			90,000
				Cash and Bank Balance	90,000	20,000	30,000
	8,70,000	4,60,000	3,80,000		8,70,000	4,60,000	3,80,000

Other Information:

(a) All the investments were made on 1.8.2017 on which date the provisions were as follows:

	B Ltd. (₹)	*C Ltd. (₹)*
General Reserves	30,000	15,000
Profit & Loss Account	50,000	25,000

(b) In December 2017, B Ltd. invoiced goods to A Ltd. for ₹ 80,000 at cost plus 25%. The closing stock of A Ltd. includes such goods valued at ₹ 10,000.

(c) C Ltd. sold to B Ltd. a machinery costing ₹ 27,000 at a profit of 25% on selling price on 31.12.2017. Depreciation at 10% per annum was provided by B Ltd. on this equipment.

(d) Debtors of A Ltd. include ₹ 12,000 being the amount due from B Ltd.

You are required to prepare the Consolidated Balance Sheet of the Group (following direct approach) as on 31.3.2018 as per Schedule III to the Companies Act, 2013. ***(16 Marks)***

4. (a) You are provided with the following details in respect of ABC Limited:

   (i) 10,000 equity shares of nominal value of ₹ 10 each were issued on 31st March, 2014;

   (ii) Exercise price of equity shares granted under ESOP was ₹ 160 per share;

   (iii) Market price of share was ₹ 400 each on the date of the grant;

   (iv) Vesting of shares was in the ratio of 30%, 60% and 100% after 1 year, 2 year and 3 year respectively from the date of grant;

   (v) Vested options can be exercised up to 1 year from the date of vesting;

   (vi) The number of shares expired and exercised are as under:

	Years ending		
Particulars	**31.03.2015**	**31.03.2016**	**31.03.2017**
Vested Options Lapsed during the year	-	200	600
Unvested Options Lapsed during the year	400	600	1,000
Options Exercised during the year		2,500	2,000

Estimated unvested options lapsed were same as actual lapses of unvested options.

From the above details you are required to calculate:

   (i) Employee Compensation Expense for the year ending 31st March, 2015, 31st March, 2016 and 31st March, 2017

   (ii) Balance of Employee Stock Option Outstanding Account as on 31st March, 2015, 31st March, 2016 and 31st March, 2017

(b) A Ltd has made a security deposit whose details are described below. Make necessary journal entries for accounting of the deposit. Assume market interest rate for a deposit for similar period to be 12% per annum.

Particulars	**Details**
Date of Security Deposit (Starting Date)	1-Apr-20X1
Date of Security Deposit (Finishing Date)	31-Mar-20X6
Description	Lease
Total Lease Period	5 years
Discount rate	12.00%
Security deposit	10,00,000
Present value annuity factor	0.567427

(10 + 6 = 16 Marks)

5 (a) Calculate the NAV of a Mutual Fund Scheme from the information given below:

At the beginning of the year:

Number of units outstanding	1 Crore units of ₹ 10 each
Investment at cost	₹ 10 crores (Market Value ₹ 16 crores)
Outstanding Liabilities	₹ 5 crores

Other Information:

(1) Additional 20 lakhs units were sold during the year at ₹ 24.

(2) No additional investments were made during the year and as at the year end, 50% of the investment at year beginning were quoted at 80% of the book value.

(3) 10% of the investments had witnessed a permanent fall of 10% below cost.

(4) The balance investments were quoted at ` 13.60 crores.

(5) Outstanding liabilities towards custodian charges, salaries and commission etc. applicable to the scheme were 1 crore.

(b) Synergy Ltd. furnishes the following Profit and Loss A/c:

Profit and Loss A/c for the year ended 31st March, 2018

Income	Notes	₹ ('000)
Turnover	1	29,872
Other Income		1,042
		30,914
Expenditure		
Operating expenses	2	26,741
Interest on 8% Debenture		987
Interest on Cash Credit	3	151
GST		1,952
		29,831
Profit before depreciation		1,083
Less: Depreciation		342
Profit before tax		741
Provision for tax	4	376
Profit after tax		365
Less: Transfer to Fixed Assets Replacement Reserve		65
		300
Less: Dividend paid		125
Retained Profit		175

Notes:

(1) Turnover is based on invoice value and net of GST.

(2) Salaries, wages and other employee benefits amounting to ₹ 14,761 ('000) are included in operating expenses.

(3) Cash Credit represents a temporary source of finance. It has not been considered as a part of capital.

(4) Transfer of ₹ 54 ('000) to the credit of deferred tax account is included in provision for tax.

Prepare value added statement for the year ended 31st March, 2018 and reconcile total value added with profit before taxation. ***(8 + 8 = 16 Marks)***

6. Following is the Balance Sheet of Suvarn Ltd. as on 31st March, 2018:

Liabilities	₹	*Assets*	₹
50,000 Equity shares of ₹ 10 each	5,00,000	Building	3,50,000
2,500, 12% Preference shares of ₹ 100 each	2,50,000	Plant and Machinery	4,30,000
Profit & Loss A/c	2,20,000	Patents	80,000
15% Debentures	1,20,000	Sundry debtors	2,00,000
General Reserve	1,80,000	Stock in trade	2,90,000
Creditors	1,50,000	Cash at Bank	70,000
	14,20,000		14,20,000

Buildings & Plant and Machinery were acquired many years ago and should be considered as worth of ₹ 5,00,000 and ₹ 6,30,000 respectively.

The Profits for the last five years were as follows:

Year	*Profit (before tax)* ₹
2013-14	1,80,000
2014-15	2,50,000
2015-16	60,000
2016-17	3,00,000
2017-18	3,50,000

The company paid a remuneration of ₹ 50,000 p.a. to the managerial personnel, but in future it will be paying ₹ 75,000, the increase having been sanctioned by the Government. During 2015-16, there was a prolonged strike, resulting in low profits. There has been no substantial change in the capital employed. The company has paid a dividend of 12 percent on equity shares consistently and proposes to stick to this rate in the foreseeable future. In the class of business to which the company belongs, the dividend rates have been fluctuating and the asset backing of an equity share is about 2 times. Equity shares with an average dividend of 15% sell at par. The company is anxious to provide funds for replacement of assets when due, for which it is proposed to make 20% provision on PAT. Assume future tax rate to be 40%. Calculate the value of an equity share of Suvarn Ltd. on yield basis.

(16 Marks)

7. Answer any four of the following:

(a) A Ltd. purchased 1,00,000 MT at₹ 100 each of raw material and introduced it in the production process and get 85,000 MT as output. Normal wastage is 5%. In the process, company incurred the following expenses:

Direct Labour	₹ 10,00,000
Direct Variable Overheads	₹ 1,00,000
Direct Fixed Overheads (Including interest ₹ 40,625)	₹ 1,00,000

Of the above 80,000 MT was sold during the year and remaining 5,000 MT remained in closing inventory. Due to fall in demand in market the selling price for the finished goods on the closing day was estimated to be ₹ 105 per MT. Calculate the value of closing inventory.

(b) Happy Ltd. provides you the following data to calculate Economic Value Added (EVA):

30 crores Equity Shares of ₹ 10 each	
1 crores, 15% Preference Shares of ₹ 100 each	
8 crores, 15% Debentures of ₹ 100 each	
Tax Rate	30%
Beta Factor	1.5
Market Rate of Return	15.5%
Equity Market Risk Premium	9%
Financial Leverage	1.5 times
Immovable Property (held as Investment)	₹ 100 crores

(c) ABC Ltd. has set up its business in a designated backward area which entitles the company to receive from the Government of India a subsidy of 20% of the cost of investment. Having fulfilled all the conditions under the scheme, the company on its investment of ₹ 10 crore in capital assets, received ₹ 2 crore from the Government in January, 2018 (accounting period being 2017-2018). The company wants to treat this receipt as an item of revenue and thereby reduce the losses on profit and loss account for the year ended 31st March, 2018.

Keeping in view the relevant Accounting Standard, discuss whether this action is justified or not.

(d) In May, 2004, XYZ Ltd. took a bank loan to be used specifically for the construction of a new factory building. The construction was completed in January, 2018 and the building was put to its use immediately thereafter. Interest on the actual amount used for construction of the building till its completion was ₹ 8 lakhs, whereas the total interest payable to the bank on the loan for the period till 31^{st} March, 2018 amounted to ₹ 10 lakhs.

Can ₹ 10 lakhs be treated as part of the cost of factory building and thus be capitalized on the plea that the loan was specifically taken for the construction of factory building?

(e) A company with a turnover of ₹ 250 crores and an annual advertising budget of ₹ 2 crore had taken up the marketing of a new product. It was estimated that the company would have a turnover of ₹ 25 crores from the new product. The company had debited to its Profit and Loss account the total expenditure of ₹ 2 crore incurred on extensive special initial advertisement campaign for the new product.

Is the procedure adopted by the company correct? ***(4 x 4 =16 Marks)***

MOCK TEST PAPER

FINAL (OLD): GROUP – I

PAPER – 1: FINANCIAL REPORTING

SUGGESTED ANSWERS/HINTS

1. (a) As per AS 13 'Accounting for Investments', where long-term investments are reclassified as current investments, transfers are made at the lower of cost and carrying amount at the date of transfer.

And where investments are reclassified from current to long term, transfers are made at lower of cost and fair value on the date of transfer.

Accordingly, the re-classification will be done on the following basis:

(i) In this case, carrying amount of investment on the date of transfer is less than the cost; hence this re-classified current investment should be carried at ₹13 lakhs in the books.

(ii) The carrying / book value of the long term investment is same as cost i.e. ₹ 14 lakhs. Hence this long term investment will be reclassified as current investment at book value of ₹ 14 lakhs only.

(iii) In this case, reclassification of current investment into long-term investments will be made at ₹ 20 lakhs as cost is less than its market value of ₹ 24 lakhs.

(iv) In this case, market value is ₹ 28 lakhs which is lower than the cost of ₹ 30 lakhs. The reclassification of current investment as long-term investments will be made at ₹ 28 lakhs.

(b) Mere gradual phasing is not considered as discontinuing operation as defined under para 3 of AS 24, 'Discontinuing Operation'.

Examples of activities that do not necessarily satisfy criterion of the definition, but that might do so in combination with other circumstances, include:

(1) Gradual or evolutionary phasing out of a product line or class of service.

(2) Shifting of some production or marketing activities for a particular line of business from one location to another and

(3) Closing of a facility to achieve productivity improvements or other cost savings.

A Reportable business segment or geographical segment as defined in AS 17, would normally satisfy criteria (b) of the definition. However, other criterias would not be satisfied.

Hence, in view of the above the answers are:

(i) No. The companys' strategic plan has no final approval from the board through a resolution and no specific time bound activities like shifting of Assets and employees and above all the new segment commercial vehicle production line and factory has started.

(ii) No. The resolution is salient about stoppage of the Car segment in definite time period. Though, some assets sales and transfer proposal was passed through a resolution to the new factory, closure road map and new segment starting road map is missing. Hence, AS 24 will not be applicable.

(iii) Yes. Phased and time bound programme resolved in the board clearly indicates the closure of the passenger car segment in a definite time frame and clear road map. Hence, this action will attract AS 24 compliances.

(c) As per para 12 of AS 9 'Revenue Recognition', 'in a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method, whichever relates the revenue to the work accomplished'.

In the given case, income accrues when the related advertisement appears before public. The advertisement service would be considered as performed on the day the advertisement is seen by public and hence revenue is recognized on that date. In this case, it is 15.03.2018, the date of publication of the magazine.

Hence, ₹ 3,00,000 (₹ 2,40,000 + ₹ 60,000) is recognized as income in March, 2018. The terms of payment are not relevant for considering the date on which revenue is to be recognized.

₹ 60,000 is treated as amount due from advertisers as on 31.03.2018 and ₹ 2,40,000 will be treated as payment received against the sale.

However, if the publication is delayed till 02.04.2018 revenue recognition will also be delayed till the advertisements get published in the magazine. In that case revenue of ₹ 3,00,000 will be recognized for the year ended 31.03.2019 after the magazine is published on 02.04.2018. The amount received from sale of advertising space on 10.03.2018 of ₹ 2,40,000 will be considered as an advance from advertisers for the year ended 31st March, 2018.

(d) (i) Present value of unguaranteed residual value = ₹ 40,000 × 0.7513 = ₹ 30,052

Present value of lease payments = ₹ 3,00,000 – ₹ 30,052 = ₹ 2,69,948.

The present value of lease payments being 89.98% $\left(\frac{2,69,948}{3,00,000}\times 100\right)$ of the fair value, i.e. being a substantial portion thereof, the lease constitutes a finance lease.

(ii) Annual lease payments = $\frac{₹\ 2,69,948}{2.4868}$ = ₹ 1,08,552 (approx.)

Calculation of unearned finance income

	₹
Gross investment in the lease [(₹ 1,08,552 × 3) + ₹ 40,000]	3,65,656
Less: Cost of the equipment	(3,00,000)
Unearned finance income	65,656

Note: - In the above solution, annual lease payment has been determined on the basis that the present value of lease payments plus residual value is equal to the fair value (cost) of the asset.

2. (a) Projected Profit and Loss Account of EF Ltd. for the period ending 31st March, 2018

Particulars	₹
Total Revenue	
Dividend Income [50,000 + 17,600]	67,600
Interest Income	11,250
	78,850
Less: Expenses	
Finance Costs (Interest on Bank Overdraft)	(1,600)
Other Expenses [Directors Fee (7,500) + Administrative Expenses (16,000) + Preliminary expenses (8,000)]	(31,500)
Profit before tax	45,750

(b) Projected Balance Sheet of EF Ltd. as on 31st March, 2018

	Particulars	Note No.	(₹)
I.	Equity and Liabilities		
	(1) Shareholders' Funds		
	(a) Share Capital	1	15,70,000
	(b) Reserves and Surplus	2	3,49,450
	(2) Non-Current Liabilities		
	(3) Current Liabilities		
	(a) Other Current Liabilities	3	23,500
	Total		19,42,950
II.	Assets		
	(1) Non-Current Assets		
	Non-Current Investments	4	14,34,000
	(2) Current Assets		
	(a) Cash and Cash Equivalents (W.N.1)		58,950
	(b) Other Current Assets		4,50,000
	Total		19,42,950

Notes to Accounts:

	Particulars		*(₹)*
1.	**Share Capital**		
	Authorised share capital		
	4,00,000 Equity shares of ₹ 10 each		40,00,000
	Issued share capital		
	1,57,000 Equity Shares of ₹ 10 each		15,70,000
	(Of the above 1,19,500 shares were issued for consideration other than cash)		
2.	**Reserves and Surplus**		
	Securities Premium [2,39,000 + 1,12,500]		3,51,500
	Profit & Loss Account	45,750	
	Less: Interim dividend (₹ 11,95,000 x 4%)	(47,800)	(2,050)
			3,49,450
3.	**Other Current Liabilities**		
	Bank Overdraft	16,000	
	Directors Fee	7,500	23,500
4.	**Non-current investment**		
	Investment in shares of AB Ltd. @ ₹ 12	10,50,000	
	Investment in shares of CD Ltd. @ ₹ 12	3,84,000	14,34,000

(c) Computation of Number of Shares to be issued to former shareholders

Particulars	*AB Ltd.*	*CD Ltd.*
	₹	₹
Future Maintainable EBIT	2,30,000	1,12,000
Less: Interest on Debentures	(20,000)	-
	2,10,000	1,1,2,000
Less: Income tax @ 50%	(1,05,000)	(56,000)
Profit after tax	1,05,000	56,000
Less: Preference Dividend	-	(8,000)
Profit to Equity Shareholders	1,05,000	48,000
PE Ratio	10	8
Capitalised Earning	10,50,000	3,84,000
Number of shares to be exchanged in EF Ltd. @ ₹ 12 (including Premium of ₹ 2 each)	87,500	32,000

Working Note:

Bank Account

Particulars	₹	*Particulars*	₹
To Equity Share Capital A/c	3,75,000	By Preliminary Expenses	8,000
To Securities Premium A/c	1,12,500	By Interest on Bank Overdraft	1,600
To Dividends from AB Ltd.	50,000	By Advance to AB Ltd.	2,50,000
To Dividends from CD Ltd.	17,600	By Advance to CD Ltd.	2,00,000
To Interest Income	11,250	By Interim Dividend	47,800
		By Balance c/d (Bal. fig.)	58,950
	5,66,350		5,66,350

3. Consolidated Balance Sheet of A Ltd. and its subsidiaries B Ltd. and C Ltd. as at 31st March 2018

Particulars	*Note No.*	₹
I. Equity and Liabilities		
Shareholder's funds		
a. Share capital	1	5,00,000
b. Reserves and surplus	2	3,03,103
Minority Interest (96,000+30,122)		1,26,122
Current liabilities		
(a) Trade payables	3	1,08,000
(b) Other current liabilities	4	40,000
Total		10,77,225
II. Assets		
Non-current assets		
(a) Fixed assets		

	Tangible assets	5	4,61,225
(b)	Non-current investment		-
	Current Assets		
(a)	Inventories	6	2,18,000
(b)	Trade receivable	7	2,58,000
(c)	Cash and Cash equivalents	8	1,40,000
	Total		10,77,225

Notes to Financial Statements

S. No.	*Particulars*	*Amount (₹)*	*Amount (₹)*
1.	**Share capital**		
	Issued, subscribed and paid up 50,000 equity shares of ₹ 10 each fully paid up		5,00,000
2.	**Reserves and Surplus**		
	Capital reserves (W.N.3)	30,000	
	Other reserves (W.N.7)	1,31,300	
	Profit & Loss account (W.N.6)	1,41,803	3,03,103
3.	**Trade Payables**		
	Sundry Creditors of A Ltd.	70,000	
	B Ltd.	20,000	
	C Ltd.	30,000	
		1,20,000	
	Less: Mutual Owings	(12,000)	1,08,000
4.	**Other Current liabilities**		
	Due to B Ltd. (40,000 – 30,000)	10,000	
	Due to C Ltd. (1,20,000 – 90,000)	30,000	40,000
5.	**Tangible assets**		
	A Ltd.	2,00,000	
	B Ltd.	1,50,000	
	C Ltd.	1,20,000	
		4,70,000	
	Less: Unrealised profit on equipment	(8,775)	4,61,225
6.	**Inventories**		
	A Ltd.	1,00,000	
	B Ltd.	60,000	
	C Ltd.	60,000	
		2,20,000	
	Less: Unrealised profit	(2,000)	2,18,000
7.	**Trade Receivable**		
	A Ltd.	1,50,000	

	B Ltd.	40,000	
	C Ltd.	80,000	
		2,70,000	
	Less: Mutual Owings	(12,000)	2,58,000
8.	**Cash and Cash Equivalents**		
	A Ltd.	90,000	
	B Ltd.	20,000	
	C Ltd.	30,000	1,40,000

Working Notes:

1. **Statement of analysis of profits of C Ltd.**

	Capital Profit	*Revenue reserve*	*Revenue profit*
	₹	₹	₹
General Reserve on 1.8.2017	15,000		
Profit and loss A/c on 1.8.2017	25,000		
Increase in reserve		35,000	
Increase in profit			35,000
	40,000	35,000	35,000
Less: Minority Interest (10%)	(4,000)	(3,500)	(3,500)
	36,000	31,500	31,500
Share of A Ltd. (30%)	12,000	10,500	10,500
Share of B Ltd. (60%)	24,000	21,000	21,000

2. **Statement of analysis of profits of B Ltd.**

	Capital Profit	*Revenue reserve*	*Revenue profit*
	₹	₹	₹
General Reserve on 1.8.2017	30,000		
Profit and loss A/c on 1.8.2017	50,000		
Increase in reserve		30,000	
Increase in profit			30,000
	80,000	30,000	30,000
Add: Share in C Ltd. (direct approach)	-	21,000	21,000
	80,000	51,000	51,000
Less: Minority interest (20%)	(16,000)	(10,200)	(10,200)
Share of A Ltd.	64,000	40,800	40,800

3. **Statement of cost of control**

	₹	₹	₹
Investment in B Ltd.			2,50,000
Investment in C Ltd.		(80,000 +1,60,000)	2,40,000
			4,90,000

Less: Paid up value of investments			
In B Ltd.	2,40,000		
In C Ltd.	1,80,000	4,20,000	
Capital Profit			
In B Ltd.	64,000		
In C Ltd. (12,000+24,000)	36,000	1,00,000	(5,20,000)
Capital reserve			30,000

4. Statement of Minority Interest

	B Ltd. (20%) ₹	C Ltd. (10%) ₹
Share capital	60,000	20,000
Capital profit	16,000	4,000
Revenue reserve	10,200	3,500
Revenue profit	10,200	3,500
Total	96,400	31,000
Less: Unrealised profit on Stock {20% of (10,000/125 x 25)}	(400)	
Unrealised profit on Machinery (10% of 8,775)	______	(878)
	96,000	30,122

5. Statement showing unrealised profit on equipment sale

	₹
Cost	27,000
Profit	9,000
Selling price	36,000
Unrealized profit = Total unrealised Profit – Depreciation thereon = [9,000 - (9,000 x 10% x 3/12)]	8,775

6. Statement showing Consolidated Profit and Loss Account

	₹
A Ltd.	1,00,000
Share in B Ltd.	40,800
Share in C Ltd.	10,500
	1,51,300
Less: Unrealised profit on machinery (90% of 8,775)	(7,897)
	1,43,403
Less: Unrealised profit on stock {80% of (10,000 / 125 x 25)}	(1,600)
	1,41,803

7. Statement showing consolidated reserves

	₹
A Ltd.	80,000
Share in B Ltd.	40,800

Share in C Ltd.	10,500
	1,31,300

4. (a) (i) Calculation of Employee Compensation Expense for the Year ended 31st March 2015, 31st March 2016 and 31st March, 2017

(Refer Working Note)

Vesting Date	Cost to be recognized in the year ending on 31st March		
as on 31st March	2015	2016	2017
Lot I	6,24,000		
Lot II	2,88,000	2,88,000	
Lot III	2,40,000	2,40,000	2,40,000
Cost for the year	11,52,000	5,28,000	2,40,000
Cumulative cost	11,52,000	16,80,000	19,20,000

(ii) Balance of ESOP Outstanding Account as on 31st March 2015, 31st March 2016 and 31st March, 2017

	Total	2015	2016	2017
ESOS outstanding A/c at the end of 1st year	11,52,000	11,52,000		
Less: Vested Options lapsed during year (200 x 240)	(48,000)			
Less: Vested Options exercised during year (2,500 x 240)	(6,00,000)			
Add: ESOP credited in the 2nd year	5,28,000			
ESOP outstanding A/c at the end of 2nd year	10,32,000		10,32,000	
Less: Vested options lapsed (600 x 240)	(1,44,000)			
Less: Vested options exercised (2,000 x 240)	(4,80,000)			
Add: ESOP credited in the 3rd year	2,40,000			
ESOP outstanding at the end of 3rd year	6,48,000			6,48,000

Working Note:

Determination of number of options expected to vest under each group

Vesting Date (Year-end) 31st March		Shares expected to vest	Value per Shares (₹) (400 – 160)	Compensation Expense (₹)
2015	(10,000 shares x 30%) - 400 shares	2,600 shares	240	6,24,000
2016	(10,000 shares x 30%) - 600 shares	2,400 shares	240	5,76,000

2017	(10,000 shares x 40%) - 1,000 shares	3,000 shares	240	7,20,000
				19,20,000

Total compensation expense of ₹ 19,20,000, determined at the grant date, is attributed to 3 years.

Note: In the absence of estimated figures regarding lapse of unvested options, it is assumed that actual lapses were in accordance with the estimation.

(b) The above security deposit is an interest free deposit redeemable at the end of lease term for ₹ 10,00,000. Hence, this involves collection of contractual cash flows and shall be accounted at amortised cost.

Upon initial measurement –

Particulars	Details
Security deposit (A)	10,00,000
Total Lease Period	5 years
Discount rate	12.00%
Present value annuity factor	0.567427
Present value of deposit at beginning (B)	5,67,427
Prepaid lease payment at beginning (A-B)	4,32,573

Journal Entries

Particulars		Amount	Amount
		₹	₹
Security deposit A/c	Dr.	5,67,427	
Prepaid expenses A/c	Dr.	4,32,573	
To Bank A/c			10,00,000

Subsequently, every annual reporting year, interest income shall be accrued @ 12% per annum and prepaid expenses shall be amortised on straight line basis over the lease term.

Year 1

Particulars		Amount	Amount
		₹	₹
Security deposit A/c (5,67,427 x 12%)	Dr.	68,091	
To Interest income A/c			68,091
Rent expense A/c (4,32,573 / 5 years)	Dr.	86,515	
To Prepaid expenses A/c			86,515

At the end of 5 years, the security deposit shall accrue to ₹ 10,00,000 and prepaid expenses shall be fully amortised. Journal entry for realisation of security deposit–

Particulars		*Amount (₹)*	*Amount (₹)*
Bank A/c	Dr.	10,00,000	
To Security deposit A/c			10,00,000

5. (a) Calculation of NAV of a Mutual Fund Scheme

Units as at the end of the year		*Units in Crores*
Number of units at the beginning of the year		1.00
Add: Units issued during the year		0.20
Units as at end of the year		1.20
Net Asset Value of the scheme		*₹ in crores*
Market value of Investments	(50% of ₹ 10 crores) x 80%	4.00
	10% x ₹ 10 crores - (10% below cost)	0.90
	Balance Investment at Market Price	13.60
Total Market Value		18.50
Less: Mutual fund scheme liabilities		(1.00)
Net asset value of the scheme		17.50
NAV per Unit= B/A=	₹ 17.50 crore/1.2 crore	₹ 14.58

(b) Synergy Ltd.

Value Added Statement for the year ended 31st March, 2018

	₹ ('000)	*₹ ('000)*	%
Turnover		29,872	
Less: Cost of bought in materials and services:			
Operating expenses (26,741 –14,761)	11,980		
GST	1,952		
Interest on Cash Credit	151	14,083	
Value added by manufacturing and trading activities		15,789	
Add: Other income		1,042	
Total value added		16,831	
Application of value added:			
To Pay to employees:			
Salaries, wages and other employee benefits		14,761	87.70
To Pay to Government:			
Corporation tax (376 – 54)		322	1.91
To Pay to providers of capital:			
Interest on 8% Debentures	987		
Dividends	125	1,112	6.61
To Provide for maintenance and expansion of the company:			
Depreciation	342		
Fixed Assets Replacement Reserve	65		

Deferred Tax Account	54		
Retained Profit	175	636	3.78
		16,831	100

Note: Deferred tax account could alternatively be shown as an item 'To pay to government'.

Reconciliation between total value added and profit before taxation

	₹ ('000)	₹ ('000)
Profit before tax		741
Add back: Depreciation	342	
Wages, salaries and other benefits	14,761	
Debenture interest	987	16,090
Total Value Added		16,831

6. Calculation of value per share on yield basis (Earnings Capitalisation Method)

Particulars	
Earnings available to equity shareholders (W.N.1)	₹ 1,01,040
Normal Rate of Return (W.N.3)	14.25%
Value of business	₹ 7,09,053
Number of equity shares outstanding	50,000
Value per share	**14.18**

Working Notes:

1. Computation of FMP available for distribution

a. Weighted average profits

Year	*Profit before tax*	*Weight*	*Product*
2013-14	1,80,000	1	1,80,000
2014-15	2,50,000	2	5,00,000
2016-17	3,00,000	3	9,00,000
2017-18	3,50,000	4	14,00,000
		10	**29,80,000**

Note: Profit of the year 2015-16 has not been considered, because it is a year of strike (Abnormal operation).

	₹
Weighted average profit = $\frac{29,80,000}{10}$	2,98,000
Less: Increase in managerial remuneration	(25,000)
PBT	2,73,000
Tax @ 40%	(1,09,200)
PAT	1,63,800

Less: Provision for replacement of fixed assets (₹ 1,63,800 x 20%)	(32,760)
	1,31,040
Less: Dividend for preference shares (₹ 2,50,000 x 12%)	(30,000)
Earnings available for distribution	1,01,040

2. Ascertainment of NRR criteria as applicable to Suvarn Ltd.

(A) Asset backing:

Particulars		₹
Total assets as per balance sheet		14,20,000
Add: Increase in the value of building	1,50,000	
Increase in the value of plant & machinery	2,00,000	3,50,000
Total		17,70,000
Less: Outside liabilities and preference share capital		
i. Sundry creditors	1,50,000	
ii. 15% debentures	1,20,000	
iii. 12% Preference share capital	2,50,000	(5,20,000)
Assets backing for equity share capital (a-b)		12,50,000
Equity share capital		5,00,000
Asset backing		2.5 times

(B) Dividend Rates:

Dividend rates have been fluctuating in the industry while Suvarn Ltd. has constant dividend rates.

3. Computation of adjusted Normal Rate of Return as applicable to Suvarn Ltd.

Particulars	*Asset backing*	*Dividend rates*
Industry standard	2 times	fluctuating
Suvarn Ltd.	2.5 times	constant
Degree of Variance from standard	+25%	N.A.
Impact on risk & consequent adjustment to NRR	↓	↓
Quantum of Adjustment to NRR (assuming 100% variance=1% change)	-0.25%	-0.50% (say)

Adjusted NRR = 15%-0.25%-0.50%=14.25%.

7. (a) Calculation of cost for closing inventory

Particulars	₹
Cost of Purchase (1,00,000 x 100)	1,00,00,000
Direct Labour	10,00,000
Variable Overhead	1,00,000

Fixed Overhead $\frac{(1,00,000 - 40,625)}{95,000}$	59,375
Cost of Production for normal output i.e. 95,000 MT	1,11,59,375
Cost of closing inventory per unit (1,11,59,375/95,000)	₹ 117.467 (approx)
Net Realisable Value per unit	₹ 105

Since, net realisable value is less than cost, closing inventory will be valued at ₹ 105. Therefore, closing inventory is ₹ 5,25,000 (5,000 x 105).

Note: Abnormal wastage of 10,000 MT i.e.10,000 MT x ₹ 117.467 = ₹ 11,74,670 will be separately accounted for in the books.

(b) Computation of EVA

Particulars	*₹ in crores*
Net Operating Profit after Tax (NOPAT)	252.00
Less: Cost of Operating Capital Employed (COCE) [13.25% of ₹ 1,100]	(145.75)
Economic Value Added (EVA)	106.25

Working Notes:

1. Cost of Debt = Interest Rate (1 – Tax Rate) = 15% (1 - 30) = 10.50%
2. Cost of Preference Share = 15%
3. Cost of Equity = Risk Free Rate + (Beta x Equity Market Risk Premium)

   = (15.5% - 9%) + (1.5 x 9) = 20%
4. Total Capital Employed = 800 + 100 + 300 = 1,200 crores
5. WACC $= \left(\frac{800}{1,200} \times 10.50\%\right) + \left(\frac{100}{1,200} \times 15\%\right) + \left(\frac{300}{1,200} \times 20\%\right)$

   = 7% + 1.25% + 5% = 13.25%
6. Financial Leverage = $\frac{\text{EBIT}}{\text{EBIT -Interest}} = \frac{\text{EBIT}}{\text{EBIT} - 120}$ = 1.5

   EBIT = (120 x 1.5)/0.5 = 360
7. Net Operating Profit after Tax = 360 - 30% of 360 = 252
8. Operating Capital Employed = Total Capital Employed - Non-Operating Capital Employed

   = 1,200 -100 = 1,100 crores

(c) As per para 10 of AS 12 'Accounting for Government Grants', where the government grants are of the nature of promoters' contribution, i.e. they are given with reference to the total investment in an undertaking or by way of contribution towards its total capital outlay (for example, central investment subsidy scheme) and no repayment is ordinarily expected in respect thereof, the grants are treated as capital reserve which can be neither distributed as dividend nor considered as deferred income.

In the given case, the subsidy received is neither in relation to specific fixed asset nor in relation to revenue. Thus, it is inappropriate to recognise government grants in the profit and loss statement, since they are not earned but represent an incentive provided by government without related costs. The correct treatment is to credit the subsidy to capital reserve. Therefore, the accounting treatment followed by the company is not proper.

(d) As per para 19 of AS 16 'Borrowing Costs', capitalization of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete. Therefore, interest on the amount that has been used for the construction of the building upto the date of completion (January, 2018) i.e. ₹ 8 lakhs alone can be capitalized. It cannot be extended to ₹ 10 lakhs.

(e) With the introduction of AS 26 'Intangible Assets', the concept of deferred revenue expenditure no longer prevails except in respect of a very few items, such as ancillary costs on borrowings, shares issue expenses etc. AS 26 does not permit the capitalization of expenses incurred on advertising or brand promotion, etc. Thus, the accounting treatment by the company of debiting the entire advertising expenditure of ₹ 2 crore to the P & L account of the year is correct.