PAPER –1: FINANCIAL REPORTING

PART – I : RELEVANT AMENDMENTS, NOTIFICATIONS AND ANNOUNCEMENTS

A. Applicable for November, 2015 examination

1. Revised Regulatory Framework for NBFCs

RBI vide notification no. DNBR (PD)CC.No. 002/03.10.001/2014-15 dated November 10, 2014 has revised the regulatory provisions relating to the functioning of NBFCs (except primary dealers) in India. The changes introduced to the regulatory framework are delineated below.

a. Requirement of Minimum NOF of ₹ 200 lakh

Although the requirement of minimum NOF stands at ₹ 200 lakh, the minimum NOF for companies that were already in existence before April 21, 1999 was retained at ₹ 25 lakh. but the revised regulatory framework has mandated all NBFCs to attain a minimum NOF of ₹ 200 lakh by the end of March 2017, as per the milestones given below:

- ₹ 100 lakh by the end of March 2016
- ₹ 200 lakh by the end of March 2017

b. Deposit Acceptance

As per extant NBFCs Acceptance of Public Deposit (Reserve Bank) Directions, 1998, an unrated Asset Finance Company (AFC) having NOF of ₹ 25 lakh or more, complying with all the prudential norms and maintaining capital adequacy ratio of not less than fifteen per cent, is allowed to accept or renew public deposits not exceeding one and half times of its NOF or up to ₹ 10 crore, whichever is lower. AFCs which are rated and complying with all the prudential regulations are allowed to accept deposits up to 4 times of their NOF.

In order to harmonise the deposit acceptance regulations across all deposit taking NBFCs (NBFCs-D), existing unrated AFCs shall have to get themselves rated by March 31, 2016. Those AFCs that do not get an investment grade rating by March 31, 2016, will not be allowed to renew existing or accept fresh deposits thereafter. Further, it has also been decided to harmonise the limit for acceptance of deposits across the sector by reducing the same for rated AFCs from 4 times to 1.5 times of NOF, with effect from the date of this circular.

c. Systemic Significance

The threshold for defining systemic significance for NBFCs-ND has been revised in the light of the overall increase in the growth of the NBFC sector with asset size of ₹ 500 crore and above as per the last audited balance sheet.

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With this revision in the threshold for systemic significance, NBFCs-ND shall be categorized into two broad categories viz.,

i. NBFCs-ND (those with assets of less than ₹ 500 crore) and

ii. BFCs-ND-SI (those with assets of ₹ 500 crore and above).

d. Multiple NBFCs

NBFCs that are part of a corporate group or are floated by a common set of promoters will not be viewed on a standalone basis. The total assets of NBFCs in a group including deposit taking NBFCs, if any, will be aggregated to determine if such consolidation falls within the asset sizes of the above two categories.

e. Prudential Norms

The regulatory approach in respect of NBFCs-ND with an asset size of less than ₹ 500 crore will be as under:

(i) They shall not be subjected to any regulation either prudential or conduct of business regulations if they have not accessed any public funds and do not have a customer interface.

(ii) Those having customer interface will be subjected only to conduct of business regulations if they are not accessing public funds.

(iii) Those accepting public funds will be subjected to limited prudential regulations but not conduct of business regulations if they have no customer interface.

(iv) Where both public funds are accepted and customer interface exist, such companies will be subjected both to limited prudential regulations and conduct of business regulations.

(v) Registration under Section 45 IA of the RBI Act will be mandatory.

All NBFCs-ND with assets of ₹ 500 crore and above, irrespective of whether they have accessed public funds or not, shall comply with prudential regulations as applicable to NBFCs-ND-SI. They shall also comply with conduct of business regulations if customer interface exists.

Prudential Regulations Applicable to NBFCs-ND with Assets less than ₹ 500 crore

NBFCs-ND with asset size of less than ₹ 500 crore are exempted from the requirement of maintaining CRAR and complying with Credit Concentration Norms.

A leverage ratio of 7 is being introduced for all such NBFCs-ND to link their asset growth with the capital they hold. For this purpose, leverage ratio is defined as Total Outside Liabilities / Owned Funds.

Prudential Regulations Applicable to NBFCs-ND-SI (asset of ₹ 500 crore and above) and all NBFCs-D

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Tier 1 Capital

All NBFCs-ND which have an asset size of ₹ 500 crore and above, and all NBFCs-D, shall maintain minimum Tier 1 Capital of 10%. The compliance to the revised Tier 1 capital will be phased in as follows:

- 8.5% by end of March 2016.
- 10% by end of March 2017.

Asset Classification

In the interest of harmonisation, the asset classification norms for NBFCs-ND-SI and NBFCs-D are being brought in line with that of banks, in a phased manner, as given below.

Lease Rental and Hire-Purchase Assets shall become NPA:

i. if they become overdue for 9 months (currently 12 months) for the financial year ending March 31, 2016;

ii. if overdue for 6 months for the financial year ending March 31, 2017; and

iii. if overdue for 3 months for the financial year ending March 31, 2018 and thereafter.

Assets other than Lease Rental and Hire-Purchase Assets shall become NPA:

i. if they become overdue for 5 months for the financial year ending March 31, 2016;

ii. if overdue for 4 months for the financial year ending March 31, 2017; and

iii. if overdue for 3 months for the financial year ending March 31, 2018 and thereafter.

For all loan and hire-purchase and lease assets, sub-standard asset would mean:

i. an asset that has been classified as NPA for a period not exceeding 16 months (currently 18 months) for the financial year ending March 31, 2016;

ii. an asset that has been classified as NPA for a period not exceeding 14 months for the financial year ending March 31, 2017; and

iii. an asset that has been classified as NPA for a period not exceeding 12 months for the financial year ending March 31, 2018 and thereafter.

For all loan and hire-purchase and lease assets, doubtful asset would mean:

i. an asset that has remained sub-standard for a period exceeding 16 months (currently 18 months) for the financial year ending March 31, 2016;

ii. an asset that has remained sub-standard for a period exceeding 14 months for the financial year ending March 31, 2017; and

iii. an asset that has remained sub-standard for a period exceeding 12 months for the financial year ending March 31, 2018 and thereafter.

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For the existing loans, a one-time adjustment of the repayment schedule, which shall not amount to restructuring will, however, be permitted.

Provisioning for Standard Assets

The provision for standard assets for NBFCs-ND-SI and for all NBFCs-D has being increased to 0.40% (at present 0.25%). The compliance to the revised norm will be phased in as given below:

- 0.30% by the end of March 2016
- 0.35% by the end of March 2017
- 0.40% by the end of March 2018

Note: The revisions brought through this circular shall be applicable to NBFCs-MFI and registered Core Investment Companies also except wherever in conflict with the provision of Non-Banking Financial Company- Micro Finance Institutions (Reserve Bank) Directions, 2011 and Core Investment Companies (Reserve Bank) Directions, 2011 respectively, in which case the Directions ibid will be followed.

For a complete text of the circular please refer to the link: http://rbi.org.in/scripts/NotificationUser.aspx?Id=9327&Mode=0

2. Dividend Distribution Tax

(a) With effect from 1st Oct, 2014 dividend and income distribution tax is leviable on gross dividend / income and not on the net dividend / income distributed to shareholders and unit holders as per Income- tax Act, 1961.

(b) The rate of DDT is fifteen per cent (excluding surcharge of 12% plus secondary and higher education cess is (2+1) 3%).

3. Amendment to Schedule VII to the Companies Act, 2013

The Central Government vide Notification No. G.S.R. 568(E) dated 6th August, 2014,made amendments in Schedule VII to the Companies Act, 2013,wherein it has added "slum area development" as one of the avenue for contribution for CSR.

The term 'slum area' shall mean any area declared as such by the Central Government or any State Government or any other competent authority under any law for the time being in force.

Further, MCA vide notification no. G.S.R. 741(E) dated 24th October, 2014 has made further amendments to Schedule VII to the Companies Act, 2013 by notifying two more avenues for incurring eligible expenditure under CSR requirements for companies. According to the said notification, the contributions to the "Swach Bharat Kosh set up for the promotion of sanitation" and "contributions to the Clean Ganga Fund set up for rejuvenation of river Ganga" will also be considered as eligible expenditure qualifying for CSR.

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4. Securities and Exchange Board of India (Share Based Employee Benefits) Regulations, 2014

SEBI vide Circular No. LAD-NRO/GN/2014-15/16/1729 dated 28th October, 2014 has formulated the SEBI (Share Based Employee Benefits) Regulations, 2014 which replaces the SEBI (Employees Stock Option Plan) Guidelines, 1999. The said Regulations deal with various provisions relating to employee stock option schemes, employee stock purchase schemes, stock appreciation rights schemes, general employee benefits schemes and retirement benefit schemes formulated by listed companies. The regulations deal with definition of eligible employees, formation of compensation committee, shareholders approvals variation of terms of issue, listing, compliances etc. For the complete text of this notification please refer to the link: http://www.sebi.gov.in/cms/sebi_data/attachdocs/1414568485252.pdf

5. Amendment to the Rule 6 of the Companies (Accounts) Rules, 2014

The Central Government vide Notification No. GSR… (E) dated 14th October, 2014, has amended the Companies (Accounts) Rules, 2014 by inserting two provisos in its Rule 6. Rule 6 talks about the manner of consolidation for the companies mandated to prepare the consolidated financial statements under section 129(3) of the Companies Act, 2013.

1. According to the first proviso added therein, an intermediate wholly-owned subsidiary company whose immediate parent is a company incorporated in India would not be required to comply with the requirements of the Rule 6 of the Companies (Accounts) Rules, 2014.

   However, the intermediate wholly-owned subsidiary company whose immediate parent is a company incorporated outside India is required to comply with the requirements of the Rule 6.

2. According to the second proviso added therein, those companies which do not have any subsidiary but have one or more associates or joint ventures or both, have been exempted from preparing Consolidated Financial Statements for the financial year 2014-15.

6. Schedule III related disclosures made in the stand-alone financial statements not to be repeated in CFS – Clarification

Under the Act, the requirements of Schedule III would apply to preparation of stand-alone financial statements as well as to the preparation of Consolidated Financial Statements.

While AS 21, 'Consolidated Financial Statements', inter alia, provides that certain information required under Schedule III to the Companies Act, 2013 given in the notes to the stand-alone financial statements of the parent and/or the subsidiary, need not be included in the Consolidated Financial Statements.

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MCA has resolved the conflict between the accounting standards and the Act by providing a clarification in this regard vide Circular No. 39/2014, dated 14th October, 2014, after consulting with the ICAI.

The clarification mentions that Schedule III of the Act read with the applicable accounting standards does not envisage a company while preparing its Consolidated Financial Statements to repeat the disclosures made by it under the stand-alone financial statements used for consolidation. In the Consolidated Financial Statements, the company would need to give all disclosures relevant to Consolidated Financial Statements only.

7. Amendment to the Companies (Corporate Social Responsibility Policy) Rules, 2014

The Central Government vide Notification No. G.S.R. 644(E) dated12th September, 2014, has amended sub-rule (6) of Rule 4 of the Companies (Corporate Social Responsibility Policy) Rules, 2014.

Earlier sub-rule (6) of Rule 4 states that Companies may build CSR capacities of their own personnel as well as those of their Implementing agencies through Institutions with established track records of at least three financial years but such expenditure shall not exceed five percent of total CSR expenditure of the company in one financial year. This sub rule has now been amended and states that such expenditure will include expenditure on administrative overheads also.

8. Amendment to Schedule II to the Companies Act, 2013

The Central Government vide Notification No. G.S.R. 627(E) dated 29th August, 2014 has amended Schedule II to the Companies Act, 2013 dealing with the useful lives of assets for calculation of depreciation. The said amendments will be voluntary for companies in respect of financial year commencing on or after 1st April, 2014 and mandatory for financial statements in respect of financial years commencing on or after 1st April, 2015.

9. Clarification on Accounting Standard 10 - Capitalization of Cost

MCA, vide general circular no. 35/2014 dated 27th August, 2014, has received a number of representations seeking clarifications on capitalization of borrowing costs incurred during extended delay in commercial production for reasons beyond the developer's control and whether capitalization of power plant should be unit wise or project wise.

On consultation with the Accounting Standard Board of the ICAI, MCA has clarified that AS 10 'Accounting for Fixed Assets' and AS 16 'Borrowing Costs' prescribe the principles of capitalization of various costs.

According to AS 10, only such expenditure should be capitalized and form part of the cost of the fixed asset which increase the worth of the asset. Cost incurred during extended delay in commencement of commercial production after the plant is otherwise ready does not increase the worth of the fixed assets. Therefore, such cost cannot be capitalized.

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AS 16, inter alia provides guidance with regard to capitalization where some units of a project are complete and ready for commercial production while construction continues for the other units. In such a case, cost should be capitalized in relation to that part once the part is ready for commercial production.

MCA further clarified that AS 10 and AS 16 are applicable irrespective of whether the power projects are 'Cost Plus Projects' or 'Competitive Bid Projects'.

10. Insertion of Paragraph 46 for Entities Other than Companies

In line with para 46 inserted by the MCA for corporate entities, the Council of the ICAI has also inserted Paragraph 46 in AS 11 for Entities other than Companies in the month of February, 2014, which is as follows:

46(1) In respect of accounting periods commencing on or after 7th December, 2006 (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 asset, can be added to or deducted from the cost of the asset and should be depreciated over the balance life of the asset, 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 asset 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.

(2) To exercise the option referred to in sub-paragraph (1), an asset or liability shall be designated as a 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 should 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."

11. Modification of Guidelines on Mortgage Guarantee Companies (MGCs)

In the wake of representations received from the industry and keeping in view the long – term beneficial impact of development of the Mortgage Guarantee industry, RBI vide Notification No. RBI/2014-15/170 DNBS (PD) CC. No.20/MGC/03.011.001/2014-15, dated August 08, 2014, has decided to make certain modifications to the existing Guidelines on Mortgage Guarantee Companies (MGCs) as under:

(a) *Capital Adequacy:* While calculating the capital adequacy of the MGC, the mortgage guarantees provided by the MGCs may be treated as Contingent Liabilities and the

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credit conversion factor applicable to these Contingent Liabilities will be fifty percent as against the present applicable credit conversion factor of hundred percent.

(b) *Contingency Reserve*

i. If provision made towards losses exceed 35% of the premium or fee earned during a financial year, the Contingency Reserves could go to a minimum of 24% of the premium or fee earned, such that the aggregate of Provisions made towards Losses and Contingency Reserves is at least 60% of the premium or fee earned during a financial year.

ii. A MGC can utilize the Contingency Reserves without the prior approval of RBI for the purpose of meeting and making good the losses suffered by the mortgage guarantee holders. Such a measure can be initiated only after exhausting all other avenues and options to recoup the losses.

(c) *Classification on Investments*: It has now been decided that investments made by MGCs towards Government securities, quoted or otherwise, government guaranteed securities and bonds not exceeding the MGC's capital may be treated as "Held To Maturity (HTM)" for the purpose of valuation and accounted for accordingly. Investment classified under HTM need not be marked to market and will be carried at acquisition cost, unless it is more than the face value, in which case the premium should be amortised over the period remaining to maturity. The book value of the security should continue to be reduced to the extent of the amount amortised during the relevant accounting period. However, if any security out of this HTM category is traded before maturity, the entire lot will be treated as securities held for trade and will have to be marked to market.

(d) *Provision for Loss on invoked Guarantees*: In case the provisions already held for loss on invoked guarantees are in excess of the contract wise aggregate of 'amount of invocation' (after adjusting the realizable value of the assets held by the company in respect of each housing loan), the excess may be reversed. However, the reversal can be done only after full recovery /closure of the invoked guarantee amount or after the account becomes standard.

12. Relevant Section of the Companies Act, 2013

The relevant Sections of the Companies Act, 2013 notified up to 31st March 2015 are applicable for November, 2015 Examination.

13. Schedule III to the Companies Act, 2013

Students may note that Schedule III to the Companies Act, 2013 gives general instructions for preparation of balance sheet and statement of profit and loss of a company. Schedule III to the Companies Act, 2013, also contains general instructions for preparation of consolidated financial statements, at its end in addition to Part I - Balance Sheet and Part II - Statement of Profit and Loss. Students are advised to go

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through complete Schedule III to the Companies Act, 2013 carefully for preparation of financial statements of companies including consolidated financial statements.

Students may refer Schedule III to the Companies Act, 2013 on the Institute's website www.icai.org>>Students>>Bos knowledge portal>>Final Course>>Paper 1 Financial Reporting>>Additional Reading Material>>Schedule III to the Companies Act, 2013.

14. Buy Back of Securities (Amendment) Regulations, 2013

In exercise of the powers conferred under section 30 of the Securities and Exchange Board of India Act, 1992, SEBI made Securities and Exchange Board of India (Buy-back of Securities) (Amendment) Regulations, 2013 to amend the Securities and Exchange Board of India (Buy back of Securities) Regulations, 1998.

The important provisions of the new regulations (applicable for listed companies) are:

(i) No offer of buy-back for fifteen per cent or more of the paid up capital and free reserves of the company shall be made from the open market.

(ii) A company shall not make any offer of buyback within a period of one year reckoned from the date of closure of the preceding offer of buy-back, if any.

(iii) The company shall ensure that at least fifty per cent of the amount earmarked for buy-back is utilized for buying back shares or other specified securities.

These new regulations can be downloaded from the link http://203.199.247.102/cms/sebi_data/ attach docs/1375961931576.pdf

B. Not applicable for November, 2015 examination

1. Ind ASs issued by the Ministry of Corporate Affairs would not be applicable for November, 2015 Examination. However, the topic of "Introduction of Indian Accounting Standards (Ind AS); Comparative study of ASs vis-a-vis Ind ASs; Carve outs/ins in Ind ASs vis-à-vis International Financial Reporting Standards (IFRSs)" would be included in the syllabus of Final Paper 1 : Financial Reporting and the same would be applicable from May, 2016 Examination.

2. The topic of "Overview of International Accounting Standards (IAS) / International Financial Reporting Standards (IFRS), Interpretations by International Financial Reporting Interpretation Committee (IFRIC), Significant differences vis-a-vis Indian Accounting Standards; Understanding of US GAAPs, Applications of IFRS and US" would be excluded from the syllabus of Final Paper 1: Financial Reporting and the same would not be applicable from November, 2015 Examination.

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PART – II : QUESTIONS AND ANSWERS

QUESTIONS

AS 2

1. (a) Aman Ltd. is engaged in a manufacturing process of food products. During the year 2014-15, the company introduces 3,00,000 units of raw material @ ₹ 10 per unit. The details of other cost of production are as under:

Item	Amount (₹)	Output (unit)	Market price per unit (₹)	Closing inventory as on 31-03-2015
Wages	16,40,000	Main Product ABC -1,25,000	80	16,000
Fixed overhead	11,60,000	Main Product XYZ -1,00,000	50	4,000
Variable overhead	8,00,000	By-product 32,000	25	
Selling overhead	95,000			

There is a profit of ₹ 90,000 on sale of by-product after incurring separate processing charges of ₹ 80,000 and special packing charges of ₹ 1,20,000. ₹ 60,000 was realised from the sale of scrap.

Calculate the value of closing inventory of MP ABC and MP XYZ as on 31-03-2015.

AS 3

(b) M Ltd. submits the following information pertaining to the year 2014-2015

	(₹ in lakhs)
Additional shares issued	16.50
CAPEX (Capital expenditure)	19.90
Proceeds from assets sold	11.60
Dividends declared	10.50
Amortisation of preliminary expenses	5.00
Gain from disposal of assets	(6.20)
Net income	8.30
Increase in Accounts Receivable	11.50
Redemption of 9% debentures	12.50
Depreciation	5.75

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Using the data given above, you are required to prepare Cash Flow Statement as per AS 3 (Revised) by indirect method and find the ending cash and bank balances given an opening figure thereof was ₹ 11.55 lakhs.

AS 4

2. (a) A company deals in petroleum products. The sale price of petrol is fixed by the government. After the Balance Sheet date, but before the finalisation of the company's accounts, the government unexpectedly increased the price retrospectively. Can the company account for additional revenue at the close of the year? Discuss.

AS 5

(b) U.P. Rajya Setu Nigam Ltd. was awarded a contract of construction of a bridge for ₹ 100 crores on 1-6-2011. Total contract cost estimated was ₹ 80 crores. The position of the contract on 31-3-2014 and 31-3-2015 was under:-

	As on 31-3-2014	As on 31-3-2015
Contract Price	100	100
Contract cost incurred up to date	25	95 (100% complete)
Estimate contract cost of completion	60	Nil

While closing books of account on 31-3-2015, the chief accountant treated excess cost of ₹ 10 crores incurred as against estimated cost of ₹ 25+60= ₹ 85 crores as on 31-3-2014 as mistakes in estimation of cost, hence classified ₹ 10 crores (95-85) as prior period expenses. Comment on the treatment made by the chief accountant.

AS 6

3. (a) The original cost of the machine shown in the books of a company as on 1stApril, 2012 is ₹ 180 lakhs which they revalued upward by 20% during 2012-13. In the year 2014-15, it appears that a 5% downward revaluation should be made to arrive at the true value of the assets in the changed economic and industry conditions. They charged 15% depreciation on W.D.V of the assets.

Show the value of the asset at which it should appear in the balance sheet dated 31stMarch, 2015 and also show the revaluation reserve account.

AS 7

(b) A firm of contractors obtained a contract work. The following details are available in the records for the year ended 31st March, 2015:

	(₹ in lakhs)
Total contract price	800
Work certified	350

Work not certified	75
Estimated further cost to completion	480
Progress payment received	380
Payment to be received	120

Find out the amount of foreseeable loss, contract work-in-progress, contract value recognised as per AS 7 and the amount due or from the customers.

AS 9

4. (a) New Spice Ltd. sells male grooming products to various dealers situated in different states in India. It allows normal credit period of 45 days to its dealers to make payment. Interest at the rate of 2% per month is charged on the dealers for delayed payments. The interest recovery on such overdue outstanding amounts from dealers is only 10%, due to various reasons. During the year 2014-15, the company wants to recognize only the interest received and not the balance 90% of interest receivable on overdue outstanding. Do you agree?

AS 10

(b) S Ltd. has constructed a fixed asset and incurred the following expenses on its construction:

	₹
Materials	7,00,000
Direct Expenses	1,80,000
Total Direct Labour (excluding the amount allocated to fixed asset constructed)	18,00,000
(1/10th of the total labour was chargeable to the fixed asset constructed)	
Total Office & Administration Expenses	1,70,000
(5% is chargeable to the fixed asset constructed)	
Total Depreciation	1,90,000
(10% is chargeable to the fixed asset constructed)	

Calculate the cost of the fixed asset constructed as per AS 10.

AS 11

5. (a) A company had imported raw material worth US$ 250,000 on 15th January, 2015 when the exchange rate was ₹ 46 per US$. The company had recorded the transaction at that rate. The payment for imports was made on 15th April, 2015 when the exchange rate was ₹ 49 per US$. However, on 31st March, 2015 the rate of

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exchange was ₹ 50 per US$. The company passed an entry on 31st March, 2015 adjusting the cost of raw materials consumed for the difference between ₹ 49 and ₹ 46 per US$. State your views as an accountant.

AS 12

(b) A Ltd. has set up its business in a designated backward area with an investment of ₹ 200 lakhs. The Company is eligible for 25% subsidy and has received ₹ 50 lakhs from the Government.

Explain the treatment for capital subsidy received from the Government in the books of the company.

AS 13

6. Naren Garments Manufacturing Company Limited invested in the shares of another company on 1st November, 2014 at a cost of ₹ 3,00,000. It also earlier purchased Gold of ₹ 3,50,000 and Silver of ₹ 1,50,000 on 1st April, 2014. Market value as on 31st March, 2015 of above investments are as follows:

	₹
Shares	2,50,000
Gold	5,00,000
Silver	2,80,000

How will the above investments be shown in the books of accounts of Naren Garments Manufacturing Company Limited for the year ending 31st March, 2015 as per the provisions of Accounting Standard 13?

AS 16

7. (a) Fragrance Limited borrowed an amount of ₹ 150 crores on 1.4.2014 for construction of boiler plant @ 11% p.a. The plant is expected to be completed in 4 years. The weighted average cost of capital is 13% p.a. The accountant of Fragrance Ltd., capitalised interest of ₹ 19.50 crores for the accounting period ending on 31.3.2015. Due to surplus fund out of ₹ 150 crores, an income of ₹ 3.50 crores was earned and credited to profit and loss account. Comment on the above treatment of accountant with reference to the relevant accounting standard.

AS 19

(b) XY Ltd. leased a machine to SB Ltd. on the following terms:

	(₹ in lakhs)
Fair value of the machine	4.00
Lease term	5 years

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Lease rental per annum	1.00
Guaranteed residual value	0.20
Expected residual value	0.40
Internal rate of return	15%

Depreciation is provided on straight line method at 10% per annum. Ascertain Unearned Finance Income. Also pass necessary journal entries in the books of the Lessee in the first year of lease.

AS 20

8. A Ltd. had 8,00,000 equity shares outstanding as on 1st April, 2013. The company earned a profit of ₹ 20,00,000 during the year 2014.15. The average fair value per share during 2014-15 was ₹ 40. The company has given share option to its employees of 1,00,000 equity shares at the option price of ₹ 20.

   Calculate Basic EPS and Diluted EPS.

AS 28

9. Famous Ltd. is in the business of manufacturing and export of its products. The Government put restriction on export of goods exported by Famous Ltd. Due to that restriction the company decide to impair its assets. The company provide you the following information:

   (i) The company acquired the identifiable assets worth ₹ 500 lakhs from Crown Ltd. on 1st April, 2011 and paid ₹ 550 lakhs. The excess amount was treated as goodwill.

   (ii) The useful life of acquired identifiable assets was 10 years and depreciation charged on straight line basis.

   (iii) The recoverable amount of assets on 31st March, 2015 was determined as ₹ 278 lakhs.

   (iv) The amortisation period of goodwill to be taken as 5 years as per AS 14.

   Calculate impairment loss and its treatment in books of accounts as per the provisions of AS 28 and also pass necessary journal entries for adjustment of impairment loss.

AS 29

10. Shishir Ltd., a public sector company, provides consultancy and engineering services to its clients. In the year 2014-15, the Government set up a commission to decide about the pay revision. The pay will be revised with respect from 1-1-2012 based on the recommendations of the commission. The company makes the provision of ₹ 1250 lakhs for pay revision in the financial year 2014-15 on the estimated basis as the report of the commission is yet to come. As per the contracts with client on cost plus job, the billing is

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done on the actual payment made to the employees and allocated to jobs based on hours booked by these employees on each job.

The company discloses through notes to accounts:

"Salaries and benefits include the provision of ₹ 1250 lakhs in respect of pay revision. The amount chargeable from reimbursable jobs will be billed as per the contract when the actual payment is made."

The Accountant feels that the company should also book/recognize the income by ₹ 1250 lakhs in Profit & Loss Account as per the terms of the contract. Otherwise, it will be the violation of matching concept & understatement of profit.

Comment on the opinion of the Accountant with reference to relevant Accounting Standards.

Corporate Financial Reporting

11. Max & Co. Ltd., had the following items under 'Reserves & Surplus" in the Balance Sheet as on 31st March, 2015:

Securities Premium	₹ 50 lakhs
Capital Reserve	₹ 30 lakhs
General Reserve	₹ 21 lakhs

The company had accumulated loss of ₹ 120 lakhs, on the same day, which it had disclosed under the head "Statement of Profit and Loss" as an 'Asset' in its Balance Sheet.

Comment on the correctness of this treatment in line with Schedule III to the Companies Act, 2013.

Accounting for Corporate Restructuring

12. The following are the Balance Sheets of A Ltd. & B Ltd. as on 31st March, 2015:

Liabilities	*A Ltd.*	*B Ltd.*
Share Capital:		
Equity Shares of ₹ 10 each fully paid	45,00,000	10,00,000
8% Preference Shares of ₹ 10 each fully paid	-	5,00,000
General Reserve	3,50,000	3,10,000
Profit and Loss Account	6,34,000	60,000
10% Debentures	-	8,00,000
Current Liabilities	6,00,000	3,80,000
Total	60,84,000	30,50,000

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Assets:		
Fixed Assets	30,50,000	7,30,000
30,000 Equity Shares in B Ltd.	3,00,000	-
90,000 Equity Shares in A Ltd.	-	10,00,000
Debtors	12,70,000	4,50,000
Stock	8,40,000	5,50,000
Bank Balance	6,24,000	3,20,000
Total	60,84,000	30,50,000

A Ltd. absorbs B Ltd. on the basis of intrinsic value of both the companies as on 31st March, 2015. It is informed that the Preference Shares of B Ltd. do not have priority over payment of capital and dividend. Before absorption, A Ltd. declared dividend of 8%, Dividend tax is 10%.

Prepare Balance sheet of A Ltd., after the absorption of B Ltd. with necessary Notes to accounts.

Consolidated Financial Statements

13. ZEE Limited is a company carrying on the business of beauty products, acquired 84,000 shares of an herbal products company Dee Limited for ₹ 9,60,000 on 31st March, 2010. The Balance Sheet of Dee Limited on that date was as under:

Particulars	₹
Equity and Liabilities	
Shareholders Fund	
1,20,000 equity shares of ₹ 10 each fully paid up	12,00,000
Reserve and surplus	
Capital Reserve	24,000
Profit and Loss Account	48,000
Current Liabilities	
Trade payables	84,000
	13,56,000
Non-Current Assets	
Fixed Assets	8,40,000
Current Assets	5,16,000
	13,56,000

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Directors of Dee Limited made bonus issue on 31st March, 2015 in the ratio of one equity share of ₹ 10 each fully paid up for every two shares held on that date. It was decided that such bonus shares would be issued out of post-acquisition profits by using revenue reserve.

On 31st March, 2015 the summarized Balance Sheets of the two companies were as follows:

Particulars	*Zee Limited (₹)*	*Dee Limited (₹)*
Equity and Liabilities		
Shareholders fund		
Equity shares of ₹ 10 each fully paid up (Before bonus issue)	36,00,000	12,00,000
Reserve and Surplus		
Capital Reserve	-	24,000
Securities Premium	7,20,000	-
Revenue Reserve	48,00,000	15,24,000
Profit and Loss Account	12,60,000	3,36,000
Current Liabilities		
Trade payable	4,44,000	1,68,000
	1,08,24,000	32,52,000
Non-current Assets		
Fixed assets	63,36,000	18,48,000
84,000 equity shares in DEE Limited at cost	9,60,000	
Current assets	35,28,000	14,04,000
	1,08,24,000	32,52,000

You are required to calculate as on 31st March, 2015 (i) Cost of Control/Capital Reserve (ii) Minority Interest (iii) Consolidated Reserves and Surplus in each of the following cases:

(i) Before issue of bonus shares.

(ii) Immediately after issue of bonus shares.

Also, prepare a Consolidated Balance Sheet of the group after the bonus issue alongwith necessary Notes to accounts.

Financial Instruments

14. (i) Surya Ltd. holds a small number of shares in Supreme Ltd. The shares are classified as 'available for sale'. On 20th December 2014, the fair value of the share

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is ₹ 240 and the cumulative gain recognised in the Investment Revaluation Reserve Account is ₹ 40. On the same day, Supreme Ltd. was acquired by Simple Ltd. a large entity. As a result, Surya Ltd. receives shares in Simple Ltd. for those it had in Supreme Ltd. of equal fair value.

Should Surya Ltd. recognise the cumulative gain of ₹ 40 recognised in Investment Revaluation Reserve Account in the Statement of Profit and Loss as per the provisions of AS 30?

(ii) Entity A which owes ₹ 25 lakhs to Entity B agrees to pay ₹ 25 lakhs to Entity C at a future date to assume its obligation to Entity B. Entity B legally releases Entity A from any further obligation under the debt. As desired by Entity C, Entity A agrees to make payment to Entity B on behalf of Entity C.

Examine the status of Entity A with respect to recognition or de-recognition of its liability towards Entity B and Entity C.

Share Based Payments

15. The following particulars in respect of stock options granted by a company are available:

Grant date	01.04.2012
Number of employees covered	400
Number of options granted per employee	60
Nominal value per share (₹)	100
Exercise price per share (₹)	125

Offer was put in three groups, Group 1 was for 20% of shares offered with vesting period 1 year, Group 2 was for 40% of shares offered with vesting period 2 years. Group 3 was for 40% for shares offered with vesting period three years. Fair value of option per share on grant date was ₹ 10 for Group 1, ₹ 12.50 for Group 2 and ₹ 14 for Group 3.

Position as on 31.03.2013	Position as on 31.03.2014
Number of employees left = 40 Estimate of number of employees to leave in 2013-14 = 36 Estimate of number of employees to leave in 2014-15 = 34 Number of employees exercise option in Group 1 = 350	Number of employees left = 35 Estimate of number of employees to leave in 2014-15 = 30 Number of employees exercising options in Group II = 319

Position on 31.03.2015

- Number of employees left = 28
- Number of employees at the end of the last vesting period = 297
- Number of employees exercising options in Group III = 295

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Options not exercised immediately on vesting, were forfeited. Compute expenses to recognize in each year and show important accounts in the books of the company.

Mutual Fund

16. The investment portfolio of a mutual fund scheme includes 25,000 shares of Sun Ltd. @ ₹ 20 each and 20,000 shares of Moon Ltd. @ ₹ 30 each acquired on 31.10.2013. The market value of these shares at the end of 2013-14 were ₹ 19 and ₹ 32 respectively. On 31.5.2014, shares of both the companies were disposed off realizing ₹ 18.50 per share of Sun Ltd. and ₹ 33.50 per share of Moon Ltd. Pass important accounting entries in the books of the fund for the accounting years 2013-14 and 2014-15.

NBFC

17. While closing its books of account on 31st March, 2015 a Non-Banking Finance Company has its advances classified as follows:

	₹ in lakhs
Standard assets	16,800
Sub-standard assets	1,340
Secured portions of doubtful debts:	
upto one year	320
one year to three years	90
more than three years	30
Unsecured portions of doubtful debts	97
Loss assets	48

Calculate the amount of provision, which must be made against the Advances.

Valuation of Shares

18. Following information from P Ltd. and Q Ltd. are available:

	P Ltd.	Q Ltd.
Earning after Tax	₹ 2,00,00,000	₹ 24,00,000
No. of Equity Shares	10,00,000	4,00,000
P.E Ratio (Times)	12	8

Q Ltd. is taken over by P Ltd.

You are required:

(i) to calculate market price of shares of P Ltd. and Q Ltd.

(ii) to find out the swap ratio based on market price

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(iii) to compute the EPS of P Ltd. after takeover of Q Ltd.

(iv) to find out the market value of shares of the merged company.

Value Added Statement

19. From the following Profit & Loss Account of Orange Ltd., prepare a gross value added statement for the year ended 31.3.2015:

Show also the reconciliation between gross value added and profit before taxation.

Profit and Loss Account for the year ended 31.3.2015

	Notes	(₹ in lakhs)	(₹ in lakhs)
Income:			
Sales			1,988
Other Income			110
			2,098
Expenditure:			
Production and operational expenses	1	1,390	
Administration expenses (Factory)	2	166	
Interest	3	58	
Depreciation		34	(1,648)
Profit before taxes			450
Provision for tax	4 and 5		(60)
Profit after taxes			390
Balance as per last Balance Sheet			20
			410
Transferred to general reserve		90	
Dividend paid		190	(280)
Surplus carried to Balance Sheet			130

Notes:

1. Production & Operation expenses: ₹ in lakhs

Consumption of raw materials	694
Consumption of stores	118
Cess and Local taxes	196
Salaries, wages, gratuities to administrative staff	164
Other manufacturing expenses	218
	1,390

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2. Administration expenses include salaries and commission to directors ₹ 18 lakhs and provision for doubtful debts ₹ 12.60 lakhs

3. Interest include:

		₹ in lakhs
(a)	Interest on loan from Axis bank for working capital	18
(b)	Interest on loan from Axis bank for Fixed loan	20
(c)	Interest on loan from ICICI Bank for fixed loan	16
(d)	Interest on Debentures	4
		58

4. The charges for taxation include a transfer of ₹ 6 lakhs to the credit of Deferred Tax Account.

5. Cess and local taxes include Excise Duty, which is equal to 1/14 of cost of bought in material and services.

Economic Value Added

20. From the following information of Capable Ltd., compute the economic value added:

(i)	Share capital	₹ 2,000 lakhs
(ii)	Reserve and surplus	₹ 4,000 lakhs
(iii)	Long-term debt	₹ 400 lakhs
(iv)	Tax rate	30%
(v)	Risk free rate	9%
(vi)	Market rate of return	16%
(vii)	Interest	₹ 40 lakhs
(viii)	Beta factor	1.05
(ix)	Profit before interest and tax	₹ 2,000 lakhs

SUGGESTED ANSWERS / HINTS

1. (a) As per para 10 of AS 2 'Valuation of Inventories', most by-products as well as scrap and waste materials, by their nature, are immaterial. They are often measured at net realizable value and this value is often deducted from the cost of the main product.

Determination of value of closing inventory of Main Products

	Main Product ABC	*Main Product XYZ*
Closing inventory in units	16,000 units	4,000 units

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Cost per unit (W.N.3)	₹ 31.68	₹ 19.80
Value of closing inventory	₹ 5,06,880	₹ 79,200

Working note:

(1) Calculation of net realizable value of by-product

	₹
Selling price of by-product (32,000 units x ₹ 25)	8,00,000
Less: Separate processing charges of by-product	(80,000)
Special packing charges	(1,20,000)
Net realizable value of by-product	6,00,000

(2) Calculation of cost of conversion for allocation between joint product ABC and XYZ

		₹
Raw Material		30,00,000
Wages		16,40,000
Fixed production overhead		11,60,000
Variable overhead		8,00,000
		66,00,000
Less: NRV of by-product	6,00,000	
Sales value of scrap	60,000	(6,60,000)
Joint cost to be allocated between ABC and XYZ		59,40,000

(3) Determination of basis of allocation and allocation of joint cost to main product ABC and XYZ

	Main Product ABC	*Main Product XYZ*
Output in units (a)	1,25,000	1,00,000
Sales price per unit (b)	₹ 80	₹ 50
Sales Value (a × b)	₹ 1,00,00,000	₹ 50,00,00
Ratio of allocation	2	1
Joint cost ₹ 59,40,000 allocated in the ratio of 2:1 (c)	₹ 39,60,000	₹ 19,80,000
Cost per unit (c/a)	₹ 31.68	₹ 19.80

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(b) **M Ltd.**

Cash Flow Statement for the year ended 31st March, 2015

	₹ in lakhs	₹ in lakhs
Cash Flows from operating activities		
Net Income	8.30	
Add: Depreciation	5.75	
Amortisation of preliminary expenses	5.00	
Loss on sale of asset	6.20	
Less: Increase in account receivables	(11.50)	
Net cash generated from operating activities		13.75
Cash Flows from investing activities		
Capital expenditure	(19.90)	
Proceeds from sale of fixed assets	11.60	
Net cash used in investing activities		(8.30)
Cash Flows from financing activities		
Proceeds from issue of additional shares	16.50	
Dividend declared	(10.50)	
Redemption of 9% debentures	(12.50)	
Net cash generated from financing activities		(6.50)
Net decrease in cash		(1.05)
Cash at the beginning of the period		11.55
Cash at the end of the period (balancing figure)		10.50

2. **(a)** According to para 8 of AS 4 'Contingencies and Events Occurring After the Balance Sheet Date', the unexpected increase in sale price of petrol by the government after the balance sheet date cannot be regarded as an event occurring after the Balance Sheet date, which requires an adjustment at the Balance Sheet date, since it does not represent a condition present at the balance sheet date. The revenue should be recognized only in the subsequent year with proper disclosure. The retrospective increase in the petrol price should not be considered as a prior period item, as per AS 5, because there was no error in the preparation of previous period's financial statements.

(b)

Cost estimated by U.P. Rajya Setu Nigam Ltd. in 2013-14	₹ 85 crores
Excess Cost incurred in 2014-15	₹ 10 crores
Treatment given by the company	Prior period item

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As per para 16 of the AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', 'prior period items' refers only to income or expenses which arise in the current period as a result of errors or omissions in the preparation of the financial statements of one or more prior periods. Since, the increase in the estimated cost is not an error, so cannot be said as prior-period item.

This increase in the cost is due to change in estimation which involves judgments based on the latest information available. A change in estimate is neither a prior period item nor an extraordinary item. Hence, the treatment given by the company is not correct.

3. (a) (i) **Computation of value of asset at which it should appear in the balance sheet on 31.3.2015**

Particulars	*₹ in lakhs*
WDV as on 1.4.2012	180.00
Add: Revaluation profit	36.00
Revised WDV	216.00
Less: Depreciation for 2012-13 @ 15%	(32.40)
WDV as on 31.3.2013	183.60
Less: Depreciation for 2013-14 @ 15%	(27.54)
WDV as on 31.3.2014	156.06
Less: Revaluation loss	(7.80)
Revised WDV	148.26
Less: Depreciation for 2014-15 @ 15%	(22.24)
WDV as on 31.3.2015	126.02

(ii) **Revaluation Reserve A/c for the years 2012-13 to 2014-15**

Revaluation Reserve A/c

Date	*Particulars*	*₹ in lakhs*	*Date*	*Particulars*	*₹ in lakhs*
31.3.2013	To balance c/d	36.00	1.4.2012	By Machinery A/c	36.00
		36.00			36.00
31.3.2014	To balance c/d	36.00	1.4.2013	By Balance b/d	36.00
		36.00			36.00
2014-15	To Machinery A/c (Revaluation loss)	7.80	1.4.2014	By Balance b/d	36.00
31.3.2015	To Balance c/d	28.20			
		36.00			36.00

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A decrease in net book value arising on revaluation of fixed assets is required to be charged to Profit and Loss A/c. However, as per AS 10, if such a decrease is considered to be related to a previous increase on revaluation that is included in revaluation reserve, the attributable amount is charged against that reserve. Hence, revaluation loss of ₹ 7.80 lakhs has been charged against revaluation reserve.

(b) (i) **Amount of foreseeable loss**

	(₹ in lakhs)
Total cost of construction (350 + 75 + 480)	905
Less: Total contract price	(800)
Total foreseeable loss to be recognized as expense	105

According to para 35 of AS 7 (Revised 2002), when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately.

(ii) **Contract work-in-progress i.e. cost incurred to date**

	(₹ in lakhs)
Work certified	350
Work not certified	75
	425
This is 46.96% or 47% (425/905× 100) of total cost of construction	

Proportion of total contract value recognised as revenue

47% of ₹ 800 lakhs = ₹ 376 lakhs

(iii) **Amount due from/to customers** = Contract costs + Recognised profits – Recognised losses – (Progress payments received + Progress payments to be received)

= [425 + Nil – 105 – (380 + 120)] ₹ in lakhs

= [425 – 105 + 500] ₹ in lakhs

Amount due to customers = ₹ 180 lakhs.

4. **(a)** As per AS 9 on Revenue Recognition, where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, e.g. for escalation of price, export incentive, interest, etc., revenue recognition is postponed to the extent of uncertainty involved. In such cases, it may be

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appropriate to recognize revenue only when it is reasonable certain that the ultimate collection will be made. Where there is no uncertainty as to ultimate collection, revenue is recognised at the time of sale or rendering of service even though payments are made by instalments.

Accordingly, New Spice Ltd. is correct in recognizing the interest on receipt basis ie. 10% of interest recovered on overdue outstanding.

(b) Calculation of cost of fixed asset constructed

	₹
Materials	7,00,000
Direct expenses	1,80,000
Direct labour	2,00,000
Office and administrative expenses (5% of ₹ 1,70,000)	8,500
Depreciation (10% of ₹ 1,90,000)	19,000
Cost of fixed asset	11,07,500

Working Note:

Calculation of direct labour allocated to fixed asset constructed

	₹
Direct labour (excluding allocation to the fixed asset constructed)	18,00,000
Total direct labour	= 18,00,000 x 10/9
	= 20,00,000
Direct labour related to fixed asset constructed	20,00,000 x 1/10
	= 2,00,000

5. (a) As per AS11 on "The Effects of Changes in Foreign Exchange Rates", monetary items denominated in a foreign currency should be reported using the closing rate. However, in certain circumstances, the closing rate not reflect with reasonable accuracy the amount in reporting currency that is likely to be realized from or required to disburse, a foreign currency monetary item at the balance sheet date. In such circumstances, the relevant monetary item should be reported in the reporting currency at the amount, which is likely to be realized from, or required to disburse, such item at the balance sheet date.

In the instant case, having regard to the fact that the amount payable for the raw material is a monetary item, the same should be shown in the balance sheet at the rate as on 31st March, 2015 i.e. ₹ 50, irrespective of the payment for the same subsequently at a lower rate.

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Hence, the treatment given by the company is wrong.

(b) Subsidy received by A Ltd. is in the nature of promoter's contribution, since, this grant is given with reference to the total investment in an undertaking and by way of contribution towards its total capital outlay and no repayment is ordinarily expected in respect thereof. Therefore, this grant should be treated as capital reserve, which can neither be distributed as dividend nor considered as deferred income.

6. As per AS 13 'Accounting for Investments', for investment in shares - if the investment is purchased with an intention to hold for short-term period then it will be shown at the realizable value of ₹ 2,50,000 as on 31st March, 2015.

If equity shares are acquired with an intention to hold for long term period then it will continue to be shown at cost in the Balance Sheet of the company. However, provision for diminution shall be made to recognize a decline, if other than temporary, in the value of the investments.

As per the standard, investment acquired for long term period shall be shown at cost. Gold and silver are generally purchased with an intention to hold it for long term period until and unless given otherwise. Hence, the investment in Gold and Silver (purchased on 1st April, 2014) shall continue to be shown at cost as on 31st March, 2015 i.e., ₹ 3,50,000 and ₹ 1,50,000 respectively, though their realizable values have been increased.

However, if held as short term investment then it should be valued at lower of cost or fair value (market price) and the resultant profit or loss to be charged to the profit and loss account.

7. **(a)** Para 10 of the AS 16 'Borrowing Cost' states that to the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation on that asset should be determined as the actual borrowing costs incurred on that borrowing during the period less any income on the temporary investment of those borrowings. The capitalisation rate should be the weighted average of the borrowing costs applicable to the borrowings of the enterprise that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. In the given case, the amount of ₹ 150 crores was specifically borrowed for construction of a boiler plant. Therefore, treatment of accountant of Fragrance Ltd. is not correct and the amount of borrowing costs to be capitalised for the financial year 2014-15 should be calculated as follows:

	(₹ in crores)
Interest paid for 2014-15(11% on ₹ 150 crores)	16.50
Less: Income on temporary investment from specific borrowings	(3.50)
Borrowing costs to be capitalised during 2014-15	13.00

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(b) Gross investment = Minimum lease payments + Unguaranteed residual value

= [Total lease rent + Guaranteed residual value (GRV)] + Unguaranteed residual value (URV)

= [(₹ 1,00,000 × 5 years) + ₹ 20,000] + ₹ 20,000

= ₹ 5,40,000 (a)

Table showing present value of Minimum lease payments (MLP) and Unguaranteed residual value (URV).

Year	*M.L.P. inclusive of URV (₹)*	*Discount factor @ 15%*	*Present Value (₹)*
1	1,00,000	0.8696	86,960
2	1,00,000	0.7561	75,610
3	1,00,000	0.6575	65,750
4	1,00,000	0.5718	57,180
5	1,00,000	0.4972	49,720
	20,000 (GRV)	0.4972	9,944
	5,20,000		3,45,164 (i)
	20,000 (URV)	0.4972	9,944 (ii)
	5,40,000	(i) + (ii)	3,55,108 (b)

Unearned Finance Income = (a) – (b)

= ₹ 5,40,000 – ₹ 3,55,108

= ₹ 1,84,892

Journal Entries in the books of SB Ltd.

	₹	₹
At the inception of lease		
Machinery account Dr.	3,45,164*	
To XY Ltd.'s account		3,45,164*
(Being lease of machinery recorded at present value of minimum lease payments)		

* As per para 11 of AS 19, the lessee should recognize the lease as an asset and a liability at an amount equal to the fair value of the leased asset at the inception of lease. However, if the fair value of the leased asset exceeds the present value of minimum lease payments from the standpoint of lessee, the amount recorded should be the present value of these minimum lease payments. Therefore, in this case, as the fair value of ₹ 4,00,000 is more than the present value amounting ₹ 3,45,164, the machinery has been recorded at ₹ 3,45,164 in the books of SB Ltd. (the lessee) at the inception of the lease. According to para 13 of the standard, at the inception of the lease, the asset and liability for the future lease payments are recognised in the balance sheet at the same amounts.

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Particulars		Dr. (₹)	Cr. (₹)
At the end of the first year of lease			
Finance charges account	Dr.	51,775	
(Refer Working Note)			
To XY Ltd.'s account			51,775
(Being the finance charges for first year due)			
XY Ltd.'s account	Dr.	1,00,000	
To Bank account			1,00,000
(Being the lease rent paid to the lessor which includes outstanding liability of ₹ 48,225 and finance charge of ₹ 51,775)			
Depreciation account[£]	Dr.	34,516	
To Machinery account			34,516
(Being the depreciation provided @ 10% p.a. on straight line method)			
Profit and loss account	Dr.	86,291	
To Depreciation account			34,516
To Finance charges account			51,775
(Being the depreciation and finance charges transferred to profit and loss account)			

Working Note:

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

Year	*Outstanding liability (opening balance)*	*Minimum lease payments*	*Finance charges*	*Reduction in principal amount*	*Outstanding liability (closing balance*
	₹	₹	₹	₹	₹
1	3,45,164	1,00,000	51,775	48,225	2,96,939
2	2,96,939	1,00,000	44,541	55,459	2,41,480
3	2,41,480	1,00,000	36,222	63,778	1,77,702
4	1,77,702	1,00,000	26,655	73,345	1,04,357
5	1,04,357	1,00,000	15,654	84,346	20,011[•]

[£]Depreciation has been provided on the basis that the machine has been leased at the beginning of the year.

[•]The difference between this figure and guaranteed residual value (₹ 20,000) is due to approximation in computing the interest rate implicit in the lease.

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8. Computation of Earnings Per Share

	Earnings ₹	*Shares*	*Earnings per share* ₹
Net profit for the year 2014-15	20,00,000		
Number of shares outstanding during the year 2014-15		8,00,000	
Basic Earnings Per Share $= \frac{20,00,000}{8,00,000}$			2.50
Number of shares under option		1,00,000	
Number of shares that would have been issued at fair value (Refer Note)			
[1,00,000 x 20/40]		(50,000)	
Diluted Earnings Per Share $= \frac{20,00,000}{8,50,000}$	20,00,000	8,50,000	2.35

Note: The earnings have not been increased as the total number of shares has been increased only by the number of shares (50,000) deemed for the purpose of the computation to have been issued for no consideration.

9. Calculation and allocation of impairment loss of the identifiable assets

₹ in lakhs

	Goodwill	*Assets*	*Total*
Historical cost on 1st April, 2011	50	500	550
Less: Accumulated depreciation (For 2011-12 to 2014-15)		(200)	(200)
Less: Amortization of goodwill (For 2011-12 to 2014-15)	(40)		(40)
	10	300	310
Recoverable amount on 31st March, 2015 was determined as ₹ 278 lakhs			
Impairment of loss =(310-278) = ₹ 32 lakhs			
Impairment loss first allocated to Goodwill and balance to other assets	10	22	32
Carrying amount of the assets after impairment	Nil	278	278

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Journal Entries *₹ in lakhs*

Date	*Particulars*		*Dr.*	*Cr.*
31.3.2015	Impairment loss A/c	Dr.	32	
	To Assets			22
	To Goodwill A/c			10
	(Being the entry for accounting of impairment loss)			
31.3.2015	Profit and loss A/c	Dr.	32	
	To Impairment loss A/c			32
	(Being the entry to transfer of impairment loss to profit and loss account)			

10. As per paras 46 and 47 of AS 29, 'Provisions, Contingent Liabilities and Contingent Assets', where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognised when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognised for the reimbursement should not exceed the amount of the provision.

Accordingly, potential loss to an enterprise may be reduced or avoided because a contingent liability is matched by a related counter-claim or claim against a third party. In such cases, the amount of the provision is determined after taking into account the probable recovery under the claim if no significant uncertainty as to its measurability or collectability exists.

In this case, the provision for salary to employees of ₹ 1,250 lakhs will be ultimately collected from the client, as per the terms of the contract. Therefore, the liability of ₹ 1,250 lakhs is matched by the counter claim from the client. Hence, the provision for salary of employees should be matched with the reimbursable asset to be claimed from the client. It appears that the whole amount of ₹ 1,250 lakhs is recoverable from client and there is no significant uncertainty about the collection. Hence, the net charge to profit and loss account should be nil.

The opinion of the accountant regarding recognition of income of ₹ 1,250 lakhs is not as per AS 29 and also the concept of prudence will not be followed if ₹ 1,250 lakhs is simultaneously recognized as income. ₹ 1,250 lakhs is not the revenue at present but only reimbursement of claim for which an asset is created. However, the accountant is correct to the extent as that non- recognition of ₹ 1,250 lakhs as income will result in the understatement of profit. To avoid this, in the statement of profit and loss, expense relating to provision may be presented net of the amount (asset) recognized for reimbursement.

11. In accordance with Note 6(B) given under part I of Schedule III to the Companies Act, 2013, the debit balance of Profit and Loss (after all allocations and appropriations), if

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any, shall be shown as a negative figure under the head 'Surplus'. Similarly 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 negative.

In this case, the debit balance of ₹ 120 lakhs, exceeds the total of all the reserves i.e. ₹ 101 lakhs. Negative balance of ₹ 19 lakhs of "Reserves and Surplus" after adjusting debit balance of 'Profit and Loss' should be disclosed on the face of Balance Sheet under the sub-heading "Reserves and Surplus" under the heading "Shareholders' Fund". Thus the treatment done by the company is incorrect.

12. Balance Sheet of A Ltd. (after absorption of B Ltd.) as on 31st March, 2015

Particulars	*Note No.*	*(₹)*
I. Equity and Liabilities		
1. Shareholders fund		
a) Share capital	1	49,73,950
b) Reserves and Surplus	2	7,56,040
2. Non-current liabilities		
Long term borrowings		8,00,000
3. Current liabilities		9,80,000
Total		75,09,990
II Assets		
Non-current Assets		
Fixed Assets		
Tangible Assets (₹ 30,50,000 + ₹ 7,30,000)		37,80,000
Current Assets		
a) Inventories		13,90,000
b) Trade receivables		17,20,000
c) Cash and Cash equivalents		6,19,990
		75,09,990

Notes to Accounts:

		₹	₹
1.	**Share Capital**		
	4,97,395 Equity Shares of ₹ 10 each fully paid		49,73,950
	(out of which, 47,395 shares were allotted to vendors for consideration other than cash)		

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2.	**Reserves and surplus**		
	General Reserve	4,46,000	
	Profit and loss account (₹ 6,34,000 – ₹ 3,60,000 – ₹ 36,000)	2,38,000	
	Securities premium reserve (47,395 shares x ₹ 1.52)	72,040	7,56,040

Workings Notes:

(1) Computation of Net Assets (excluding inter-company investments)

	A Ltd.	*B Ltd.*
	₹	₹
Total Assets		
Assets Excluding invest	57,84,000	20,50,000
Dividend receivable	-	72,000
(A)	57,84,000	21,22,000
External Liabilities		
Current Liabilities	6,00,000	3,80,000
Proposed dividend	3,60,000	-
Dividend Distribution tax @ 10%	36,000	-
10% Debentures	-	8,00,000
(B)	9,96,000	11,80,000
Net Assets (A)-(B)	47,88,000	9,42,000

Note: (1) Dividend distribution tax has been calculated without grossing up.

(2) Since the Preference Shares of B Ltd. do not have priority over the payment of capital and dividend, they have to be treated at par with the equity shares. Both types of shares have the same paid up value.

(2) In view of the above, the proportion of shareholding in B Ltd. is worked out, as follows:

(a) **A Ltd. in B. Ltd.**

$$\frac{\text{Number of shares held by B Ltd.}}{\text{Total number of Equity and Preference Shares of B Ltd.}} = \frac{30{,}000}{1{,}00{,}000 + 50{,}000} = \frac{1}{5}$$

(b) **B Ltd. in A Ltd.**

$$\frac{\text{Number of shares held by B Ltd.}}{\text{Total number of Equity and A Ltd.}} = \frac{90{,}000}{4{,}50{,}000} = \frac{1}{5}$$

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(3) Calculation of intrinsic value of shares:

Let 'a' be the intrinsic value of shares of A Ltd. and 'b' be the intrinsic value of shares of B Ltd.

Now, a = ₹ 47,88,000 + 1/5 x b

b = ₹ 9,42,000 + 1/5 x a

By substituting the value of a in b, we get

b = ₹ 9,42,000 + 1/5 (₹ 47,88,000 + 1/5 x b)

b = ₹ 9,42,000 + 9,57,600 + b/25

$\frac{24\ b}{25}$ = ₹ 18,99,600

$b = \frac{₹ 18,99,600 \times 25}{24}$

b= ₹ 19,78,750

$a = ₹\ 47,88,000 + \frac{19,78,750}{5} = ₹\ 51,83,750$

Intrinsic value of shares of A. Ltd. = $\frac{₹\ 51,83,750}{4,50,000}$ = 11.52

Intrinsic value of shares of B. Ltd. = $\frac{₹\ 19,78,750}{1,00,000 + 50,000}$ = ₹ 13.19

(4) **Calculation of Purchase Consideration:**

No. of shares held by outside shareholders of B Ltd.

=1,00,000 – 30,000 + 50,000 = 1,20,000

Intrinsic value of shares = 1,20,000 x ₹ 13.19 per share

= 15,82,800

Shares to be issued on the basis of intrinsic value of shares

$= \frac{₹\ 15,82,800}{₹\ 11.52}$ = 1,37,395.83 shares

Less: Shares already held by A Ltd. = 90,000.00 Shares

Number of shares to be issued = 47,395.83 shares

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(5) Total Purchase price

	₹
Additional shares in A. Ltd. (47,395 shares of ₹ 11.52)	5,45,990
Cash for fractional shares (0.83 x ₹ 11.52)	10
	5,46,000
Value of 30,000 shares already held by A Ltd. (30,000 shares x ₹ 13.19)	3,96,000*
Total	9,42,000

* Approximate figure has been considered.

(6) General Reserve

	₹
As per balance sheet	3,50,000
Add: Appreciation in the value of shares held B. Ltd. (₹ 3,96,000 – ₹ 3,00,000)	96,000
Closing balance	4,46,000

(7) Bank Balance

		A Ltd. ₹	*B Ltd.* ₹
As per balance sheet		6,24,000	3,20,000
Dividend received		-	72,000
		6,24,000	3,92,000
Less: Dividend payment	3,60,000		
Dividend tax @ 10%	36,000		
Cash for fraction shares	10	(3,96,010)	-
		2,27,990	3,92,000
Total bank balance			6,19,990

13. (i) Before issue of bonus shares

		₹	₹
(i)	**Cost of control**		
	Investment ion DEE Limited		9,60,000
	Less: Face Value of investments	8,40,000	

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	Capital Profits (W.N.)	50,400	(8,90,400)
	Cost of control		69,600
(ii)	Minority Interest		
	Share capital	3,60,000	
	Capital Profit (W.N.)	21,600	
	Revenue profit (W.N.) (86,400 + 4,57,200)	5,43,600	9,25,200
(iii)	Consolidated Profit and Loss account of ZEE Ltd.		
	Balance	12,60,000	
	Add: Share in post-acquisition profit of DEE Limited (W.N.)	2,01,600	14,61,600
(iv)	Consolidated Revenue reserve account of ZEE Ltd.		
	Balance	48,00,000	
	Add: Post-acquisition share of DEE Limited (W.N.)	10,66,800	58,66,800

(ii) Immediately after issue of bonus shares

		₹	₹
(i)	Cost of control		
	Face value of Investment in DEE Limited (8,40,000 + 4,20,000)	12,60,000	
	Add: Capital profits (W.N.)	50,400	
		13,10,400	
	Less: Value of investments	(9,60,000)	
	Cost of control(Capital reserve)		3,50,400
(ii)	Minority Interest		
	Share Capital (3,60,000 + 1,80,000)	5,40,000	
	Pre-acquisition Capital Profit (W.N.)	21,600	
	Post-acquisition Revenue Profit (W.N)		
	R/R 2,77,200		
	P/L 86,400	3,63,600	9,25,200
(iii)	Consolidated Profit and loss account of ZEE Ltd.		
	Balance	12,60,000	
	Add: Share in Post-acquisition profit of DEE Limited (W.N.)	2,01,600	14,61,600

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(iv)	Consolidated Revenue reserve account of ZEE Ltd.		
	Balance	48,00,000	
	Add: Post-acquisition share of DEE Limited (W.N.)	6,46,800	54,46,800

Consolidated Balance Sheet of ZEE Limited and its subsidiary DEE Limited as on 31st March, 2015

Particulars	*Note No.*	₹
Equity and Liabilities		
(1) Shareholders fund		
(a) Equity Share Capital		36,00,000
(b) Reserves and surplus	1	79,78,800
(2) Minority Interest (W.N)		9,25,200
(3) Current Liabilities		
Trade payable	2	6,12,000
		1,31,16,000
Assets		
(1) Non-current Assets		
Fixed assets	3	81,84,000
(2) Current assets	4	49,32,000
		1,31,16,000

Notes to Accounts:

		₹	₹
1	Reserves and Surplus		
	Capital Reserve	3,50,400	
	Securities premium reserve	7,20,000	
	Profit and loss account	14,61,600	
	Revenue Reserve	54,46,800	79,78,800
2	Trade Payable		
	Zee Ltd.	4,44,000	
	Dee Ltd.	1,68,000	6,12,000
3.	Fixed assets		
	Zee Ltd.	63,36,000	

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	Dee Ltd.	18,48,000	81,84,000
4.	Current assets		
	Zee Ltd.	35,28,000	
	Dee Ltd.	14,04,000	49,32,000

Working Notes:

1. Shareholding Pattern

	Number of shares	*% of holding*
Total shares of Dee Ltd. before bonus issue	1,20,000	100%
Total shares of Dee Ltd. after bonus issue	1,80,000	100%
(i) Purchased by Zee Ltd. on 31st March, 2010	84,000	
(ii) Bonus issue (84,000/2)	42,000	
	1,26,000	70%
Minority Interest (36,000 + 18,000)	56,000	30%

2. **Analysis of profits of DEE Limited**

	Capital profit (before and after issue of bonus shares)	*Revenue profits (before bonus issue)*		*Revenue profits (After bonus issue)*	
		Revenue Reserve	*Profit and Loss A/c*	*Revenue Reserve*	*Profit and Loss A/c*
Pre-acquisition profits	24,000				
Profit and loss account on 31st March, 2010	48,000				
	72,000				
Revenue Reserve		15,24,000		15,24,000	
Less: Bonus Shares				(6,00,000)	
Add: Profit during the period 1st April, 2010 to 31st March, 2015 (3,36,000-48,000)			2,88,000		2,88,000
	72,000	15,24,000	2,88,000	9,24,000	2,88,000

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ZEE Limited's share (70%)	50,400	10,66,800	2,01,600	6,46,800	2,01,600
Minority's share (30%)	21,600	4,57,200	86,400	2,77,200	86,400

14. (i) This transaction qualifies for de-recognition under AS 30. Paragraph 61(b) of AS 30 requires that the cumulative gain or loss that has been recognised in the Investment Revaluation Reserve Account in respect of an "available for sale" financial asset be recognized in the Statement of Profit and Loss when the asset is de-recognized.

In the exchange of shares, Surya Limited disposes of the shares it had in Supreme Limited and receives shares in Simple Limited. Hence the company can recognize the cumulative gain of ₹ 40 in the Statement of Profit and Loss as per the provisions of AS 30.

(ii) If a debtor agrees to pay a third party in respect of an obligation to a creditor and obtains a legal release from its creditor, the debtor has extinguished the debt. However, if the debtor agrees to make payment in the debt to the third party or direct to its original creditor, the debtor recognizes the new debt obligation to the third party.

Here,

Entity A de-recognizes its obligation to pay ₹ 25 lakhs to Entity B and Entity C recognizes a new obligation to pay ₹ 25 lakhs to Entity C.

15. 1. Computation of Shares/Fair value expected to vest at the end of each Accounting Period

(a) Shares Graded Every Year

Particulars	*Options Vesting*	*Vesting Period*
Total shares under ESOP	60	-
Group 1 20% of 60	12	1 Year
Group 2 40% of 60	24	2 Years
Group 3 40% of 60	24	3 Years

(b) Value of Options Vesting

Group	*Year*	*No. of Employees expected to qualify*		*Shares vested per employee*	*Total No. of Shares expected to vest*	*Fair value of the Option per share*	*Fair value of the Option*
						₹	₹
I	2012-13	Actual	400-40=360	12	4,320	10.00	43,200
II	2012-13	Expected	400-40-	24	7,776	12.50	97,200

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			36=324				
	2013-14	Actual	400-40-35=325	24	7800	12.50	97,500
III	2012-13	Expected	400-40-36-34=290	24	6960	14.00	97,440
	2013-14	Expected	400-40-35-30=295	24	7080	14.00	99,120
	2014-15	Actual	297	24	7,128	14.00	99,792

No. of Employees = Opening employees– Employees left – Employee expected to leave

(c) Options forfeited and value to be transferred to General Reserve

Particulars	*Group 1 2012-13*	*Group 2 2013-14*	*Group 3 2014-15*
Number of employee qualifying	360	325	297
Less: Number of employees actually exercising	(350)	(319)	(295)
Number of employee not exercising (forfeitures)	10	6	2
Number of options per employee	12	24	24
Number of options forfeited	120	144	48
Fair value	₹ 10	₹ 12.50	₹ 14
Total value forfeited and transferred to General Reserve	₹ 1,200	₹ 1,800	₹ 672

2. Computation of Employee Compensation Expenses to be recognised

(a) For Year 2012-13

Particulars	*Group 1 2012-13*	*Group 2 2013-14*	*Group 3 2014-15*
Total fair value to be recognized as expense	4,320	97,200	97,440
Vesting period	1 year	2 years	3 years
Amount of expense to be recognized (Total value ÷ vesting period	43,200	48,600 (97,200/2)	32,480 (97,440/3)
		1,24,280	

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(b) For Year 2013-14

Particulars	*Group 2 2013-14*	*Group 3 2014-15*
Total fair value to be recognized as expense	97,500	99,120
Vesting period	2 years	3 years
Cumulative amount of expense to be recognized (Total value ÷ Vesting period × period completed)	97,500 (97,500/2 ×2)	66,080 (99,120/3 ×2)
Less: Amount of expense recognised till 2012-13	(48,600)	(32,480)
Amount of expenses to be recognized in 2013-14	48,900	33,600

Total = ₹ 48,900 + ₹ 33,600 = ₹ 82,500

(c) For the year 2014-2015

Particulars	*Group 3*
Total Fair Value to be recognized as expense	99,792
Less: Amount of Expense Recognised till 2013-14	(66,080)
Amount of Expense to be recognized in 2014-15	33,712

3. Ledger Accounts

(a) Employees' Compensation Amount

Year	*Particulars*	₹		*Particulars*	₹
2012-13	To ESOP Outstanding A/c	1,24,280	2012-13	By Profit and Loss Account	1,24,280
		1,24,280			1,24,280
2013-14	To ESOP Outstanding A/c	82,500	2013-14	By Profit and Loss Account	82,500
		82,500			82,500
2014-15	To ESOP Outstanding A/c	33,712	2014-15	By Profit and Loss Account	33,712
		33,712			33,712

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(b) ESOP Outstanding A/c

Year	Particulars	₹		Particulars	₹
2012-13	To General Reserve (120 × ₹ 10)	1,200	2012-13	By Employees' Compensation A/c	1,24,280
	To Share Capital (4,200 × ₹ 100)	4,20,000		By Bank (4,200 × ₹ 125)	5,25,000
	To Securities Premium (4,200 × ₹ 35)	1,47,000			
	To Balance c/d	81,080			
		6,49,280			6,49,280
2013-14	To General Reserve (144 × ₹ 12.50)	1,800	2013-14	By Balance b/d	81,080
	To Share Capital (7,656 × ₹ 100)	7,65,600		By Employees' Compensation A/c	82,500
	To Securities Premium (7,656 × ₹ 37.50)	2,87,100		By Bank (7,656 × ₹ 125)	9,57,000
	To Balance c/d	66,080			-
		11,20,580			11,20,580
2014-15	To General Reserve (48 x ₹ 14)	672	2014-15	By Balance b/d	66,080
	To Share Capital (7,080 ₹ 100)	7,08,000		By Employees' Compensation A/c	33,712
	To Securities Premium (7,080 × ₹ 39)	2,76,120		By Bank (7,080 ₹ 125)	8,85,000
		9,84,792			9,84,792

Working Note:

Calculation of Securities Premium

Particulars	*Group 1 2012-13*	*Group 3 2013-14*	*Group 3 2014-15*
Excise Price Received per share (Bank)	125.00	125.00	125.00
Add: Value of service received per share	10.00	12.50	14.00
Consideration received per share	135.00	137.50	139.00
Less: Nominal value per share	(100.00)	(100.00)	(100.00)
Securities premium per share	35.00	37.50	39.00

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16. Books of Mutual Fund Company

Date	*Particulars*		*Dr.* ₹	*Cr.* ₹
	Year 2013-14			
31.10.13	Investment in Sun Limited	Dr.	5,00,000	
	Investment in Moon Limited		6,00,000	
	To Bank A/c			11,00,000
	(Being purchase of Sun Limited, 25,000 shares @ ₹ 20 each and 20,000 shares of Moon Limited @ ₹ 30 each)			
31.03.14	Revenue A/c	Dr.	25,000	
	To Provision for depreciation			25,000
	(Being market value of Sun Limited depreciated by Re. 1 each for 25,000 shares)			
31.03.14	Investment in Moon Limited	Dr.	40,000	
	To Unrealised Appreciation Reserve			40,000
	(Being the appreciation in the value of shares of Moon Ltd. by ₹ 2 per share)			
	Year 2014-15			
31.05.14	Bank Account	Dr.	4,62,500	
	Loss on disposal of investment	Dr.	37,500	
	To Investment in Sun Limited			5,00,000
	(Being Investment of ₹ 5,00,000 in shares of Sun Limited sold for ₹ 4,62,500 and Loss ₹ 37,500 incurred)			
31.5.14	Provision for depreciation	Dr.	25,000	
	Revenue A/c	Dr.	12,500	
	To Loss on disposal of investment			37,500
	(Earlier depreciation provision provided being reserved on disposal of total shares of Sun Limited and the balance amount debited to revenue account)			
31.05.14	Bank account	Dr.	6,70,000	
	To Investment in Moon Limited			6,40,000
	To Profits on disposal of investment			30,000
	(Being 20,000 shares of Moon Limited sold @ ₹ 33.50)			

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31.05.14	Profit on disposal of investment	Dr.	30,000	
	Unrealized Appreciation Reserve	Dr.	40,000	
	To Revenue A/c			70,000
	(Being profit not booked last year and kept in the reserve now booked to Revenue Account)			

17. Calculation of provision required on advances as on 31st March, 2015

	Amount ₹ in lakhs	*Percentage of provision*	*Provision ₹ in lakhs*
Standard assets	16,800	0.25	42
Sub-standard assets	1,340	10	134
Secured portions of doubtful debts			
–upto one year	320	20	64
– one year to three years	90	30	27
–more than three years	30	50	15
Unsecured portions of doubtful debts	97	100	97
Loss assets	48	100	48
			427

18. (i) Calculation of Market Price of shares of P Ltd. and Q Ltd.

Market price = EPS x P/E ratio

	P Ltd.	*Q Ltd.*
	₹	₹
Earnings after tax	2,00,00,000	24,00,000
No. of equity shares	10,00,000	4,00,000
EPS	$\frac{2,00,00,000}{10,00,000}$ = ₹ 20	$\frac{24,00,000}{4,00,000}$ = ₹ 6
P/E ratio	12	8
	12 x ₹ 20 = ₹ 240	8 x ₹ 6 = ₹ 48

(ii) Calculation of Swap ratio based on Market Price

$$\text{Swap ratio} = \frac{\text{Market price per share of Q Ltd.}}{\text{Market price per share of P Ltd.}}$$

= 48/240 or 0.2

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Swap ratio = 20 shares of P Ltd. for every 100 shares of Q Ltd.

Or 1 share of P Ltd. for every 5 shares of Q Ltd.

(iii) Computation of EPS of P Ltd. after takeover of Q Ltd.

Number of shares issued to Q Ltd. = $4,00,000 \times \frac{20}{100} = 80,000$ shares

Total number of shares of P. Ltd. after takeover

= 10,00,000 + 80,000 = 10,80,000

Total earnings of P Ltd. after takeover of Q Ltd.

= ₹ 2,00,00,000 + ₹ 24,00,000

= ₹ 2,24,00,000

EPS of P Ltd. after takeover of Q Ltd. = $\frac{₹ 2,24,00,000}{10,80,000 \text{ shares}}$ = ₹ 20.74

(iv) Determination of market value of shares of the merged company

Market price =PE ratio × EPS

P Ltd. after takeover =12 × ₹ 20.74 = ₹ 248.88

Market value of P Ltd. =Total No. of shares x Market Price per share

=10,80,000× ₹ 248.88 = ₹ 26,87,90,400

Note: PE ratio of P Ltd. before takeover has been used for calculation of Market Price of Share of P Ltd. after take over

19. Gross Value Added Statement for the year ended 31st March, 2015

Particular	*₹ in lakhs*	*₹ in lakhs*
Sales		1988
Less: Cost of bought in materials and services:		
Production and operational and services expenses (694 + 118 + 218)	1030	
Administration expenses (166-18)	148	
Interest on loan for working capital	18	
Excise duty (W.N.)	92	1288
Value added by manufacturing and trading activities		700
Add: Other income		110
Total value added		810

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Application of value added

	₹ *in lakhs*	₹ *in lakhs*	%
To Employees			
Salaries, wages, gratuities etc.		164	20.25
To Directors			
Salaries and commission		18	2.22
To Government			
Cess and local taxes (196-92)	104		
Income Tax [60-6 (deferred tax)]	54	158	19.51
To Providers of capital			
Interest on Debentures	4		
Interest on fixed loans	36		
Dividends	190	230	28.39
To Provide for maintenance and expansion of the company			
Depreciation	34		
General reserve	90		
Deferred tax	6		
Retained Profit (130-20)	110	240	29.63
		810	100.00

Note: Deferred tax account could alternatively be shown as an items to pay to government

Statement showing reconciliation of Gross Value Added with profit before taxation

	₹ *in lakhs*	₹ *in lakhs*
Profit before taxes		450
Add: Depreciation	34	
Director's remuneration	18	
Salaries, wages, gratuities etc.	164	
Cess and local taxes	104	
Interest on Debentures	4	
Interest on fixed loan	36	360
Total value added		810

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Working Note:

(1) Calculation of Excise Duty

Let cost of bought in materials and services is X

So, excise duty is 1/14th of X = X/14

X = 1,030 + 148 + 18 + X/14

X = 1,196 + X/14

13x/14 = 1,196

X = 1,288

Hence Excise duty = ₹ 1,1288-1,196 = ₹ 92 lakhs

20. Capable Limited

Computation of Economic Value Added

	₹ in lakhs
Net Operating Profit after Tax (Refer Working Note 5)	1,372.00
Add: Interest on Long-term Fund (Refer Working Note 2)	28.00
	1,400.00
Less: Cost of Capital ₹ 6,400 lakhs × 15.77% (Refer working notes 3 and 4)	1,009.28
Economic Value Added	390.72

Working Notes:

(1) **Cost of Equity** = Risk free Rate + Beta Factor (Market Rate – Risk Free Rate)

9% + 1.05 (16 – 9) = 9% + 7.35% = 16.35%

(2) **Cost of Debt**

Interest	₹ 40 lakhs
Less: Tax (30%)	(₹ 12 lakhs)
Interest after Tax	₹ 28 lakhs

Cost of Debt = $\frac{28}{400} \times 100 = 7\%$

(3) **Weighted Average Cost of Capital**

Cost of Equity	₹ 6,000 lakhs × 16.35%	(W.N.1)	₹ 981 lakhs
Cost of Debt	₹ 400 lakhs × 7%	(W.N.2)	₹ 28 lakhs
			₹ 1,009 lakhs

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$$\text{WACC} = \frac{1,009}{6,400} \times 100 = 15.77\% \text{ (approx.)}$$

(4) **Capital Employed**

	₹ in lakhs
Share Capital	2,000
Reserves and Surplus	4,000
Long term debts	400
	6,400

(5) **Net Operating Profit after Tax**

Profit before Interest and Tax	2,000
Less: Interest	40
	1,960
Tax 30% on 1,960 lakhs	588
Net Operating Profit after Tax	1,372

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