PAPER – 1 : FINANCIAL REPORTING

Question No.1 is compulsory. Candidates are required to 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 answers.

Question 1

(a) Ram Ltd. furnishes the following information. You are required to compute the basic earnings per share as per paragraphs 10 and 26 of Accounting Standards 20:

Accounting period: 1st January, 2020 to 31st December, 2020

Net profit for the year 2020: ₹ 25,00,000 and for the year 2021: ₹ 37,50,000

No. of shares outstanding prior to right issue: 12,50,000 shares

Right issue: One new share for each four outstanding shares

Right issue price: ₹ 20 each

Last date of exercise of rights: 31.3.2021

Fair rate of one equity share immediately prior to exercise of rights on 31.3.2021: ₹ 25.

(b) (i) A Ltd. had acquired 80% share in the B Ltd. for ₹ 45 lac. The net assets of B Ltd. on the day are ₹ 66 lac. During the year, A Ltd. sold the investment for ₹ 90 lac and Net assets of B Ltd. on the date of disposal was ₹ 105 lac. Calculate the profit or loss on disposal of this investment to be recognised in consolidated financial statement.

(ii) Mahasukh Corporation is dealing in seasonal products. Sales pattern of the product, quarter wise is as follows:

1st quarter 30th June	*10%*
2nd quarter 30th September	*10%*
3rd quarter 31st December	*60%*
4th quarter 31st March	*20%*

Information regarding the 1st quarter ending on 30th June, 2020 is as follows:

Sales	*₹ 200 crore*
Salary and other expenses	*₹ 150 crore*
Advertisement expenses (routine)	*₹ 10 crore*
Administrative and selling expenses	*₹ 20 crore*

While preparing interim financial report for first quarter Mahasuhk Corporation wants to defer ₹ 25 crore expenditure to third quarter on the argument that third quarter is *having more sales therefore third quarter should be debited by more expenditure. Considering the seasonal nature of business and the expenditures are uniform throughout all quarters, calculate the result of the first quarter as per Accounting Standard 25. Whether Company's view is correct?*

(c) (i) Bay Ltd. has an existing freehold property where it operates an amusement park, which it intends to knock down and redevelop. During the redevelopment period the company will move its facilities to another nearby (temporary) site. The following incremental costs will be incurred:

- *Setup costs of ₹ 5 lakh to install the facilities in the new location*
- *Rent of ₹ 3 lakh*
- *Removal costs of ₹ 2 lakh including transportation of the structures /machinery from the old location to the temporary location.*

Can these costs be capitalised into the cost of the new amusement park?

(ii) After redevelopment of facilities, Bay Ltd. made a 'soft' opening to the public, to trial run its attractions. Tickets are sold at a 70% discount during this period and the operating capacity is 90%. The official opening day of the amusement park is two months later. Management claim that the soft opening is a trial run necessary for the amusement park to be in the condition capable of operating in the intended manner and accordingly, the net operating costs incurred during soft launch should be capitalised.

You are required to advise the management regarding proper treatment of the above events in the financial statements of the company Bay Ltd. keeping in mind the relevant applicable accounting standards.

(d) Mohan Ltd. gives the following estimates of cash flows relating to fixed asset on 31.12.2020. The discount rate is 15%.

Year	*Cash Flow (₹ in lakh)*
2021	*9,000*
2022	*13,500*
2023	*13,500*
2024	*18,000*
2025	*9,000*

Residual value at the end of 2025 = ₹ 2,250 lakh

Fixed assets purchased on 1.1.2021 = ₹ 90,000 lakh*

Useful life = 8 years

* **PS:** Read '1.1.2021' as '1.1.2018'.

Net selling price on 31.12.2020 = ₹ 45,000 lakh

Calculate on 31.12.2020

(a) Carrying amount at the end of 2020

(b) Value in use on 31.12.2020

(c) Recoverable amount on 31.12.2020

(d) Impairment loss to be recognised for the year ended 31.12.2020

(e) Revised carrying amount

(f) Depreciation charge for 2021.

(Discount factor @ 15% for 1, 2, 3, 4 and 5 years are 0.870, 0.756, 0.658, 0.572 and 0.497 respectively) ***(4 x 5 = 20 Marks)***

Answer

(a) Computation of Basic Earnings Per Share

(as per paragraphs 10 and 26 of AS 20 on Earnings Per Share)

	Year 2020 ₹	*Year 2021* ₹
EPS for the year 2020 as originally reported		
$\frac{\text{Net profit of the year attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$		
= (₹ 25,00,000 / 12,50,000 shares)	2.00	
EPS for the year 2020 restated for rights issue		
= [₹ 25,00,000 / (12,50,000 shares × 1.04*)]	1.92 (approx.)	
EPS for the year 2021 including effects of rights issue		
$\frac{37,50,000}{\left(12,50,000 \text{ shares x } 1.04 \text{ x} \frac{3}{12}\right) + (15,62,500 \text{ shares x} \frac{9}{12})}$		
$\frac{37,50,000}{(3,25,000 \text{ shares}) + (11,71,875 \text{ shares})}$		2.51 (approx.)

* Refer working note 2.

Working Notes:

1. Computation of theoretical ex-rights fair value per share

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

$$= \frac{(₹\ 25 \times 12,50,000 \text{ shares}) + (₹\ 20 \times 3,12,500 \text{ shares})}{12,50,000 \text{ shares} + 3,12,500 \text{ shares}}$$

= 3,75,00,000 / 15,62,500 = ₹ 24

2. Computation of adjustment factor

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

$$= \frac{₹\ 25}{₹\ 24 \text{ (Refer Working Note 1)}} = 1.04 \text{ (approx.)}$$

(b) (i) Calculation of Profit/Loss on disposal of investment in subsidiary

Particulars	₹	₹
Net assets of B Ltd. on the date of disposal		1,05,00,000
Less: Minority Interest (1,05,00,000 x 20%)		(21,00,000)
A Ltd.'s share in net assets (80%)		84,00,000
Proceeds from the sale of investment		90,00,000
Less: A Ltd.'s share in net assets		(84,00,000)
		6,00,000
Add: Capital reserve in the consolidated financial statement		
A Ltd.'s share in net asset on the acquisition date (66,00,000 x 80%)	52,80,000	
Less: Cost of investment	(45,00,000)	7,80,000
Profit on disposal of investment		13,80,000

(ii) Calculation of revised result of 1st quarter ended on 30th June, 2020

Particulars		*(₹ in crore)*
Result of first quarter ending 30th June, 2020		
Turnover (Sales)	200	
Other Income	Nil	
Total (a)		200
Less: Changes in inventories		Nil
Salaries and other cost		150
Administrative and selling expenses (10 + 20)		30
Total (b)		180
Profit (a) - (b)		20

According to AS 25, the income and expense should be recognized when they are earned and incurred respectively. Seasonal expenses are deferred when they are not incurred uniformly. Since, expenditure has been incurred uniformly, the expenses should be recognised in the quarter in which it is incurred irrespective of the seasonal income being higher in third quarter.

Therefore, the company's view that expenditure can be deferred to third quarter is not correct and is not in accordance with AS 25.

(c) (i) Costs of relocating or reorganising part or all of the operations of an enterprise are not capitalised and not included in the cost of the asset as per AS 10 since they are not directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by the management.

Set up cost, rent of temporary site and removal cost are not directly attributable cost. Hence, will not be capitalised. Such expenses of incidental operations are recognised in the Statement of Profit and Loss.

(ii) The facility has been redeveloped and the soft opening is for trial run its attractions. Further, though the amusement park is not running at its full operating capacity, it is operating at 90% capacity which is substantial. Hence, the net operating costs should not be capitalized. It should be recognised in the Statement of Profit and Loss.

(d) (a) Calculation of carrying amount at the end of 2020:

Original cost = ₹ 90,000 lakh

Depreciation for 3 years = [(90,000-2,250)×3/8] = ₹ 32,906.25 lakh

Carrying amount on 31.12.2020 = [90,000-32,906.25] = ₹ 57,093.75 lakh

(b) Calculation of value in use on 31.12.2020

Year	*Cash Flow (in lakh)*	*Discount @ 15%*	*Discounted cash flow*
2021	9,000	0.870	7,830.00
2022	13,500	0.756	10,206.00
2023	13,500	0.658	8,883.00
2024	18,000	0.572	10,296.00
2025	9,000	0.497	4,473.00
2025	(residual) 2,250	0.497	1,118.25
			42,806.25

(c) Recoverable amount on 31.12.2020

Net Selling Price = ₹ 45,000 lakh

Value in use = ₹ 42,806.25 lakh

Recoverable amount = Higher of value in use and net selling price i.e. ₹ 45,000 lakh.

(d) Impairment Loss for the year ended 31.12.2020

Carrying value as on 31.12.2020 = ₹ 57,093.75 lakh

Recoverable amount = ₹ 45,000 lakh

Impairment loss = ₹ (57,093.75 - 45,000) = ₹ 12,093.75 lakh

(e) Revised carrying amount = Recoverable value = ₹ 45,000 lakh

(f) Depreciation charge for 2021

Revised carrying amount = ₹ 45,000 lakh

Depreciation = (Revised carrying amount – Residual value) / Remaining useful life

= (45,000 - 2,250) / 5 = ₹ 8,550 lakh

Question 2

Blue Limited and Green Limited both are engaged in the business of trading in essential commodities. Blue Limited proposes to absorb the business of Green Limited as part of its business strategy. The summarized Balance Sheets of Blue Limited and Green Limited as on 31st March, 2021 are as follows:

Particulars	*Blue Limited (₹)*	*Green Limited (₹)*
(I) Equity and Liabilities:		
(1) Shareholder's fund		
(a) Share capital		
Equity shares of ₹ 10 each	*30,00,000*	*15,00,000*
10% Preference share capital of ₹ 100 each	*9,00,000*	
12% Preference share capital of ₹ 100 each		*4,80,000*
(b) Reserves and surplus		
Statutory reserve	*50,000*	*80,000*
General reserve	*19,50,000*	*12,50,000*
(2) Non-current liabilities		
Secured loans		
14% Debentures	*4,00,000*	
12% Debentures		*5,00,000*
(3) Current liabilities		
Trade payables	*7,80,000*	*8,20,000*
Total	*70,80,000*	*46,30,000*
(II) Assets:		
(1) Non -current assets		
(a) Property, Plant and Equipment	*38,00,000*	*20,00,000*
(b) Non-current investments	*5,00,000*	*4,00,000*
(2) Current assets		
(a) Inventories	*14,00,000*	*11,60,000*
(b) Trade receivables	*12,40,000*	*9,68,000*
(c) Cash at bank	*1,40,000*	*1,02,000*
Total	*70,80,000*	*46,30,000*

The following terms and conditions were agreed for absorption:

(i) 12% preference shareholders of Green Limited will receive 10% preference shares of Blue Limited in sufficient number to increase their present income by 15%

(ii) The equity shareholders of Green Limited will receive equity shares in Blue Limited on the following terms:

- *The equity shares of Green Limited will be valued at ₹ 30 per share.*

- *The market price of equity shares of Blue Limited is ₹ 50 per share.*
- *The number of shares to be issued to equity shareholders of Green Limited will be based on the 75% of market price of the shares of Blue Limited.*

(iii) 12% Debenture holders of Green Limited are to be paid at 10% premium by issue of 14% Debentures in Blue Limited issued at a discount of 12%.

(iv) 12% Debenture holders of Green Limited are to be paid Debenture interest of last year which was not accounted for due to omission and it was decided to make necessary provisions.

(v) Trade Receivables of Green Limited includes ₹ 18,000 receivable from Blue Limited.

(vi) Trade Payables of Green Limited includes ₹ 6,000 due to Blue Limited.

(vii) ₹ 9,000 is to be paid by Blue Limited to Green Limited for liquidation expenses.

(viii) Property, Plant and Equipment of both the companies are to be valued at 20% above book value. Inventory in trade is taken over at 10% less than their book value. A provision for bad debt is to be provided for at 10% on the Receivables of Green Limited from other outside parties.

(ix) Statutory reserve has to be maintained as it is at same level.

You are required to:

(I) Compute the purchase consideration.

(II) Prepare Balance Sheet of Blue Limited as at 31st March, 2021 after absorption, as per Schedule III to the Companies Act, 2013 alongwith Notes to the accounts. ***(16 Marks)***

Answer

(I) Computation of Purchase Consideration

	₹
For Preference Shareholders	
Present income of preference shareholders of Green Ltd. (4,80,000× 12%)	57,600
Add: Required 15% increase	8,640
	66,240
10% Preference shares to be issued of [₹ 6,62,400 (66,240/10) x 100]	6,62,400
For Equity Shareholders	
Number of equity shares to be issued at 75% of market price i.e. 75% of ₹ 50 = ₹ 37.50	
$\frac{1,50,000x30}{37.50}$ = 1,20,000 shares	

Equity share capital = 1,20,000 x ₹ 10 = ₹ 12,00,000		
Securities premium = 1,20,000 x ₹ 27.50 = ₹ 33,00,000		
₹ 45,00,000		45,00,000
Purchase consideration		51,62,400

(II) Balance Sheet of Blue Ltd. (after absorption of Green Ltd.) as on 31.3.2021

Particulars	*Note No.*	*(₹)*
I. Equity and Liabilities		
(1) Shareholder's funds		
(a) Share capital	1	57,62,400
(b) Reserves and surplus	2	59,85,000
(2) Non-current liabilities		
(a) Long-term borrowings	3	10,25,000
(3) Current liabilities		
(a) Trade payables	4	15,76,000
(b) Other current liability (provision for interest on debentures of Green Ltd.)		60,000
Total		1,44,08,400
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment	5	69,60,000
(b) Intangible assets	6	17,82,400
(c) Non-current investments	7	9,00,000
(2) Current assets		
(a) Inventories	8	24,44,000
(b) Trade receivables	9	20,89,000
(c) Cash and cash equivalents [(1,40,000+1,02,000-9,000)]		2,33,000
Total		1,44,08,400

Notes to Accounts

		₹	₹
1.	**Share Capital**		
	4,20,000 Equity shares of ₹ 10 each fully paid	42,00,000	
	(1,20,000 shares have been allotted as fully paid-up for consideration other than cash)		
	10%, 15,624 Preference shares of ₹ 100 each fully paid	15,62,400	57,62,400
	(Out of the above, 6,624 preference shares of ₹ 100 each have been allotted as fully paid up for consideration other than cash)		
2.	**Reserves and surplus**		
	Statutory reserve [50,000 + 80,000]	1,30,000	
	Revaluation reserve (38,00,000 x 20%)	7,60,000	
	General reserve	19,50,000	
	Securities premium (33,00,000-75,000)	32,25,000	
	Amalgamation adjustment reserve	(80,000)	59,85,000
3.	**Long-term borrowings**		
	Secured borrowings		
	14% Debentures (4,00,000 + 6,25,000 W.N.2)		10,25,000
4.	**Trade payables** (7,80,000 – 18,000 + 8,20,000-6,000)		15,76,000
5.	**Property, plant and equipment** [(38,00,000+7,60,000) + (20,00,000+4,00,000)]		69,60,000
6.	**Intangible asset**		
	Goodwill (17,73,400 W.N.1 + 9,000)		17,82,400
7.	**Non-current investment** (5,00,000 + 4,00,000)		9,00,000
8.	**Inventories** (14,00,000 + 10,44,000)		24,44,000
9.	**Trade receivables** [(12,40,000 - 6,000) + (9,68,000-18,000) x 90%]		20,89,000

Note:

1. 'Discount on issue of debentures' may alternatively be shown as 'Other non-current asset' and amortised over the tenure of debenture.
2. Liquidation expenses has been routed through goodwill in the above solution. However, alternatively, same may be written off as an adjustment to general reserve.

Working Notes:

1. Computation of Goodwill on absorption

	₹	₹	₹
Purchase Consideration			51,62,400
Assets taken over			
Property, plant and equipment	20,00,000		
Add: Increase by 20%	4,00,000	24,00,000	
Investments		4,00,000	
Current Assets:			
Inventory	11,60,000		
Less: Reduction in value by 10%	(1,16,000)	10,44,000	
Trade Receivables	9,68,000		
Less: Provision for doubtful debts [(9,68,000 – 18,000) x 10%]	(95,000)	8,73,000	
Cash at Bank		1,02,000	
		48,19,000	
Less: Outside Liabilities:			
12% Debentures at 10% premium	5,50,000		
Trade Payables	8,20,000		
Provision for interest on debentures	60,000	(14,30,000)	(33,89,000)
Goodwill			17,73,400

2. Number of debentures of Blue Ltd. issued to Green Ltd.

12% Debentures of Green Ltd.	5,00,000
Taken over by Blue Ltd. at 10% premium	50,000
	5,50,000

Issued 14% Debentures of Blue Ltd. at 12% discount = 5,50,000 / 88% = 6,25,000.

Question 3

A Ltd, a listed Company, entered into an expansion programme on 1st April, 2020. On that date the Company purchased from B Ltd. its investments in two Private Limited Companies. The purchase was of

(a) The entire share capital of C Ltd. and

(b) 50% of the share capital of D Ltd.

Both the investments were previously owned by B Ltd. After acquisition by A Limited, D Ltd. was to be run by A Ltd. and B Ltd. as a jointly controlled entity.

A Ltd. makes its financial statements up to 31st March each year. The terms of acquisition were:

C Ltd.

The total consideration was based on price earnings (P/E) of 12 applied to the reported profit of ₹ 45 lakh of C Ltd. for the year 31st March, 2020. The consideration was settled by A Ltd. issuing 8% debentures for ₹ 315 lakh (at par) and the balance by a new issue of ₹ 1 equity shares, based on its market value of ₹ 2.50 each.

D Ltd.

The market value of D Ltd. on 1st April, 2020 was mutually agreed as ₹ 843.75 lakh. A Ltd. satisfied its share of 50% of this amount by issuing 168.75 lakh ₹ 1 equity shares (market value ₹ 2.50 each) to B Ltd.

A Ltd. has not recorded in its books the acquisition of the above investments or the discharge of the consideration.

The summarised statements of financial position of the three entities at 31st March, 2021 are:

(₹ in thousand)

	A Ltd.	*C Ltd.*	*D Ltd.*
Liabilities			
Equity capital ₹ 1 each	*22,500.00*	*45,000.00*	*56,250.00*
Retained earnings	*46,800.00*	*33,750.00*	*10,125.00*
Trade and other payables	*38,520.00*	*11,857.50*	*31,725.00*
Overdraft	*3,465.00*		
Provision for taxes	*12,690.00*	*5,400.00*	*1,710.00*
	1,23,975.00	*96,007.50*	*99,810.00*
Assets			
Property, plant and equipment	*77,085.00*	*60,750.00*	*47,385.00*
Inventories	*21,690.00*	*16,200.00*	*41,940.00*
Trade receivables	*25,200.00*	*11,385.00*	*10,395.00*
Cash		*7,672.50*	*90.00*
	1,23,975.00	*96,007,50*	*99,810.00*

Additional information are as follows:

(i) The book values of the net assets of C Ltd. and D Ltd. on the date of acquisition were considered to be a reasonable approximation to their fair values.

(ii) The current profit of C Ltd. and D Ltd. for the year ended 31st March, 2021 were ₹ 180 lakh and ₹ 45 lakh respectively. No dividends were paid by any of the companies during the year.

(iii) D Ltd. the jointly controlled entity is to be accounted for using proportionate consolidation, in accordance with AS 27 "Interest in Joint Venture".

(iv) Goodwill in respect of the acquisition of D Ltd. has been impaired by ₹ 22.50 lakh at 31st March, 2021. Gain on acquisition, if any, will be separately accounted.

You are required to prepare Consolidated Balance Sheet of A Ltd. and its subsidiaries as at 31st March, 2021. ***(16 Marks)***

Answer

Consolidated Balance Sheet of A Ltd.

with its Subsidiary C Ltd. and Jointly controlled D Ltd. as at 31st March, 2021

Particulars	*Note No.*	*(₹)*
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	4,83,75,000
(b) Reserves and Surplus	2	11,03,62,500
(2) Non-current Liabilities		
(a) Long-term borrowings	3	3,15,00,000
(3) Current Liabilities		
(a) Trade Payables	4	6,62,40,000
(b) Short-term borrowings	5	34,65,000
(c) Short-term provisions	6	1,89,45,000
Total		27,88,87,500
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment	7	16,15,27,500
(b) Intangible assets (W.N.6)		90,00,000
(2) Current assets		
(a) Inventories	8	5,88,60,000

	(b) Trade receivables	9	4,17,82,500
	(c) Cash and cash equivalents	10	77,17,500
	Total		27,88,87,500

Notes to Accounts

			₹
1.	**Share capital**		
	Equity capital ₹ (2,25,00,000 + 90,00,000 + 1,68,75,000)		4,83,75,000
	(Out of the above 2,58,75,000 thousand shares have been issued for consideration other than cash)		
2.	**Reserves and surplus**		
	Retained earnings (W.N.4)	6,48,00,000	
	Capital reserve (W.N.5)	67,50,000	
	Securities premium	3,88,12,500	11,03,62,500
3.	**Long-term borrowings**		
	8% Debentures		3,15,00,000
4.	**Trade payables**		
	(3,85,20,000 + 1,18,57,500 + 1,58,62,500)		6,62,40,000
5.	**Short-term borrowings**		
	Overdraft		34,65,000
6.	**Short-term provisions**		
	Provision for taxes (1,26,90,000 + 54,00,000 + 8,55,000)		1,89,45,000
7.	**Property, plant and equipment**		
	Tangible assets (7,70,85,000 + +6,07,50,000 + 2,36,92,500)		16,15,27,500
8.	**Inventories**		
	(2,16,90,000 + 1,62,00,000 + 2,09,70,000)		5,88,60,000
9.	**Trade receivables**		
	(2,52,00,000 + 1,13,85,000 + 51,97,500)		4,17,82,500
10.	**Cash and cash equivalents**		
	Cash (76,72,500 + 45,000)		77,17,500

Working Notes:

1. **Purchase consideration paid to C Ltd.**

   Earnings per share for the year 31st March, 2020

   $$= \frac{45,00,000}{4,50,00,000} = ₹\ 0.10 \text{ per share}$$

   Market price per share = ₹ 0.10 x 12 (i.e. P/E ratio) = ₹ 1.20 per share

   Purchase consideration = ₹ 1.20 x 4,50,00,000 shares = ₹ 5,40,00,000

   Purchase consideration to be paid as under:

8% Debentures	₹ 3,15,00,000
Equity Shares (90,00,000 shares of ₹ 2.50 each)	₹ 2,25,00,000
	₹ 5,40,00,000

2. **Consideration paid to D Ltd.**

	(₹)
Total market value (as given)	8,43,75,000
50% Shares acquired by A Ltd. (1,68,75,000 shares @ ₹ 2.50 each)	4,21,87,500

3. **Analysis of retained earnings of C Ltd. as on 31st March, 2021**

	(₹)
Retained earnings given in balance sheet on 31.3.2021	3,37,50,000
Less: Current profits for the year ended 31.3.2021 (Post-acquisition)	(1,80,00,000)
Pre-acquisition retained earnings	1,57,50,000

   A Ltd. has 100% share in pre and post-acquisition profits of C Ltd.

4. **Retained Earnings in the Consolidated Balance Sheet**

	₹
Balance in A Ltd.'s balance sheet	4,68,00,000
Add: Share in post-acquisition profits of C Ltd.	1,80,00,000
Add: Share in post-acquisition profits of D Ltd. (joint venture)	22,50,000
	6,70,50,000
Less: Goodwill (written off)	(22,50,000)
	6,48,00,000

5. Capital Reserve

		₹
Amount Paid for shares of C Ltd.		5,40,00,000
Less: Paid up value of shares	4,50,00,000	
Pre-acquisition profit	1,57,50,000	(6,07,50,000)
Capital Reserve		67,50,000

6. Goodwill

	₹
Amount paid for shares of D Ltd.	4,21,87,500
Less: Paid up value of shares (₹ 5,62,50,000 x 50%)	(2,81,25,000)
Pre-acquisition profit [(1,01,25,000 – 45,00,000) x 50%]	(28,12,500)
Goodwill	1,12,50,000
Less: Impairment loss (Written off)	(22,50,000)
	90,00,000

Question 4

(a) ABC Ltd. is an NBFC providing hire purchase solutions for acquiring consumer durables. The following information is extracted from its books for the year ended 31st March, 2021:

Asset Funded	*Interest overdue but recognise in profit and loss*		*Net book value of assets outstanding (₹ in lakh)*
	Period overdue	*Interest Amount (₹ in lakh)*	
Television	*Up to 12 months*	*960.00*	*40,246*
Washing Machine	*For 24 months*	*204.00*	*4,820*
Refrigerators	*For 30 months*	*101.00*	*2,560*
Air-Conditions	*For 45 months*	*53.50*	*1,294*

Calculate the amount of provision to be made. ***(5 Marks)***

(b) On 1st April, 2020, A Ltd issued ₹ 52,50,000, 6% convertible debentures of face value of ₹ 100 each at par. The debentures are redeemable at a premium of 10% on 31.3.2024 or these may be converted into ordinary shares at the option of the holder, the interest rate for equivalent debentures without conversion rights would have been 10%.

Being compound financial instrument you are required to separate equity and debt portion as on 1.4.2020. ***(5 Marks)***

(c) Explain the carve out in Ind AS 28 from IAS 28 along with the reasons. ***(6 Marks)***

Answer

(a) Table showing provision to be made with respect to hire purchase:

			(₹ in lakh)
(a)	Where hire charges are overdue upto 12 months	Nil	-
(b)	Where hire charges are overdue for more than 12 months but upto 24 months	10% of the net book value 10% x 4,820	482.00
(c)	Where hire charges are overdue for more than 24 months but upto 36 months	40 percent of the net book value 40% x 2,560	1024.00
(d)	Where hire charges or lease rentals are overdue for more than 36 months but upto 48 months	70 percent of the net book value 70% x 1,294	905.80
		Total	2,411.80

(b) Computation of Equity and Debt Component of Convertible Debentures as on 1.4.2020

	₹
Present value of the principal repayable after four years [52,50,000 x 1.10 x 0.683]	39,44,325
Present value of Interest [3,15,000 x 3.17 (4 years cumulative 10% discount factor)]	9,98,550
Value of debt component	49,42,875
Value of equity component (balancing figure)	3,07,125
Proceeds of the issue	52,50,000

(c) ***As per IFRS:*** IAS 28 requires that for the purpose of applying equity method of accounting in the preparation of investor's financial statements, uniform accounting policies should be used. In other words, if the associate's accounting policies are different from those of the investor, the investor should change the financial statements of the associate by using same accounting policies while drawing consolidated financial statements.

Carve out 1: In Ind AS 28, the phrase, 'unless impracticable to do so' has been added in the relevant requirements

Reasons: Certain associates, e.g., regional rural banks (RRBs), being associates of nationalized banks, are not in a position to use the Ind AS as these may be too advanced for the RRBs. Accordingly, the above-stated words have been included to exempt such associates.

Carve out 2: Further, in IAS 28, when Investors share in Net Assets exceeds Cost of Investment, the same is recognised in profit or loss while in Ind AS 28 the same is recognised in capital reserve.

Reasons: Modification has been done on the lines of Ind AS 103, *'Business Combinations'*, to transfer excess of the investor's share of the net fair value of the investee's identifiable assets and liabilities over the cost of investment. Recognition of such gains in profit or loss would result into recognition of unrealised gains, which may get distributed in the form of dividends. Moreover, such a treatment may lead to structuring through acquisitions, which may not be in the interest of the stakeholders of the company.

Question 5

(a) *The directors of a public limited company are considering the acquisition of the entire share capital of an existing company Ramlal Ltd. which is engaged in a line of business suited to them. The directors feel that acquisition of Ramlal Ltd. will not create any further risk to their business interest.*

The following is the summarized Balance sheet of Ramlal Limited as at 31st December, 2020:

Liabilities	*Amount*
Share Capital	
9,000 Equity shares of ₹ 10 each fully paid up	*9,00,000*
Reserve & Surplus	
General Reserve	*6,75,000*
Current Liability	
Bank Overdraft	*5,40,000*
Trade Payables	*6,75,000*
	27,90,000
Assets	*Amount*
Fixed Assets	
Freehold Properties	*13,50,000*
Current Assets	
Inventory	*4,50,000*
Trade Receivables	*7,65,000*
Cash & Bank balance	*2,25,000*
	27,90,000

Ramlal Ltd.'s financial records for the five years were as under:

	Amount (₹)				
	2020	2019	2018	2017	2016
Profit	1,80,000	1,66,500	1,57,500	1,35,000	1,39,500
Extraordinary items	7,875	9,000	(13,500)	(18,000)	(2,250)
	1,87,875	1,75,500	1,44,000	1,17,000	1,37,250
Less: Dividends	(1,08,000)	(90,000)	(90,000)	(72,000)	(72,000)
	79,875	85,500	54,000	45,000	65,250

Additional information:

(i) *There were no changes in the issued capital of Ramlal Ltd. during this period.*

(ii) *The estimated valued of Ramlal Ltd.'s assets on 31.12.2020 are:*

	Replacement Cost	Realizable value
Free hold properties	18,00,000	12,15,000
Inventory	6,75,000	7,20,000

(iii) *For realization purpose, it is anticipated that 1% of the trade receivables may prove to be difficult to be realized.*

(iv) *The cost of capital to the acquiring company is 10%.*

(v) *The current return of an investment of the acquiring company is 10%. Quoted companies with similar business and activities as Ramlal Ltd. have a P/E ratio approximating to 8, although these companies tend to be larger than Ramlal Ltd.*

You are required to estimate the value of the total equity capital of Ramlal Ltd. on 31.12.2020 using each of the following bases:

(1) *Balance Sheet Value*

(2) *Replacement Cost*

(3) *Realizable value*

(4) *P/E ratio model.* ***(8 Marks)***

(b) *From the following information, calculate the value of share if buyer wants to*

(i) *Buy a small lot of shares*

(ii) *Buy a controlling interest in the Company*

Year	Profit (₹ in thousand)	Capital employed (₹ in thousand)	Dividend (%)
2017	13,750.00	85,937.50	12

2018	*40,000.00*	*2,00,000.00*	*15*
2019	*55,000.00*	*2,50,000.00*	*18*
2020	*62,500.00*	*2,50,000.00*	*20*

The market expectation is 12%. ***(8 Marks)***

Answer

(a) Computation of total equity of Ramlal Ltd. on 31.3.2020

			₹	₹
(a)	**Balance Sheet Value**			
	Capital		9,00,000	
	Reserve		6,75,000	15,75,000
(b)	**Replacement cost value**			
	Capital		9,00,000	
	Reserve		6,75,000	
	Appreciation:			
	Freehold properties (18,00,000 - 13,50,000)	4,50,000		
	Inventory (6,75,000 – 4,50,000)	2,25,000	6,75,000	22,50,000
(c)	**Realizable value**			
	Capital		9,00,000	
	Reserve		6,75,000	
	Appreciation in inventory (7,20,000 - 4,50,000)		2,70,000	
	Depreciation in freehold properties (13,50,000 – 12,15,000)		(1,35,000)	
	Book debts (Bad) (7,65,000 x 1%)		(7,650)	17,02,350

(d) P/E ratio model

Comparable quoted companies have a P/E ratio of 8. Ramlal Ltd. is prima facie a small company.

If a P/E ratio of 6 is adopted, the valuation will be 1,80,000 x 6 = ₹ 10,80,000.

If a P/E ratio of 7 were to be adopted, the valuation will be 1,80,000 x 7 = ₹ 12,60,000.

(b) (i) Buying a small lot of shares: If the purpose of valuation is to provide data base to aid a decision of buying a small (non-controlling) position of the equity of a company, dividend yield method is most appropriate. Since dividend rate is rising continuously, weighted average will be more appropriate for calculation of average dividend.

Year	*Rate of dividend*	*Weight*	*Product*
2017	12	1	12
2018	15	2	30
2019	18	3	54
2020	20	4	80
		10	176

Average dividend rate = $\frac{176}{10}$ = 17.6%

Value of a share on the basis of dividend for buying a small lot of shares will be

$$\frac{\text{Average dividend rate}}{\text{Market expectation rate}} \times 100 = \frac{17.6}{12} \times 100 = ₹\ 146.67 \text{ per share.}$$

(ii) Buying a controlling interest in the company: If the purpose of valuation is to provide data base to aid a decision of buying controlling interest in the company, total profit will be relevant to determine the value of shares as the shareholders have capacity to influence the decision of distribution of profit. As the profit is rising, weighted average will be more appropriate for calculation of average profit/yield.

Year	*Yield % (Profit/Capital employed) x 100*	*Weight*	*Product*
2017	16	1	16
2018	20	2	40
2019	22	3	66
2020	25	4	100
		10	222

Average yield = $\frac{222}{10}$ = 22.2%

If controlling interest in the company is being taken over, then the value per share will be = $\frac{\text{Average yield rate}}{\text{Market expectation rate}} \times 100 = \frac{22.2}{12} \times 100$ = ₹ 185 per share.

Note: Nominal value of shares has been assumed as ₹ 100 each.

Question 6

(a) Following information is provided in respect of Jack Ltd. as on 31st March, 2021:

	(₹ in lakh)
Turnover (including discounts worth ₹ 10 lakh)	*2,020*
Plant and machinery (net)	*700*
Depreciation on plant and machinery	*105*
Trade Receivables	*190*
Dividend to Equity shareholders	*75*
Trade Payables	*170*

Stock (₹ in lakh)	*Raw-Materials*	*WIP & Finished*
Opening stock 1.4.2020	*80*	*40*
Closing stock 31.3.2021	*120*	*10*

Raw material purchased during the year	*500*
Cash at bank	*125*
Travelling & Conveyance	*25*
Audit fee expenses	*10*
Wages and salaries	*250*
Employees State Insurance expenses	*20*
Provident fund contribution	*30*
Retained profit (opening balance)	*800*
Retained profit for the year	*325*
Transfer to reserve	*100*
Rent paid	*60*
Other overhead expenses	*70*
Ordinary share capital (₹ 100 each)	*1,500*
Interest on borrowings	*50*
Income tax for the year	*400*

Number of employees working in the company Jack Ltd. is 90 during the financial year 2020-2021.

You are required to:

(i) Prepare Value Added Statement and its application for the year ended 31.3.2021

(ii) Value Added per Employee for the year

(iii) Average Earnings per Employee for the year

(iv) Sales per Employee for the year. ***(8 Marks)***

(b) Reshma Ltd. grants 1,000 employee stock options on 1.4.2017 at ₹ 80 when the market price is ₹ 320. The vesting period is two and half years and the maximum exercise period is one year. 300 unvested options lapsed on 1.5.2019. 600 options were exercised on 30.6.2020, 100 vested options lapsed at the end of the exercise period. Pass journal entries with suitable narrations. ***(8 Marks)***

Answer

(a) (i) **Value Added Statement of Jack Ltd. for the period ended on 31.3.2021**

		(₹ in lakh)
Sales (net) (2,020 – 10)		2,010
Less: Cost of bought in materials and services:		
Raw material consumed (80 + 500 – 120)	460	
Change in stock of WIP & Finished goods (40 - 10)	30	
Travelling & conveyance	25	
Auditors' remuneration	10	
Rent paid	60	
Other overhead expenses	70	(655)
Value added by manufacturing and trading activities		1,355

Application of Value Added

		(₹ in lakh)	*(₹ in lakh)*	%
To	Pay Employees:			
	Wages and salaries	250		
	Employees state insurance	20		
	Provident fund contribution	30	300	22.14
To	Pay Government:			
	Income-tax		400	29.52
To	Pay Providers of Capital:			
	Interest on borrowings	50		
	Dividend	75	125	9.23

To	Provide for maintenance and expansion of the company:			
	Depreciation	105		
	Transfer to reserve	100		
	Retained profit	325	530	39.11
			1,355	100

(ii) Value Added per Employee = Value Added / No. of Employees

= 1,355 \ 90 = 15.06

(iii) Average Earnings per Employee = Average Earnings of Employee / No. of Employees

= (250 + 20 + 30) / 90 = 3.33

(iv) Sales per Employee = Sales / No. of Employees

= 2,010 / 90 = 22.33

(b) Journal Entries in the books of Reshma Ltd.

Date	*Particulars*		*Dr. (₹)*	*Cr. (₹)*
31.3.2018	Employees compensation expenses account (W.N.1)	Dr.	96,000	
	To Employees stock option outstanding account (W.N.1)			96,000
	(Being compensation expenses recognized in respect of the employees stock option i.e. 1,000 options granted to employees at a discount of ₹ 240 each (320-80), amortised on straight line basis over $2\frac{1}{2}$ years)			
	Profit and loss account	Dr.	96,000	
	To Employees compensation expenses account			96,000
	(Being expenses transferred to profit and loss account at the end of the year)			
31.3.2019	Employees compensation expenses account	Dr.	96,000	
	To Employees stock option outstanding account			96,000

	(Being compensation expenses recognized in respect of the employee stock option i.e. 1,000 options granted to employees at a discount of ₹ 240 each, amortised on straight line basis over $2\frac{1}{2}$ years)			
	Profit and loss account	Dr.	96,000	
	To Employees compensation expenses account			96,000
	(Being expenses transferred to profit and loss account at the end of the year)			
31.3.2020	Employees stock option outstanding account (W.N.2)	Dr.	24,000	
	To General Reserve account (W.N.2)			24,000
	(Being excess of employees compensation expenses transferred to general reserve account)			
30.6.2020	Bank A/c (600 x ₹ 80)	Dr.	48,000	
	Employees stock option outstanding account (600 x ₹ 240)	Dr.	1,44,000	
	To Equity share capital account (600 x ₹ 10)			6,000
	To Securities premium account (600 x ₹ 310)			1,86,000
	(Being 600 employees stock option exercised at an exercise price of ₹ 80 each)			
1.10.2020	Employees stock option outstanding account	Dr.	24,000	
	To General reserve account			24,000
	(Being Employees stock option outstanding A/c transferred to General Reserve A/c on lapse of 100 vested options at the end of the exercise period)			

Note: In the Journal entry passed above on 30.6.2020, it is assumed that the nominal price of a share is ₹ 10 each.

Working Note:

1. Annual Cost

Number of employees		1,000
Cost of option	(320-80)	240
Total Cost		2,40,000
Per year cost	2,40,000 /2.50	96,000

2. On 31.3.2020, Reshma Ltd. will examine its actual forfeitures and make necessary adjustments, if any, to reflect expenses for the number of options that have actually vested. 700 employees stock options have completed 2.5 years vesting period, the expense to be recognized during the year is in negative i.e.

	₹
Number of options actually vested (700 x ₹ 240)	1,68,000
Less: Expenses recognized till 31.3.2019 (96,000 + 96,000)	(1,92,000)
Excess expenses transferred to general reserve	(24,000)

Question 7

*Answer any **four** of the following:*

(A) *Explain whether the following will constitute a change in accounting policy or not as per AS 5:*

(i) *Introduction of a formal retirement gratuity scheme by an employer in place of adhoc ex-gratia payments to employees on retirement.*

(ii) *Management decided to pay pension to those employees who have retired after completing 5 years of service in the organization. Such employees will get pension of ₹ 15,000 per month. Earlier there was no such scheme of pension in the organization.*

(b) *What is the meaning of 'valuation of liabilities'? State the purpose of valuation of liabilities in financial accounting and reporting.*

(c) *X Ltd. a parent company with subsidiaries holds 25% of the equity shares in Y Ltd. During the year, X Ltd. makes sales of ₹ 15,00,000 to Y Ltd. at cost plus a 25% mark up. At the end of the year, Y Ltd. has all these goods still in inventories. State the entries to be passed if associate has made sale to parent company and goods are still in inventories of parent company.*

(d) *What is interim period and what is interim period Financial Report as per Ind AS 34?*

(e) *The Balance Mutual Fund raised ₹ 500 lakh on 1st April, 2020 by issue of 5 lakh units of ₹ 100 per unit. The fund invested in several capital market instruments both in debt and equity to build a portfolio of ₹ 475 lakh. The initial expenses amounted to ₹ 12 lakh. During the financial year 2020-2021, the fund sold certain securities of cost ₹ 200 lakh for ₹ 215 lakh. Fund further invested in shares for ₹ 60 lakh on 1st June, 2020 and purchased certain other securities for ₹ 70 lakh on 30th September, 2020.*

During the financial year, the fund management expenses on an average amounted to ₹ 3.50 lakh per month of which ₹ 3.50 lakh was in arrears at the end of the year. The dividend earned during the period was ₹ 20 lakh. 60% of the realized earnings were distributed. The market value of the portfolio on 31.3.2021 was ₹ 525 lakh. You are required to determine the NAV of the fund at 31.3.2021. ***(4 x 4 = 16 Marks)***

Answer

(a) As per para 31 of AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy.

(i) Accordingly, introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is not a change in an accounting policy.

(ii) Similarly, the adoption of a new accounting policy for events or transactions which were not in place previously or were immaterial, will not be treated as a change in an accounting policy.

(b) Valuation of liability means measurement of item in monetary terms.

Proper valuation of liabilities is required to ensure true and fair financial position of the business entity. In other words, all matters which affect the financial position of the business has to be disclosed.

Under-valuation or over-valuation of liabilities may not only affect the operating results and financial position of the current period but will also affect the financial statements of next accounting period.

(c) Unrealised gain = [(15,00,000 / 125%) x 25%] = ₹ 3,00,000

Share of holding company in associate's unrealized gain = ₹ 3,00,000 x 25% = ₹ 75,000

In consolidated financial statements

Entry for elimination of unrealized profit would be:

Consolidated profit and loss account	Dr.	75,000	
To Investment in Associate A/c			75,000

(d) Interim period is a financial reporting period shorter than a full financial year.

Interim financial report means a financial report containing either a complete set of financial statements or a set of condensed financial statements for an interim period. An interim Financial Report shall include, at minimum, the following:

(i) A condensed Balance-sheet

(ii) A condensed statement of Profit and Loss

(iii) A condensed statement of changes in equity

(iv) A condensed statement of cash flows

(v) Selected Explanatory notes

(e) Table showing determination closing NAV of the Mutual Fund

	₹ in lakh	*₹ in lakh*	
Amount Raised in Scheme	500.00		
Less: Investment in Securities	(475.00)		
Initial Expenses on Issue	(12.00)		
Balance	13.00		
Add: Proceeds from sale of securities	215.00		
Dividend received	20.00	248.00	
Less: Cost of securities (60 + 70)	130.00		
Fund management expenses [(3.50 x 12) – 3.50]	38.50		
Distribution on realised earning –Capital gains and dividend earned [60% of {(215.00 – 200.00) + 20}]	21.00	(189.50)	
Closing bank balance		58.50	
Closing market value of portfolio		525.00	
		583.50	
Less: Arrears of expenses		(3.50)	
Closing net assets		580.00	
Number of units			5,00,000
Closing Net Assets Value (NAV)			₹ 116.00