

## PAPER –1: FINANCIAL REPORTING

### PART – I : RELEVANT AMENDMENTS, NOTIFICATIONS AND ANNOUNCEMENTS

#### A. Applicable for May, 2018 Examination

##### 1. Amendments in Accounting Standards

The Ministry of Corporate Affairs (MCA) has notified Companies (Accounting Standards) Amendment Rules, 2016 (G.S.R. 364(E) dated 30.03.2016). It has omitted AS 6, Depreciation Accounting and amended the following Accounting Standards issued under Companies (Accounting Standards) Rules, 2006:

- (i) AS 2, Valuation of Inventories
- (ii) AS 4, Contingencies and Events Occurring After the Balance Sheet Date
- (iii) AS 10, Property, Plant and Equipment
- (iv) AS 13, Accounting for Investments
- (v) AS 14, Accounting for Amalgamations
- (vi) AS 21, Consolidated Financial Statements
- (vii) AS 29, Provisions, Contingent Liabilities and Contingent Assets

With the view to harmonise Accounting Standards issued by the ICAI for non-corporate entities and the amendments to the Accounting Standards notified by the Central Government, the Council of the ICAI decided that the amendments notified by the Central Government shall also be incorporated in the Accounting Standards issued by the ICAI for non-corporate entities.

Following table summarises the changes made by the Companies (Accounting Standards) Amendment Rules, 2016 vis-a-vis the Companies (Accounting Standards) Rules, 2006 in the following accounting standards:

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
AS 2	4 (an extract)	Inventories do not include machinery spares which can be used only in	Inventories do not include spare parts, servicing equipment and standby equipment which	Now, inventories also do not include servicing equipment and standby equipment other

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
		connection with an item of fixed asset and whose use is expected to be irregular; such machinery spares are accounted for in accordance with Accounting Standard (AS) 10, Accounting for Fixed Assets.	meet the definition of property, plant and equipment as per AS 10, Property, Plant and Equipment. Such items are accounted for in accordance with Accounting Standard (AS) 10, Property, Plant and Equipment.	than spare parts if they meet the definition of property, plant and equipment as per AS 10, Property, Plant and Equipment.
	27	Common classifications of inventories are raw materials and components, work in progress, finished goods, stores and spares, and loose tools.	Common classifications of inventories are: (a) Raw materials and components (b) Work-in-progress (c) Finished goods (d) Stock-in-trade (in respect of goods acquired for trading) (e) Stores and spares (f) Loose tools (g) Others (specify nature)".	Para 27 of AS 2 requires disclosure of inventories under different classifications. One residual category has been added to the said paragraph i.e. 'Others'.

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
AS 4	Footnote to AS 4	Pursuant to AS 29, Provisions, Contingent Liabilities and Contingent Assets, becoming mandatory in respect of accounting periods commencing on or after 1-4-2004, all paragraphs of this Standard that deal with contingencies (viz. paragraphs 1(a), 2, 3.1, 4 (4.1 to 4.4), 5 (5.1 to 5.6), 6, 7 (7.1 to 7.3), 9.1 (relevant portion), 9.2, 10, 11, 12 and 16) stand withdrawn except to the extent they deal with impairment of assets not covered by other Indian Accounting	All paragraphs of this Standard that deal with contingencies are applicable only to the extent not covered by other Accounting Standards prescribed by the Central Government. For example, the impairment of financial assets such as impairment of receivables (commonly known as provision for bad and doubtful debts) is governed by this Standard.	Footnote has been modified.

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
		Standards. For example, impairment of receivables (commonly referred to as the provision for bad and doubtful debts), would continue to be covered by AS 4.		
	8.5	There are events which, although they take place after the balance sheet date, are sometimes reflected in the financial statements because of statutory requirements or because of their special nature. Such items include the amount of dividend proposed or declared by the enterprise after the balance sheet date in respect of the	There are events which, although they take place after the balance sheet date, are sometimes reflected in the financial statements because of statutory requirements or because of their special nature. For example, if dividends are declared after the balance sheet date but before the financial statements are approved for issue, the dividends are not recognised as a	No liability for proposed dividends has to be created now. Such proposed dividends are to be disclosed in the notes.

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
		period covered by the financial statements.	liability at the balance sheet date because no obligation exists at that time unless a statute requires otherwise. Such dividends are disclosed in the notes.	
	14	Dividends stated to be in respect of the period covered by the financial statements, which are proposed or declared by the enterprise after the balance sheet date but before approval of the financial statements, should be adjusted.	If an enterprise declares dividends to shareholders after the balance sheet date, the enterprise should not recognise those dividends as a liability at the balance sheet date unless a statute requires otherwise. Such dividends should be disclosed in notes.	No liability for proposed dividends has to be created now. Such proposed dividends are to be disclosed in the notes.
AS 10	All	Accounting for Fixed Assets	Property, Plant and Equipment	Entire standard has been revised with the title AS 10 : 'Property, Plant and Equipment' by replacing AS 6 'Depreciation

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
				Accounting' and AS 10 'Accounting for Fixed Assets'.
AS 13	20	The cost of any shares in a co-operative society or a company, the holding of which is directly related to the right to hold the investment property, is added to the carrying amount of the investment property.	An investment property is accounted for in accordance with cost model as prescribed in Accounting Standard (AS) 10, Property, Plant and Equipment. The cost of any shares in a co-operative society or a company, the holding of which is directly related to the right to hold the investment property, is added to the carrying amount of the investment property.	Accounting of investment property was not stated in this para but now incorporated i.e. at cost model.
	30	An enterprise holding investment properties should account for them as long term	An enterprise holding investment properties should account for them in accordance with cost model	Accounting of investment property shall now be in accordance with AS 10 i.e. at cost model

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
		investments.	as prescribed in AS 10, Property, Plant and Equipment.	
AS 14	3(a)	Amalgamation means an amalgamation pursuant to the provisions of the Companies Act, 1956 or any other statute which may be applicable to companies.	Amalgamation means an amalgamation pursuant to the provisions of the Companies Act, 2013 or any other statute which may be applicable to companies and includes 'merger'.	Definition of Amalgamation has been made broader by specifically including 'merger'.
	18 and 39	In such cases the statutory reserves are recorded in the financial statements of the transferee company by a corresponding debit to a suitable account head (e.g., 'Amalgamation Adjustment Account') which is disclosed as a part of 'miscellaneous expenditure' or	In such cases the statutory reserves are recorded in the financial statements of the transferee company by a corresponding debit to a suitable account head (e.g., 'Amalgamation Adjustment Reserve') which is presented as a separate line item. When the identity of the statutory	Corresponding debit on account of statutory reserve in case of amalgamation in the nature of purchase is termed as 'Amalgamation Adjustment Reserve' and is now to be presented as a separate line item since there is not sub-heading like 'miscellaneous expenditure' in Schedule III to the Companies

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
		other similar category in the balance sheet. When the identity of the statutory reserves is no longer required to be maintained, both the reserves and the aforesaid account are reversed.	reserves is no longer required to be maintained, both the reserves and the aforesaid account are reversed.	Act, 2013
AS 21	9	A parent which presents consolidated financial statements should consolidate all subsidiaries, domestic as well as foreign, other than those referred to in paragraph 11.	A parent which presents consolidated financial statements should consolidate all subsidiaries, domestic as well as foreign, other than those referred to in paragraph 11. Where an enterprise does not have a subsidiary but has an associate and/or a joint venture such an enterprise should also prepare	Amendment has been made in line with the provisions of the Companies Act, 2013.

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
			consolidated financial statements in accordance with Accounting Standard (AS) 23, Accounting for Associates in Consolidated Financial Statements, and Accounting Standard (AS) 27, Financial Reporting of Interests in Joint Ventures respectively.	
	Illustration (vi)	A statement showing the computation of net profits in accordance with section 349 of the Companies Act, 1956, with relevant details of the calculation of the commissions payable by way of percentage of such profits to the directors (including	A statement showing the computation of net profits in accordance with section 198 of the Companies Act, 2013, with relevant details of the calculation of the commissions payable by way of percentage of such profits to the directors (including managing directors) or	Reference to the Companies Act, 2013 has been inserted by removing the reference of the Companies Act, 1956.

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
		managing directors) or manager (if any).	manager (if any).	
AS 29	35 (An extract)	The amount of a provision should not be discounted to its present value.	The amount of a provision should not be discounted to its present value except in case of decommissioning, restoration and similar liabilities that are recognised as cost of Property, Plant and Equipment. The discount rate (or rates) should be a pre-tax rate (or rates) that reflect(s) current market assessments of the time value of money and the risks specific to the liability. The discount rate(s) should not reflect risks for which future cash flow estimates have been adjusted. Periodic unwinding of	Now discounting of provision for decommissioning, restoration and similar liabilities has to be done as per the pre-tax discount rate as mentioned therein.

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
			discount should be recognised in the statement of profit and loss.	
	73		<b><u>Transitional Provisions</u></b> All the existing provisions for decommissioning, restoration and similar liabilities (see paragraph 35) should be discounted prospectively, with the corresponding effect to the related item of property, plant and equipment.	Discounting of above existing provisions and similar liabilities should be prospectively, with the corresponding effect to the related item of property, plant and equipment.

## 2. Indian Accounting Standards

The topic "Introduction of Indian Accounting Standards (Ind AS); Comparative study of ASs vis-à-vis Ind ASs; Carve outs/ins in Ind ASs vis-à-vis International Financial Reporting Standards (IFRSs)" had been included in the syllabus and is applicable for May, 2018 Examination.

However, considering the extensive coverage of the contents covered in this topic, small simple problems involving conceptual or application issues may be asked in the examination.

It may be noted that Accounting Standards will continue to be applicable for May, 2018 examination for all chapters except Chapter 2 as mentioned above and Chapter 6 on 'Accounting and Reporting of Financial Instruments' which would be based on Ind AS 32, 107 and 109.

**3. Companies (Indian Accounting Standards) (Amendment) Rules, 2016**

MCA has issued Companies (Indian Accounting Standards) (Amendment) Rules, 2016 to amend Companies (Indian Accounting Standards) Rules, 2015. The amended Rules, inter alia, provide the following:

- ◆ Roadmap for implementation of Ind AS by Non-Banking Financial Companies;  
As per the notification,
  - (a) The following NBFCs shall comply with the Indian Accounting Standards (Ind AS) for accounting periods beginning on or after the 1st April, 2018, with comparatives for the periods ending on 31st March, 2018, or thereafter—
    - (A) NBFCs having net worth of rupees five hundred crore or more;
    - (B) holding, subsidiary, joint venture or associate companies of companies covered under item (A),
  - (b) The following NBFCs shall comply with the Indian Accounting Standards (Ind AS) for accounting periods beginning on or after the 1st April, 2019, with comparatives for the periods ending on 31st March, 2019, or thereafter—
    - (A) NBFCs whose equity or debt securities are listed or in the process of listing on any stock exchange in India or outside India and having net worth less than rupees five hundred crore;
    - (B) NBFCs, that are unlisted companies, having net worth of rupees two-hundred and fifty crore or more but less than rupees five hundred crore; and
    - (C) holding, subsidiary, joint venture or associate companies of companies covered under item (A) or item (B) of sub-clause (b),
- ◆ Omission of Ind AS 115, 'Revenue from Contracts with Customers', and insertion of Ind AS 11, 'Construction contracts' and Ind AS 18, 'Revenue';
- ◆ Consequential amendments to other Ind AS on the omission of Ind AS 115 and inclusion of Ind AS 11 and Ind AS 18.
- ◆ MCA also made certain amendments in some notified Ind AS to reflect the amendments made by the IASB to the IFRS either on account of narrow-focus improvements to disclosure requirements that the IASB had identified to International Accounting Standard (IAS) 1, 'Presentation of Financial Statements'

or due to the annual improvement cycle\* 2012–2014 or amendments to IFRS 10, 'Consolidated Financial Statements'; IFRS 12, 'Disclosure of Interests in Other Entities'; and IAS 28, 'Investments in Associates and Joint Ventures', to address issues that have arisen in relation to the exemption from consolidation for investment entities or amendment in Ind AS 101, 'First-time adoption of Indian Accounting Standards', to remove the option to use fair value for investment property as the deemed cost on the date of transition.

The key amendments to Ind AS pursuant to the Companies (Indian Accounting Standards) (Amendments) Rules, 2016 are listed below:

Ind AS	Significant amendments
Ind AS 1, 'Presentation of Financial Statements'	<ul style="list-style-type: none"> <li data-bbox="619 775 847 808">• <b>On Materiality</b></li> <li data-bbox="619 808 1329 1010">The amendments clarify that while aggregating information in the financial statements, an entity must not reduce the understandability of its financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures or functions.</li> <li data-bbox="619 1010 1329 1211">The amendments further accentuated that even when a standard requires a specific disclosure, the information must be assessed as to that its insufficiency may not prevent users of financial statements to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.</li> <li data-bbox="619 1211 1031 1245">• <b>On presentation of Subtotals</b></li> <li data-bbox="619 1245 1329 1424">An entity shall present additional line items (including by disaggregating the line items listed in paragraph 54), headings and subtotals in the balance sheet when such presentation is relevant to an understanding of the entity's financial position.</li> <li data-bbox="619 1424 1329 1606">An entity has to present additional subtotals in the balance sheet or the statement of profit and loss labelled it in a manner that makes the line items understandable. Also as per the amendment, such sub totals shall be consistent from period to period and not be displayed with more prominence</li> </ul>

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\* The 'annual improvements process of IASB' is a vehicle for making non-urgent but necessary amendments to the standards. These amendments are limited to the changes that either clarify the wordings in an IFRS or correct relatively minor unintended consequences, oversights or conflicts between the existing requirements of the IFRS.

Ind AS	Significant amendments
	<p>than the subtotals and totals required in Ind AS.</p> <p>The amendments require that additional subtotals in the statement of profit and loss should be reconciled to the subtotals and totals required by Ind AS 1.</p> <ul style="list-style-type: none"> <li> <b>On Systematic Grouping and Presentation of Notes</b> <p>The management of an entity shall consider the understandability and comparability of the financial statements when it determines the group or order of the notes. An entity might, for example, present more significant notes first, or present linked areas sequentially. Such flexibility allows management to alter their presentation to their circumstances.</p> <p>The notification also states that the share of other comprehensive income arising from investments accounted for under the equity method is grouped based on whether the items will or will not subsequently be reclassified to profit or loss. Each group should then be presented as a single line item in the statement of other comprehensive income.</p> </li> <li> <b>On Disclosure of Accounting Policies</b> <p>Paragraph 120 of Ind AS 1 has been deleted which included the examples of significant accounting policies i.e., the income taxes accounting policy and the foreign currency accounting policy since they were not found significant.</p> </li> </ul>
Ind AS 19, 'Employee benefits'	<p><b>Actuarial Assumptions: Discount Rate</b></p> <p>The amendment clarifies that for determining the discount rate for post-employment benefit obligations, with respect to currencies other than Indian rupee for which there is deep market in high quality corporate bonds, the market yields (at the end of the reporting period) on such high quality corporate bonds denominated in that currency shall be used.</p>
Ind AS 28, 'Investments in associates and joint ventures'	<p>As per the amendment, if an entity that is not itself an investment entity has an interest in an associate or joint venture that is an investment entity, the entity may, when applying the equity method, retain the fair value measurement applied by that investment entity associate or joint venture to its interest in subsidiaries.</p>
Ind AS 34, 'Interim financial'	<p>Ind AS 34 requires entities to disclose information in the notes to the interim financial statements, 'if not disclosed elsewhere in the interim financial report'.</p>

Ind AS	Significant amendments
reporting'	Amendment in Ind AS 34 clarified that such disclosures shall be given either in the interim financial statements or incorporated by cross-reference from the interim financial statements to some other statement (such as management commentary or risk report) that is available to users of the financial statements on the same terms as the interim financial statements and at the same time. If users of the financial statements do not have access to the information incorporated by cross-reference on the same terms and at the same time, the interim financial report is incomplete. The information shall normally be reported on a financial year-to-date basis.
Ind AS 101, 'First-time adoption of Indian Accounting Standards'	Ind AS 40 only permits the cost model for measurement of investment properties after initial recognition. Hence, the amendment has been made to remove the option to use fair value for investment property as the deemed cost under Ind AS 101 on the date of transition.
Ind AS 105, 'Non-current Assets held for Sale and Discontinued Operations'	<p>The amendment clarifies that when an asset (or disposal group) is reclassified from 'held for sale' to 'held for distribution', or vice versa, then the change in classification is considered a continuation of the original plan of disposal.</p> <p>The entity shall apply the classification, presentation and measurement requirements as are applicable to the new method of disposal and shall measure such asset at lower of its carrying amount and fair value less costs to sell/distribute, as the case may be, and recognise any reduction or increase on it.</p> <p>The amendment also clarifies that changing the disposal method does not change the date of classification.</p>
Ind AS 107, 'Financial Instruments: Disclosures'	If an entity transfers a financial asset to a third party under conditions which allow the transferor to derecognise the asset, Ind AS 107 requires disclosure of all types of continuing involvement that the entity might still have in the transferred assets. The amendment in Ind AS 107 illustrates the term 'continuing involvement' in context of service contracts.
Ind AS 110, 'Consolidated Financial	<p><b>Exemptions for application of Ind AS 110</b></p> <ul style="list-style-type: none"> <li>● Paragraph 31 of Ind AS 110 requires an investment entity to measure an investment in a subsidiary at fair</li> </ul>

Ind AS	Significant amendments
Statements'	<p>value through profit or loss in accordance with Ind AS 109, 'Financial instruments'. It has been clarified that, as an exception to this, an investment entity would consolidate a subsidiary only if it is not an investment entity itself, and if it acts as an extension of the investment entity by providing services that support the investment entity's activities. All subsidiaries that are themselves investment entities are measured at fair value through profit and loss.</p> <ul style="list-style-type: none"> <li>• Another exemption for non-application of this Ind AS 110 is on post-employment benefit plans or other long-term employee benefit plans to which Ind AS 19, Employee Benefits, applies.</li> <li>• Ind AS 110 was amended to clarify that the exemption from preparing consolidated financial statements contained in paragraph 4(a) of Ind AS 110 is available to a parent entity that is a subsidiary of an investment entity (provided all other conditions in paragraph 4(a) are met) even when the investment entity measures all of its subsidiaries at fair value.</li> </ul>
Ind AS 112, 'Disclosure of Interests in Other Entities'	<p>The amendment clarifies the application of the standard to investment entities. An investment entity, that prepares separate financial statements in which all of its subsidiaries are measured at fair value through profit or loss in accordance with Ind AS 109, requires to present the disclosures in respect of such investment entities as per Ind AS 112. This amendment to Ind AS 112 is consequential to the amendments to Ind AS 28 and Ind AS 110.</p>

**4. Applicability of Amendments to Ind AS 7 and Ind AS 102 issued by the MCA dated 17th March 2017**

To align Ind AS with IFRS, the recent amendments made in IAS 7 and IFRS 2 by the IASB have been incorporated in Ind AS 7 'Statement of Cash Flows' and Ind AS 102 'Share-based Payment' by way of a notification issued by the Ministry of Corporate Affairs on 17th March, 2017.

**A. Amendments in Ind AS 7 'Statement of Cash Flows'**

**(i) Disclosure requirements**

The amendments made to Ind AS 7 require certain additional disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.

In addition to the above, the disclosure is required for changes in financial assets (for example, assets that hedge liabilities arising from financing activities) if cash flows from those financial assets were, or future cash flows will be, included in cash flows from financing activities.

As per the amendment, one of the way for disclosure is providing a reconciliation between the opening and closing balances in the balance sheet for liabilities arising from financing activities, including the changes identified, by linking items included in the reconciliation to the balance sheet and the statement of cash flows for the sake of information to the users.

If an entity provides disclosures of changes in other assets and liabilities besides changes in liabilities arising from financing activities, it shall disclose the later changes separately from changes in those other assets and liabilities.

(ii) Transitional provisions and applicability of the amendment

Further, with respect to these amendments, an entity is not required to provide comparative information for preceding periods since these amendments will be applicable for the annual periods beginning on or after 1 April, 2017.

**B. Amendments in Ind AS 102 'Share-based Payment'**

(i) The amendments cover following accounting areas:

"Measurement of cash-settled share-based payments

Under Ind AS 102, the measurement basis for an equity-settled share-based payment should not be 'fair value' in accordance with Ind AS 113, 'Fair value measurement'. However, 'fair value' was not defined in connection with a cash-settled share-based payment. The amendment clarifies that the fair value of a cash-settled award is determined on a basis consistent with that used for equity-settled awards. Market-based performance conditions and non-vesting conditions are reflected in the 'fair value', but non-market performance conditions and service conditions are reflected in the estimate of the number of awards expected to vest.

The amendment to Ind AS 102 with respect to measurement of cash-settled awards has most impact where an award vests (or does not vest) based on a non-marketing condition. Absent this clarification, it may be argued that the fair value of a cash-settled award is to be determined using the guidance in Ind AS 113 and reflecting the probability that non-market and service vesting conditions would be met. The amendment clarifies that non-market and service vesting conditions are ignored in the measurement of fair value.

"Classification of share-based payments settled net of tax withholdings

Tax laws or regulations may require the employer to withhold some of the shares to which an employee is entitled under a share-based payment, and to remit the tax payable on it to the tax authority.

Ind AS 102 would require such share based payment to be split into a cash settled component for the tax payment and an equity settled component for the net shares issued to the employee. The amendment now adds an exception that requires the share based payment to be treated as equity-settled in its entirety. The cash payment to the tax authority is treated as if it was part of an equity settlement. The exception would not apply to any equity instruments that the entity withholds in excess of the employee's tax obligation associated with the share-based payment.

"Accounting for a modification of a share-based payment from cash-settled to equity-settled

As per the amendment, if the terms and conditions of a cash-settled share-based payment transactions are modified with the result that it becomes an equity-settled share-based payment transaction, the transaction is accounted for as such from the date of the modification. Specifically:

- o The equity-settled share-based payment transaction is measured by reference to the fair value of the equity instruments granted at the modification date. The equity-settled share-based payment transaction is recognised in equity on the modification date to the extent to which goods or services have been received.
- o The liability for the cash-settled share-based payment transaction as at the modification date is derecognised on that date.
- o Any difference between the carrying amount of the liability derecognised and the amount of equity recognised on the modification date is recognised immediately in profit or loss.
- o The amendment requires any change in value to be dealt with before the change in classification. Accordingly, the cash-settled award is remeasured, with any difference recognised in the statement of profit and loss before the remeasured liability is reclassified into equity.

(ii) Transitional provisions

The transition provisions specify that the amendments apply to share based payment that are not settled as at the date of first application or to modifications that happen after the date of first application, without restatement of prior periods. There is no income statement impact as a result of any reclassification from liability to equity in respect of 'net settled awards'; the recognised liability is reclassified to equity without any adjustment.

The amendments can be applied retrospectively, provided that this is possible without hindsight and that the retrospective treatment is applied to all of the amendments.

(iii) Applicability date of the amendment

The amendment rules shall be applicable from annual periods beginning on or after 1 April 2017. Accordingly, these amendments are not applicable to Phase I entities preparing their first Ind AS financial statements for the year ended 31 March 2017. However, such entities would need to provide relevant disclosures under Ind AS 8, 'Accounting policies, changes in accounting estimates and errors' in their first Ind AS financial statements.

#### 5. Applicability of Guidance Notes

Following three new Guidance Notes are applicable to you for the forthcoming examinations

1. Guidance Note on Accounting for Expenditure on Corporate Social Responsibility Activities.
2. Guidance Note on Accounting for Derivative Contracts.
3. Guidance Note on Accounting for Real Estate Transactions (Revised 2012). (Refer Appendix at the end of this Part I)

For full text, students are advised to refer the following links respectively:

1. <https://resource.cdn.icai.org/38254asb27888csr.pdf>
2. <https://resource.cdn.icai.org/38253asb27888dc.pdf>
3. <https://resource.cdn.icai.org/25896asb15443.pdf>

#### 6. Amendment in Schedule III to the Companies Act, 2013

Ministry of Corporate Affairs has amended Schedule III to the Companies Act, 2013 by inserting Division II to the Schedule which provides

- (a) General Instructions for preparation of financial statements of a company required to comply with Ind AS
- (b) Format for 'Part I Balance Sheet' as per Ind AS
- (c) Format for 'Statement of Changes in Equity'
- (d) General Instructions for Preparation of Balance Sheet
- (e) Part II – Statement of Profit and Loss
- (f) General Instructions for Preparation of Statement of Profit and Loss
- (g) Part III- General Instructions for the Preparation of Consolidated Financial Statements

Pursuant to the above amendment, Schedule III contains two Division viz-

**Division I** - Financial Statements for a company whose Financial Statements are required to comply with the Companies (Accounting Standards) Rules, 2006.

**Division II** - Financial Statements for a company whose Financial Statements are drawn up in compliance of the Companies (Indian Accounting Standards) Rules, 2015.

**7. Relevant Sections of the Companies Act, 2013**

The relevant Sections of the Companies Act, 2013 notified up to 31<sup>st</sup> October, 2017 are applicable for May, 2018 Examination.

## Appendix

### Guidance Note on Accounting for Real Estate Transactions

#### Objective

This Guidance Note recommends the accounting treatment for seller/developer/builder enterprises dealing in 'Real Estate' i.e. land as well as buildings and rights in relation thereto.

#### Scope

This Guidance Note covers all forms of transactions in real estate. For example :

- (a) Sale of plots of land (including long term sale type leases) without any development.
- (b) Sale of plots of land (including long term sale type leases) with development in the form of common facilities like laying of roads, drainage lines and water pipelines, electrical lines, sewage tanks, water storage tanks, sports facilities, gymnasium, club house, landscaping etc.
- (c) Development and sale of residential and commercial units, row houses, independent houses, with or without an undivided share in land.
- (d) Acquisition, utilisation and transfer of development rights.
- (e) Redevelopment of existing buildings and structures.
- (f) Joint development agreements for any of the above activities.

The Guidance Note primarily provides guidance on application of percentage of completion method (as per AS 7) on such transactions and activities of real estate which have the same economic substance as construction contracts. In respect of transactions of real estate which are in substance similar to delivery of goods, principles of AS 9 are applied.

Real estate transactions of the nature covered by AS 10, AS 12, AS 19 and AS 26, are outside the scope of this Guidance Note.

This Guidance Note should be applied to all projects in real estate which are commenced on or after April 1, 2012 and also to projects which have already commenced but where revenue is being recognised for the first time on or after April 1, 2012. Application from earlier date is also permissible.

## Definitions

1. **Project** – Project is the smallest group of units/plots/saleable spaces which are linked with a common set of amenities in such a manner that unless the common amenities are made available and functional, these units / plots / saleable spaces cannot be put to their intended effective use.

A larger venture can be split into smaller projects if the basic conditions as set out above are fulfilled. For example, a project may comprise a cluster of towers or each tower can also be designated as a project. Similarly, a complete township can be a project or it can be broken down into smaller projects.

2. **Project Costs** – Project costs in relation to a project ordinarily comprise:
  - (a) **Cost of land and cost of development rights** – All costs related to the acquisition of land, development rights in the land or property including cost of land, cost of development rights, rehabilitation costs, registration charges, stamp duty, brokerage costs and incidental expenses.
  - (b) **Borrowing Costs** – In accordance with AS 16, Borrowing Costs which are incurred directly in relation to a project or which are apportioned to a project.
  - (c) **Construction and development costs** – These would include costs that relate directly to the specific project and costs that may be attributable to project activity in general and can be allocated to the project.

Construction costs and development costs that relate directly to a specific project include:

- (a) land conversion costs, betterment charges, municipal sanction fee and other charges for obtaining building permissions;
- (b) site labour costs, including site supervision;
- (c) costs of materials used in construction or development of property;
- (d) depreciation of plant and equipment used for the project;
- (e) costs of moving plant, equipment and materials to and from the project site;
- (f) costs of hiring plant and equipment;
- (g) costs of design and technical assistance that is directly related to the project;
- (h) estimated costs of rectification and guarantee work, including expected warranty costs; and
- (i) claims from third parties.

The following costs should not be considered part of construction costs and development costs if they are material:

- (a) General administration costs;

- (b) selling costs;
- (c) research and development costs;
- (d) depreciation of idle plant and equipment;
- (e) cost of unconsumed or uninstalled material delivered at site; and
- (f) payments made to sub-contractors in advance of work performed.

Costs that may be attributable to project activity in general and can be allocated to specific projects include:

- (a) insurance;
- (b) costs of design and technical assistance that is not directly related to a specific project; and
- (c) construction or development overheads; and
- (d) borrowing costs.

Such costs are allocated using methods that are systematic and rational and are applied consistently to all costs having similar characteristics. The allocation is based on the normal level of project activity. Construction overheads include costs such as the preparation and processing of construction personnel payroll.

3. **Project revenues** – Project revenues include revenue on sale of plots, undivided share in land, sale of finished and semi-finished structures, consideration for construction, consideration for amenities and interiors, consideration for parking spaces and sale of development rights.

Project revenues are measured as the consideration received or receivable. The amount of project revenue may increase or decrease from one reporting period to the next.

### **Accounting for Real Estate Transactions**

The natures of real estate activities are such that often the date when the activity is commenced and the date when the activity is completed usually fall into different accounting periods. It is not unusual for such activities to spread over two or more accounting periods.

For recognition of revenue in case of real estate sales, it is necessary that all the conditions specified in paragraphs 10 and 11 of AS 9 are satisfied. The point of time at which all significant risks and rewards of ownership can be considered as transferred, is required to be determined on the basis of the terms and conditions of the agreement for sale.

In case of real estate sales, the seller usually enters into an agreement for sale with the buyer at initial stages of construction. This agreement for sale is also considered to have the effect of transferring all significant risks and rewards of ownership to the buyer provided the agreement is legally enforceable and subject to the satisfaction of conditions which signify transferring of significant risks and rewards even though the legal title is not transferred or the possession of the real estate is not given to the buyer. Once the seller has transferred all the

significant risks and rewards to the buyer, any acts on the real estate performed by the seller are, in substance, performed on behalf of the buyer in the manner similar to a contractor. Accordingly, revenue in such cases is recognised by applying the percentage of completion method as per AS 7.

Further, where individual contracts are part of a single project, although risks and rewards may have been transferred on signing of a legally enforceable individual contract but significant performance in respect of remaining components of the project is pending, revenue in respect of such an individual contract should not be recognised until the performance on the remaining components is considered to be completed on the basis of the aforesaid principles.

This Guidance Note, thus, provides guidance in the application of:

- Principles of AS 9 in respect of sale of goods for recognising revenue, costs and profits from transactions of real estate which are in substance similar to delivery of goods where the revenues, costs and profits are recognised when the revenue recognition process is completed; and
- Percentage completion method for recognising revenue, costs and profits from transactions and activities of real estate which have the same economic substance as construction contracts.

The application of the methods described above requires a careful analysis of the elements of the transaction, agreement, understanding and conduct of the parties to the transaction to determine the economic substance of the transaction. The economic substance of the transaction is not influenced or affected by the structure and/or legal form of the transaction or agreement.

#### **Application of Principles of AS 9 in respect of Sale of Goods to a Real Estate Project**

The application of principles of AS 9 in respect of sale of goods requires recognition of revenues on completion of the transaction/activity when the revenue recognition process in respect of a real estate project is completed.

Where transfer of legal title is a condition precedent to the buyer taking on the significant risks and rewards of ownership and accepting significant completion of the seller's obligation, revenue should not be recognised till such time legal title is validly transferred to the buyer.

#### **Application of Percentage Completion Method**

The percentage completion method should be applied in the accounting of all real estate transactions/activities in the situations described above, i.e., where the economic substance is similar to construction contracts. Some further indicators of such transactions/activities are:

- (a) The duration of such projects is beyond 12 months and the project commencement date and project completion date fall into different accounting periods.
- (b) Most features of the project are common to construction contracts, viz., land development, structural engineering, architectural design, construction, etc.

- (c) While individual units of the project are contracted to be delivered to different buyers these are interdependent upon or interrelated to completion of a number of common activities and/or provision of common amenities.
- (d) The construction or development activities form a significant proportion of the project activity.

This method is applied when the outcome of a real estate project can be estimated reliably and when all the following conditions are satisfied:

- (a) total project revenues can be estimated reliably;
- (b) it is probable that the economic benefits associated with the project will flow to the enterprise;
- (c) the project costs to complete the project and the stage of project completion at the reporting date can be measured reliably; and
- (d) the project costs attributable to the project can be clearly identified and measured reliably so that actual project costs incurred can be compared with prior estimates.

When the outcome of a project can be estimated reliably, project revenues and project costs associated with the project should be recognised as revenue and expenses respectively applying the percentage of completion method as per AS 7.

Further to the above conditions, there is a rebuttable presumption that the outcome of a real estate project can be estimated reliably and that revenue should be recognised under the percentage completion method only when the events in (a) to (d) below are completed.

- (a) All critical approvals necessary for commencement of the project have been obtained. These include, wherever applicable:
  - (i) Environmental and other clearances.
  - (ii) Approval of plans, designs, etc.
  - (iii) Title to land or other rights to development/ construction.
  - (iv) Change in land use.
- (b) When the stage of completion of the project reaches a reasonable level of development. A reasonable level of development is not achieved if the expenditure incurred on construction and development costs is less than 25% of the construction and development costs.
- (c) At least 25% of the saleable project area is secured by contracts or agreements with buyers.
- (d) At least 10% of the total revenue as per the agreements of sale or any other legally enforceable documents are realised at the reporting date in respect of each of the contracts and it is reasonable to expect that the parties to such contracts will comply with the payment terms as defined in the contracts. To illustrate - If there are 10 Agreements

of sale and 10% of gross amount is realised in case of 8 agreements, revenue can be recognised with respect to these 8 agreements.

When the outcome of a real estate project can be estimated reliably and the conditions stipulated above are satisfied, project revenue and project costs associated with the real estate project should be recognised as revenue and expenses by reference to the stage of completion of the project activity at the reporting date.

For computation of revenue the stage of completion is arrived at with reference to the entire project costs incurred including land costs, borrowing costs and construction and development costs. Whilst the method of determination of stage of completion with reference to project costs incurred is the preferred method, this Guidance Note does not prohibit other methods of determination of stage of completion, e.g., surveys of work done, technical estimation, etc. However, computation of revenue with reference to other methods of determination of stage of completion should not, in any case, exceed the revenue computed with reference to the 'project costs incurred' method.

The project costs which are recognised in the statement of profit and loss by reference to the stage of completion of the project activity are matched with the revenues recognised resulting in the reporting of revenue, expenses and profit which can be attributed to the proportion of work completed. Costs incurred that relate to future activity on the project and payments made to sub- contractors in advance of work performed under the sub-contract are excluded and matched with revenues when the activity or work is performed. This method provides useful information to the extent of contract activity and performance during a period.

The recognition of project revenue by reference to the stage of completion of the project activity should not at any point exceed the estimated total revenues from 'eligible contracts'/other legally enforceable agreements for sale. 'Eligible contracts' means contracts/agreements where at least 10% of the contracted amounts have been realised and there are no outstanding defaults of the payment terms in such contracts.

When it is probable that total project costs will exceed total eligible project revenues, the expected loss should be recognised as an expense immediately. The amount of such a loss is determined irrespective of:

- (a) commencement of project work; or
- (b) the stage of completion of project activity.

The percentage of completion method is applied on a cumulative basis in each reporting period to the current estimates of project revenues and project costs. Therefore, the effect of a change in the estimate of project costs, or the effect of a change in the estimate of the outcome of a project, is accounted for as a change in accounting estimate. The changed estimates are used in determination of the amount of revenue and expenses recognised in the statement of profit and loss in the period in which the change is made and in subsequent periods.

The changes to estimates also include changes arising out of cancellation of contracts and cases where the property or part thereof is subsequently earmarked for own use or for rental purposes. In such cases any revenues attributable to such contracts previously recognised should be reversed and the costs in relation thereto shall be carried forward and accounted in accordance with AS 10.

#### Accounting for Sale of Land or Plots

##### A. Sale of plots of land without any development

Revenue from sale of land or plots should be recognised when all the conditions as per AS 9 are met.

##### B. Sale of developed plots

Where the development activity is significant and if the projects meet the criteria specified earlier, the percentage completion method is used to account for such sales.

#### Transferable Development Rights

Transferable Development Rights (TDRs) are generally acquired in following different ways:

- (a) Direct purchase.
- (b) Development and construction of built-up area.
- (c) Giving up of rights over existing structures or open land.

When development rights are acquired by way of direct purchase or on development or construction of built-up area, **cost of acquisition would be the cost of purchases or amount spent on development or construction of built-up area**, respectively.

Where development rights are acquired by way of giving up of rights over existing structures or open land, **the development rights should be recorded either at fair market value or at the net book value of the portion of the asset given up whichever is less**. For this purpose, fair market value may be determined by reference either to the asset or portion thereof given up or to the fair market value of the rights acquired whichever is more clearly evident.

When development rights are utilised in a real estate project by an enterprise, the cost of acquisition should be added to the project costs.

When development rights are sold or transferred, revenue should be recognised when both the following conditions are fulfilled:

- (a) title to the development rights is transferred to the buyer; and
- (b) it is not unreasonable to expect ultimate realisation of revenue.

#### Transactions with Multiple Elements

An enterprise may contract with a buyer to deliver goods or services in addition to the construction/development of real estate [e.g. property management services, sale of

decorative fittings (excluding fittings which are an integral part of the unit to be delivered), rental in lieu of unoccupied premises, etc.]. **In such cases, the contract consideration should be split into separately identifiable components** including one for the construction and delivery of real estate units.

**The consideration received or receivable for the contract should be allocated to each component on the basis of the fair market value of each component.**

#### Disclosure

An enterprise should disclose:

- (a) the amount of project revenue recognised as revenue in the reporting period;
- (b) the methods used to determine the project revenue recognised in the reporting period; and
- (c) the method used to determine the stage of completion of the project.

An enterprise should also disclose each of the following for projects in progress at the end of the reporting period:

- (a) the aggregate amount of costs incurred and profits recognised (less recognised losses) to date; and
- (b) the amount of advances received;
- (c) the amount of work in progress and the value of inventories;
- (d) excess of revenue recognised over actual bills raised (unbilled revenue).

**PART – II : QUESTIONS AND ANSWERS**  
**QUESTIONS**

**AS 5**

1. (a) The Accountant of **Stable Limited** has sought your **opinion with relevant reasons**, whether the following transactions will be treated as change in **Accounting Policy** or not (in accordance with the provisions of relevant Accounting Standard) for the year ended 31<sup>st</sup> March, 2017:
- (i) Provision for doubtful debts was created @ 2% till 31<sup>st</sup> March, 2016. From the Financial year 2016-2017, the rate of provision has been changed to 3%.
  - (ii) During the year ended 31<sup>st</sup> March, 2017, the management has introduced a formal gratuity scheme in place of ad-hoc ex-gratia payments to employees on retirement.
  - (iii) Till the previous year the furniture was depreciated on straight line basis over a period of 5 years. From current year, the useful life of furniture has been changed to 3 years.
  - (iv) 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 ₹ 20,000 per month. Earlier there was no such scheme of pension in the organization.
  - (v) During the year ended 31<sup>st</sup> March, 2017, there was change in cost formula in measuring the cost of inventories.

**AS 9**

- (b) Pricy Limited is engaged in manufacturing of readymade garments. They provide you the following information on 31<sup>st</sup> March, 2017:
- (i) On 15<sup>th</sup> January, 2017 garments worth ₹ 4,00,000 were sent to Ansh on consignment basis of which 25% garments unsold were lying with Ansh as on 31<sup>st</sup> March, 2017.
  - (ii) Garments worth ₹ 1,95,000 were sold to Glow boutique on 25<sup>th</sup> March, 2017 but at the request of Glow Boutique, these were delivered on 15<sup>th</sup> April, 2017.
  - (iii) On 1<sup>st</sup> November, 2016 garments worth ₹ 2,50,000 were sold on approval basis. The period of approval was 4 months after which they were considered sold. Buyer sent approval for 75% goods up to 31<sup>st</sup> December, 2016 and no approval or disapproval received for the remaining goods till 31<sup>st</sup> March, 2017.
- You are required to advise the accountant of Pricy Limited, the amount to be recognised as revenue in above cases in the context of AS 9.

**AS 10**

2. (a) Arush Ltd. is installing a new plant in its factory. It provides you the following information:

Cost of the plant (cost as per supplier's invoice)	₹ 31,25,000
Estimated dismantling costs to be incurred after 5 years	₹ 2,50,000
Initial operating losses before commercial production	₹ 3,75,000
Initial delivery and handling costs	₹ 1,85,000
Cost of site preparation	₹ 4,50,000
Consultants used for advice on the acquisition of the plant	₹ 6,50,000

Please advise Arush Ltd. on the costs that can be capitalised for plant in accordance with AS 10 'Property, Plant and Equipment'.

**AS 11**

- (b) Palash Ltd. purchased fixed assets costing ₹ 5,000 lakh on 01.04.2016 payable in foreign currency (US\$) on 05.04.2017. Exchange rate of 1 US\$ = ₹ 50.00 and ₹ 54.98 as on 01.04.2016 and 31.03.2017 respectively.

The company also obtained a soft loan of US\$ 1 lakh on 01.04.2016 payable in three annual equal instalments. First instalment was due on 01.05.2017.

You are required to state, how these transactions would be accounted for in the books of accounts ending 31<sup>st</sup> March, 2017 as per the relevant Accounting Standards.

**AS 12**

3. Explain the treatment of refund of Government Grants as per AS 12 'Accounting for Government Grants'.

**AS 15**

4. (a) Neerav Ltd., is in engineering industry. The company received an actuarial valuation for the first time for its pension scheme which revealed a surplus of ₹ 6 lakhs. It wants to spread the same over the next 2 years by reducing the annual contribution to ₹ 2 lakhs instead of ₹ 5 lakhs. The average remaining life of the employee is estimated to be 6 years.

You are required to advise the company in accordance with AS 15.

**AS 16**

- (b) Vital Limited borrowed an amount of ₹ 150 crores on 1.4.2016 for construction of boiler plant @ 11% p.a. The plant is expected to be completed in 4 years. Since the weighted average cost of capital is 13% p.a., the accountant of Vital Ltd.

capitalized ₹ 19.50 crores for the accounting period ending on 31.3.2017. 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 relevant accounting standard.

**AS 17**

5. (a) ABC Limited has three segments viz. A, B and C. The total assets of the company is ₹ 15 crores. The assets of Segment A is ₹ 1.85 crores, Segment B is ₹ 6.15 crores and Segment C is ₹ 7.00 crores. Assets of each segment include deferred tax assets of ₹ 0.50 crores in A, ₹ 0.40 crores in B and ₹ 0.30 crores in C. The accountant of ABC Limited contends that all segments are reportable segments. Based on segment assets criteria described in AS 17, determine the veracity of the contention of the accountant.

**AS 18**

- (b) Arohi Ltd. sold goods for ₹ 90 lakhs to Anya Ltd. during financial year ended 31-3-2017. The Managing Director of Arohi Ltd. own 100% of Anya Ltd. The sales were made to Anya Ltd. at normal selling prices followed by Arohi Ltd. The Chief accountant of Arohi Ltd contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per the accounting standard. Is the Chief Accountant correct? Comment in accordance with AS 18.

**AS 19**

6. (a) A Ltd. sold machinery having WDV of ₹ 40 lakhs to B Ltd. for ₹ 50 lakhs and the same machinery was leased back by B Ltd. to A Ltd. The lease back is operating lease. Comment as per AS 19, if –
- (a) Sale price of ₹ 50 lakhs is equal to fair value.  
 (b) Fair value is ₹ 60 lakhs.  
 (c) Fair value is ₹ 45 lakhs and sale price is ₹ 38 lakhs.  
 (d) Fair value is ₹ 40 lakhs and sale price is ₹ 50 lakhs.  
 (e) Fair value is ₹ 46 lakhs and sale price is ₹ 50 lakhs  
 (f) Fair value is ₹ 35 lakhs and sale price is ₹ 39 lakhs.

**AS 20**

- (b) For Accounting year 1-4-2016 to 31-3-2017

Net profit attributable to equity shareholders	₹ 1,00,00,000
No. of equity shares outstanding	20,00,000
Average fair value of one equity share during the year	₹ 75.00

Potential Equity Shares	
Options	1,00,000 with exercise price of ₹ 60
Convertible Preference Shares	8,00,000 shares entitled to a cumulative dividend of ₹ 8 per share. Each preference share is convertible into 2 equity shares.
Attributable tax, e.g., corporate dividend tax	10%
12% Convertible Debentures of ₹ 100 each	Nominal amount ₹ 10,00,00,000. Each debenture is convertible into 4 equity shares.
Tax rate	30%

Calculate diluted earnings per share as per AS 20.

#### AS 22

7. (a) A company, ABC Ltd., prepares its accounts annually on 31<sup>st</sup> March. The company has incurred a loss of ₹ 1,00,000 in the year 20x1 and made profits of ₹ 50,000 and 60,000 in year 20x2 and year 20x3 respectively. Under the tax laws, loss can be carried forward for 8 years and tax rate is 40% and at the end of year 20x1, it was virtually certain, supported by convincing evidence, that the company would have sufficient taxable income in the future years against which unabsorbed depreciation and carry forward of losses can be set-off. Also there is no difference between taxable income and accounting income except that set-off of loss is allowed in years 20x2 and 20x3 for tax purposes. Current tax in the year 20x3 is Rs. 4,000. Show the effect of above transactions by preparing the Statement of Profit and Loss.

#### AS 24

- (b) Arav Ltd. is in the business of manufacture of Refrigerators and Washing Machines. The company is working on a strategic plan to shift from the Refrigerator segment over the coming 5 years. However, no specific plans have been drawn up for sale of neither the division nor its assets. As part of its plan, it will reduce the production of Refrigerator by 20% annually. It also plans to commence another new factory for the manufacture of Washing Machines and transfer surplus employees in a phased manner.
- You are required to comment if mere gradual phasing out in itself can be considered as a 'Discontinuing Operation' within the meaning of AS 24.
  - If the company passes a resolution to sell some of the assets in the Refrigerator division and also to transfer few other assets of the Refrigerator division to the new factory, does this trigger the application of AS 24?
  - Would your answer to the above be different if the company resolves to sell the assets of the Refrigerator Division in a phased but time bound manner?

**AS 25**

8. Estimated annual income	₹ 1 lakh
(inclusive of Estimated Capital Gains (earned in Quarter II))	₹ 20,000
The estimated income of each quarter is	₹ 25,000
Tax Rates:	
On Capital Gains	10%
On other income:	
First ₹ 40,000	30%
Balance income	40%

There is no difference between the estimated taxable income and the estimated accounting income. Calculate tax expense for each quarter and for the year.

**AS 28**

9. (a) M Ltd. produces a single product and owns plants A, B and C. Each plant is located in a different continent. Plant A produces a component that is assembled in either plant B or plant C. The combined capacity of plants B and C is not fully utilised. M Ltd.'s products are sold world-wide from either plants B or C i.e. plant B's production can be sold in plant C's continent if the products can be delivered faster from plant B than from plant C. Utilisation levels of plant B and plant C depend on the allocation of sales between the two sites.

For each of the following cases, what are the cash-generating units for plants A, B and C?

**Case 1:** There is an active market for plant A's products.

**Case 2:** There is no active market for plant A's products.

**AS 29**

- (b) During 2015-16, A Ltd. gives a guarantee of certain borrowings of B Ltd., whose financial condition at that time is sound. During 2016-17, the financial condition of B Ltd. deteriorates and at 30 September 2016, B Ltd. goes into liquidation. State whether a provision is required
- (a) At 31 March 2016
- (b) At 31 March 2017

**Indian Accounting Standards (Ind AS)**

10. Explain

- (a) Carve Out in Ind AS 32 "Financial Instruments: Presentation" from IAS 32 "Financial Instruments: Presentation" alongwith the reason.
- (b) Differences between Ind AS 37 "Provisions, Contingent Liabilities and Contingent Assets" and AS 29 "Provisions, Contingent Liabilities and Contingent Assets".

**Accounting for Corporate Restructuring**

11. The following are the summarized Balance Sheets of A Ltd. and B Ltd., as at 31.12.2017:

**A Ltd.**

Liabilities	Amount (₹)	Assets	Amount (₹)
Share capital		Fixed assets	3,400
3,00,000 Equity shares of ₹ 10 each	3,000	Inventory (pledged with secured loan trade payables)	18,400
10,000 Preference shares of ₹ 100 each	1,000	Other Current assets	3,600
General reserve	400	Profit and Loss account	16,600
Secured loans (secured against pledge of inventories)	16,000		
Unsecured loans	8,600		
Current liabilities	13,000		
	42,000		42,000

**B Ltd.**

Liabilities	Amount (₹)	Assets	Amount (₹)
Share capital		Fixed assets	6,800
1,00,000 Equity shares of ₹ 10 each	1,000	Current assets	9,600
General reserve	2,800		
Secured loans	8,000		
Current liabilities	4,600		
	16,400		16,400

Both the companies go into liquidation and C Ltd., is formed to take over their businesses. The following information is given:

- (a) All current assets of two companies, except pledged inventory are taken over by C Ltd. The realisable value of all current assets are 80% of book values in case of A Ltd. and 70% for B Ltd. fixed assets are taken over at book value.
- (b) The break-up of current liabilities is as follows:

	A Ltd. ₹	B Ltd. ₹
Statutory liabilities (including ₹ 22 lakhs in case of A Ltd. in case of a claim not having been admitted shown as contingent liability)	72,00,000	10,00,000
Liability to employees	30,00,000	18,00,000

The balance of current liability is miscellaneous trade payables.

- (c) Secured loans include ₹16,00,000 accrued interest in case of B Ltd.
- (d) 2,00,000 equity shares of ₹10 each are allotted by C Ltd. at par against cash payment of entire face value to the shareholders of A Ltd. and B Ltd. in the ratio of shares held by them in A Ltd. and B Ltd.
- (e) Preference shareholders are issued Equity shares worth ₹ 2,00,000 in lieu of present holdings.
- (f) Secured loan payables agree to continue the balance amount of their loans to C Ltd. after adjusting value of pledged security in case of A Ltd. and after waiving 50% of interest due in the case of B Ltd.
- (g) Unsecured loans are taken over by C Ltd. at 25% of Loan amounts.
- (h) Employees are issued fully paid Equity shares in C Ltd. in full settlement of their dues.
- (i) Statutory liabilities are taken over by C Ltd. at full values and trade payables are taken over at 80% of the book value.

Show the opening Balance Sheet of C Ltd. Workings should be part of the answer.

**Consolidated Financial Statements**

12. From the following summarised Balance Sheets of A Ltd. and its subsidiary B Ltd., prepare a Consolidated Balance Sheet:

**Balance Sheet as on 31st March, 2017**

Equity and Liabilities	A Ltd. ₹	B Ltd. ₹	Assets	A Ltd. ₹	B Ltd. ₹
Share Capital			Sundry Assets	93,000	32,000
Equity Shares of ₹ 10 each	1,00,000	20,000	Shares in B Ltd. 1,200 shares at ₹ 15 each	18,000	
Profit on sale of shares	3,000				
Profit and Loss A/c Brought forward	6,000	7,200			
For the year	<u>2,000</u>	<u>4,800</u>			
	<u>1,11,000</u>	<u>32,000</u>		<u>1,11,000</u>	<u>32,000</u>

A Ltd. bought in earlier year 1,600 equity shares in B Ltd. @ ₹ 15 when the Profit and Loss Account balance in B Ltd. was ₹ 4,400. A Ltd. sold 400 shares @ ₹ 22.50, credited the difference between the sale proceeds and cost to "Profit on sale of investment account" on 30th September, 2014 and crediting the balance to the investment account. Profit during the year accrued uniformly.

**Accounting and Reporting of Financial Instruments**

13. XYZ Ltd. grants loans to its employees at 4% amounting to ₹ 10,00,000 at the beginning of 2016-17. The principal amount is repaid over a period of 5 years whereas the accumulated interest computed on reducing balance at simple interest is collected in 2 equal annual instalments after collection of the principal amount.

Assume that the benchmark interest rate is 8%.

Show the accounting entries on 1-4-2016 and 31-3-2017.

**Accounting for Share Based Payments**

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

Number of shares	4,00,000
Grant date	April 1, 2013
Number of employees covered	600
Number of options granted per employee	100

Vesting condition: Continuous employment for 3 years	
Nominal value per share (₹)	10
Exercise price per share (₹)	45
Vesting date	March 31, 2016
Exercise Date	May 31, 2017
Fair value of option per share on grant date (₹)	15

**Position on 31/03/14**

- (a) Number of employees expected to satisfy service condition = 540
- (b) Number of employees left = 15
- (c) Profit before amortisation of ESOP cost = ₹ 11.90 lakh
- (d) Fair value per share = ₹ 60

**Position on 31/03/15**

- (a) Number of employees expected to satisfy service condition = 552
- (b) Number of employees left = 20
- (c) Profit before amortisation of ESOP cost = ₹ 12.62 lakh
- (d) Fair value per share = ₹ 66

**Position on 31/03/16**

- (a) Number of employees left = 11
- (b) Number of employees entitled to exercise option = 554
- (c) Profit before amortisation of ESOP cost = ₹ 13.79 lakh
- (d) Fair value per share = ₹ 72

**Position on 31/05/17**

- (a) Number of employees exercising the option = 550
- (b) Number of employees not exercising the option = 4

Show Employees Compensation A/c, ESOP Outstanding A/c from 2013-14 to 2016-17.

Compute basic and diluted EPS for the years 2013-14 to 2015-16.

**Mutual Funds**

15. Ankush Gupta has invested in three mutual funds. From the details given below, find out effective yield on per annum basis in respect of each of the schemes to Ankush Gupta upto 31-03-2017:

Mutual Fund	X	Y	Z
Date of Investment	1-12-2016	1-1-2017	1-3-2017
Amount of investment (₹)	1,00,000	2,00,000	1,00,000
NAV at the date of investment (₹)	10.50	10.00	10.00
Dividend received upto 31-3-2017 (₹)	1,900	3,000	Nil
NAV as on 31-3-2017 (₹)	10.40	10.10	9.80

### Valuation of Shares

16. From the following information, calculate the value of a share if you want to

- buy a small lot of shares;
- buy a controlling interest in the company.

Year	Profit (₹)	Capital Employed (₹)	Dividend %
2014	55,00,000	3,43,75,000	12
2015	1,60,00,000	8,00,00,000	15
2016	2,20,00,000	10,00,00,000	18
2017	2,50,00,000	10,00,00,000	20

The market expectation is 12%.

### Valuation of Business

17. The summarized Balance Sheet of Flower Limited for the year ended on 31<sup>st</sup> March, 2015, 2016 and 2017 are as follows:

	(₹ in thousands)		
	31 <sup>st</sup> March, 2015	31 <sup>st</sup> March 2016	31 <sup>st</sup> March 2017
Liabilities			
6,40,000, Equity shares of ₹ 10 each fully paid up	6,400	6,400	6,400
General Reserves	4,800	5,600	6,400
Profit and Loss Account	560	640	960
Trade Payable	2,400	3,200	4,000
Total	14,160	15,840	17,760

Assets			
Goodwill	4,000	3,200	2,400
Tangible Assets (Net)	5,600	6,400	6,400
Inventories	4,000	4,800	5,600
Trade Receivable	80	640	1,760
Cash and Cash Equivalents	480	800	1,600
Total	14,160	15,840	17,760

**Additional Information:**

(i) Actual valuations were as under:

	31.3.2015	31.3.2016	31.3.2017
Tangible Assets	7,200	8,000	8,800
Inventories	4,800	5,600	6,400
Net Profit (Including Opening Balance after writing off depreciation, goodwill, tax provision and transfers to general reserves)	1,680	2,480	3,280

- (ii) Capital employed in the business at market value at the beginning of 2014-2015 was ₹ 1,46,40,000 which included cost of goodwill. The normal annual return on average capital employed in the line of business in which Flower Limited is engaged is 12.50%.
- (iii) The balance in general reserve as on 1st April, 2014 was ₹ 40 lacs.
- (iv) The goodwill shown as on 31st March, 2015 was purchased on 1st April, 2014 for ₹ 40 lacs and the balance in profit and loss account as on 1st April, 2014 was ₹ 4,80,000.
- (v) Goodwill is to be valued at 5 years' purchase of super profit by using simple average method.

Find out the average capital employed in each year and total value of business as on 31st March, 2017.

**Value Added Statement**

18. Prepare a value added statement for the year ended on 31.3.2017 and reconciliation of total value added with profit before taxation, from the Profit and Loss Account of Great Ltd. for the year ended on 31.3.2017:

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

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

The following additional Information are given:

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

#### Economic Value Added

19. Detail Ltd. has provided the following information:

	(₹ in lacs)
Equity Share Capital (₹ 10 each)	400
15% Preference Share Capital (₹ 10 each)	200
Reserves and Surplus	220
15% Debentures	1600
10% Non-trade Investments (Nominal Value ₹ 100 lacs)	140
Land and Building held as Investment	20

Advance given for Purchase of Plant	10
Capital Work in Progress	30
Underwriting Commission (not written off)	20
Earnings per share	16
Tax rate	30%
Beta factor	1.65
Market rate of return	16.25%
Risk free rate	9.85%

Calculate Economic Value Added by the company.

### Human Resource Accounting

20 The following information is supplied to you about Opportunity Ltd.

Capital & Reserves	
Equity Shares of ₹ 100 each of which ₹ 75 has been called up	5,00,000
Equity Shares in respect of which calls are in arrear @ 25 per share	₹ 1,00,000
General Reserve	₹ 10,00,000
Profit & Loss account (balance at beginning of the year)	₹ (25,00,000)
Profit/(loss) for the year	₹ (1,80,000)
Industry Average Profitability	12.50%
8% Debentures of ₹ 10 each	8,00,000
Opportunity Ltd. is proposing to hire the services of Mr. X to turn the company around.	
Minimum take home salary per month demanded by Mr. X	₹ 4,00,000
Average Income tax rate on salaries above ₹ 3 lakhs per annum	25%
Provident Fund contribution by Employer per month	₹ 50,000
Profits over and above target expected by hiring Mr. X	10%

You are required to analyze the proposal and see whether it is worthwhile to employ Mr. X and also suggest the maximum emoluments that could be paid to him.

Note:

- (i) PF contributions are tax exempt.
- (ii) Take home salary is that remaining after employee's contribution to PF @ ₹ 50,000 per month and after deduction of Income-tax on salary.

## ANSWERS

1. (a) (i) In the given case, Stable limited created 2% provision for doubtful debts till 31<sup>st</sup> March, 2016. Subsequently in 2016-17 the company revised the estimates based on the changed circumstances and wants to create 3% provision. Thus, change in rate of provision of doubtful debt is a change in the estimate and not change in accounting policy. This change will affect only current year.
- (ii) As per AS 5, 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. Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is a transaction which is substantially different from the previous policy, will not be treated as change in an accounting policy. Infact it will be treated as an introduction of new policy.
- (iii) Change in useful life of furniture from 5 years to 3 years is a change in estimate and is not a change in accounting policy as per revised AS 10 'Property, Plant and Equipment'.
- (iv) Adoption of a new accounting policy for events or transactions which did not occur previously should not be treated as a change in an accounting policy. Hence the introduction of new pension scheme is not a change in accounting policy.
- (v) Change in cost formula used in measurement of cost of inventories is a change in accounting policy
- (b) As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:
1. the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and
  2. no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.
- Accordingly, in the cases as given in the question:
- (i) 25% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 3,00,000 (75% of ₹ 4,00,000) for the year ended on 31<sup>st</sup> March, 2017. In case of consignment sale, revenue should not be recognized until the goods are sold to a third party.

- (ii) The sale is complete but delivery has been postponed at buyer's request. Pricy Ltd. should recognize the entire sale of ₹ 1,95,000 for the year ended 31<sup>st</sup> March, 2017.
- (iii) In case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting ₹ 2,50,000 as the time period for rejecting the goods had expired.

Thus total revenue amounting ₹ 7,45,000 (3,00,000+1,95,000+2,50,000) will be recognized for the year ended 31<sup>st</sup> March, 2017 in the books of Pricy Ltd.

2. (a) According to AS 10 'Property, Plant and Equipment', following costs will be capitalized by Arush Ltd.:

	₹
Cost of the plant	31,25,000
Initial delivery and handling costs	1,85,000
Cost of site preparation	4,50,000
Consultants' fee	6,50,000
Estimated dismantling costs to be incurred after 5 years	<u>2,50,000</u>
Total cost of Plant	<u>46,60,000</u>

**Note:** Operating losses before commercial production amounting to ₹ 3,75,000 will not be capitalized as per AS 10. They should be written off to the Statement of Profit and Loss in the period they are incurred.

- (b) As per AS 11 'The Effects of Changes in Foreign Exchange Rates', exchange differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognised as income or as an expense in the period in which they arise. However, Ministry of Corporate Affairs has amended AS 11 according to which exchange difference 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 requisition of depreciable capital asset, can be added to or deducted from cost of asset. The MCA has given an option for the enterprises to capitalize the exchange differences arising on reporting of long term foreign currency monetary items. Thus the company can capitalize the exchange differences arising due to long term loans linked with the acquisition of fixed assets.

**Transaction 1: Calculation of exchange difference on fixed assets**

$$\text{Foreign Exchange Liability} = \frac{5,000}{50} = \text{US \$ 100 lakhs}$$

$$\text{Exchange Difference} = \text{US \$ 100 lakhs} \times (\text{₹ 54.98} - \text{₹ 50}) = \text{₹ 498 lakhs.}$$

Loss due to exchange difference amounting ₹ 498 lakhs will be capitalised and added in the carrying value of fixed assets. Depreciation on the unamortised amount will be provided in the remaining years

**Transaction 2: Soft loan exchange difference (US \$ 1 lakh i.e. ₹ 50 lakhs)**

$$\text{Value of loan 31.3.17} = \text{US \$ 1 lakh} \times 54.98 = \text{₹ 54,98,000}$$

AS 11 also provides that in case of liability designated as long-term foreign currency monetary item (having a term of 12 months or more at the time of origination) the exchange difference is to be accumulated in the Foreign Currency Monetary Item Translation Difference (FCMITD) and should be written off the useful life of such long-term liability, by recognition as income or expenses in each of such periods.

Exchange difference between reporting currency (INR) and foreign currency (USD) as on 31.03.2017 = US \$ 1.00 lakh  $\times$  ₹ (54.98 – 50) = ₹ 4.98 lakh.

Loan account is to be increased to 54.98 lakh and FCMITD account is to be debited by 4.98 lakh. Since loan is repayable in 3 equal annual instalments, ₹ 4.98 lakh/3 = ₹ 1.66 lakh is to be charged in Profit and Loss Account for the year ended 31<sup>st</sup> March, 2017 and balance in FCMITD A/c ₹ (4.98 lakh – 1.66 lakh) = ₹ 3.32 lakh is to be shown on the 'Equity & Liabilities' side of the Balance Sheet as a negative figure under the head 'Reserve and Surplus' as a separate line item.

**Note:** The above answer is given on the basis that the company has availed the option under para 46A of AS 11.

3. Para 11 of AS 12, "Accounting for Government Grants", explains treatment of refund government grants in following situations:

**(i) When government grant is related to revenue**

- (a) When deferred credit account has a balance: The amount of government grant refundable will be adjusted against unamortized deferred credit balance remaining in respect of the grant. To the extent that the amount refundable exceeds any such deferred credit the amount is immediately charged to profit and loss account.
- (b) Where no deferred credit account balance exists: The amount of government grant refundable will be charged to profit and Loss account.

## (ii) When government grant is related to specific fixed assets

- (a) Where at the time of receipt, the amount of government grant reduced the cost of asset: The amount of government grant refundable will increase the book value of the asset.
- (b) Where at the time of receipt, the amount of government grant was credited to "Deferred Grant Account": The amount of government grant refundable will reduce the capital reserve or unamortized balance of deferred grant account as appropriate.

## (iii) When government grant is in the nature of Promoter's contribution

The amount of government grant refundable in part or in full on non-fulfilment of specific conditions, the relevant amount recoverable by the government will be reduced from capital reserve.

A government grant that becomes refundable is treated as an extra-ordinary item.

4. (a) According to para 92 of AS 15 (Revised) "Employee Benefits", actuarial gains and losses should be recognized immediately in the statement of profit and loss as income or expense. Therefore, surplus of ₹ 6 lakhs in the pension scheme on its actuarial valuation is required to be credited to the profit and loss statement of the current year. Hence, Neerav Ltd. cannot spread the actuarial gain of ₹ 6 lakhs over the next 2 years by reducing the annual contributions to ₹ 2 lakhs instead of ₹ 5 lakhs. It has to contribute ₹ 5 lakhs annually for its pension schemes.
- (b) Para 10 of AS 16 'Borrowing Costs' states that to the extent the 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. Hence, in the above case, treatment of accountant of Vital Ltd. is incorrect. The amount of borrowing costs capitalized for the financial year 2016-17 should be calculated as follows:

Actual interest for 2016-17 (11% of ₹ 150 crores)	₹ 16.50 crores
<i>Less:</i> Income on temporary investment from specific borrowings	(₹ 3.50 crores)
Borrowing costs to be capitalized during year 2016-2017	₹ 13.00 crores

5. (a) Statement showing percentage of Segment net assets to Total assets of the company

₹ in crores

Particulars	Segments			Total
	A	B	C	
Segment assets	1.85	6.15	7.00	15.00
<i>Less:</i> Deferred tax assets	<u>(0.50)</u>	<u>(0.40)</u>	<u>(0.30)</u>	<u>(1.20)</u>
Net segment assets	<u>1.35</u>	<u>5.75</u>	<u>6.70</u>	<u>13.80</u>
Percentage to total net segment assets	9.78%	41.67%	48.55%	100%

As per the definition given in para 5 of AS 17 'Segment Reporting', segment assets do not include income tax assets. Therefore, for identification of reporting segment on the basis of segment assets, deferred tax assets have been deducted from segment assets to arrive at net segment assets for the purpose of AS 17.

Further, as per para 27 of AS 17, one of the basis of segment asset criteria for identification of a business segment or geographical segment as a reportable segment is when its segment assets are 10% or more of the total assets of all segments. Accordingly, the reportable segments will be segments B and C only. Therefore, the contention of the accountant that all the segments are reportable segments is not tenable.

- (b) As per paragraph 13 of AS 18 'Related Party Disclosures', Enterprises over which the key management personnel is able to exercise significant influence are related parties. This includes enterprises owned by directors or major shareholders of the reporting enterprise that have a member of key management in common with the reporting enterprise.

In the given case, Arohi Ltd. and Anya Ltd. are related parties and hence disclosure of transaction between them is required irrespective of whether the transaction was done at normal selling price.

Hence the contention of Chief Accountant of Arohi Ltd. is wrong.

6. (a) Following will be the treatment in the given cases:
- When sales price of ₹ 50 lakhs is equal to fair value, A Ltd. should immediately recognize the profit of ₹ 10 lakhs (i.e. 50 – 40) in its books.
  - When fair value is ₹ 60 lakhs then also profit of ₹ 10 lakhs should be immediately recognized by A Ltd.
  - When fair value of leased machinery is ₹ 45 lakhs & sales price is ₹ 38 lakhs, then loss of ₹ 2 lakhs (40 – 38) to be immediately recognized by A Ltd. in its books provided loss is not compensated by future lease payment.

- (d) When fair value is ₹ 40 lakhs & sales price is ₹ 50 lakhs then, profit of ₹ 10 lakhs is to be deferred and amortized over the lease period.
- (e) When fair value is ₹ 46 lakhs & sales price is ₹ 50 lakhs, profit of ₹ 6 lakhs (46 - 40) to be immediately recognized in its books and balance profit of ₹ 4 lakhs (50 - 46) is to be amortised/deferred over lease period.
- (f) When fair value is ₹ 35 lakhs & sales price is ₹ 39 lakhs, then the loss of ₹ 5 lakhs (40 - 35) to be immediately recognized by A Ltd. in its books and profit of ₹ 4 lakhs (39 - 35) should be amortised/deferred over lease period.
- (b) **Increase in Earnings Attributable to Equity Shareholders on Conversion of Potential Equity Shares**

	Increase in Earnings	Increase in no. of Equity Shares	Earnings per Incremental Share
<b>Options</b>			
Increase in earnings	Nil		
No. of incremental shares issued for no consideration {1,00,000 x (75 - 60) / 75}		20,000	Nil
<b>Convertible Preference Shares</b>			
Increase in net profit attributable to equity shareholders as adjusted by attributable tax [(₹ 8 x 8,00,000) + 10% (8 x 8,00,000)]	₹ 70,40,000		
No. of incremental shares {2 x 8,00,000}		16,00,000	₹ 4.40
<b>12% Convertible Debentures</b>			
Increase in net profit {₹ 10,00,00,000 x 0.12 x (1-0.30)}	₹ 84,00,000		
No. of incremental shares {10,00,000 x 4}		40,00,000	₹ 2.10

It may be noted from the above that options are most dilutive as their earnings per incremental share is nil. Hence, for the purpose of computation of diluted earnings per share, options will be considered first. 12% convertible debentures being second most dilutive will be considered next and thereafter convertible preference shares will be considered.

## Conversion of Diluted Earnings Per Shares

	Net Profit Attributable (₹)	No. of Equity Shares	Net profit attributable Per Share (₹)	
As reported	1,00,00,000	20,00,000	5.00	
Options	<u>-</u>	<u>20,000</u>		
	1,00,00,000	20,20,000	4.95	Dilutive
12% Convertible Debentures	<u>84,00,000</u>	<u>40,00,000</u>		
	1,84,00,000	60,20,000	3.06	Dilutive
Convertible Preference Shares	<u>70,40,000</u>	<u>16,00,000</u>		
	<u>2,54,40,000</u>	<u>76,20,000</u>	3.34	Anti- Dilutive

Since diluted earnings per share is increased when taking the convertible preference shares into account (from ₹ 3.06 to ₹ 3.34), the convertible preference shares are anti-dilutive and are ignored in the calculation of diluted earnings per share. Therefore, diluted earnings per share is ₹ 3.06.

7. (a) Statement of Profit and Loss (for the three years ending 31st March, 20X1, 20X2, 20X3)

(₹ in thousands)

	20X1	20X2	20X3
Profit (loss)	(100)	50	60
Less: Current tax	—	—	(4)
Deferred tax:			
Tax effect of timing differences originating during the year	40		
Tax effect of timing differences reversing during the year		(20)	(20)
Profit (loss) after tax effect	(60)	30	36

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

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

- (1) Gradual or evolutionary phasing out of a product line or class of service.
- (2) Shifting of some production or marketing activities for a particular line of business from one location to another and
- (3) Closing of a facility to achieve productivity improvements or other cost savings.

A Reportable business segment or geographical segment as defined in AS 17, would normally satisfy criteria (b) of the definition.

Considering the above, following can be concluded:

- (i) No. The company's strategic plan has no final approval from the board through a resolution and no specific time bound activities like shifting of assets and employees and above all the new segment washing machine production line and factory has started.
- (ii) No. The resolution is salient about stoppage of the Refrigerator segment in definite time period. Though, some assets sales and transfer proposal was passed through a resolution to the new factory, closure roadmap and new segment starting roadmap is missing. Hence, AS 24 will not be applicable.
- (iii) Yes. Phased and time bound programme resolved in the board clearly indicates the closure of the Refrigerator segment in a definite time frame and clear roadmap. Hence, this action will attract AS 24 compliance.

#### 8. Tax Expense:

On Capital Gains portion of annual income:

10% of ₹ 20,000	₹ 2,000
On other income: 30% of ₹ 40,000 + 40% of ₹ 40,000	<u>₹ 28,000</u>
Total:	₹ 30,000

Weighted Average Annual Effective Tax Rate:

On Capital Gains portion of annual income:  $\frac{2,000}{20,000} \times 100 = 10\%$

On other income:  $\frac{28,000}{80,000} \times 100 = 35\%$

When income of ₹ 25,000 for 2<sup>nd</sup> Quarter includes capital gains of ₹ 20,000, the tax expense for each quarter will be calculated as below:

		Income	Tax Expense		
Quarter I		₹ 25,000	35% of ₹ 25,000 =		₹ 8,750
Quarter II	Capital Gains:	₹ 20,000	10% of ₹ 20,000 =	₹ 2,000	
	Other:	₹ 5,000	35% of ₹ 5,000 =	<u>₹ 1,750</u>	₹ 3,750
Quarter III		₹ 25,000	35% of ₹ 25,000 =		₹ 8,750
Quarter IV		₹ 25,000	35% of ₹ 25,000 =		<u>₹ 8,750</u>
Total tax expense for the year					<u>₹ 30,000</u>

9. (a) **Case 1:** It is likely that A is a separate cash-generating unit because there is an active market for its products.

Although there is an active market for the products assembled by B and C, cash inflows for B and C depend on the allocation of production across the two sites. It is unlikely that the future cash inflows for B and C can be determined individually. Therefore, it is likely that B and C together is the smallest identifiable group of assets that generates cash inflows from continuing use that are largely independent.

In determining the value in use of A and B plus C, M Ltd. adjusts financial budgets/forecasts to reflect its best estimate of future market prices for A's products.

**Case 2:** It is likely that the recoverable amount of each plant cannot be assessed independently because:

- there is no active market for A's products. Therefore, A's cash inflows depend on sales of the final product by B and C; and
- although there is an active market for the products assembled by B and C, cash inflows for B and C depend on the allocation of production across the two sites. It is unlikely that the future cash inflows for B and C can be determined individually.

As a consequence, it is likely that A, B and C together (i.e., M Ltd. as a whole) is the smallest identifiable group of assets that generates cash inflows from continuing use that are largely independent.

## (b) (a) At 31 March 2016

**Present obligation as a result of a past obligating event** - The obligating event is the giving of the guarantee, which gives rise to an obligation.

**An outflow of resources embodying economic benefits in settlement** - No outflow of benefits is probable at 31 March 2016.

**Conclusion** - No provision is recognised. The guarantee is disclosed as a contingent liability unless the probability of any outflow is regarded as remote.

## (b) At 31 March 2017

**Present obligation as a result of a past obligating event** - The obligating event is the giving of the guarantee, which gives rise to a legal obligation.

**An outflow of resources embodying economic benefits in settlement** - At 31 March 2017, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation.

**Conclusion** - A provision is recognised for the best estimate of the obligation.

## 10. (a) Carve Out in Ind AS 32 vis-à-vis IAS 32

**As per IFRS**: As per accounting treatment prescribed under IAS 32, equity conversion option in case of foreign currency denominated convertible bonds is considered a derivative liability which is embedded in the bond. Gains or losses arising on account of change in fair value of the derivative need to be recognised in the Statement of Profit and Loss as per IAS 32.

**Carve out**: In Ind AS 32, an exception has been included to the definition of 'financial liability' in paragraph 11 (b) (ii), whereby conversion option in a convertible bond denominated in foreign currency to acquire a fixed number of entity's own equity instruments is classified as an equity instrument if the exercise price is fixed in any currency.

**Reasons**: This treatment as per IAS 32 is not appropriate in instruments, such as, Foreign Currency Convertible Bonds (FCCBs) since the number of shares convertible on the exercise of the option remains fixed and the amount at which the option is to be exercised in terms of foreign currency is also fixed; merely the difference in the currency should not affect the nature of derivative, i.e., the option. Further, the fair value of the option is based on the fair value of the share prices of the company. If there is decrease in the share price, the fair value of derivative liability would also decrease which would result in recognition of gain in the statement of profit and loss. This would bring unintended volatility in the statement of profit and loss due to volatility in share prices. This will also not give a true and fair view of the liability as in this situation, when the share prices fall, the option will not be exercised. However, it has been considered that if such option is classified as equity, fair value changes would not be required to be recognised. Accordingly, the exception has been made in definition of financial liability in Ind AS 32.

- (b) Significant differences between Ind AS 37 vis a vis AS 29:
- (i) **Constructive obligations and Change in the Definition of Provision and Obligating Event:** Unlike AS 29, Ind AS 37 requires creation of provisions in respect of constructive obligations also. [However, AS 29 requires creation of provisions arising out of normal business practices, custom and a desire to maintain good business relations or to act in an equitable manner]. This has resulted in some consequential changes also. For example, definitions of provision and obligating event have been revised in Ind AS 37, while the terms 'legal obligation' and 'constructive obligation' have been inserted and defined in Ind AS 37. Similarly, the portion of AS 29 pertaining to restructuring provisions has been revised in Ind AS 37.
  - (ii) **Discounting Provisions:** AS 29 prohibits discounting the amounts of provisions except in case of decommissioning, restoration and similar liabilities that are recognised as cost of Property, Plant and Equipment. Ind AS 37 requires discounting the amounts of provisions, if effect of the time value of money is material.
  - (iii) **Disclosure of Contingent Assets:** AS 29 notes the practice of disclosure of contingent assets in the report of the approving authority but prohibits disclosure of the same in the financial statements. Ind AS 37 requires disclosure of contingent assets in the financial statements when the inflow of economic benefits is probable. The disclosure, however, should avoid misleading indications of the likelihood of income arising.
  - (iv) **Onerous Contracts:** Ind AS 37 makes it clear that before a separate provision for an onerous contract is established, an entity should recognise any impairment loss that has occurred on assets dedicated to that contract in accordance with Ind AS 36. There is no such specific provision in AS 29.
  - (v) **Future Operating Losses:** AS 29 states that identifiable future operating losses up to the date of restructuring are not included in a provision. Ind AS 37 gives an exception to this principle viz. such losses related to an onerous contract.
  - (vi) **Appendix:** Ind AS 37 gives guidance on:
    - (a) Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds
    - (b) Liabilities arising from Participating in a Specific Market — Waste Electrical and Electronic Equipment
    - (c) Levies (imposed by government).AS 29 does not give such guidance.

11. Balance sheet of C Ltd. as at 31<sup>st</sup> December, 2017

Particulars	Note No.	(₹ '000)
<b>I. Equity and Liabilities</b>		
(1) <b>Shareholder's Funds</b>		
Share Capital	1	7,000
(2) <b>Non-Current Liabilities</b>		
Long-term borrowings	2	10,630
(3) <b>Current Liabilities</b>		
(a) Trade Payables	3	5,440
(b) Other current liabilities	7	8,200
Total		31,270
<b>II. Assets</b>		
(1) <b>Non-current assets</b>		
(a) Fixed assets		
i. Tangible assets	4	10,200
ii. Intangible assets	5	9,470
(2) <b>Current assets</b>		
(a) Cash and cash equivalents		2,000
(b) Other current assets	6	9,600
Total		31,270

## Notes to Accounts

		(₹ 000)
1.	Share Capital	
	Issued, subscribed & paid up:	
	7,00,000 equity shares of ₹ 10 each, fully paid up (W.N.5)	7,000
	(of the above 5,00,000 shares have been issued for consideration other than cash)	
2.	Long Term Borrowings	
	Secured loans (₹ 1,280 + ₹ 7,200) – W.N. 2	8,480
	Unsecured Loans (25% of ₹ 8,600)	<u>2,150</u>
		10,630

3.	Trade Payables (W.N.1)		
	A Ltd.	4,000	
	B Ltd.	<u>1,440</u>	5,440
4.	Tangible Assets		
	Fixed Assets (₹ 3,400 + ₹ 6,800)		10,200
5.	Intangible assets		
	Goodwill (W.N.4)		9,470
6.	Other Current Assets		
	A Ltd.	2,880	
	B Ltd.	<u>6,720</u>	9,600
7.	Other Current liabilities		
	A Ltd.	7,200	
	B Ltd.	<u>1,000</u>	8,200

**Working Notes:****1. Value of trade payables taken over by C Ltd. (₹ '000)**

	A Ltd.	B Ltd.
Given in balance sheet	13,000	4,600
Less: Statutory liabilities [72 lakhs – 22 lakhs]	(5,000)	(1,000)
Liability to employees	<u>(3,000)</u>	<u>(1,800)</u>
Trade payables	<u>5,000</u>	<u>1,800</u>
80% thereof	<u>4,000</u>	<u>1,440</u>

**2. Value of total liabilities taken over by C Ltd. (₹ '000)**

	A Ltd.		B Ltd.	
Current liabilities				
Statutory liabilities	7,200		1,000	
Liability to employees	3,000		1,800	
Trade payables (W.N.1)	<u>4,000</u>	14,200	<u>1,440</u>	4,240
Secured loans				
Given in Balance Sheet	16,000		8,000	
Interest waived	-		<u>800</u>	7,200
Value of Inventory (80% of ₹ 184 lakhs)	<u>14,720</u>	1,280		
Unsecured Loans (25% of ₹ 86 lakhs)		<u>2,150</u>		
		<u>17,630</u>		<u>11,440</u>

## 3. Assets taken over by C Ltd. (₹ '000)

	A Ltd. ₹	B Ltd. ₹
Fixed Assets	3,400	6,800
Current Assets 80% and 70% respectively of book value	<u>2,880</u>	<u>6,720</u>
	<u>6,280</u>	<u>13,520</u>

## 4. Goodwill / Capital Reserve on amalgamation (₹ '000)

Liabilities taken over (W.N. 2)	17,630	11,440
Equity shares to be issued to Preference Shareholders	<u>200</u>	-
A	17,830	11,440
Less: Total assets taken over (W.N. 3)	<u>(6,280)</u>	<u>(13,520)</u>
B	11,550	(2,080)
A-B	Goodwill	Capital Reserve
Net Goodwill	9,470	

## 5. Equity shares issued by C Ltd.

		Number
(i) For Cash		2,00,000
For consideration other than cash		
(ii) In Discharge of Liabilities to Employees	4,80,000	
(iii) To Preference shareholders	<u>20,000</u>	<u>5,00,000</u>
		<u>7,00,000</u>
Value of shares (₹ 10 x 7,00,000)	₹ 70 lakhs	

12. Consolidated Balance Sheet of A Ltd., and its subsidiary B Ltd.  
as at 31<sup>st</sup> March, 2017

Particulars	Note No.	(₹)
<b>I. Equity and Liabilities</b>		
<b>(1) Shareholder's Funds</b>		
(a) Share Capital	1	1,00,000
(b) Reserves and Surplus	2	15,560

(2) Minority Interest (W.N iii)		12,800
<b>Total</b>		<b>1,28,360</b>
<b>II. Assets</b>		
(1) Non-current assets		
Fixed assets		
(i) Tangible assets (93,000+32,000)		1,25,000
(ii) Intangible assets	3	3,360
<b>Total</b>		<b>1,28,360</b>

**Notes to Accounts**

		₹
1.	<b>Share Capital</b> 10,000 equity shares of ₹ 10 each	1,00,000
2.	<b>Reserves and Surplus</b> Profit & Loss Account (W.N iv)	15,560
3.	<b>Intangible assets</b> Goodwill (W.N ii)	3,360

**Working Notes:****(i) Analysis of Profit of B Ltd.**

	Capital Profit ₹	Revenue Profit ₹
Profit and Loss A/c balance on the date of acquisition	4,400	
Increase in the balance after acquisition		2,800
Profit for the year	<u>4,400</u>	<u>4,800</u>
<i>Less: Minority Interest (40 per cent)</i>	<u>1,760</u>	<u>3,040</u>
Share of A Ltd	<u>2,640</u>	<u>4,560</u>

**(ii) Cost of Control**

Cost of Investments		18,000
<i>Less: Paid-up value of shares</i>	12,000	

Share of Capital Profits	<u>2,640</u>	<u>(14,640)</u>
Goodwill		<u>3,360</u>

## (ii) Minority Interest (40 per cent)

Paid-up value of shares held	8,000
Share of Capital Profits	1,760
Share of Revenue Profits	<u>3,040</u>
	<u>12,800</u>

## (iv) Consolidated Revenue Profit

Balance as per Profit and Loss A/c of A Ltd.	8,000
Add: Profit on sale of shares	<u>3,000</u>
	11,000
Share in Revenue Profit of B Ltd.	<u>4,560</u>
	<u>15,560</u>

## (v) Investment in B Ltd.

Particulars	₹	Particulars	₹
To Balance b/d	24,000	By Bank	9,000
To Profit on Sale	<u>3,000</u>	By Balance c/d	<u>18,000</u>
	<u>27,000</u>		<u>27,000</u>

## 13. Computation of Fair Value at Initial Recognition

Year	Estimated Cash Flows	PVIF @8%	Present Value
	₹		₹
1/4/2016		1	Nil
31/3/2017	2,00,000	0.9259	1,85,180
31/3/2018	2,00,000	0.8573	1,71,460
31/3/2019	2,00,000	0.7938	1,58,760
31/3/2020	2,00,000	0.7350	1,47,000
31/3/2021	2,00,000	0.6806	1,36,120
31/3/2022	60,000	0.6302	37,812
	See Working note		
31/3/2023	60,000	0.5835	<u>35,010</u>
	See Working note		
<b>Fair Value of Loan</b>			<u><b>8,71,342</b></u>

## Working Notes:

## Computation of Interest to be paid on 31/3/2022 and 31/3/2023

Year	Cash Flows	Principal outstanding	Interest	Cumulative Interest
	₹	₹	₹	₹
31/3/2017	2,00,000	8,00,000	40,000	40,000
31/3/2018	2,00,000	6,00,000	32,000	72,000
31/3/2019	2,00,000	4,00,000	24,000	96,000
31/3/2020	2,00,000	2,00,000	16,000	1,12,000
31/3/2021	2,00,000	Nil	8,000	1,20,000
31/3/2022	60,000 (1,20,000/2)			
31/3/2023	60,000 (1,20,000/2)			

## Computation of Fair Value Loss

	₹
Fair Value of Loan	8,71,342
Loan Amount	<u>(10,00,000)</u>
Fair Value Loss	<u>(1,28,658)</u>

## Journal Entry at Initial Recognition

Date	Particulars	Dr.	Cr.
		₹	₹
1/4/2016	Loans to Employee A/c Dr. Employee Benefits A/c Dr. To Bank A/c	8,71,342 1,28,658	10,00,000

**Note:** The fair value measurement is of other than level 1. Therefore, an entity should defer the day 1 gain / loss over the term of the financial asset. Hence, ₹ 1,28,358 will be amortised over a period of 7 years. Since, there is no guidance on how to amortise the same, the simplest way is to amortise the difference in line with the interest accruals so that there is no impact on Profit or Loss.

Employee benefit is transferred to Statement of Profit and Loss.

## Computation of Interest on Amortised Cost

Year	Opening Balance (1) ₹	Interest @ 8% (2) ₹	Repayment (3) ₹	Closing Balance (1+2-3) ₹
1/4/2016				8,71,342
31/3/2017	8,71,342	69,707	2,00,000	7,41,049
31/3/2018	7,41,049	59,284	2,00,000	6,00,333
31/3/2019	6,00,333	48,027	2,00,000	4,48,360
31/3/2020	4,48,360	35,869	2,00,000	2,84,229
31/3/2021	2,84,229	22,738	2,00,000	1,06,967
31/3/2022	1,06,967	8,557	60,000	55,524
31/3/2023	55,524	4,476	60,000	Nil

## Journal Entry on 31/3/2017

Date	Particulars	Dr. ₹	Cr. ₹
31/3/2017	Loans to Employee A/c To Interest Accrued A/c	69,707	69,707
31/3/2017	Bank A/c To Loan to Employees	2,00,000	2,00,000

Note: Similar entries would be done at the end of each year.

14. Year 2013-14

Fair value of option per share = ₹ 15

Number of options expected to vest under the scheme = 540 x 100 = 54,000

Fair value = 54,000 x ₹ 15 = ₹ 8,10,000

Vesting period = 3 years

Value of option recognised as expense in 2013-14 = ₹ 8,10,000 / 3 = ₹ 2,70,000

Year 2014-15

Fair value of option per share = ₹ 15

Number of options expected to vest under the scheme = 552 x 100 = 55,200

Fair value = 55,200 x ₹ 15 = ₹ 8,28,000

Vesting period = 3 years

Number of years expired = 2 years

Cumulative value of option to recognise as expense in 2013-14 and 2014-15

$$= (\text{₹ } 8,28,000 / 3) \times 2 = \text{₹ } 5,52,000$$

Value of option recognised as expense in 2014-15

$$= \text{₹ } 5,52,000 - \text{₹ } 2,70,000 = \text{₹ } 2,82,000$$

#### Year 2015-16

Fair value of option per share = ₹ 15

Number of options actually vested under the scheme = 554 × 100 = 55,400

Fair value = 55,400 × ₹ 15 = ₹ 8,31,000

Cumulative value of option to recognise as expense in 3 years = ₹ 8,31,000

Value of option recognised as expense in 2013-14

$$= \text{₹ } 8,31,000 - \text{₹ } 5,52,000 = \text{₹ } 2,79,000$$

#### Year 2016-17

Fair value of option per share = ₹ 15

Number of shares not subscribed = (554 – 550) × 100 = 400

Value of option forfeited = 400 × ₹ 15 = ₹ 6,000

#### Employees' Compensation A/c

Year		₹	Year		₹
2013-14	To ESOP Outstanding A/c	<u>2,70,000</u>	2013-14	By Profit & Loss A/c	<u>2,70,000</u>
		<u>2,70,000</u>			<u>2,70,000</u>
2014-15	To ESOP Outstanding A/c	<u>2,82,000</u>	2014-15	By Profit & Loss A/c	<u>2,82,000</u>
		<u>2,82,000</u>			<u>2,82,000</u>
2015-16	To ESOP Outstanding A/c	<u>2,79,000</u>	2015-16	By Profit & Loss A/c	<u>2,79,000</u>
		<u>2,79,000</u>			<u>2,79,000</u>

#### ESOP Outstanding A/c

Year		₹	Year		₹
2013-14	To Balance c/d	2,70,000	2013-14	By Employees' Compensation A/c	<u>2,70,000</u>
		<u>2,70,000</u>			<u>2,70,000</u>
2014-15	To Balance c/d	5,52,000	2014-15	By Balance b/d	2,70,000
		<u>5,52,000</u>		By Employees' Compensation A/c	<u>2,82,000</u>
		<u>5,52,000</u>			<u>5,52,000</u>

2015-16	To	Balance c/d	8,31,000	2015-16	By	Balance b/d	5,52,000
					By	Employees' Compensation A/c	<u>2,79,000</u>
			<u>8,31,000</u>				<u>8,31,000</u>
2016-17	To	General Reserve (400 × 15)	6,000	2016-17	By	Balance b/d (55,400 × 15)	8,31,000
	To	Share Capital (55,000 × 10)	5,50,000		By	Bank (55,000 × 45)	24,75,000
	To	Securities Premium (55,000 × 50)	<u>27,50,000</u>				
			<u>33,06,000</u>				<u>33,06,000</u>

Note: Securities Premium

	₹
Exercise price received per share	45
Value of service received per share	<u>15</u>
Consideration received per share	60
Less: Nominal value per share	<u>(10)</u>
Securities premium per share	<u>50</u>

#### Computation of Basic EPS

	2013-14 ₹ 000	2014-15 ₹ 000	2015-16 ₹ 000
Profit before amortisation of ESOP costs	1,190	1,262	1,379
Less: ESOP cost amortised	<u>(270)</u>	<u>(282)</u>	<u>(279)</u>
Net profit for shareholders	<u>920</u>	<u>980</u>	<u>1,100</u>
Number of shares outstanding ('000)	400	400	400
Basic EPS	2.30	2.45	2.75

#### Potential Equity

	2013-14	2014-15	2015-16
A. Actual number of employees	585	565	554
B. Option granted per employee	100	100	100
C. Number of options outstanding	58,500	56,500	55,400
D. Unamortised ESOP cost per option (₹)	10*	5**	Nil

E. Exercise Price (₹ 45)	45	45	45
F. Expected exercise price to be received (C x E): ₹ 000	2,632.5	2,542.5	2,493.0
G. Unamortised ESOP cost (C x D): ₹ 000	<u>585.0</u>	<u>282.5</u>	<u>Nil</u>
H. Total proceeds: ₹ 000	<u>3,217.5</u>	<u>2,825.0</u>	<u>2,493.0</u>
I. Fair value per share (₹)	60	66	72
J. Number of shares issued for consideration (H/I)	53,625	42,803	34,625
K. Potential Equity (C – J)	4,875	13,697	20,775

\*  $[15 - (15/3)] = 10$

\*\*  $[15 - \{(15/3) \times 2\}] = 5$

#### Computation of Diluted EPS

	2013-14 ₹	2014-15 ₹	2015-16 ₹
Net profit for shareholders	9,20,000	9,80,000	11,00,000
Number of shares outstanding	4,00,000	4,00,000	4,00,000
Potential Equity	4,875	13,697	20,775
Total number of shares	4,04,875	4,13,697	4,20,775
Diluted EPS	2.27	2.37	2.61

15. Calculation of effective yield on per annum basis in respect of three mutual fund schemes of Ankush Gupta upto 31.03.2017

		X	Y	Z
1	Amount of Investment (₹)	1,00,000	2,00,000	1,00,000
2	Date of investment	1.12.2016	1.1.2017	1.3.2017
3	NAV at the date of investment (₹)	10.50	10.00	10.00
4	No. of units on date of investment [1/3]	9,523.809	20,000	10,000
5	NAV per unit on 31.03.2017 (₹)	10.40	10.10	9.80
6	Total NAV of mutual fund investments on 31.03.2017 [4 x 5]	99,047.61	2,02,000	98,000
7	Increase/ decrease of NAV [6-1]	(952.39)	2,000	(2,000)
8	Dividend received upto 31.3.2017	1,900	3,000	Nil
9	Total yield [7+8]	947.61	5,000	(2,000)
10	Yield % [9/1] x 100	0.95%	2.5%	(2%)
11	Number of days	121	90	31
12	Effective yield p.a. [10/11] x 365 days	2.87%	10.14%	(23.55%)

16. (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. Dividend rate is rising continuously, weighted average will be more appropriate for calculation of average dividend.

Year	Rate of dividend	Weight	Product
2014	12	1	12
2015	15	2	30
2016	18	3	54
2017	20	<u>4</u>	<u>80</u>
		<u>10</u>	<u>176</u>

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

Value of 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
2014	16	1	16
2015	20	2	40
2016	22	3	66
2017	25	<u>4</u>	<u>100</u>
		<u>10</u>	<u>222</u>

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

If controlling interest in the company is being taken over, then the value per share

$$\text{will be} = \frac{\text{Average yield rate}}{\text{Market expectation rate}} \times 100 = \frac{22.2}{12} \times 100 = ₹ 185 \text{ per share.}$$

## 17. Total value of business as on 31.03.2017

	₹ in thousands
Closing Capital Employed as on 31.3.2017	16,960
<i>Less:</i> Goodwill appearing in the Balance Sheet as purchased goodwill	(2,400)
<i>Add:</i> Goodwill	<u>8,225</u>
Total Value of Business	<u>22,785</u>

## Working Notes:

## 1. Calculation of Average Capital Employed

	31.3.2015 ₹ in thousands	31.3.2016 ₹ in thousands	31.3.2017 ₹ in thousands
Purchased Goodwill*	4,000	3,200	2,400
Tangible Assets	7,200	8,000	8,800
Inventories	4,800	5,600	6,400
Trade Receivables	80	640	1,760
Cash & Cash Equivalents	<u>480</u>	<u>800</u>	<u>1,600</u>
	16,560	18,240	20,960
<i>Less:</i> Trade payables	<u>(2,400)</u>	<u>(3,200)</u>	<u>(4,000)</u>
Closing Capital Employed	14,160	15,040	16,960
<i>Add:</i> Opening Capital Employed	<u>14,640</u>	<u>14,160</u>	<u>15,040</u>
Total	<u>28,800</u>	<u>29,200</u>	<u>32,000</u>
Average Capital Employed (ACE)	<u>14,400</u>	<u>14,600</u>	<u>16,000</u>

\*Since the goodwill has been purchased, it is taken as a part of capital employed. However, writing off of the goodwill is an extra-ordinary item, therefore not considered while calculating Future Maintainable Profit.

## 2. Valuation of Goodwill

## (i) Future Maintainable Profit

	31.3.2015 ₹ in thousands	31.3.2016 ₹ in thousands	31.3.2017 ₹ in thousands
Future Maintainable Profit	1,680	2,480	3,280
<i>Less:</i> Opening Profit	(480)	(560)	(640)
<i>Add:</i> Appreciation of closing inventory	800	800	800

Less: Appreciation of opening inventory	-	(800)	(800)
Add: Transferred to General Reserve	800	800	800
Goodwill written off		<u>800</u>	<u>800</u>
	2,800	3,520	4,240
Less: Normal Return @ 12.5% on ACE	<u>(1,800)</u>	<u>(1,825)</u>	<u>(2,000)</u>
(ii) Super Profit	<u>1,000</u>	<u>1,695</u>	<u>2,240</u>

$$(iii) \text{ Average Super Profit} = \left[ \frac{1,000 + 1,695 + 2,240}{3} \right] = 1,645 \text{ thousands}$$

(iv) Value of Goodwill at five years' purchase

$$= ₹ 1,645 \text{ thousands} \times 5 = ₹ 8,225 \text{ thousands.}$$

#### 18. Value Added Statement of Great Ltd.

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

<b>Reconciliation</b>		
Profit before tax		868
Depreciation		405
Wages, salaries and other benefits		8,250
Debenture interest		<u>1,200</u>
		<u>10,723</u>

### 19. Computation of Economic Value Added (EVA)

Particulars	(₹ in lacs)
Net Operating Profit after Tax (NOPAT)	831.00
Less: Weighted average cost of operating capital employed (13.35% of 2,200) (See W.N.7)	<u>(293.70)</u>
Economic Value Added (EVA)	<u>537.30</u>

#### Working Notes:

##### 1. Net Operating Profit after Tax (NOPAT)

Earnings per share	₹ 16
No. of Equity Shares	40 lacs
	₹ in lacs
Profit after Interest, Tax & Preference Dividend [40 lacs x ₹ 16]	640.00
Add: Preference Dividend (15% of ₹ 200 lacs)	<u>30.00</u>
Profit after Tax	670.00
Add: Tax @ 30% [670/70 x 30]	<u>287.14</u>
Profit before Tax	957.14
Add: Interest on Debentures [15% of ₹ 1,600 lacs]	<u>240.00</u>
Profit before Interest & Tax	1,197.14
Less: Income from Non-Trade Investment [10% of ₹ 100 lacs]	<u>(10.00)</u>
Net Operating Profit before Tax	1,187.14
Less: Tax @ 30%	<u>(356.14)</u>
Net Operating Profit after Tax [NOPAT]	<u>831.00</u>

2. Cost of Equity = Risk Free Rate + Beta Factor x (Market Rate - Risk Free Rate)

$$= 9.85\% + 1.65 (16.25 - 9.85) = 20.41\%$$

3. Cost of Preference shares = 15%

4. Cost of Debt = Interest Rate x (1 - tax rate) = 15% x (1 - 0.30) = 10.5%
5. Total Capital Employed = [Equity Share Capital + Retained Earnings + Preference Share Capital + Debentures]  
= [400 + (220 - 20) + 200 + 1,600] = 2,400
6. Weighted Average Cost of Capital (WACC)  
=  $\left(\frac{600}{2,400} \times 20.41\%\right) + \left(\frac{200}{2,400} \times 15\%\right) + \left(\frac{1,600}{2,400} \times 10.5\%\right)$   
= 5.10 + 1.25 + 7% = 13.35%
7. Operating Capital Employed

		₹ in lacs
Total Capital		2,400
<i>Less:</i> Non-operating Capital Employed		
10% Non-Trade Investment	140	
Land and Building held as Investment	20	
Advance given for purchase of a Plant	10	
Capital work-in-progress	<u>30</u>	<u>(200)</u>
Operating Capital Employed		<u>2,200</u>

20. Cost to Company in employing to Mr. X

	₹
Salary before tax ₹ 4,00,000 x 12 = $\frac{48,00,000}{0.75}$	64,00,000*
<i>Add:</i> Employee's PF contribution (50,000 x 12)	<u>6,00,000</u>
	70,00,000
<i>Add:</i> Employer's PF contribution (50,000 x 12)	<u>6,00,000</u>
	<u>76,00,000</u>

Capital base

	₹
Equity Share Capital paid up (5,00,000 shares of ₹ 75 each)	3,75,00,000
<i>Less:</i> Calls in arrears	<u>(1,00,000)</u>
	3,74,00,000
General Reserve	10,00,000

Profit & Loss A/c (balance) at the beginning of the year	(25,00,000)
Loss for the year	(1,80,000)
8% Debentures	<u>80,00,000</u>
Capital base	<u>4,37,20,000</u>
Target Profit 12.5% of capital base (4,37,20,000)	54,65,000
Profits achieved due to Mr. X [54,65,000 + 10% (54,65,000)]	60,11,500

Maximum emoluments that can be paid to Mr. X = ₹ 60,11,500

Thus, the company is advised not to hire him as his CTC ₹ 76,00,000 is more than ₹ 60,11,500.

**Note:** It is assumed that the average income tax rate of 25% given in the question is after considering the impact of ₹ 3 lakhs p.a. i.e., the exemption amount.