FINAL – November 2017

ACCOUNTING STANDARDS

Test Code – P13

Branch (MULTIPLE) (Date : 18.06.2017)

(50 Marks)

Note: All questions are compulsory.

Question 1(5 marks)

Revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods, rendering of services and the use by others of enterprise resources yielding interest, royalties and dividends. **(2 ½ Marks)**

In the given case, Shashi Ltd., the subsidiary has set up an office and establishment in India to render services to the head office for which the later has reimbursed the expenditure on salaries and other expenses amounting to ` 420 lakhs including margin of profit of ` 70 lakhs, hence the turnover to be shown in the books shall be ` 420 lakhs. **(2 ½ Marks)**

Question 2(5 Marks)

As per paragraph 3 of AS 24 'Discontinuing Operations', a discontinuing operation is a component of an enterprise:

(i) that the enterprise, pursuant to a **single plan**, is:

(1) disposing of substantially in its entirety,

(2) disposing of piecemeal, or

(3) terminating through abandonment; and

(ii) that represents a separate **major line** of business or geographical area of operations; and

(iii) that can be distinguished operationally and for financial reporting purposes. **(1 Mark)**

As per para 8 of the standard, business enterprises frequently close facilities, abandon products or even product lines, and change the size of their work force in response to market forces. While those kinds of terminations generally are not, in themselves, discontinuing operations, they can occur in connection with a discontinuing operation. **(1 Mark)**

As per para 9, examples of activities that do not necessarily satisfy criterion of discontinuing operation are gradual or evolutionary phasing out of a product line or class of service, discontinuing, even if relatively abruptly, several products within an ongoing line of business; **(1 Mark)**

In the given case, the company has enforced a gradual enforcement of change in product line and does not represent a separate major line of business and hence is not a discontinued operation. If it were a discontinuing operation, the initial disclosure event is the occurrence of one of the following, whichever occurs earlier:

(i) the enterprise has entered into a binding sale agreement for substantially all of the assets attributable to the discontinuing operation; or

(ii) the enterprises board of directors or similar governing body has both approved a detailed, formal plan for discontinuance and made an announcement of the plan. **(2 Marks)**

Question 3 (6 Marks)

(b) Statement showing calculation of Deferred Tax Asset (DTA) and Deferred Tax Liability (DTL)

S. No.	Particulars	Amount of difference	Nature of difference	DTA @ 40%	DTL @ 40%
		Rs.		Rs.	Rs.
(i)	Excess allowable depreciation as per income-tax law**(1 Mark)**	61,250	Timing	-	24,500
(ii)	Provision for doubtful debts - disallowed as per income-tax law in the current year but reversible in future years. **(1 Mark)**	27,150	Timing	10,860	-
(iii)	Share issue expenses charged in the accounting books but allowedas deduction in the income-tax law from the next year**(1 Mark)**	3,11,750	Timing	1,24,700	-
(iv)	Disallowed expenses as per income tax law**(1 Mark)**	3,92,250	Permanent	-	-
(v)	Donation debited to Profit & Loss Account				
	Allowed as per income tax**(1mark)**	50,000	No difference	-	-
	Disallowed as per income Tax**(1 mark)**	50,000	Permanent	-	-
				1,35,560	24,500

Question 4(5 Marks)

In the given case, Aqua Ltd. offers to pay ` 60 per share to Bose Ltd. The share exchange ratio would be $= \frac{60}{150} = 0.40$

It means, Aqua Ltd. would give 0.4 share for every one share of Bose Ltd. In other words, Aqua Ltd. would give 2 shares for 5 shares of Bose Ltd. **(1 mark)**

The total number of shares to be issued by Aqua Ltd. to Bose Ltd. = 3,00,000× 0.4

= 1,20,000 shares**(1 mark)**

Total number of shares of Aqua Ltd. after acquisition of Bose Ltd.

= 7,20,000 + 1,20,000 = 8,40,000 shares **(1 mark)**

Calculation of E.P.S. of the amalgamated company = $\frac{\text{Total Net Profit after Interest and Tax}}{\text{Total Number of shares}}$

= 43,20,000 / 8,40,000 = ` 5.14 per share

After amalgamation, the EPS of Aqua Ltd., will improve from ` 5 to ` 5.14. **(1 mark)**

Note: Earnings per share of Bose Ltd., i.e. ` 2.50 per share as given in the question, does not tally with the calculation i.e. 7,20,000 / 3,00,000 = ` 2.40 per share. However, the above solution has been given on the basis of EPS of Bose Ltd. as given in the question.

Question 5(5 Marks)

As per para 29 of AS 25 'Interim Financial Reporting', income tax expense is recognized in each interim period based on the best estimate of the weighted average annual income tax rate expected for the full financial year. **(1 Mark)**

		`
Estimated Annual Income	(A)	10,00,000
Tax expense:		
30% on ` 5,00,000		1,50,000

40% on remaining ` 5,00,000	2,00,000
(B)	3,50,000

Weighted average annual income tax rate $=\frac{A}{B}$ = $\frac{3,50,000}{10,00,000}$ = 35% **(2 Marks)**

Tax expense to be recognised in each of the quarterly reports **(2 Marks)**	`
Quarter I - ` 75,000 x 35%	26,250
Quarter II - ` 2,50,000 x 35%	87,500
QuarterIII - ` 3,75,000 x 35%	1,31,250
Quarter IV - ` 3,00,000 x 35%	1,05,000
` 10,00,000	3,50,000

Question 6 (6 Marks)

(i) As per paragraph 14 of AS 29, a provision should be recognized when:

1. an enterprise has a present obligation as a result of a past event
2. it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and
3. a reliable estimate can be made of the amount of obligation. **(1 Mark)**

If these conditions are not met, no provisions should be recognized.

As per paragraph 10.4 of AS 29, a contingent liability is:

(1) a possible obligation that arises from past events and the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise; or

(2) a present obligation that arises from past events but is not recognized because:

(a) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or

(b) a reliable estimate of the amount of the obligation cannot be made.

4. In this case company is required to assess the probability of occurrence of contingencies on the basis of such events taken place in earlier period. **(1 Mark)**

Though there is a present obligation based on such past event and it is probable that an outflow of resources will be required, a reliable estimate of amount of obligation cannot be made.

Hence no provision for the same is to be created and the same is to be disclosed as contingent liability. **(1 Mark)**

(ii) Treatment of Provision already created in the Balance Sheet:

1. Reversal of provision should be netted off against the relevant expenditure and should not be shown as "Other Income". **(1 Mark)**
2. Where the reversal is greater than the current year's expenditure, the net amount would be negative which may be reflected as other income. **(1 Mark)**
3. If such provision is related to earlier year, then the same should be disclosed as prior period income. **(1/2 Mark)**
4. As required by AS 29, specific disclosure should be given for reversal of provision in the notes to accounts and reference of note should be given in the specific line item of expenditure in which reversal of provision is made. **(1/2 Mark)**

Question 7 (5 Marks)

As per para 13 of AS 11 (Revised 2003) '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 recognized as income or expenses in the period in which they arise.

Thus exchange differences arising on repayment of liabilities incurred for the purpose of acquiring fixed assets are recognized as income or expense. **(2 Marks)**

Calculation of Exchange Difference:

Foreign currency loan = $\frac{3000\ Lakhs}{Rs.40}$ = 75 lakhs US Dollars
(1 Mark)

Exchange difference = 75 lakhs US Dollars (42.50 – 40.00) =

Rs. **187.50 lakhs (1 Mark)**

(including exchange loss on payment of first instalment)

Therefore, entire loss due to exchange differences amounting Rs. 187.50 lakhs should be charged to profit and loss account for the year.**(1 Mark)**

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Question 8(5 marks)

Computation of Expected Returns on Plan Assets as on 31st March, 2016, as per AS 15 **(2 ½ Marks)**

	`
Return on opening value of plan assets of ` 2,00,000 (held for the year) @ 10.25%	20,500
Add: Return on net gain of ` 30,000 (i.e. ` 55,000 – ` 25,000) during the year i.e. held for six months @ 5% (equivalent to 10.25% annually, compounded every six months)	1,500
Expected return on plan assets as on 31st March, 2016	22,000

Computation of Actual Returns on Plan Assets as on 31st March, 2016, as per AS 15**(2 ½ Marks)**

	`	`
Fair value of Plan Assets as on 31st March, 2016		3,00,000
Less: Fair value of Plan Assets as on 1st April, 2015	2,00,000	
Add: Contribution received as on 30th September, 2015	55,000	(2,55,000)
		45,000
Add: Benefits paid as on 30th September, 2015		25,000
Actual returns on Plan Assets as on 31st March, 2016		70,000

Question 9 (4 marks) Intel LLC

Cash Flow Statement for the year ended 31st March, 2016

	` in millions	*` in millions*
Cash flows from operating activities (1 Mark)		
Net income	3.30	

Add: Depreciation & amortization	0.75	
Loss from disposal of assets	1.20	
Less: Increase in accounts receivables	(1.50)	
Net cash generated from operating activities		3.75
Cash flows from investing activities(1 Mark)		
Capital expenditure	(9.90)	
Proceeds from sale of fixed assets	1.60	
Net cash used in investing activities		(8.30)
Cash flows from financing activities(1 Mark)		
Proceeds from issuance of additional shares	6.50	
Dividend declared	(0.50)	
Redemption of 4.5% debentures	(2.50)	
Net cash generated from financing activities (1 Mark)		3.50
Net decrease in cash		(1.05)
Cash at beginning of the period		1.55
Cash at end of the period (Balancing figure)		**0.50**

Question 10 (4 marks)

P Ltd. has direct economic interest in R Ltd. to the extent of 14%, and through Q Ltd. (in which it is the majority shareholders) it has further control of 12% in R Ltd. (60% of Q Ltd.'s 20%). **These two taken together (14% + 12%) make the total control of 26%. (1 Mark)**

AS 18 'Related Party Disclosures', defines *related party* as one that has at any time during the reporting period, the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions. (1 Mark)

Since, P Ltd. has total control of 26% (directly and indirectly by Q Ltd.) in R Ltd. which is less than half of the voting power of R Ltd., P Ltd. is said to have significant influence over R Ltd. Also it is given in the question that R Ltd. is a listed company and regularly supplies goods to P Ltd. **Therefore, related party disclosure, as per AS 18, is required by R Ltd. in its financial statements, in respect of goods supplied to P Ltd. (2 marks)**

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