# FINAL – November 2017

**PAPER 1: FINANCIAL REPORTING**

**Test Code: PR 1**
**Branch(MULTIPLE) (Date :25.09.2017)**

**(100 Marks)**

**Note:** ***Question No.1 is compulsory. Candidates are required to answer any five questions from the remaining six questions.***

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

***Working notes should form part of the answers.***

**Question 1**

**a. Calculation of Defined Benefit Obligation**

Expected last drawn salary = ` 14,90,210 x 110% x 110% x 110% x 110% x 110%
= ` 24,00,000

Defined Benefit Obligation (DBO) = ` 24,00,000 x 25% x 5 = ` 30,00,000

Amount of ` 6,00,000 will be charged to Profit and Loss Account of the company every year as cost for Defined Benefit Obligation. **(2 marks)**

**Calculation of Current Service Cost (1 ½ marks)**

| *Year* | *Equal apportioned amount of DBO [i.e. ` 30,00,000/ 5 years]* | *Discounting @ 8% PV factor* | *Current service cost (Present Value)* |
|---|---|---|---|
| *a* | *b* | *c* | *d = b x c* |
| 1 | 6,00,000 | 0.735 (4 Years) | 4,41,000 |
| 2 | 6,00,000 | 0.794 (3 Years) | 4,76,400 |
| 3 | 6,00,000 | 0.857 (2 Years) | 5,14,200 |
| 4 | 6,00,000 | 0.926 (1 Year) | 5,55,600 |
| 5 | 6,00,000 | 1 (0 Year) | 6,00,000 |

**Calculation of Interest Cost to be charged per year(1 ½ marks)**

| *Year* | *Opening balance* | *Interest cost* | *Current service cost* | *Closing balance* |
|---|---|---|---|---|
| *a* | *b* | *c = b x 8%* | *d* | *e = b + c + d* |
| 1 | 0 | 0 | 4,41,000 | 4,41,000 |
| 2 | 4,41,000 | 35,280 | 4,76,400 | 9,52,680 |
| 3 | 9,52,680 | 76,214 | 5,14,200 | 15,43,094 |
| 4 | 15,43,094 | 1,23,447 | 5,55,600 | 22,22,141 |
| 5 | 22,22,141 | 1,77,859* | 6,00,000 | 30,00,000 |

**b.**

(a) Interest for the period 2014-15
= US$ 10 lakhs x 4% × ` 62 per US$ = ` 24.80 lakhs
(b) Increase in the liability towards the principal amount
= US $ 10 lakhs × ` (62 - 56) = ` 60 lakhs
(c) Interest that would have resulted if the loan was taken in Indian currency
= US$ 10 lakhs × ` 56 x 10.5% = ` 58.80 lakhs

**(1 ½ marks)**

Difference between interest on local currency borrowing and foreign currency borrowing = ` 58.80 lakhs - ` 24.80 lakhs = ` 34 lakhs. Therefore, out of ` 60 lakhs increase in the liability towards principal amount, only ` 34 lakhs will be considered as the borrowing cost. Thus, total borrowing cost would be ` 58.80 lakhs being the aggregate of interest of ` 24.80 lakhs on foreign currency borrowings plus the exchange difference to the extent of difference between interest on local currency borrowing and interest on foreign currency borrowing of ` 34 lakhs.

**(2 marks)**

Hence, ` 58.80 lakhs would be considered as the borrowing cost to be accounted for as per AS 16 and the remaining ` 26 lakhs (60 - 34) would be considered as the exchange difference to be accounted for as per AS 11.

**(1 ½ marks)**

**c.** As per paragraph 3 of AS 24 'Discontinuing Operations', a discontinuing operation isa 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 ½ 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.

**(1 ½ mark)**

d.

| **(a) Calculation of carrying amount as on 31.03.2015: ` (3 marks)** | |
|---|---|
| Cost of the asset purchased on 01.04.2008 | 10,00,000 |
| *Less:* Depreciation 3 years – upto 31.03.2011 (3/10) | (3,00,000) |
| Carrying amount as on 31.03.2011 | 7,00,000 |
| *Add:* Upward revaluation as on 01.04.2011 credited to Revaluation Reserve | 1,40,000 |
| Carry amount as on 01.04.2011 | 8,40,000 |
| *Less:* Depreciation 3 years – upto 31.03.2014 (3/7) | (3,60,000) |
| 4,80,000 | |
| *Less:* Impairment loss due to recoverable amount being ` 4,30,000 | (50,000) |
| Carrying amount as on 01.04.2014 | 4,30,000 |
| *Less:* Depreciation for 2014-15 (4,30,000/4) | (1,07,500) |
| 3,22,500 | |
| *Add:* Reversal of impairment (as per Working Note 2) | 37,500 |
| Carrying amount as on 31.03.2015 | 3,60,000 |

**Working Notes:**

| **1. Statement showing balance of Revaluation Reserve ` (1 mark)** | |
|---|---|
| Revaluation Reserve credited on 01.04.2011 | 1,40,000 |
| *Less:* Excess depreciation charges due to revaluation for 3 years upto 31.03.2014 [(1,40,000/7) x 3] | (60,000) |
| Revaluation Reserve balance on 31.03.2014 | 80,000 |
| *Less:* Impairment loss on 31.03.2014 | (50,000) |
| Revaluation Reserve balance on 01.04.2014 | 30,000 |
| *Less:* Depreciation charge for 2014-15 | (7,500) |
| 22,500 | |
| *Add:* Reversal of impairment on 31.03.2015 | 37,500 |
| Revaluation Reserve balance on 01.04.2015 | 60,000 |

| **Treatment of Impairment loss: (1 mark)**<br>Reversal of impairment loss should not exceed the carrying amount that would have been determined (net of depreciation) has no impairment loss been recognized for the asset in prior accounting periods.<br>` | |
|---|---|
| Carrying amount of the asset before impairment as on 31.03.2014 | 4,80,000 |
| *Less:* Depreciation for the year 2014-15 | (1,20,000) |
| Carrying amount of the asset as on 31.03.2015 | 3,60,000 |
| Carrying amount as calculated after impairment | (3,22,500) |
| Reversal of impairment to be transferred to Revaluation surplus | 37,500 |
| **Impairment gain to be ignored:** | |
| Recoverable amount on 31.03.2015 | 5,00,000 |
| *Less:* Carrying amount on 31.03.2015 | (3,60,000) |
| 1,40,000 | |

**Question 2**

**(i) Before issue of bonus shares**

| | | ` | ` |
|---|---|---|---|
| (i) | **Cost of control** | | |
| | Investment ion DEE Limited | | 9,60,000 |
| | *Less:* Face Value of investments | 8,40,000 | |
| | Capital Profits (W.N.) | 50,400 | (8,90,400) |
| | Cost of control | | 69,600 |
| (ii) | Minority Interest | | |
| | Share capital | 3,60,000 | |
| | Capital Profit (W.N.) | 21,600 | |
| | Revenue profit (W.N.) (86,400 + 4,57,200) | 5,43,600 | 9,25,200 |
| (iii) | Consolidated Profit and Loss account of ZEE Ltd. | | |
| | Balance | 12,60,000 | |
| | *Add:* Share in post-acquisition profit of DEE Limited (W.N.) | 2,01,600 | 14,61,600 |
| (iv) | Consolidated Revenue reserve account of ZEE Ltd. | | |
| | Balance | 48,00,000 | |
| | *Add:* Post-acquisition share of DEE Limited (W.N.) | 10,66,800 | 58,66,800 |

**(3 marks)**

**(ii) Immediately after issue of bonus shares**

| | | ` | ` |
|---|---|---|---|
| (i) | Cost of control | | |
| | Face value of Investment in DEE Limited (8,40,000 + 4,20,000) | 12,60,000 | |
| | *Add:* Capital profits (W.N.) | 50,400 | |
| | | 13,10,400 | |
| | *Less:* Value of investments | (9,60,000) | |
| | Cost of control(Capital reserve) | | 3,50,400 |
| (ii) | Minority Interest | | |
| | Share Capital (3,60,000 + 1,80,000) | 5,40,000 | |
| | Pre-acquisition Capital Profit (W.N.) | 21,600 | |
| | Post-acquisition Revenue Profit (W.N) | | |
| | R/R 2,77,200 | | |
| | P/L 86,400 | 3,63,600 | 9,25,200 |
| (iii) | Consolidated Profit and loss account of ZEE Ltd. | | |
| | Balance | 12,60,000 | |
| | *Add:* Share in Post-acquisition profit of DEE Limited (W.N.) | 2,01,600 | 14,61,600 |
| (iv) | Consolidated Revenue reserve account of ZEE Ltd. | | |
| | Balance | 48,00,000 | |
| | *Add:* Post-acquisition share of DEE Limited (W.N.) | 6,46,800 | 54,46,800 |

**(3 marks)**

**Consolidated Balance Sheet of ZEE Limited and its subsidiary DEE Limited as on 31st March, 2015 (4 marks)**

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

**Notes to Accounts: (2 marks)**

| | | ` | ` |
|---|---|---|---|
| 1 | Reserves and Surplus | | |
| | Capital Reserve | 3,50,400 | |
| | Securities premium reserve | 7,20,000 | |
| | Profit and loss account | 14,61,600 | |
| | Revenue Reserve | 54,46,800 | 79,78,800 |
| 2 | Trade Payable | | |
| | Zee Ltd. | 4,44,000 | |
| | Dee Ltd. | 1,68,000 | 6,12,000 |
| 3. | Fixed assets | | |
| | Zee Ltd. | 63,36,000 | |
| | Dee Ltd. | 18,48,000 | 81,84,000 |
| 4. | Current assets | | |
| | Zee Ltd. | 35,28,000 | |
| | Dee Ltd. | 14,04,000 | 49,32,000 |

**Working Notes: (4 marks)**

1. Shareholding Pattern

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

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

| | *Capital profit (before and after issue of bonus shares)* | *Revenue profits (before bonus issue)* | | *Revenue profits (After bonus issue)* | |
|---|---|---|---|---|---|
| | | *Revenue Reserve* | *Profit and Loss A/c* | *Revenue Reserve* | *Profit and Loss A/c* |
| Pre-acquisition profits | 24,000 | | | | |
| Profit and loss account on 31st March, 2010 | 48,000 | | | | |
| | 72,000 | | | | |
| Revenue Reserve | | 15,24,000 | | 15,24,000 | |
| *Less:* Bonus Shares | | | | (6,00,000) | |
| *Add:* Profit during the period 1st April, 2010 to 31st March, 2015 (3,36,000-48,000) | | | 2,88,000 | | 2,88,000 |
| | 72,000 | 15,24,000 | 2,88,000 | 9,24,000 | 2,88,000 |
| ZEE Limited's share (70%) | 50,400 | 10,66,800 | 2,01,600 | 6,46,800 | 2,01,600 |
| Minority's share (30%) | 21,600 | 4,57,200 | 86,400 | 2,77,200 | 86,400 |

**Question 3**

**a.** (i) Calculation of initial recognition amount of loan to employees **(2 marks)**

| *Year end* | *Cash Inflow* | | *Total* | *P.V. factor @10%* | *Present value* |
|---|---|---|---|---|---|
| | *Principal* ` *Rs* | *Interest @ 4%* ` *Rs* | *R` s* | | ` *Rs* |
| 2014 | 20,00,000 | 4,00,000 | 24,00,000 | 0.9090 | 21,81,600 |
| 2015 | 20,00,000 | 3,20,000 | 23,20,000 | 0.8263 | 19,17,016 |
| 2016 | 20,00,000 | 2,40,000 | 22,40,000 | 0.7512 | 16,82,688 |
| 2017 | 20,00,000 | 1,60,000 | 21,60,000 | 0.6829 | 14,75,064 |
| 2018 | 20,00,000 | 80,000 | 20,80,000 | 0.6208 | 12,91,264 |
| Present value or Fair value | | | | | 85,47,632 |

(ii) . Calculation of amortised cost of loan to employees **(2 marks)**

| *Year* | *Amortised cost (Opening balance) [1]* ` | *Interest to be recognised@10% [2]* ` | *Repayment (including interest) [3]* ` | *Amortised Cost (Closing balance) [4]=[1]+ [2] – [3]* ` |
|---|---|---|---|---|
| 2014 | 85,47,632 | 8,54,763 | 24,00,000 | 70,02,395 |
| 2015 | 70,02,395 | 7,00,240 | 23,20,000 | 53,82,635 |
| 2016 | 53,82,635 | 5,38,264 | 22,40,000 | 36,80,899 |
| 2017 | 36,80,899 | 3,68,090 | 21,60,000 | 18,88,989 |
| 2018 | 18,88,989 | 1,91,011* | 20,80,000 | Nil |

**(iii) Journal Entries in the books of Friendly Ltd. (4 marks)**
**for the year ended 31st December, 2014 (regarding loan to employees)**

| | | *Dr. Amount (`)* | *Cr. Amount (`)* |
|---|---|---|---|
| Staff loan A/c | Dr. | 1,00,00,000 | |
| To Bank A/c | | | 1,00,00,000 |
| (Being the disbursement of loans to staff) | | | |
| Staff cost A/c ` (1,00,00,000–85,47,632) [Refer | Dr. | 14,52,368 | |

| Particulars | | Dr. (`) | Cr. (`) |
|---|---|---|---|
| part (ii)]<br>To Staff loan A/c*<br>(Being the write off of excess of loan balance over<br>present value thereof in order to reflect the loan at its<br>present value of ` 85,47,632) | | | 14,52,368 |
| Staff loan A/c<br>To Interest on staff loan A/c<br>(Being the charge of interest @ market rate of 10% on<br>the loan) | Dr. | 8,54,763 | 8,54,763 |
| Bank A/c<br>To Staff loan A/c<br>(Being the repayment of first instalment with interest for<br>the year) | Dr. | 24,00,000 | 24,00,000 |
| Interest on staff loan A/c<br>To Profit and loss A/c<br>(Being transfer of balance of staff loan Interest account<br>to profit and loss account) | Dr. | 8,54,763 | 8,54,763 |
| Profit and loss A/c<br>To Staff cost A/c<br>(Being transfer of balance of staff cost account to profit<br>and loss account) | Dr. | 14,52,368 | 14,52,368 |

• The difference of ` 2,112 (` 1,91,011 – ` 1,88,899) is due to approximation in computations.

* Loans and receivables should be measured at amortized cost using the effective rate of interest method as per AS 30 'Financial Instruments: Recognition and Measurement'.

**b. Employees Compensation Account (1 mark)**

| Year | | ` | Year | | ` |
|---|---|---|---|---|---|
| 2010-11 | To Provision for Liability (W.N. 3) | 1,27,200 | 2010-11 | By Profit & Loss A/c | 1,27,200 |
| 2011-12 | To Provision for Liability (W.N. 3) | 1,52,633 | 2011-12 | By Profit & Loss A/c | 1,52,633 |
| 2012-13 | To Provision for Liability (W.N. 3) | 2,02,867 | 2012-13 | By Profit & Loss A/c | 2,02,867 |

**Provision for Liability Component Account (1 mark)**

| Year | | ` | Year | | ` |
|---|---|---|---|---|---|
| 2010-11 | To Balance c/d | 1,27,200 | 2010-11 | By Employees Compensation A/c | 1,27,200 |
| 2011-12 | To Balance c/d | 2,79,833 | 2011-12 | By Balance b/d | 1,27,200 |
| | | | | By Employees Compensation A/c | 1,52,633 |
| | | 2,79,833 | | | 2,79,833 |
| 2012-13 | To Balance c/d | 4,82,700 | 2012-13 | By Balance b/d | 2,79,833 |
| | | | | By Employees Compensation A/c | 2,02,867 |
| | | 4,82,700 | | | 4,82,700 |

**If Employee opts for Cash settlement**

**Provision for Liability Component Account (1/2 mark)**

| Year | Particulars | ` | Year | Particulars | ` |
|---|---|---|---|---|---|
| 2013-14 | To Bank (5000 x ` 96.54) | 4,82,700 | 2013-14 | By Balance c/d | 4,82,700 |

**If employee opts for Equity Settlement**

**Provision for Liability Component Account (1/2 mark)**

| Year | Particulars | ` | Year | Particulars | ` |
|---|---|---|---|---|---|
| 2013-14 | To ESOP outstanding A/c | 4,82,700 | 2013-14 | By Balance c/d | 4,82,700 |

**ESOP Outstanding Account**
**(1 mark)**

| *Year* | | ` | *Year* | | ` |
|---|---|---|---|---|---|
| 2013-14 | To Equity Share Capital A/c (6000 x ` 10) | 60,000 | 2013-14 | By Provision for Liability Component A/c | 4,82,700 |
| | To Securities Premium A/c | 12,86,700 | | By Bank (6,000 x ` 144) | 8,64,000 |
| | | 13,46,700 | | | 13,46,700 |

**Working Notes:**

**(b) Computation of Fair Values (2 mark)**

| | |
|---|---|
| Fair value of shares subject to lock in as on 1st April, 2010 | ` 60 |
| % of increase in fair value of shares not subjected to lock in | 20% |
| Fair value as on 1st April, 2010 of shares not subject to lock in (60+20%) | ` 72 |
| % increase over previous value in respect of fair value on 31.03.2011 | 6% |
| Fair value of shares not subject to lock in restriction on 31.03.2011 (72 + 6%) | ` 76.32 |
| % increase over previous value in respect of fair value on 31.03.2012 | 10% |
| Fair value of shares not subject to lock in restriction on 31.03.2012 (76.32 + 10%) | ` 83.95 |
| % increase over previous value in respect of fair value on 31.03.2013 | 15% |
| Fair value of shares not subject to lock in restriction on 31.03.2013 (83.95 + 15%) | ` 96.54 |

2. **Expense to be recognized in respect of Equity Component (1 mark)**

| | |
|---|---|
| Fair value under Equity Settlement Option (6,000 x ` 60 ) | 3,60,000 |
| *Less*: Fair value under cash settlement (liability component) option (5,000 x ` 72) | 3,60,000 |
| Equity component | Nil |
| Expenses to be recognized each year for equity component | Nil |

3. **Expenses to be recognized for Liability Component (1 mark)**

| | *2010-11* | *2011-12* | *2012-13* |
|---|---|---|---|
| Number of shares (A) | 5000 | 5000 | 5000 |

| Fair value at the end of each year (B) | 76.32 | 83.95 | 96.54 |
|---|---|---|---|
| Expenses to be recognized* | 1,27,200 | 1,52,633 | 2,02,867 |

*Expenses to be recognized each year has been calculated on the basis:

$\frac{\text{Fair Value} \times \text{No. of years Expired}}{\text{Vesting Period}}$ −Expenditure recognised till previous year

**Question 4**

**a. Maximum Value that can be quoted by Shobhit Garments Ltd. (5 marks)**

| | ` *in lakhs* | ` *in lakhs* |
|---|---|---|
| Present Value of Incremental Cash Flows (W.N.) | | 3726.49 |
| *Add:* Cash to be collected immediately by disposal of assets: | | |
| Tangible Fixed Assets | 90 | |
| Investments | 424 | |
| Stock & Receivables | 940 | 1454.00 |
| *Less:* Current Liabilities [including 20% of 14.10] | 800 | |
| Contingent Liability [14.10 x 80%] | 11.28 | |
| Retrenchment Compensation | 260 | |
| Renovation of Plant [50 + (50 x 0.6944)] | 84.72 | (1156.00) |
| Goodwill | | 300.00 |
| Maximum Value that can be quoted | | 4324.49 |
| Maximum Price per Share [4324.49/20 lakh shares] | | 216.22 |

**Working Note:**

**Calculation of Present Value of Incremental Cash Flows (3 marks)**

| *Year* | *Cash Flows before takeover* | *Cash Flows after takeover* | *Incremental Cash Flows* | *Discount Factor* | *Discounted Cash Flow* |
|---|---|---|---|---|---|
| | | | *D=C-B* | *@ 20%* | *F = D x E* |
| *A* | *B* | *C* | | *E* | |
| 1 | 3000 | 3600 | 600 | 0.8333 | 499.98 |
| 2 | 3400 | 3800 | 400 | 0.6944 | 277.76 |
| 3 | 4000 | 4600 | 600 | 0.5787 | 347.22 |
| 4 | 5000 | 5900 | 900 | 0.4823 | 434.07 |
| 5 | 6000 | 7000 | 1000 | 0.4019 | 401.90 |
| 6 | 6800 | 8000 | 1200 | 0.3349 | 401.88 |

| | | | | | |
|---|---|---|---|---|---|
| 7 | 7600 | 9000 | 1400 | 0.2791 | 390.74 |
| 8 | 9000 | 10600 | 1600 | 0.2326 | 372.16 |
| 9 | 10000 | 11600 | 1600 | 0.1938 | 310.08 |
| 10 | 12000 | 13800 | 1800 | 0.1615 | 290.70 |
| | | | | | 3726.49 |

b. **As per IFRS:** On the basis of principles of the IAS 18, IFRIC 15, Agreement for Construction of Real Estate, prescribes that construction of real estate should be treated as sale of goods and revenue should be recognised when the entity has transferred significant risks and rewards of ownership and retained neither continuing managerial involvement nor effective control. **(2 ½ marks)**

**Carve out:** IFRIC 15 has not been included in Ind AS 18 to scope out such agreements from Ind AS 18. A separate guidance note on accounting for real estate developers (for Ind AS compliant entities) has been issued by the ICAI to address the matter. (**2 ½ marks)**

**Reason:** It was observed that requirement will lead to recognition of revenue in the financial statements by real estate developers based on the completion method, i.e., only in the last year of the completion of project. It was felt that in case the revenue for the whole project is recognised in the last year of completion of project, it will not reflect the true performance of the business of the real estate developer. Further, it was felt that since Ind AS 11 requires recognition of revenue of all construction contracts by reference to stage of completion, it may lead to inappropriate accounting in case of certain real estate development projects in case this Ind AS is applied for all real estate development projects. Therefore, it was considered appropriate that rather than making changes in Ind AS 11 or Ind AS 18, a separate Guidance note (for Ind AS-compliant entities) should be issued in line with the Guidance note on Accounting for Real Estate Transactions issued by the Institute of Chartered Accountants of India (for entities on which AS are applicable). **(3 marks)**

**Question 5**

**(a) (i)** **Value Added Statement of Pradeep Ltd.**
**for the period ended on 31.3.2016**
**(2 marks)**

| | | *(` in lakhs)* |
|---|---|---|
| Sales (net) (2,500 – 35) | | 2,465 |
| *Less:* Cost of Bought in Materials and Services: | | |
| Raw material consumed (180 + 714 – 240) | 654 | |
| Printing and stationary | 24 | |
| Auditors' remuneration | 15 | |
| Rent paid | 172 | |
| Other expenses | 88 | (953) |
| Value added by manufacturing and trading activities | | 1,512 |

**Application of Value Added**
**(3 marks)**

| | | (` in lakh) | (` in lakh) | % |
|---|---|---|---|---|
| To | Pay Employees: | | | |
| | Wages and salaries | 352 | | |
| | Employees state insurance | 32 | | |
| | Provident fund contribution | 26 | 410 | 27.12 |
| | Income-tax | | 280 | 18.52 |
| To | Pay Providers of Capital: | | | |
| | Interest on borrowings | 40 | | |
| | Dividend | 85 | 125 | 8.27 |
| To | Provide for maintenance and expansion of the company: | | | |
| | Depreciation | 132 | | |
| | Transfer to reserve (assumed) (balancing figure) | 120 | | |
| | Retained profit | 445 | 697 | 46.09 |
| | | | 1,512 | 100 |

**Value Added Per Employee = Value Added/ No. of Employees (1/2 mark)**

1,512 \ 87 = 17.38

**Average Earnings Per Employee = Average Earnings of Employee / No. of Employees**

410/87 = 4.71

**(1/2 mark)**

**Sales Per Employee = Sales / No. of Employees(1/2 mark)**

2,465 / 87 = 28.33

**Note:** There is a missing figure in the question of ` 120 lakhs which has been assumed as 'transfer to reserves' in the above solution. However, one may assume some other item like either excise duty or manufacturing expenses etc. and may solve accordingly.

For verification of missing figure, summarised Profit and Loss Account for the year ended 31st March, 2016 has been prepared for better understanding, though not required in the question.

**Summarised Profit & Loss Account for the year ended 31.3.2016 (1 ½ marks)**

| | | Amount<br>(` in lakhs) |
|---|---|---|
| Income | | |
| Sales | | 2,465 |
| *Less:* Expenditure | | |
| Raw material consumed | 654 | |
| Auditors' remuneration | 15 | |
| Rent paid | 172 | |
| Other expenses | 88 | |
| Depreciation | 132 | |
| Interest on Borrowings | 40 | |
| Wages and Salaries | 352 | |
| Employees State Insurance | 32 | |
| Provident Fund Contribution | 26 | (1,535) |
| Profit before tax | | 930 |
| Less: Provision for tax | | (280) |
| Profit after tax | | 650 |
| Appropriations: | | |
| Dividend to ordinary shareholders | | (85) |
| Retained Profit for the year (as calculated) | | 565 |
| Retained Profit for the year (as given in the question) | | 445 |
| Difference (assumed as transfer to reserves) | | 120 |

(b) (a) NAV of the Fund **(2 marks)**

$$= \frac{` 1,85,000 + ` 1,34,54,000 + ` 26,36,000 + ` 4,31,70,000 + ` 5,53,000}{5,00,000}$$

$$= \frac{` 5,99,98,000}{5,00,000} = `119.996 \text{ rounded off as } ` 120.$$

(b) The revised position of the fund on 1st April, 2016 shall be as follows: **(3 marks)**

| *Shares* | *No. of shares* | *Price* | *Amount (`)* |
|---|---|---|---|
| A Ltd. | 10,000 | 18.50 | 1,85,000 |
| B Ltd. | 35,000 | 384.40 | 1,34,54,000 |
| C Ltd. | (10,000 + 15,000) 25,000 | 263.60 | 65,90,000 |
| D Ltd. | 75,000 | 575.60 | 4,31,70,000 |
| E Ltd. | 20,000 | 27.65 | 5,53,000 |
| Cash[ 75,00,000 – (15,000 x 263.60)] | | | 35,46,000 |
| | | | 6,74,98,000 |

$$\text{No. of units of fund} = 5,00,000 + \frac{75,00,000}{120} = 5,62,500 \text{ units}$$

(c) On 2nd April 2016, the new NAV of the fund will be as follows: **(3 marks)**

| *Shares* | *No. of shares* | *Price* | *Amount (`)* |
|---|---|---|---|
| A Ltd. | 10,000 | 21.30 | 2,13,000 |
| B Ltd. | 35,000 | 417.00 | 1,45,95,000 |
| C Ltd. | 25,000 | 289.80 | 72,45,000 |
| D Ltd. | 75,000 | 512.20 | 3,84,15,000 |
| E Ltd. | 20,000 | 35.00 | 7,00,000 |
| Cash | | | 35,46,000 |
| | | | 6,47,14,000 |

$$\text{NAV as on 2nd April 2016} = \frac{` 6,47,14,000}{5,62,500} = `115.047 \text{ per unit}$$

**Question 6**

**Calculation of Net Assets (3 marks)**

| | Good Ltd. (` in '000) | | Better Ltd. (` in '000) | |
|---|---|---|---|---|
| Goodwill (given to be of nil value) | | | | |
| Machines and Plant | 510 | | 195 | |
| Other Fixed Assets | 90 | | 15 | |
| | 600 | | | 210 |
| *Add*: 15% increase in price | 90 | 690 | | |
| Current Assets | | | | |
| Inventories | | 185 | 35 | |
| (25 thousand x 25/ 125) | | | 5 | 30 |
| Debtors | | 100.50 | 35 | |
| *Less*: Debtors considered bad | | | 20 | 15 |
| Prepaid expenses | | 24.50 | | 2 |
| Cash in Hand & Bank | 178 | | | 25 |
| *Less*: Payment of Dividend (10% of ` 800 thousand) | (80) | 98 | | - |
| Value of Total Assets | | 1,098 | | 282 |
| *Less* : Liabilities | | | | |
| Trade Payables | | 45 | | 24 |
| Provisions | 95 | | | 12 |
| *Less*: Dividend paid and adjusted in cash | (80) | 15 | | |
| (assumed that proposed dividend was included in provisions) | | | | |
| Value of Net Assets of the Company | | 1,038 | | 246 |

**Working Notes:**
**(3 marks)**

**1 Calculation of Intrinsic Value of Shares**

| | Good Ltd. | Better Ltd. |
|---|---|---|
| Net assets value as on 31.03.2017 (` *in '000)* | 1,038 | 246 |
| No. of shares of the company (*in '000)* | 80 | 20 |
| Intrinsic value per share | 12.975 | 12.30 |

**2. Calculation of Purchase Consideration**

| | Good Ltd. | Better Ltd. |
|---|---|---|
| Intrinsic value per share | 12.975 | 12.30 |

| | | |
|---|---|---|
| Premium to be paid by Best Ltd. | 5.00 | 3.00 |
| Amount to be paid per share | 17.975 | 15.30 |
| No. of shareholders agreeing to amalgamation (*in '000)* | 79.90 | 20 |
| Total amount to be paid by Best Ltd. (` *in '000)* | 1,436.202 | 306 |
| | | 30,600 |
| share (` 2 paid in cash) | | |
| Total number of equity shares | 1,74,220 | |
| Payment to dissenting shareholders (100 shares x 22.98) | ` 2.298 thousand | |
| Total purchase consideration (` *in '000)* | 1,438.50 | 306.00 |

**Entries in Books of Best Ltd.**
**(4 marks)**

| | | (` *in '000)* | (` *in '000)* |
|---|---|---|---|
| Business Purchase A/c | Dr. | 1,744.50 | |
| To Liquidators of Good Ltd. | | | 1,438.50 |
| To Liquidators of Better Ltd. | | | 306.00 |
| (Being the purchase of Good Ltd. and Better Ltd.) | | | |
| Fixed Assets | Dr. | 900.00 | |
| Inventories | Dr. | 215.00 | |
| Debtors | Dr. | 115.50 | |
| Prepaid Expenses | Dr. | 26.50 | |
| Cash & Bank | Dr. | 123.00 | |
| Goodwill (balancing figure) | Dr. | 460.50 | |
| To Trade Payables | | | 69.00 |
| To Provisions | | | 27.00 |
| To Business Purchase A/c | | | 1,744.50 |
| (Being the assets and liabilities of the companies taken over at revalued values) | | | |
| Liquidators of Good Ltd. | Dr. | 1,438.50 | |
| Liquidators of Better Ltd. | Dr. | 306.00 | |
| To Equity Share Capital A/c | | | 1,742.20 |
| To Cash A/c | | | 2.30 |
| (Being payment made to liquidators of amalgamating companies) | | | |
| Amalgamation Adjustment Reserve | Dr. | 24.00 | |
| To Statutory Funds | | | 24.00 |
| (Being the statutory reserves of Good Ltd. and Better Ltd. taken by Best Ltd. with corresponding debit to Amalgamation | | | |

| Adjustment Reserve) | | |
|---|---|---|

**Balance Sheet of Best Ltd. as on 31st March, 2017**
**(6 marks)**

| | Note No. | ` in '000 |
|---|---|---|
| Equity and liabilities | | |
| Shareholders' Funds | | |
| (a) Share Capital | | 1,742.20 |
| (b) Reserves and Surplus | | |
| Statutory Funds 24 | | |
| Amount Adjusted Reserve (24) | | Nil |
| Non-Current liabilities | | |
| Long-term borrowings | | - |
| Current liabilities | | |
| (a) Trade Payables | | 69 |
| (b) Other Current liabilities | | |
| (c) Short-term provisions | | 27 |
| Total | | 1,838.20 |
| Assets | | |
| Non-Current Assets | | |
| Fixed Assets | | |
| (i) Tangible Assets | | 900 |
| (ii) Intangible Assets | | 460.50 |
| Current Assets | | |
| (a) Inventories | | 215 |
| (b) Trade Receivables | | 115.50 |
| (c) Cash and Bank Balances | | 120.70 |
| (d) Short-term loans and advances | | 26.50 |
| Total | | 1,838.20 |

**Question 7**

a. IFRS 3 requires bargain purchase gain arising on business combination to be recognised in profit or loss as income.

**Carve out:** Ind AS 103 requires the bargain purchase gain to be recognised in other comprehensive income and accumulated in equity as capital reserve, unless there is no clear evidence for the underlying reason for classification of the business combination as a

bargain purchase, in which case, it shall be recognised directly in equity as capital reserve. **(2 marks)**

**Reasons:** At present, since bargain purchase gain occurs at the time of acquiring a business, these are considered as capital reserve. Recognition of such gains in profit or loss would result into recognition of unrealised gains, which may get distributed in the form of dividends. Moreover, such a treatment may lead to structuring through acquisitions, which may not be in the interest of the stakeholders of the company. **(2 marks)**

b. The present case falls under the category of defined benefit scheme under Para 49 of AS 15 (Revised) "Employee Benefits". The said para encompasses cases where payment promised to be made to an employee at or near retirement presents significant difficulties in the determination of periodic charge to the statement of profit and loss. The contention of the Company that the settlement allowance will be accounted for on claim basis is not correct even if company's obligation under the scheme is uncertain and requires estimation. In estimating the obligation, assumptions may need to be made regarding future conditions and events, which are largely outside the company's control. **(2 marks)**

Thus,

(1) Settlement allowance payable by the company is a defined retirement benefit, covered by AS 15 (Revised).

(2) A provision should be made every year in the accounts for the accruing liability on account of settlement allowance. The amount of provision should be calculated according to actuarial valuation.

(3) Where, however, the amount of provision so determined is not material, the company can follow some other method of accounting for settlement allowances.

**(2 marks)**

c. As per AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', due to uncertainties inherent in business activiti es, many financial statement items cannot be measured with precision but can only be estimated. The estimation process involves judgments based on the latest information available. An estimate may have to be revised if changes occur regarding the circums tances on which the estimate was based, or as a result of new information, more experience or subsequent developments. Accordingly, the basis of provisioning either on 'number of issues' or on 'technical evaluation' is the basis of making estimates.

**(1 mark)**

The decision of making provision for non-moving inventories on the basis of technical evaluation does not amount to change in accounting policy. Accounting policy of a company may require that provision for non-moving inventories should be made. **(1 mark)**

The method of estimating the amount of provision may be changed in case a more prudent estimate can be made. Further, if the company is able to demonstrate satisfactorily that having

regard to circumstances, provision made on the basis of 'technical evaluation' provides more satisfactory results than provision based on 'number of issues' then the company can change the basis of making the provision. **(1/2 mark)**

In the given case, considering the total value of inventory, the change in the amount of required provision of non-moving/slow moving inventory from ` 4.5 lacs to ` 5.5 lacs is also not material. The following disclosure shall be made for such change in the financial statements of the company for the current year. **(1/2 mark)**

"The company has provided for non-moving/slow moving inventories on the basis of technical evaluation unlike preceding years. Had the same method been followed as in the previous year, the profit for the year and the corresponding effect on the year end net assets would have been higher by ` 1 lac." **(1 mark)**

d. As per AS 16, 'Borrowing Costs', an asset will be considered as a qualifying asset only when it takes substantial period of time to get ready for its intended use. Ordinarily, a period of twelve months is considered as substantial period of time unless a shorter or longer period can be justified on the basis of facts and circumstances of the case. In the given case, since the asset was under construction for the period of six months from its acquisition, it is considered as a non-qualifying asset in ordinary case. Accordingly, borrowing cost will not be capitalized at all. **(1 mark)**

Further, a company may opt to capitalize the exchange difference 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, or to recognised as income or as expenses in the period in which they arise **(1 mark)**

Applying the provisions of AS 11 (option to capitalize) amount to be capitalized in each of the years will be as follows: **(2 marks)**

| *Purpose* | | *Amount to be capitalised* | *Interest to be charged to profit and loss account* |
|---|---|---|---|
| | | ` | ` |
| Initial cost at the time of acquisition of fixed asset | US $ 1,25,000 x ` 61.50 | 76,87,500 | |
| On payment of 1st instalment | US $ 25,000 x ` (61.60 - 61.50) | 2,500 | |
| Interest paid with 1st instalment | (1,00,000 x 8% x 6/12)x61.60 | | 2,46,400 |
| On payment of 2nd instalment | US $ 25,000 x ` (61.80 - 61.50) | 7,500 | |
| Interest paid with 2nd | (75,000 x 8% x 6/12) x 61.80 | | 1,85,400 |

| | | | |
|---|---|---|---|
| instalment | | | |
| Exchange difference on closing balance of long term foreign currency | US $ 50,000 x ` (61.80 - 61.50) | 15,000 | |
| At the end of the year 1 | | 77,12,500 | 4,31,800 |

| | | | |
|---|---|---|---|
| On payment of 3rd instalment | US $ 25,000 x ` (61.90 - 61.80) | 2,500 | |
| Interest paid with 3rd instalment | (50,000 x 8% x 6/12) x 61.90 | | 1,23,800 |
| On payment of 4th instalment | US $ 25,000 x ` (62.10 - 61.80) | 7,500 | |
| Interest paid with 4th instalment | (25,000 x 8% x 6/12) x 62.10 | | 62,100 |
| At the end of the year 2 | | 10,000 | 1,85,900 |

The entire amount of exchange difference of ` 35,000 (15,000 + 10,000) will be capitalized to 'Fixed Asset account'. This capitalized exchange difference will be depreciated over the useful life of the asset.

e. As per the Central Excise Act, 1944, excise duty is levied upon the manufacture or production of excisable goods. According to Central Excise Rules, 2002, excise duty should be collected at the time of removal of goods from factory premises or factory warehouse. The levy of excise duty is upon the manufacture or production, the collection part of it is shifted to the stage of removal.

Guidance Note on Accounting Treatment for Excise Duty says that excise duty is a duty on manufacture or production of excisable goods in India. As explained in the Guidance Note, the liability for excise duty arises at the point of time at which the manufacture is completed. The excise duty paid or provided on finished goods should, therefore, be included in the inventory valuation. **(1 mark)**

Further, the Guidance Note states that excise duty should be considered as a manufacturing expense and like other manufacturing expenses are considered as an element of cost for the purpose of inventory valuation, excise duty should also be considered as an element of cost while valuing the inventory. **(1 mark)**

Therefore, in the given case of HS Ltd., the management's contention that excise duty is payable only on clearance of goods and hence is not a cost, is incorrect. Excise duty on the goods meant for local sales should be provided for at the rate of 12.36% on the selling price, that is, ` 100 lacs for valuation of stock. **(1 mark)**

Excise duty on goods meant for exports, should be provided for, since the liability for excise duty arises when the manufacture of the goods is completed. However, if it is assumed that all the

conditions specified in the Rule 19 of the Central Excise Rules, 2002 regarding export of excisable goods without payment of duty are fulfilled by HS Ltd., excise duty may not be provided for.

Thus, Excise duty should be considered as a manufacturing expense and like other manufacturing expenses be considered as an element of cost for inventory valuation. **(1 mark)**

***************