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SUBJECT- Accounts & Advanced Accounts

Test Code – CIM 8705

BRANCH - () (Date :)

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Topic : Investment Account, Buy Back and ESOP

NOTES: (1) WORKING NOTES SHOULD FORM PART OF ANSWERS.

(2) INTERNAL WORKING NOTES SHOULD ALSO BE CONSIDERED BY PAPER CHECKER.

(3) NEW QUESTION SHOULD BE ON NEW PAGE

Answer 1 :

Points for Consideration

- Sale Proceeds of Rights is to be credited to P&L A/c and not Investment A/c.
- Reduce the Dividend on Shares acquired on 1st September 2017 from the cost of acquisition, to arrive at the Net Cost of Shares as on 31st March 2018, since it is Pre-Acquisition Dividend.

Working Notes

Particulars	Computation	Result
1. No. of Bonus Shares	(4,000 + 1,000) ÷ 5x2	2,000 Shares
2. No. of Rights Shares eligible	(4,000 + 1,000 + 2,000) x $\frac{2}{7}$	2,000 Shares
3. No. of Rights Shares Renounced	2,000 x 1/2 = 1,000 Shares at Rs. 8 will be taken to P&L	Rs. 8,000
4. No. of Rights Shares subscribed	2,000 - 1,000 = 1,000 Shares at Rs. 10 + 25% Premium	Rs. 12,500
5. Total Dividend Received	On OB + Fresh Pure. = 5,000 Shares x Rs. 10 x 20%	Rs. 10,000
(a) Dividend on OB Shares taken to P&L	4,000 x Rs. 10 x 20%	Rs. 8,000
(b) Dividend on Shares pure, on 01.09.2017	1,000 x Rs. 10 x 20% is adjusted in Investment A/c.	Rs. 2,000
6. Cost of Shares sold on 01.02.2018	(60,000+ 14,000 + 12,500 - 2,000) x $\frac{4,000}{8,000}$	Rs. 42,250
7. Net Sale Proceeds for sale on 01.02.2018	8,000 Shares x $\frac{1}{2}$ x (Rs. 10 + Rs. 4)	Rs. 56,000
8. Profit on Sale of Shares on 01.02.2018	Net Sale Proceeds Rs. 56,000 less Cost Rs. 42,250	Rs. 13,750

(5 Marks)

Investment (Equity Shares in Akash Ltd) Account

Date	Particulars	Shares Nos.	Rs.	Date	Particulars	Shares Nos.	Rs.
01.04.17	To balance b/d at Rs. 15	4,000	60,000	20.01.18	By Bank (Dvd) (WN 5b)	-	2,000
01.09.17	To Bank at RS. 14 (10+4)	1,000	14,000	01.02.18	By Bank (Sale of Shares)(WN 7)	4,000	56,000
30.09.17	To Bonus (WN 1)	2,000	-	31.03.18	By balance c/d (Note)	4,000	42,250
31.12.17	To Bank(Rights) (WN4)	1,000	12,500				
31.03.18	To P&L- Pft tfr (WN 8)	-	13,750				
	Total	**8,000**	**1,00,250**		**Total**	**8,000**	**1,07,250**

(5 Marks)

Note: 50% of the Shareholdings are sold, for which cost is Rs. 42,250 as per WN 6. Hence, Cost of Balance 50% Shareholdings at period-end is also Rs. 42,250. Market Price = 4,500 x Rs. 13 = Rs. 58,500. Hence, Carrying Amount of current investment = Cost of Market Price, whichever is lower = Rs. 42,250.

Answer 2:

Journal entries in the books of Lucky Ltd.

Date	Particulars		Rs.	Rs.
31.3.2015	Employees compensation expense A/c	Dr.	21,30,000	
	To ESOS outstanding A/c			21,30,000
	(Being compensation expense recognized in respect of the ESOP i.e. 100 options each granted to 1,500 employees at a discount of Rs. 30 each, amortised on straight line basis over vesting years (Refer W.N.)			
	Profit and Loss A/c	Dr.	21,30,000	
	To Employees compensation expenses A/c			21,30,000
	(Being expenses transferred to profit and Loss A/c)			
31.3.2016	Employees compensation expenses A/c	Dr.	5,90,000	
	To ESOS outstanding A/c			5,90,000
	(Being compensation expense recognized in respect of the ESOP- Refer W.N.)			
	Profit and Loss A/c	Dr.	5,90,000	
	To Employees compensation expenses A/c			5,90,000
	(Being expenses transferred to profit and Loss A/c)			

31.3.2017	Employees compensation Expenses A/c	Dr.	12,40,000	
	To ESOS outstanding A/c			12,40,000
	(Being compensation expense recognized in respect of the ESOP- Refer W.N.)			
	Profit and Loss A/c	Dr.	12,40,000	
	To Employees compensation expenses A/c			12,40,000
	(Being expenses transferred to profit and Loss A/c)			
2018-19	Bank A/c (1,250 x100 x40)	Dr.	50,00,000	
	ESOS outstanding A/c [(39,60,000 x 1,25,000/ 1,32,000]	Dr.	37,50,000	
	To Equity share capital (1250 x 100 x 10)			12,50,000
	To Securities premium A/c [(1250 x 100 x (70-10)]			75,00,000
	(Being 1,25,000 options exercised at an exercise price of Rs. 40 each)			
31.3.2019	ESOS outstanding A/c	Dr.	2,10,000	
	To General Reserve A/c			2,10,000
	(Being ESOS outstanding A/c on lapse of 7,000 options at the end of exercise of option period transferred to General Reserve A/c)			

(7 Marks)

Working Note:

Statement showing compensation expense to be recognized at the end of:

Particulars	Year 1 2014-15	Year 2 2015-16	Year 3 2016-17
Number of options expected to vest*	1,42,000 options	1,36,000 options	1,32,000 options
Total compensation	Rs.42,60,000	Rs.40,80,000	Rs.39,60,000
expense accrued (70-40)			
Compensation expense of the year	42,60,000 x 1/2 = Rs. 21,30,000	40,80,000 x 2/3 = Rs. 27,20,000	Rs. 39,60,000
Compensation expense recognized previously	Nil	Rs. 21,30,000	Rs. 27,20,000
Compensation expenses to be recognized for the year	Rs. 21,30,000	Rs. 5,90,000	Rs. 12,40,000

*It is assumed that each share is of Rs. 10 each and Lucky Ltd. expects all the options to be vested after deducting actual lapses during the year.

(3 Marks)

<u>Answer 3:</u>

Determination of maximum no. of shares that can be bought back as per the Companies Act, 2013

1. Shares Outstanding Test

Particulars	(Shares)
Number of shares outstanding	1,70,000
25% of the shares outstanding	42,500

(1 Mark)

2. Resources Test: Maximum permitted limit 25% of Equity paid up capital + Free Reserves

Particulars	
Paid up capital (Rs.)	17,00,000
Free reserves (Rs.) (23,50,000 + 2,50,000 + 2,00,000)	28,00,000
Shareholders' funds (Rs.)	45,00,000
25% of Shareholders fund (Rs.)	11,25,000
Buy back price per share	Rs. 30
Number of shares that can be bought back (shares)	37,500
Actual Number of shares proposed for buy back	35,000

(2 Marks)

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Shareholder's Funds post Buy Back

	Particulars	*Rs.*
(a)	Loan funds (Rs.) (22,50,000+8,50,000+15,50,000)	46,50,000
(b)	Minimum equity to be maintained after buy back in the ratio of 2:1 (Rs.) (a/2)	23,25,000
(c)	Present equity/shareholders fund (Rs.)	45,00,000
(d)	Future equity/shareholders fund (Rs.) (see W.N.) (45,00,000 – 5,43,750)	39,56,250*
(e)	Maximum permitted buy back of Equity (Rs.) [(d) – (b)]	16,31,250
(f)	Maximum number of shares that can be bought back @ Rs. 30 per share	54,375 shares
(g)	Actual Buy Back Proposed	35,000 Shares

(4 Marks)

Summary statement determining the maximum number of shares to be bought back

Particulars	Number of shares
Shares Outstanding Test Resources Test	42,500 37,500
Debt Equity Ratio Test	54,375
Maximum number of shares that can be bought back	37,500
[least of the above]	

Company qualifies all tests for buy-back of shares and it can buy back maximum 37,500 shares on 1st April, 2018.

However, company wants to buy-back only 35,000 equity shares @ Rs. 30. Therefore, buy-back of 35,000 shares, as desired by the company is within the provisions of the Companies Act, 2013.

(2 Marks)

Working Note:

Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.

Then

(45,00,000 – x) – 23,25,000 = y (1)

$\left(\frac{y}{30} \times 10\right) = x$ Or 3x = y (2)

by solving the above equation, we get

x = Rs. 5,43,750

y = Rs.16,31,250

(1 Mark)

* As per Section 68 (2) (d) of the Companies Act 2013, the ratio of debt owed by the company should not be more than twice the capital and its free reserves after such buy-back. Further under Section 69 (1), on buy-back of shares out of free reserves a sum equal to the nominal value of the share bought back shall be transferred to Capital Redemption Reserve (CRR). As per section 69 (2) utilization of CRR is restricted to fully paying up unissued shares of the Company which are to be issued as fully paid-up bonus shares only. It means CRR is not available for distribution as dividend. Hence, CRR is not a free reserve. Therefore, for calculation of future equity i.e. share capital and free reserves, amount transferred to CRR on buy-back has to be excluded from the present equity.

Answer 4:

Books of Alpha Ltd.

Investment in 13.5% Debentures in Pergot Ltd. Account

(Interest payable on 31st March & 30th September)

Date 2017	Particulars	Nominal Rs.	Interest Rs.	Amount Rs.	Date 2017	Particulars	Nominal Rs.	Interest Rs.	Amount Rs.
May 1	To Bank	5,00,000	5,625	5,19,375	Sept.30	By Bank(6 months Int)		50,625	
Aug.1	To Bank	2,50,000	11,250	2,45,000	Oct.1	By Bank	2,00,000		2,06,000
Oct.1	To P&L A/c			2,167	Dec.31	By Balance c/d	5,50,000	18,563	5,60,542
Dec.31	To P&L A/c		52,313						
		7,50,000	**69,188**	**7,66,542**			**7,50,000**	**69,188**	**7,66,542**

Note: Cost being lower than Market Value the debentures are carried forward at Cost.

(8 Marks)

Working Notes:

1. Interest paid on Rs. 5,00,000 purchased on May 1st, 2017 for the month of April 2017, as part of purchase price: 5,00,000 x 13.5% x 1/12 = Rs. 5,625
2. Interest received on 30th Sept. 2017

   On Rs. 5,00,000 = 5,00,000 x 13.5% x ½ = Rs.33,750

   On Rs. 2,50,000 = 2,50,000 x 13.5% x ½ = Rs.16,875

   Total Rs. 50,625
3. Interest paid on Rs. 2,50,000 purchased on Aug. 1st 2017 for April 2017 to July 2017 as part of purchase price:

   2,50,000 x 13.5% x 4/12 = Rs. 11,250
4. Loss on Sale of Debentures

   Cost of acquisition

   (Rs. 5,19,375 + Rs. 2,45,000) x Rs. 2,00,000/Rs. 7,50,000 = 2,03,833

   Less: Sale Price (2,000 x 103) = 2,06,000

   Profit on sale = Rs. 2,167
5. Cost of Balance Debentures

   (Rs. 5,19,375 + Rs. 2,45,000) x Rs. 5,50,000/Rs. 7,50,000 = Rs. 5,60,542
6. Interest on Closing Debentures for period Oct.-Dec. 2017 carried forward (accrued interest)

   Rs. 5,50,000 x 13.5% x 3/12 = Rs. 18,563

(2 Marks)