SUGGESTED SOLUTION

CA FINAL NOVEMBER 2016 EXAM

FINANCIAL REPORTING

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BRANCH - (MUMBAI) (Date : 31.07.2016)

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Answer-1 :

Consolidated Balance Sheet of A Ltd. and its subsidiaries B Ltd. and C Ltd. as at 31st March 2014

	Particulars		Note No.	Rs.
1.	**Equity and Liabilities**			
	Shareholder's funds			
	a.	Share capital	1	5,00,000
	b.	Reserves and surplus	2	2,53,103
	Minority Interest (96,000+30,122)			1,26,122
	Current liabilities			
	(a)	Trade payables	3	1,08,000
	(b)	Short term provision - Proposed Dividend		50,000
	(c)	Other current liabilities	4	40,000
		Total		**10,77,225**
II.	**Assets**			
	Non-current assets			
	(a)	Fixed assets		
		Tangible assets	5	4,61,225
	(b)	Non-current investment		-
	Current Assets			
	(a)	Inventories	6	2,18,000
	(b)	Trade receivable	7	2,58,000
	(c)	Cash and Cash equivalents	8	1,40,000
		Total		**10,77,225**

(5 Marks)

Notes to Financial Statements

S.No.	Particulars	Amount.(Rs.)	Amount(Rs.)
1.	**Share capital**		
	Issued, subscribed and paid up 50,000 equity shares of Rs. 10 each fully paid up		5,00,000
2.	**Reserves and Surplus**		
	Capital reserves (W.N.3)	30,000	
	Other reserves (W.N.7)	1,31,300	
	Profit & Loss account (W.N.6)	91,803	2,53,103
3.	**Trade Payables**		
	Sundry Creditors of		
	A Ltd.	70,000	
	B Ltd.	20,000	
	C Ltd.	30,000	
		1,20,000	
	Less: Mutual Owings	(12,000)	1,08,000
4.	**Other Current liabilities**		
	Due to B Ltd. (40,000-30,000)	10,000	
	Due to C Ltd. (1,20,000-90,000)	30,000	40,000
5.	**Tangible assets**		
	A Ltd.	2,00,000	
	B Ltd.	1,50,000	
	C Ltd.	1,20,000	
		4,70,000	
	Less: Unrealised profit on equipment	-(8,775)	4,61,225
6.	**Inventories**		
	A Ltd.	1,00,000	

	B Ltd.	60,000	
	C Ltd.	60,000	
		2,20,000	
	Less: Unrealised profit	(2,000)	2,18,000
7.	**Trade Receivable**		
	A Ltd.	1,50,000	
	B Ltd.	40,000	
	C Ltd.	80,000	
		2,70,000	
	Less: Mutual Owings	(12,000)	2,58,000
8.	**Cash and Cash Equivalents**		
	A Ltd.	90,000	
	B Ltd.	20,000	
	C Ltd.	30,000	1,40,000

(8 x 0.5 = 4 Marks)

Working Notes:

1. Statement of analysis of profits of C Ltd.

	Capital Profit Rs.	Revenue Reserve Rs.	Revenue Profit Rs.
General Reserve on 1.8.13	15,000		
Profit and loss A/c on 1.8.13	25,000		
Increase in reserve		35,000	
Increase in profit			35,000
	40,000	35,000	35,000
Less: Minority Interest (10%)	(4,000)	(3,500)	(3,500)
	36,000	31,500	31,500
Share of A Ltd. (30%)	12,000	10,500	10,500
Share of B. Ltd. (60%)	24,000	21,000	21,000

2. Statement of analysis of profits of B Ltd.

	Capital Profit Rs.	Revenue Reserve Rs.	Revenue Profit Rs.
General Reserve on 1.8.13	30,000		
Profit and loss A/c on 1.8.13	50,000		
Increase in reserve		30,000	
Increase in profit			30,000
	80,000	30,000	30,000
Add: Share in C Ltd. (direct approach)	-	21,000	21,000
	80,000	51,000	51,000
Less: Minority interest (20%)	(16,000)	(10,200)	(10,200)
Share of A Ltd.	64,000	40,800	40,800

3. Statement of cost of control

	Rs.	Rs.	Rs.
Investment in B Ltd.			2,50,000
Investment in C Ltd.		(80,000 + 1,60,000)	2,40,000
			4,90,000
Less: Paid up value ofinvestments			

In B Ltd.	2,40,000		
In C Ltd.	1,80,000	4,20,000	
Capital Profit In B Ltd.	64,000		
In C Ltd. (12.000 + 24,000)	36,000	1,00,000	(5,20,000)
Capital reserve			30,000

4. Statement of Minority Interest

	B Ltd. (20%)Rs.	CLtd.(10%)Rs.
Share capital	60,000	20,000
Capital profit	16,000	4,000
Revenue reserve	10,200	3,500
Revenue profit	10,200	3,500
Total	96,400	31,000
Less: Unrealised profit on Stock {20% of (10,000/125 x 25)}	(400)	
Unrealised profit on Machinery (10% of 8,775)		(878)
	96,000	30,122

5. Statement showing unrealised profit on equipment sale

	Rs.
Cost	27,000
Profit	9,000
Selling price	36,000
Unrealized profit = Total unrealised Profit - Depreciation thereon = [9,000 - (9,000 x 10% x 3/12)]	8,775

6. Statement showing Consolidated Profit and Loss Account

Item	Rs.
A Ltd.	1,00,000
Less : Proposed dividend	(50,000)
	50,000
Share in B Ltd.	40,800
Share in C Ltd.	10,500
	1,01,300
Less : Unrealised profit on machinery (90% of 8,775)	(7,897)
	93,403
Less : Unrealised profit on stock (80% of (10,000/125 x 25)]	(1,600)
	91,803

7. Statement showing consolidated reserves

Item	Rs.
A Ltd.	80,000
Share in B Ltd.	40,800
Share in C Ltd.	10,500
	1,31,300

(7 x 1 = 7 Marks)

Answer-2 :

Consolidated Balance Sheet as on 31.3.2015

		Particulars	**Note No.**	**Rs.**
I.	Equity and Liabilities			
	(1)	Shareholder's Funds		
		(a) Share Capital	1.	1,00,000
		(b) Reserves and Surplus	2	1,20,700
	(2)	Minority Interest (W.N.)		20,000
	(3)	Current Liabilities		
		(a) Trade Receivables	3	23,000
		(b) Short Term Provisions	4	12,500
		(c) Other Current Liabilities	5	10,000
		Total		2,86,200
II.	Assets			
	(1)	Non-current assets		
		(a) Fixed Assets	6	2,15,500
		(b) Non current investment	7	17,200
	(2)	Current Assets	8	53,500
		Total		2,86,200

(6 Marks)

			Rs.	**Rs.**
1.	Share Capital			
		Called up equity shares of Rs. 1 each		1,00,000
2.	Reserves and Surplus			
		General Reserve	40,000	
		Profit and Loss A/c (W.N.3)	80,700	1,20,700
3.	Trade Receivables .			
		Holding & Subsidiary	20,000	
		Joint Venture (50%)	3,000	23,000
4.	Short term provisions			
		Provisions for Tax		
		Holding & Subsidiary	9,000	
		Joint Venture (50%)	3,500	12,500
5.	Other Current Liabilities			
		Proposed Dividend		
		Holding & Subsidiary	10,000	
		Joint Venture (50%)	2,000	
			12,000	
		Less: Mutual owings	(2,000)	10,000
6.	Fixed Assets			
		Holding & Subsidiary	1,95,000	
		Joint Venture (50%)	20,500	2,15,500
7.	Non-current investment			
		Investment in Associate (W.N.4)		17,200
8.	Current Asset			
		Holding & Subsidiary	21,000	
		Joint Venture	34,500	
			55,500	
		Less: Mutual Owings (Dividend Receivable from Joint Venture included in Current Asset)	(2,000)	53,500

(8 x 0.5 = 4 Marks)

Working Notes:

1. Analysis of Profit & Loss of Associate / Joint Venture

	Pre-acquisition Rs.	Post-acquisition Rs.
Profit as on 31.3.2015 27,000	16,000	11,000
Share of Associate company (20%)	3,200	2,200
Analysis of Profit and Loss of Joint Venture	Nil	83,000
Share of Joint Venture (50%)		41,500

(2 Marks)

2. Calculation of Goodwill / Capital Reserve

		Associate Rs.		Joint Venture Rs.
Investment		15,000		5,000
Less: Nominal Value	8,000		5,000	
Capital Profit	3,200	(11,200)	-	(5,000)
Goodwill		3,800		Nil

(1 Mark)

3. Calculation of Consolidated Profit and Loss Account

	Rs.
Profit and Loss Account of Holding & Subsidiary	37,000
Add: Share of Associate	2,200
Joint Venture	41,500
	80,700

(1 Mark)

4. Calculation of Investment in Associate

	Rs.
Goodwill (VV.N.2)	3,800
Net worth	11,200
Cost	15,000
Add: Share of Revenue Profit	2,200
	17,200

(1 Mark)

Notes:

1. Dividend income is booked without the receipt. This meant that income was on receivable stage appearing on the asset side.
2. JCE was formed, by the Venturers two years ago. All the reserves as on the date of consolidation are to be treated as revenue.
3. Out of Rs. 17,000 existed at the time of acquisition, only Rs. 16,000 (Opening Balance) is continuing in the books of the associate. Therefore, Rs. 16,000 is taken as capital profit assuming that it is a part of that Rs. 17,000 existed at the time of acquisition.

(1 Mark)

Answer-3 :

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1. Calculation of Capital employed (CE) Rs. in lakhs

	As on 31.3.14	As on 31.3.15
Replacement Cost of Fixed Assets	1,100.00	1,250.00
Trade Investment (50%)	125.00	125.00
Current cost of inventory		
$130 + 130 \times \frac{120}{100}$	286.00	
$150 + 150 \times \frac{120}{100}$		330.00
Trade Receivables	170.00	111.40
Cash at Bank	46.00	45.00
Total (A)	**1,727.00**	**1,861.40**
Less: Outside Liabilities		
18% term loan	180.00	165.00
Trade Payables	35.00	48.60
Provision for tax	11.00	13.00
Total (B)	**226.00**	**226.60**
Capital employed (A-B)	1501.00	1634.80

Average Capital employed at current value

$$= \frac{\text{Opening Capital employed + closing capital employed}}{2}$$

$$= \frac{1501 + 1634.80}{2} = 1567.90 \text{ lakhs}$$

(4 Marks)

2. Future Maintainable Profit

		Rs. in lakhs
Increase in General Reserve	25	
Increase in Profit and Loss Account	30	
Proposed Dividends	125	
Profit After Tax 180		
Pre-tax Profit = $\frac{180}{1-0.5}$		360
Less: Non-Trading investment income (10% of Rs. 125)	12.50	
Subsidy	60.00	
Exchange Loss on Trade Payables [0.6 lakhs x (39-33)]	3.60	
Additional Depreciation on increase in value of Fixed Assets (current year) $\left(1{,}250\text{-}650\text{-}600\text{x}\frac{5}{100}\right)$ i.e.,	30.00	(106.10)
		253.90
Add: Exchange Gain on trade receivables [0.35 lakhs x (39-35)]	1.40	
Research and development expenses written off	125.00	
Inventory Adjustment (30-26)	4.00	130.40
		384.30
Add: Expected increase of 10%		38.43
Future Maintainable Profit before Tax		422.73
Less: Tax @ 40% (40% of Rs. 422.73)		(169.09)
Future Maintainable Profit		253.64

(4 Marks)

3. Valuation of Goodwill Rs. in lakhs

(i) According to Capitalisation of Future Maintainable Profit Method

Capitalised value of Future Maintainable Profit	
$= \frac{253.64}{15} x100$	1,690.93
Less: Average capital employed	<u>1,567.90</u>
Value of Goodwill	<u>123.03</u>
Or	
(ii) According to Capitalization of Super Profit Method	
Future Maintainable Profit	253.64
Less: Normal Profit @ 15% on average capital employed	
(1,567.90 x 15%)	<u>235.19</u>
Super Profit	<u>18.45</u>
Capitalised value of super profit $\frac{18.45}{15}$ x 100 i.e. Goodwill	123.00

(4 Marks)

Goodwill exists; hence director's fear is not valid.

Leverage Effect on Goodwill

		Rs. in lakhs
Future Maintainable Profit on equity fund		253.64
Future Maintainable Profit on Long-term Trading Capital employed		
Future Maintainable Profit After Tax	253.64	
Add: Interest on Long-term Loan (Term Loan)		
(After considering Tax) 165 x 18% = 29.7 x $\frac{(100-40)}{100}$	<u>17.82</u>	271.46
Average capital employed (Equity approach)		1,567.90
Add: 18% Term Loan (180+165)/2		<u>172.50</u>
Average capital employed (Long-term Fund approach)		<u>1,740.40</u>
Value of Goodwill		

(3 Marks)

(A)	Equity Approach	
	Capitalised value of Future Maintainable Profit = $\frac{253.64}{15} x100=$	1,690.93
	Less: Average capital employed	<u>(1,567.90)</u>
	Value of Goodwill	<u>123.03</u>
(B)	Long-Term Fund Approach	
	Capitalized value of Future Maintainable Profit = $\frac{271.46}{12} x100$	2262.17
	Less: Average capital employed	<u>(1,740.40)</u>
	Value of Goodwill	521.77

Comments on Leverage effect of Goodwill: Adverse Leverage effect on goodwill is 398.74lakhs (i.e., Rs. 521.77 – 123.03). In other words, Leverage Ratio of Popular Ltd. is low for whichits goodwill value has been reduced when calculated with reference to equity fund ascompared to the value arrived at with reference to long term fund.

Working Notes:

			Rs. in lakhs
(1)	Inventory adjustment		
	(i)	Excess current cost of closing inventory over its Historical cost (330 – 300)	30.00

	(ii)	Excess current cost of opening inventory over its Historical cost (286-260)	<u>26.00</u>
	(iii)	Difference [(i– ii)]	<u>4.00</u>
(2)	Trade Receivables' adjustment		
	(i)	Value of foreign exchange Trade Receivables at the closing exchange rate ($35,000 x 39)	13.65
	(ii)	Value of foreign exchange Trade Receivables at the original exchange rate ($35,000 x 35)	<u>12.25</u>
	(iii)	Difference [(i) – (ii)]	<u>1.40</u>
(3)	Trade Payables' adjustment		
	(i)	Value of foreign exchange Trade Payables at the closing exchange rate ($ 60,000 x 39)	23.40
	(ii)	Value of foreign exchange Trade Payables at the original exchange rate($60,000 x 33)	<u>19.80</u>
	(iii)	Difference [(i) – (ii)]	3.60

(3 x 1 = 3 Marks)