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(Question Book)

FOR CA. FINAL OLD SYLLABUS (BOOSTER)

By

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Important Note:

Join Telegram group of Jai Sir to ask you quries or doubts – “Jai Chawla Sir Doubts & Discussion”

COURSE CONTENT:

Total No. of Questions = 193

VALUATION

Valuation of Goodwill

Trend Average Method

Q1.

B K Ltd. gives the following profit figures for the last five years:

Year	Profits ('000)
1996	37,20
1997	42,00
1998	47,50
1999	53,50
2000	57,20

Since past profits show increasing trend, time series trend may be used to determine future maintainable profit. Applying Linear trend equation three to five years profit may be predicated and average of such future profits may be taken as future maintainable profit. Calculate FMP for next three years.

Ans. **(Study Material)**

Year	X	Y	XY	X2
1996	- 2	37,20	- 74,40	4
1997	- 1	42,00	- 42,00	1
1998	0	47,50	0	0
1999	1	53,50	53,50	1
2000	2	57,20	114,40	4
	0	237,40	51,50	10

$$A = \frac{Y}{n} = \frac{237{,}40}{5} = 47{,}48$$

B = $\frac{XY}{XY2} = \frac{51{,}50}{10} = 5{,}15$

Trend Equation given by:

Y = 4748 + 515 X

Ans.: FMP T6293, 6808, 7323.

Goodwill and leverage effect

Q2.

The following is the extract from the Balance Sheets of Popular Ltd.:

Liabilities	As at 31.3.2016 Rs in lakhs	As at 31.3.2017 Rs in lakhs	Assets	As at 31.3.2016 Rs in lakhs	As at 31.3.2017 Rs in lakhs
Share capital	500	500	Fixed assets	550	650
General reserve	400	425	10% Investment	250	250
Profit and Loss account	60	90	Inventory	260	300
18% Term loan	180	165	Trade Receivables	170	110
Trade Payables	35	45	Cash at bank	46	45
Provision for tax	11	13	Fictitious assets	10	8
Dividend payable	100	125			
	1,286	1,363		1,286	1,363

Additional information:

(i) Replacement values of fixed assets were Rs 1,100 lakhs on 31.3.16 and Rs 1,250 lakhs on 31.3.2017 respectively.

(ii) Rate of depreciation adopted on fixed assets was 5% p.a.

(iii) 50% of the inventory is to be valued at 120% of its book value.

(iv) 50% of investments were trade investments.

(v) Trade Receivables on 31st March, 2017 included foreign trade receivables of $ 35,000 recorded in the books at Rs 35 per U.S. Dollar. The closing exchange rate was $ 1= Rs 39.

(vi) Trade Payables on 31st March, 2017 included foreign trade payables of $ 60,000 recorded in the books at $ 1 = Rs 33. The closing exchange rate was $ 1 = Rs 39.

(vii) Profits for the year 2016-2017 included Rs 60 lakhs of government subsidy which was not likely to recur.

(viii) Rs 125 lakhs of Research and Development expenditure was written off to the Profit and Loss Account in the current year. This expenditure was not likely to recur.

(ix) Future maintainable profits (pre-tax) are likely to be higher by 10%.

(x) Tax rate during 2016-2017 was 50%, effective future tax rate will be 40%.

(xi) Normal rate of return expected is 15%.

One of the directors of the company Arvind, fears that the company does not enjoy goodwill in the prevalent market circumstances.

Critically examine this and establish whether Popular Ltd. has or has not any goodwill.

If your answers were positive on the existence of goodwill, show the leverage effect it has on the company's result.

Industry average return was 12% on long-term funds and 15% on equity funds.

Answer

1. Calculation of Capital employed (CE)	**Rs in lakhs**	
	As on 31.3.16	**As on 31.3.17**
Replacement Cost of Fixed Assets	1,100.00	1,250.00
Trade Investment (50%)	125.00	125.00
Current cost of inventory		
130 + 130 × 120 ÷ 100	286.00	
150 + 150 × 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
= Opening capital employed + closing capital employed / 2
=lakhs 1501 + 1634.80 /2 = 1567.90

2. Future Maintainable Profit	**Rs in lakhs**	
Increase in General Reserve	25	
Increase in Profit and Loss Account	30	
Dividends	125	
Profit After Tax	180	
Pre-tax Profit = 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 × (39-33)]	3.60	
Additional Depreciation on increase in value of Fixed Assets (current year) (1250-650)×5÷100 i.e.,	30.00	(106.10)
		253.90
Add: Exchange Gain on trade receivables [0.35 lakhs × (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
3. Valuation of Goodwill	Rs in lakhs	
(i) According to Capitalisation of Future Maintainable Profit Method Capitalised value of Future Maintainable		1,690.93

Profit = 253.64×100÷15		
Less: Closing capital employed		1,634.80
Value of Goodwill		56.13
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 ×15%)		235.19
Super Profit		18.45
Capitalised value of super profit 18.45×100÷15 i.e. Goodwill		123.00

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× 18% = 29.7 × (100 – 40) ÷ 100 = 17.82 Add: 10% Increase of FMP = 1.78	19.602	273.242
Average capital employed (Equity approach)		1,567.90
Add: 18% Term Loan (180+165)/2		172.50
Average capital employed (Long-term Fund approach)		1,740.40
Value of Goodwill		
(A) Equity Approach		
Capitalised value of Future Maintainable Profit = = 273.242×100÷15		1,690.93
Less: Average capital employed		(1,567.90)
Value of Goodwill		123.03
(B) Long-Term Fund Approach		
Capitalized value of Future Maintainable Profit = 271.46×100÷12		2277.00
Less: Average capital employed		(1,740.40)
Value of Goodwill		536.62

Comments on Leverage effect of Goodwill: Adverse Leverage effect on goodwill is 413.59 lakhs (i.e., Rs 536.62 – 123.03). In other words, Leverage Ratio of Popular Ltd. is low for which its goodwill value has been reduced when calculated with reference to equity fund as compared 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)	26.00

	(iii)	Difference [(i- ii)]	4.00
(2)	Trade Receivables' adjustment		
	(i)	Value of foreign exchange Trade Receivables at the closing exchange rate ($35,000×39)	13.65
	ii)	Value of foreign exchange Trade Receivables at the original exchange rate ($35,000×35)	12.25
	(iii)	Difference [(i) – (ii)]	1.40
(3)	Trade Payables' adjustment		
	(i)	Value of foreign exchange Trade Payables at the closing exchange rate ($ 60,000×39)	23.40
	(ii)	Value of foreign exchange Trade Payables at the original exchange rate($60,000×33)	19.80
	(iii)	Difference [(i) – (ii)]	3.60

Q3.

The Balance Sheet of D Ltd. on 31st March, 2017 is as under:

Liabilities	Rs	Assets	Rs
1,25,000 shares of Rs 100 each fully paid up	1,25,00,000	Goodwill	10,00,000
		Building	80,00,000
Bank overdraft	46,50,000	Machinery	70,00,000
Trade Payables	52,75,000	Inventory	80,00,000
Provision for taxation	12,75,000	Trade receivables (all considered good)	50,00,000
Profit and loss account	53,00,000		
	2,90,00,000		**2,90,00,000**

In 2000, when the company started its activities the paid up capital was the same. The Profit/Loss for the last five years is as follows:
2012-2013: Loss (13,75,000), 2013-2014: Profit Rs 24,55,000, 2014-2015: Profit Rs 29,25,000, 2015-2016: Profit Rs 36,25,000, 2016-2017: Profit Rs 42,50,000.
Income-tax rate so far has been 40% and the above profits have been arrived at on the basis of such tax rate. From 2016-2017, the rate of income-tax should be taken at 45%. 10% dividend in 2013-2014, 2014-2015 and 15% dividend in 2015-2016 and 2016-2017 has been paid. Market price of this share on 31st March, 2017 is Rs 125. With effect from 1st April, 2017, the Managing Directors remuneration will be Rs 20,00,000 instead of Rs 15,00,000. The company has secured a contract from which it can earn an additional Rs 10,00,000 per annum for the next five years.
Calculate the value of goodwill at 3 years purchase of super profit. (For calculation of future maintainable profits weighted average is to be taken).

Answer

(i) **Future Maintainable Profit**

Year	Profit (P) Rs	Weight (W)	Products (PW) Rs
2013-2014	24,55,000	1	24,55,000
2014-2015	29,25,000	2	58,50,000

2015-2016	36,25,000	3	1,08,75,000
2016-2017	42,50,000	4	1,70,00,000
	10		3,61,80,000
Weighted average annual profit (after tax)= 3,61,80,00010/10 = Rs 36,18,000			

Weighted average annual profit before tax is 36,18,000×100/60	60,30,000
Less: Increase in Managing Director's remuneration	(5,00,000)
	55,30,000
Add: Contract advantage	10,00,000
	65,30,000
Less: Tax @ 45%	(29,38,500)
Future maintainable profit	35,91,500

(ii) **Average Capital Employed**

	Rs.	
Assets		
Building		80,00,000
Machinery		70,00,000
Inventory		80,00,000
Trade Receivables		50,00,000
		2,80,00,000
Liabilities		
Bank Overdraft	46,50,000	
Trade Payables	52,75,000	
Provision for taxation	12,75,000	
Additional provision for taxation**	3,54,167	(1,15,54,167)
Capital employed at the end of the year		1,64,45,833
Less: ½ profit after tax for the year [(42,50,000-3,54,167)/2]		(19,47,917)
Average capital employed		**1,44,97,916**

- ❖ Loss amounting Rs 13,75,000 for the year 2012-2013 has not been considered in calculation of weighted average profit assuming that the loss was due to abnormal conditions.
- ❖ Additional provision for taxation 5% of Rs 70,83,333 (Rs 42,50,000/60%) has also been created assuming that the necessary rectification is being done in the financial statements for the year 2016-2017.

(iii) **Normal Profit**

Average dividend for the last four years

= 12.5 = 10+10+15+15 / 4

Market Price of share =Rs 125

Normal rate of return= 12.5/125×100=10%

Normal profit 10% of Rs 1,44,97,916 Rs 14,49,792

(iv) **Valuation of Goodwill**

	Rs
Future maintainable profit Less: Normal profit	35,91,500 (14,49,792)
Super Profit	21,41,708

Goodwill at 3 years' purchase of super profits (Rs 21,41,708 x 3)	64,25,124

Q4. The following is the Balance Sheet (as at 31st December, 2006) of Sun Ltd:

Equity & Liabilities	**Rs.**
Shareholders Fund	
80,000 Equity shares of Rs.10 each fully paid up	800,000
50,000 Equity shares of Rs.10 each Rs.8 paid up	400,000
36,000 Equity shares of Rs.5 each fully paid up	180,000
30,000. Equity shares of Rs.5 each Rs. 4 paid-up	120,000
3,000 10% Preference shares of Rs.100 each fully paid	300,000
General reserve	140,000
Profit and Loss account	210,000
Preliminary Expenses	- 10,000
Non-Current Liabilities	
Secured Loan: 12% debenture	200,000
Unsecured loan: 15% term loan	150,000
Deposits	100,000
Current Liabilities	
Bank Loan	50,000
Creditors	150,000
Outstanding expenses	20,000
Provision for tax	200,000
Proposed Dividend:	
Equity	150,000
Preference	30,000
	3,190,000
Assets	**Rs.**
Non-Current Assets	
Goodwill	1,00,000
Plant and Machinery	8,00,000
Land and Building	10,00,000
Furniture and Fixtures	1,00,000
Vehicles	2,00,000
Investments	3,00,000
Current Assets	
Stock	2,10,000
Debtors	1,95,000
Prepaid Expenses	40,000
Advance	45,000
Cash and Bank balance	2,00,000

31,90,000

Additional Information:

(1) In 2004 a new machinery costing Rs 50,000 was purchased, but wrongly charged to revenue (no rectification has yet been made for the same).

(2) Stock is overvalued by Rs 10,000 in 2005. Debtors are to be reduced by Rs 5,000 in 2006, some old furniture (Book value Rs 10,000) was disposed of for Rs 6,000.

(3) Fixed assets are worth 5 percent more than their actual book value. Depreciation on appreciated value of Fixed assets except machinery is not to be considered for valuation of goodwill.

(4) Of the investment 20 per cent is trading and the balance is non-trading. All trade investments are to be valued at 20 per cent below cost. Trade investment was purchased on 1st January, 2006. 50 percent of the nontrade investments were acquired on 1st January, 2005 and the rest on 1st January, 2004. A uniform rate of dividend of 10 percent is earned on all investments.

(5) Expected increase in expenditure without commensurate increase in selling price is Rs.20,000.

(6) Research and Development expenses anticipated in future Rs.30,000 per annum.

(7) In a similar business a normal return on capital employed is 10%.

(8) Profit (after tax) are as follows:

In 2004 - Rs. 2,10,000, in 2005 – Rs. 1,90,000 and in 2006 - Rs.2,00,000,

(9) Current income tax rate is 50%, expected income tax rate will be 40%.

From the above, ascertain the ex-dividend and cum-dividend intrinsic value for different categories of Equity shares. For this purpose goodwill may be taken as 3 years purchase of super profits, Depreciation is charged on machinery @ 10% on reducing system.

(Answer: FMP-202581; Goodwill – 5557; CCE – 2106273; ACE – 2007286; IV (Ex) – 1.23 Per Rupee) (May 2007; 16 Marks)

Q5. Find out Leverage effect on Goodwill from the following information:

(i)	Average capital employed (Equity Approach)	Rs. 11,50,000
(ii)	FMP on equity fund (After Tax)	Rs. 1,80,000
(iii)	10% Long Term Loan	Rs. 4,50,000
(iv)	Tax Rate	40%
(v)	**Normal Rate of return**	
	On equity capital employed	15%
	On Long term capital employed	12%

(May18 & Nov15, 6 Marks)

Solution:

Determination of leverage effect on goodwill

		Rs.	
A	Profit available for equity fund after tax		1,80,000
B	Profit (as per long term fund approach)		
	Profit for equity fund	1,80,000	
	Add: Interest on long term loan (net of tax 4,50,000×{10%×(1-0.4)]	27,000	2,07,000
C	Capital employed (by Equity approach)		11,50,000
D	Capital employed as per long term fund approach		
	Capital employed (by Equity approach)	11,50,000	
	Add: 10% long term loan	4,50,000	16,00,000
E	Value of goodwill		
	(a) By equity approach		
	Capitalized value of profit as per equity approach (1,80,000/15×100)		12,00,000
	Less: capital employed as per equity approach		(11,50,000)
	value of Goodwill		50,000
	(b) By long term fund approach		
	Capitalized value of profit as per long-term fund approach (2,07,000/12×100)		17,25,000
	Less: capital employed as per long term fund approach		16,00,000
	Value of Goodwill		1,25,000

Leverage effect on Goodwill:
Adverse leverage effect on goodwill is Rs 75,000 (i.e. Rs 1,25,000 – Rs 50,000)
In other words, leverage ratio is low for which its goodwill value has been reduced when calculated with reference to equity fund as compared to value arrived at with reference to long term fund.

Q6: The summarised Balance Sheet of Domestic Ltd. as on 31st March, 2017 is as under:

Liabilities	(Rs in lakhs)	Assets	(Rs in lakhs)
Equity shares of Rs 10 each	3,000	Patent	744
		Premises and Land at cost	400
Reserves (including provision for taxation of Rs 300 lakhs)	1,000	Plant and Machinery	3,000
5% Debentures	2,000	Motor vehicles (purchased on 1.10.16)	40
Secured loans	200	Raw materials at cost	920
Trade Payables	300	Work-in-progress at cost	130
Profit & Loss A/c:		Finished goods at cost	180
Balance from previous year	32	Trade Receivables	400

Profit for the year (after taxation)	1,100	Investment (meant for replacement of plant and machinery)	1,600
		Cash at bank and cash in hand	192
		Discount on debentures	10
		Underwriting commission	16
	7,632		**7,632**

1. The resale value of premises and land is Rs 1,200 lakhs and that of plant and machinery is Rs 2,400 lakhs. Patent appearing in the balance sheet is of no use and should be ignored for the valuation purpose.
2. Depreciation @ 20% is applicable to motor vehicles.
3. Applicable depreciation on premises and land is 2% and that on plant and machinery is 10%.
4. Market value of the investments is Rs 1,500 lakhs.
5. 10% of trade receivables are bad.
6. The company also revealed that the depreciation was not charged to Profit and Loss account and the provision for taxation already made is sufficient.
7. In a similar company the market value of equity shares of the same denomination is Rs 25 per share and in such company dividend is consistently paid during last 5 years @ 25%. Contrary to this, Domestic Ltd. is having a marked upward or downward trend in the case of dividend payment.
8. In 2011-2012 and in 2012-2013, the normal business was hampered. The profit earned during 2011-2012 is Rs 67 lakhs, but during 2012-2013 the company incurred a loss of Rs 1,305 lakhs.

   Past 3 years' profits of the company were as under:

2013-2014	Rs 469 lakhs
2014-2015	Rs 546 lakhs
2015-2016	Rs 405 lakhs

The unusual negative profitability of the company during 2012-2013 was due to the lock out in the major manufacturing unit of the company which happened in the beginning of the second quarter of the year 2011-2012 and continued till the last quarter of 2012-2013.

Value the goodwill of the company on the basis of 4 years' purchase of the super profit.

Answer

1. Rectification of current year's profit i.e. 2016-2017

Profit after Tax = Rs 1,100 lakhs

Provision for taxation = Rs 300 lakhs

Profit before Tax = PAT + Provision for taxation

= Rs 1,100 lakhs + Rs 300 lakhs = Rs 1,400 lakhs

Rate of tax = $\frac{\text{Provision for tax}}{\text{Profit before tax}} \times 100$ = 300÷1400×100 = 21.43% (approx.)

	Rs in lakhs
Profit for the year after tax	1,100
Less: Depreciation net of tax on motor vehicles (Rs 40 lakhs x 20% x 6/12) x (100-21.43)%	(3.1428)
Depreciation net of tax on Premises and Land (Rs 400 lakhs x 2%) x (100-21.43)%	(6.2856)

Depreciation net of tax on Plant and Machinery (Rs 3,000 lakhs x 10%) x (100-21.43)%	(235.71)
Provision for doubtful receivables net of tax (Rs 400 lakh x 10%) x (100-21.43)%	(31.428)
Rectified profit of 2016-2017	823.43

2. **Calculation of Capital Employed**

	(Rs in lakhs)	(Rs in lakhs)
Premises and land		1,200
Plant and machinery		2,400
Motor vehicles (book value less depreciation for ½ year)		36
Raw materials		920
Work-in-progress		130
Finished goods		180
Trade Receivables (400 x 90%)		360
Investments (market value)		1,500
Cash at bank and in hand		192
		6,918
Less: Liabilities:		
Provision for taxation	300	
5% Debentures	2,000	
Secured loans	200	
Trade Payables	300	(2,800)
Total capital employed on 31.3.2017		4,118
Less: Half of current year's rectified profit (823.43 x 1/2)		(411.72)
Average Capital Employed		3,706.28

3. **Calculation of Future Maintainable Profits**

	(Rs in lakhs)			
	2013-14	2014-15	2015-16	2016-17
Profit after tax	469	546	405	823.43
Less: Depreciation net of tax on Premises and Land (Rs 400 lakhs x 2%) x (100-21.43)%	(6.29)	(6.29)	(6.29)	
Depreciation net of tax on Plant and Machinery (Rs 3,000 lakhs x 10%) x (100-21.43)%	(235.71)	(235.71)	(235.71)	
Adjusted Profit	227	304	163	823.43
Average adjusted profit (227+304+163+823.43)/4				379.36
Less: Excess depreciation (net of tax) due to upward revaluation of premises and land [(1,200-400) x 2%] x (100 - 21.43)%				(12.57)
Depreciation on motor vehicle (net of tax) for remaining six months (in future depreciation on motor vehicle will be charged for full year) (Rs 40 lakhs x 20% x 6/12) x (100-21.43)%				(3.14)
Add: Short depreciation (net of tax) due to downward revaluation of plant and machinery [(3,000 - 2,400) x 10%] x (100 - 21.43)%				47.14
Future Maintainable Profit				410.79

4. **Calculation of General Expectation**
   Similar Company pays Rs 2.5 as dividend (25%) for each share of Rs 10.
   Market value of an equity share of the same denomination is Rs 25 which fetches dividend of 25%.
   Therefore, share of Rs 10 (Face value of shares of Domestic Ltd.) is expected to fetch (2.5/25) x 100 = 10% return.
   A nominal rate of 1% or 2% may be added as Risk premium, to the normal rate of return for uncertainty associated with dividend distribution.
   Since, Domestic Ltd. is not having a stable record in payment of dividend, therefore, the expectation from it may be assumed to be slightly higher, say 11% instead of 10%.
5. **Calculation of value of goodwill of Domestic Ltd.**

	(Rs in lakhs)
Future maintainable profit	410.79
Less: Normal profit i.e. 11% of average capital employed (3,706.28x11%)	(407.69)
Super Profit	3.1
Goodwill at 4 years' purchase of Super Profit (3.1 × 4)	12.4

Notes:

(1) It is assumed that 'Provision for Taxation' included in reserves is made in the current year only.

(2) It is assumed that plant and machinery given in the balance sheet is at cost.

(3) It is assumed that depreciation on 'Premises and Land' and 'Plant and Machinery' is charged on Straight Line method.

(4) It is assumed that resale value of 'Premises and Land' and 'Plant and Machinery' given in the question is for depreciated value of respective assets. Therefore, no adjustment for depreciation has been made in such assets while calculating capital employed.

(5) It is assumed that profit for the year 2013-2014, 2014-2015 and 2015-2016 given in the questions is after tax and no depreciation was charged in the earlier years also.

(6) Average Capital employed has been taken for valuation of goodwill.

(7) While considering past profits for determining average profit, the years 2011-2012 and 2012-2013 have been left out, as during these years normal business was hampered.

Valuation of Shares

INTRINSIC VALUE METHOD

Q7. The Balance Sheet of Mulyan Ltd. as on 31st December, 2016 is as follows:

Liabilities	Rs	Rs	Assets	Rs
Share Capital:				
Equity shares of Rs 10 each less, calls in arrear (Rs 2 for final call)	5,00,000 10,000	4,90,000	Fixed Assets: Machinery Factory shed	 2,30,000 3,00,000
8% Preference shares of Rs 10 each fully paid		2,00,000	Vehicles Furniture	60,000 25,000
Reserve and Surplus:			Investments	1,00,000
General Reserve		1,50,000	Current Assets:	
Profit & Loss A/c		1,40,000	Inventory	2,10,000
Current Liabilities:			Trade Receivables	3,50,000
Trade Payables		2,70,000	Cash at bank	75,000
Bank Loan		1,00,000		
		13,50,000		13,50,000

Additional Information:

(i) Fixed assets are worth 20% above their actual book value, depreciation on appreciated portion of fixed assets is to be ignored for valuation of goodwill.

(ii) Of the investments, 80%, is non-trading and the Balance is trading. All trade investments are to be valued at 20% below cost. A uniform rate of dividend of 10% is earned on all investments.

(iii) For the purpose of valuation of shares, Goodwill is to be considered on the basis of 6 year's purchase of the super profits based on **simple average profit** of the last 3 years. Profits after tax @ 50%, are as follows:

Year	Rs
2014	1,90,000
2015	2,00,000
2016	2,50,000

(iv) In a similar business, return on capital employed is 20%. In 2014, a new furniture costing Rs 10,000 was purchased but wrongly charged to revenue. No effect has yet been given for rectifying the same. Depreciation is charged on furniture @ 10% p.a. (Diminishing Balance Method).

Find out the value of each fully paid and partly paid equity share.

Answer

Valuation of an equity share-

Value of an equity share = Net assets available to equity shareholders (W.N. 6) / Number of equity shares

= 9,47,746/50,000 = Rs. 18.95492

Value of a Rs 10 fully paid up share = Rs 18.95492 per share

Value of Rs 10 share, Rs 8 per share paid up = (Rs 18.95492 – Rs 2) per share
= Rs. 16.95492 per share

Working Notes:

1. **Capital employed**

	Rs	
Fixed Assets:		
Machinery	2,30,000	
Factory shed	3,00,000	
Furniture (Rs 25,000 + Rs 7,290)	32,290	
Vehicles	60,000	
	6,22,290	
Add: 20% increase	1,24,458	
	7,46,748	
Trade investments (Rs 1,00,000 × 20% ×80%)	16,000	
Inventory in trade	2,10,000	
Trade Receivables	3,50,000	
Cash at bank	75,000	13,97,748
Less: Outside liabilities:		
Bank Loan	1,00,000	
Trade Payables	2,70,000	(3,70,000)
Capital employed		10,27,748

2. **Calculation of average adjusted profit**

	2014 Rs	2015 Rs	2016 Rs
Profit after tax	1,90,000	2,00,000	2,50,000
Add: Tax @ 50%	1,90,000	2,00,000	2,50,000
Profit before tax	3,80,000	4,00,000	5,00,000
Add: Capital expenditure on furniture	10,000		
Less: Depreciation on furniture*	(1,000)	(900)	(810)
Income from non-trade investments	(8,000)	(8,000)	(8,000)
	3,81,000	3,91,100	4,91,190
Less: Tax @ 50%	(1,90,500)	(1,95,550)	(2,45,595)
Adjusted profit	1,90,500	1,95,550	2,45,595

	Rs
Total adjusted profit for three years (1,90,500 + 1,95,550 + 2,45,595)	6,31,645
Adjusted Average profit (Rs 6,31,645/3)	2,10,548

3. **Normal Profit:** 20% on capital employed i.e. 20% on Rs 10,27,748 = Rs 2,05,550

* Furniture is assumed to be purchased at the beginning of the year and therefore, depreciation is charged for the whole year in 2014.

4. **Super profit:** Average Adjusted profit – Normal profit
= Rs 2,10,548 – Rs 2,05,550 = Rs 4,998

5. **Goodwill:** 6 years' purchase of super profit
= Rs 4,998 × 6 = Rs 29,988

6. Net assets available to equity shareholders

	Rs
Capital employed (W.N.1)	10,27,748
Goodwill (W.N.5)	29,998
Add: Non-trade investments	80,000
	11,37,746
Less: Preference share capital	(2,00,000)
	9,37,746
Add: Notional calls received for calls in arrears	10,000
Net assets for equity shareholders	9,47,746

Q8. The following is the summarized Balance Sheet of N Ltd. as on 31st March, 2017:

Balance Sheet

Liabilities	Rs	Assets	Rs
4,00,000 Equity shares of Rs 10 each fully paid	40,00,000	Building	24,00,000
13.5% Redeemable preference shares of Rs 100 each fully paid	20,00,000	Machinery Furniture	22,00,000 10,00,000
General Reserve	10,00,000	Vehicles	18,00,000
Profit and Loss Account	3,20,000	Investments	16,00,000
Bank Loan (Secured against fixed assets)	12,00,000	Inventory	11,00,000
Trade Payables	37,00,000	Trade Receivables	18,00,000
		Bank Balance	3,20,000
	1,22,20,000		1,22,20,000

Further information:

(i) Return on capital employed is 20% in similar businesses.

(ii) Fixed assets are worth 30% more than book value. Inventory is overvalued by Rs 1,00,000, Trade Receivables are to be reduced by Rs 20,000. Trade investments, which constitute 10% of the total investment are to be valued at 10% below cost.

(iii) Trade investments were purchased on 1.4.2016. 50% of Non-Trade Investments were purchased on 1.4.2014 and the rest on 1.4.2015. Non-Trade Investments yielded 15% return on cost.

(iv) In 2014-2015 new machinery costing Rs 2,00,000 was purchased, but wrongly charged to revenue. This amount should be adjusted taking depreciation at 10% on reducing value method.

(v) In 2015-2016 furniture with a book value of Rs 1,00,000 was sold for Rs 60,000.

(vi) For calculating goodwill two years purchase of super profits **based on simple average profits** of last four years are to be considered. Profits of last four years are as under:
2013-2014 Rs 16,00,000, 2014-2015 Rs 18,00,000, 2015-2016 Rs 21,00,000, 2016-2017 Rs 22,00,000.

(vii) Additional depreciation provision at the rate of 10% on the additional value of Plant and Machinery alone may be considered for arriving at average profit.

Find out the intrinsic value of the equity share. Income-tax and Dividend tax are not to be considered.

Answer

Calculation of intrinsic value of equity shares of N Ltd.

1. **Calculation of Goodwill**

(i) Capital employed

Fixed Assets	Rs	Rs
Building	24,00,000	
Machinery (Rs 22,00,000 + Rs 1,45,800)	23,45,800	
Furniture	10,00,000	
Vehicles	18,00,000	
	75,45,800	
Add: 30% increase	22,63,740	
	98,09,540	
Trade investments (Rs 16,00,000 × 10% × 90%)	1,44,000	
Trade Receivables (Rs 18,00,000 – Rs 20,000)	17,80,000	
Inventory (Rs 11,00,000 – Rs 1,00,000)	10,00,000	
Bank balance	3,20,000	1,30,53,540
Less: Outside liabilities		
Bank Loan	12,00,000	
Trade Payables	37,00,000	(49,00,000)
Capital employed		81,53,540

(ii) Future maintainable profit

Calculation of average profit

	2013-2014	2014-2015	2015-2016	2016-2017
	Rs	Rs	Rs	Rs
Profit given	16,00,000	18,00,000	21,00,000	22,00,000
Add: Capital expenditure of machinery charged to revenue		2,00,000		
Loss on sale of furniture	______	______	40,000	______
	16,00,000	20,00,000	21,40,000	22,00,000
Less: Depreciation on machinery		(20,000)	(18,000)	(16,200)
Income from non-trade investments		(1,08,000)	(2,16,000)	(2,16,000)
Reduction in value of inventory				(1,00,000)
Bad debts	______	______	______	(20,000)
Adjusted profit	16,00,000	18,72,000	19,06,000	18,47,800
				(Rs.)
Total adjusted profit for four years (2013-2014 to 2016-2017)				72,25,800
Average profit (Rs 72,25,800/4)				18,06,450

Less: Depreciation at 10% on additional value of machinery (22,00,000 + 1,45,800) × 30/100 i.e. Rs 7,03,740	(70,374)
Adjusted average profit	17,36,076

(iii) Normal Profit: 20% on capital employed i.e. 20% on Rs 81,53,540 = Rs 16,30,708

(iv) Super profit: Expected profit – normal profit
Rs 17,36,076 - Rs 16,30,708 = Rs 1,05,368

(v) Goodwill: 2 years' purchase of super profit
Rs 1,05,368 × 2 = Rs. 2,10,736

2. Net assets available to equity shareholders

	Rs	
Goodwill as calculated in 1(v) above		2,10,736
Sundry fixed assets		98,09,540
Trade and Non-trade investments		15,84,000
Trade Receivables		17,80,000
Inventory		10,00,000
Bank balance		3,20,000
		1,47,04,276
Less: Outside liabilities		
Bank loan	12,00,000	
Trade Payables	37,00,000	
		(49,00,000)
Preference share capital		(20,00,000)
Net assets for equity shareholders		78,04,276

3. Valuation of equity shares

Value of equity share = Net assets available to equity shareholders / Number of equity shares

= Rs 78,04,276 / 4,00,000 = Rs 19.51

Note:

1. Depreciation on the overall increased value of assets (worth 30% more than book value) has not been considered. Depreciation on the additional value of only plant and machinery has been considered taking depreciation at 10% on reducing value method while calculating average adjusted profit.
2. Loss on sale of furniture has been taken as non-recurring or extraordinary item.
3. It has been assumed that preference dividend has been paid till date.

Valuation of Shares: Yield Basis

Q9. The Capital Structure of XYZ Ltd., on 31st March, 2017 was as follows:

	Rs.
Equity Capital – 18,000 Shares of Rs 100 each	18,00,000
12% Preference Capital – 5,000 Shares of Rs 100 each	5,00,000
12% Secured Debentures	5,00,000
Reserves	5,00,000
Profit earned before Interest and Taxes during the year	7,20,000
Tax Rate	40%

Generally the return on equity shares of this type of Industry is 15%.

Subject to:

(a) The profit after tax covers Fixed Interest and Fixed Dividends at least 4 times.
(b) The Debt Equity ratio shall be at least 2;
(c) Yield on shares is calculated at 60% of distributed profits and 10% of undistributed profits;
(d) The Company has been paying regularly an Equity dividend of 15%.
(e) The risk premium for Dividends is generally assumed at 1%.

Find out the value of Equity shares of the Company.

Answer

Calculation of profit after tax (PAT)	**Rs**	**Rs**
Profit before interest & tax (PBIT)		7,20,000
Less: Debenture interest (Rs 5,00,000 × 12/100)		(60,000)
Profit before tax (PBT)		6,60,000
Less: Tax @ 40%		(2,64,000)
Profit after tax (PAT)		3,96,000
Less: Preference dividend (Rs 5,00,000 × 12 / 100)	60,000	
Equity dividend (Rs 18,00,000 × 15 / 100)	2,70,000	(3,30,000)
Retained earnings (undistributed profit)		66,000

Calculation of Interest and Fixed Dividend Coverage

=PAT + Debenture interest / Debenture interest + Preference dividend

Rs 3,96,000 + Rs 60,000 / Rs 60,000 + Rs 60,000 = Rs 4,56,000 / Rs 1,20,000 = 3.8 times

Calculation of Debt Equity Ratio

Debt Equity Ratio = Debt (long term loans) / Equity (shareholders' funds)

Debentures / Preference share capital + Equity share capital + Reserves

5,00,000 / 5,00,000 + 18,00,000 + 5,00,000

Debt Equity Ratio = Rs 5,00,000 / Rs 28,00,000 = .179

The ratio is less than the prescribed ratio.

Calculation of Yield on Equity Shares

Yield on equity shares is calculated at 60% of distributed profits and 10% of undistributed profits:

60% of distributed profits (60% of Rs 2,70,000)	1,62,000
10% of undistributed profits (10% of Rs 66,000)	6,600
	1,68,600

Yields on equity shares = Yield on shares × 100 / Equity share capital

Rs 1,68,600 × 100 / Rs 18,00,000 = 9.37%

Calculation of Expected Yield on Equity Shares	
Normal return expected	15%
Add: Risk premium for low interest and fixed dividend coverage (3.8 < 4)	1%*
Risk for debt equity ratio not required	Nil**
	16%
Value of an Equity Share = Actual yield × Paid up value of a share / Expected yield = 9.37 × 100 / 16 = 58.56	

* When interest and fixed dividend coverage is lower than the prescribed norm, the riskiness of equity investors is high. They should claim additional risk premium over and above the normal rate of return.
** The debt equity ratio is lower than the prescribed ratio that means outside funds (Debts) are lower as compared to shareholders' funds. Therefore, the risk is less for equity shareholders. Therefore, no risk premium is required to be added in this case.
Ans.: Earning Rate 9.37%, Earning 168600, Value of equity share 58.56 NRR 16% (without considering advantages)

Q10. The following abridged Balance Sheet as at 31st March, 2017 pertains to Glorious Ltd.

Liabilities	Rs in lakhs	Assets	Rs in lakhs
Share Capital:		Goodwill, at cost	420
180 lakhs Equity shares of Rs 10 each, fully paid up	1,800	Other Fixed Assets Current Assets	11,166 2,910
90 lakhs Equity shares of Rs 10 each, Rs 8 paid up	720	Loans and Advances	933
150 lakh Equity shares of Rs 5 each, fully paid-up	750		
Reserves and Surplus	5,457		
Secured Loans	4,500		
Current Liabilities	1,242		
Provisions	960		
	15,429		15,429

You are required to calculate the following for each one of the three categories of equity shares appearing in the above mentioned Balance Sheet:
(i) Intrinsic value on the basis of ***book values*** of Assets and Liabilities including goodwill;
(ii) Value per share on the basis of dividend yield.
Normal rate of dividend in the concerned industry is 15%, whereas Glorious Ltd. has been paying 20% dividend for the last four years and is expected to maintain it in the next few years; and
(iii) Value per share on the basis of EPS.
For the year ended 31st March, 2017 the company has earned Rs 1,371 lakhs as profit after tax, which can be considered to be normal for the company. Average EPS for a fully paid share of Rs 10 of a Company in the same industry is Rs 2.

Answer

(i) Intrinsic value on the basis of book values

	Rs in lakhs	Rs in lakhs
Goodwill		420
Other Fixed Assets		11,166
Current Assets		2,910
Loans and Advances		933
		15,429
Less: Secured loans	4,500	

Current liabilities	1,242	
Provisions	960	(6,702)
		8,727
Add: Notional call on 90 lakhs equity shares @ Rs 2 per share		180
		8,907

Equivalent number of equity shares of Rs 10 each.

	No. of Equity shares
Fully paid shares of Rs 10 each	180
Partly-paid shares after notional call	90
Fully paid shares of Rs 5 each, [150 lakhs × 5 /10]	75
	345

Value per equivalent share of Rs 10 each = Rs 8,907 lakhs /345 lakhs = Rs25.82
Hence, intrinsic values of each equity share are as follows:
Value of fully paid share of Rs 10 = Rs 25.82 per equity share.
Value of share of Rs 10, Rs 8 paid-up = Rs 25.82 – Rs 2 = Rs 23.82 per equity share.
Value of fully paid share of Rs 5 = 25.82 / 2 = Rs 12.91 per equity share.

(ii) **Valuation on dividend yield basis:**
Value of fully paid share of Rs 10 = 20 × 10 / 15 = Rs 13.33
Value of share of Rs 10, Rs 8 paid-up = 20 × 8 / 15 = Rs 10.67
Value of fully paid share of Rs 5 = 20 × 5 /15 = Rs 6.67

(iii) Valuation on the basis of EPS:
Profit after tax = Rs 1,371 lakhs
Total share capital = Rs (1,800 + 720 + 750) lakhs = Rs 3,270 lakhs
Earning per rupee of share capital = 1,371 lakhs / 3,270 lakhs = Rs 0.419
Earnings per fully paid share of Rs 10 = Rs 0.419 × 10 = Rs 4.19
Earnings per share of Rs 10 each, Rs 8 paid-up = Rs 0.419 × 8 = Rs 3.35
Earnings per share of Rs 5, fully paid-up = Rs 0.419 × 5 = Rs 2.10
Value of fully paid share of Rs 10 = 4.19 × 10 / 2 = Rs 20.95
Value of share of Rs 10, Rs 8 paid-up = 3.35 × 10 / 2 = Rs 16.75
Value of fully paid share of Rs 5 = 2.10 × 10 / 2 = Rs 10.50

Q11. Yogesh Ltd. showed the following performance over 5 years ended 31st March, 2015:

Year Ended on 31st March	*Net Profit before Tax		Prior Period adjustment	Remarks
2011	4,00,000	(-)	1,00,000	Relating to 2009-10
2012	3,50,000	(-)	2,50,000	Relating equally to 09-10 and 10-11
2013	6,50,000	(+)	1,50,000	Relating to 11-12
2014	5,50,000	(-)	1,75,000	Relating to 11-12
2015	6,00,000	(-)	1,00,000	Relating to 11-12
2015		(+)	25,000	Relating to 13-14

*Net Profit before tax is after debiting or crediting the figures of loss (-) or gains (+) mentioned under columns for prior period adjustments.

The net worth of the business as per balance sheet of 31st march, 2010 is Rs. 6,00,000 backed by 10,000 fully paid equity shares of Rs. 10 each. Reserves and surplus constitute the balance net worth. Yogesh Ltd. has not declared any dividend till date.

You are asked to value Equity Shares on :

(a) Yield basis as on 31.03.2015, assuming:

(i) 40% Tax Rate

(ii) Anticipated after tax yield of 20%

(iii) Differential weight of 1 to 5 given for 5 years starting on 1.04.2010 for the actual profits of the respective years.

(b) Net Asset basis as per corrected balance sheets for each of the Six years ended 31.03.2015

Looking to the performance of the company over 5 years period, would you invest in the company? **(RTP – May 2015)**

(Answer: 184/- on yield basis and (46.50, 69, 97.5, 127.5, 172.5 and 213 on net asset basis)

Solution:

(a) Valuation of Shares on Yield basisas on 31st March, 2015

Year ended 31st March	Profits as given	Adjustment		Revised Profits	Tax Provision	After tax Profits	weight	Weighted Profits
		Increase	decrease					
		Rs	Rs	Rs	Rs	Rs		Rs
2011	4,00,000	1,00,000	1,25,000	3,75,000	1,50,000	2,25,000	1	2,25,000
2012	3,50,000	2,50,000 1,50,000	1,00,000 ,1,75,000	4,75,000	1,90,000	2,85,000	2	5,70,000 .
2013	6,50,000	Nil	1,50,000	5,00,000	2,00,000	3,00,000	3	9,00,000
2014	5,00,000	1,75,000 25,000	Nil	7,50,000	3,00,000	4,50,000	4	18,00,000
2015	6,00,000	1,00,000	25,000	6,75,000	2,70,000	4,05,000	5	20,25,000
							15	55,20,000

Weighted average profit (after tax) = Rs 55,20,000 / 15 = Rs 3,68,000
Value of business =Rs 3,68,000 / 20% = 18,40,000
Value of equity share =Rs 18,40,000 / 10,000 = Rs 184

(c) Valuation of Shares on Net Asset Basis

(i)	Revised net worth as on 31st March, 2010	Rs	Rs
	Net worth		6,00,000
	Less: Adjustments relating to		
	2010-11	1,00,000	
	2011-12	1,25,000	
		2,25,000	
	Less: Relief from tax @ 40%	(90,000)	(1,35,000)
			4,65,000
(ii)	**Net asset value** (No. of shares = 10,000)		
	As on 31st March	Rs	
	2010: Revised net worth	4,65,000	
	Value per share		46.50
	2011: Revised net worth as on 31.3.2010	4,65,000	
	Add: After tax revised profits of 2010-11	2,25,000	
	Net worth as on 31.3.2011	6,90,000	
	Value per share		69.00
	2012: Revised net worth as on 31.3.2011	6,90,000	
	Add: After tax revised profits of 2011-12	2,85,000	
	Net worth as on 31.3.2012	9,75,000	
	Value per share		97.50
	2013: Revised net worth as on 31.3.2012	9,75,000	
	Add: After tax revised profits of 2012-13	3,00,000	
	Net worth as on 31.3.2013	12,75,000	
	Value per share		127.50
	2014: Revised net worth as on 31.3.2013	12,75,000	
	Add: After tax revised profits of 2013-14	4,50,000	
	Net worth as on 31.3.2014 Value per share		172.50
	2015: Revised net worth as on 31.3.2014	17,25,000	
	Add: After tax revised profits of 2014-15	4,05,000	
	Net worth as on 31.3.2015	21,30,000	
	Value per share		213.00

Performance Appraisal

Revised net worth as on 31st March		Profit during the year ended 31st March		Return on net Worth
	Rs		Rs	%
2010	4,65,000	2011	2,25,000	48.39
2011	6,90,000	2012	2,85,000	41.30
2012	9,75,000	2013	3,00,000	30.77
2013	12,75,000	2014	4,50,000	35.29
2014	17,25,000	2015	4,05,000	23.48

The company's return has fallen from 48.39% to 23.48%. This may be perhaps due to the fact that the company has been ploughing back its profits without having adequate reinvestment opportunities. Unless the company has profitable investment opportunities, it may not be advisable to invest in the company.

Note: Return on net worth may also be calculated on the basis of average net worth during the relevant year.

VALUATION OF SHARES: FAIR VALUE

Q12. A Company Q is willing to sell its business. The purchaser has sought professional advice for the valuation of the goodwill of the company. He has the last audited financial statements together with some additional information. Help him to ascertain the correct price for the purpose of purchase:

The extract of the Balance Sheet as on 31-3-2016 is as under:

Liabilities	Rs	Assets	Rs
Equity Share Capital (shares of Rs 100 each)	9,50,000	Land & Building	5,45,000
8% Preference Share Capital (shares of Rs 100 each)	2,25,000	Plant & Machinery Investments in shares Inventories	4,55,000 4,85,000 3,80,000
Reserves & Surplus	7,50,500	Trade Receivables (net)	4,25,620
9% Debentures	5,60,000	Cash & Bank balance	5,20,520
Current Liabilities	3,25,640		
	28,11,140		28,11,140

(1) The purchaser wants to acquire all the equity shares of the company.

(2) The Debentures will be redeemed at a discount of 25% of the value in Balance Sheet and investments in share will be sold at their present market value which is quoted as Rs 4,95,200. The above will be prior to the purchase of the equity shares.
For the purpose of pricing of Goodwill:

(3) The normal rate of return on net assets for equity shares is 10%.

(4) Profits for the past three years after debenture interest but before Preference Share Dividend have been as under:

31-3-2016	Rs 2,95,000
31-3-2015	Rs 4,99,000
31-3-2014	Rs 3,25,000

(5) Goodwill is valued at three years purchase of the adjusted average super profit.

(6) In the year 2015, 20% of the profit mentioned above was due to non-recurring transaction resulting in increase of profit.

(7) The Land & Building has a current rental value of Rs 62,400 and 8% return is expected from the property.

(8) On 31-3-2016, 8% of debtors existing on the date had been written as bad and charged to Profit and Loss Account as Provision for Bad debts. The same are now recoverable. Tax is applicable at 35%.

(9) A claim of compensation long contingent of Rs 25,000 has perspired and is to be accounted for.

(10) No Debenture interest shall be payable in future due to its redemption.

Answer

Valuation of goodwill: Super profits method

Particulars	Rs	Rs
Net trading assets attributable to equity share holders		
As computing in (WN 1)	23,18,506	
Less: Preference share Capital	(2,25,000)	20,93,506
Normal Rate of Return (NRR) to equity share holders		10%
Normal Profit available to equity share holders (a × b)		2,09,351
Future Maintainable Profits (FMP) to equity share holders		
As computed in (WN 3)	3,75,096	
Less: Preference dividend* (8% of 2,25,000)	(18,000)	3,57,096
Super profits to equity share holders		1,47,745
Goodwill (1,47,745 x 3)		4,43,235

*Since, NRR is given as percentage of net assets attributable to equity shareholders, preference share capital and preference share dividend have been deducted from the net assets and future maintainable profit respectively.

Value Per Equity Share

Net Trading Assets attributable to equity shareholders	Rs 20,93,506
Add: Goodwill	Rs 4,43,235
	Rs 25,36,741

Number of Equity Shares = 9,500 shares,

Value per share =25,36,741/9,500= Rs 267 (approx.)

Working Notes:

1. **Computation of net trading assets**

	Particulars	Rs	Rs
Sundry assets			
i	Land & Building (62,400 ÷ 8%)	7,80,000	
ii	Plant and Machinery	4,55,000	
iii	Inventory	3,80,000	
iv	Trade receivables (4,25,620 ÷ 92%)	4,62,630	
v	Bank balance (given balance 5,20,520 + Sale of investment 4,95,200 - redemption of debentures 5,60,000 × 75%)	5,95,720	26,73,350
Less: Outside liabilities:			
i	Current Liabilities	3,25,640	
ii	Contingent Liability now to be accounted for	25,000	
iii	Tax provision (WN 2)	4,204	(3,54,844)
Net assets			23,18,506

2. **Calculation of tax provision**

	Rs
Profit on reversal of provision for bad debts	37,010
Loss on recognizing omitted claim (assuming tax deductible)	(25,000)
Net incremental profit on which tax is payable	12,010
Tax provision 35%	4,204

3. **Computation of future maintainable profit for the year ended on 31st March**

Particulars	2014	2015	2016
Profit after tax	3,25,000	4,99,000	2,95,000
Less: Non-recurring profits (after tax) (20% of 2015 Profit)	-	(99,800)	-
Less: Claims not recorded (after tax) [25,000 x (1-35%)]	-	-	(16,250)
Add: Provision no longer required (net of tax) [4,25,620 × 8/92 × (1-35%)]	-	-	24,057
Adjusted profits after tax	3,25,000	3,99,200	3,02,807

Simple average of the profits (as profits are fluctuating)	3,42,336
Adjustments for items which will not be reflected in future	
Add: Debenture interest (net of tax) [5,60,000 × 9% × (1 – 0.35)]	32,760
Future maintainable profit [for shareholders- both preference and equity)	3,75,096

Assumptions

1. Tax effect has been ignored on profit on sale of investments and discount on redemption of debentures.
2. Assets and liabilities are recorded at realizable value or fair value. In the absence of information, book values are assumed to be fair values.
3. Additional depreciation on revaluation of property is ignored.
4. Profits for past three years given in the question have been assumed as profits after tax.

VALUATION OF BUSINESS

Q13. Jayadev Ltd. has earned a PAT of Rs. 48 lakhs for the year ended 2013. It wants you to ascertain the value of its Business, based on the following information:

(a) Tax rate for the year 2013 was 36%. Future Tax rate is estimated at 34%.

(b) The company's equity shares are quoted at Rs. 120 at the Balance Sheet date. The company had an equity share capital of Rs. 100 lakhs, dividend into shares of Rs. 50 Each.

(c) Profits for the year 2013 have been calculated after considering the following in the Profit and Loss Account:

(i) Subsidy of Rs. 2 lakhs received from the Government towards fulfillment of certain social obligations. The govt. has withdrawn this subsidy and hence this amount will not be received in future.

(ii) Interest of Rs. 8 lakhs on term loan. The final installment of this term loan was fully settled this year.

(iii)Managerial remuneration Rs. 15 Lakhs. The Shareholders have approved an increase of Rs. 6 lakhs in the overall managerial remuneration from the next year onwards.

(iv)Loss on sale of Fixed assets and investment amounting to Rs. 8 lakhs.

(RTP – May 2014)

Solution:

Computation of Future Maintainable Profits

Particulars	Rs
Profit after tax for the year 2013	48,00,000
Add: Tax epense (Tax is 36%, So, PAT = 64%. Hence, Tax = 48,00,000 x 36/64)	27,00,000
Profit before tax for the year 2013	75,00,000
Add/ (Less) Adjustments in respect of non-recurring items	
Subsidy income not receivable in future	(2,00,000)
Interest on term loan not payable in future, hence saved	8,00,000
Additional managerial remuneration Loss on sale of fixed assets	(6,00,000)
and investments (nonrecurring)	8,00,000
Future maintainable profits before tax	83,00,000
Less: Tax expense at 34%	(28,22,000)
Future maintainable profits after tax equity earnings	54,78,000

Computation of capitalization rate and value of business

Particulars	**Rs.**
(a) Profit after tax for the year 2013 Rs	48 Lakhs
(b) Number of equity shares (Rs 100 lakhs / Rs 50 per share)	2 lakhs
(c) Earnings per share (EPS) = PAT/Number of Equity Shares	24/-
(d) Market price per share on balance sheet date	120/-
(e) Price Earnings Ratio = MPS / EPS	5
(f) Capitalisation Rate = (1 / PE Ratio) x 100	20%
Value of Business = Future Maintainable Profits /Capitalisation Rate= Rs 54.78 Lakhs / 20%	273.90 Lakhs

Q14. The summarized Balance Sheet of R Ltd. for the year ended on 31st March, 2015, 2016 and 2017 are as follows:

	(Rs in thousands)		
Liabilities	31.3.2015	31.3.2016	31.3.2017
3,20,000 equity shares of Rs 10 each, fully paid	3,200	3,200	3,200
General reserve	2,400	2,800	3,200
Profit and Loss account	280	320	480
Trade Payables	1,200	1,600	2,000
	7,080	**7,920**	**8,880**
Assets			

Goodwill	2,000	1,600	1,200
Building and Machinery less, depreciation	2,800	3,200	3,200
Inventory	2,000	2,400	2,800
Trade Receivables	40	320	880
Bank balance	240	400	800
	7,080	7,920	8,880

Additional information:

(a) Actual valuations were as under

Building and machinery less, depreciation	3,600	4,000	4,400
Inventory	2,400	2,800	3,200
Net profit (including opening balance after writing off depreciation, goodwill, tax provision and transferred to general reserve)	840	1,240	1,640

(b) Capital employed in the business at market value at the beginning of 2014-2015 was Rs 73,20,000 which included the cost of goodwill. The normal annual return on average capital employed in the line of business engaged by R Ltd. is $12\frac{1}{2}$%.

(c) The balance in the general reserve on 1st April, 2014 was Rs 20 lakhs.

(d) The goodwill shown on 31.3.2015 was purchased on 1.4.2014 for Rs 20 lakhs on which date the balance in the Profit and Loss account was Rs 2,40,000. Find out the average capital employed in each year.

(e) Goodwill is to be valued at 5 year's purchase of Super profit (Simple average method). Find out the total value of the business as on 31.3.2017.

Answer

Total value of business	**Rs**
Total net Asset as on 31.3.2017	84,80,000
Less: Goodwill as per Balance Sheet	(12,00,000)
Add: Goodwill as calculated in Working Note 2	41,12,500
Value of Business	1,13,92,500

Working Notes:

1. Capital Employed at the end of each year

	31.3.2015 Rs	**31.3.2016 Rs**	**31.3.2017 Rs**
Goodwill	20,00,000	16,00,000	12,00,000
Building and Machinery (Revaluation)	36,00,000	40,00,000	44,00,000
Inventory (Revalued)	24,00,000	28,00,000	32,00,000
Trade Receivables	40,000	3,20,000	8,80,000
Bank Balance	2,40,000	4,00,000	8,00,000
Total Assets	**82,80,000**	**91,20,000**	**10480000**
Less: Trade Payables	(12,00,000)	(16,00,000)	(20,00,000)
Closing Capital	**70,80,000**	**75,20,000**	**84,80,000**
Add: Opening Capital	73,20,000	70,80,000	75,20,000
Total	1,44,00,000	1,46,00,000	1,60,00,000
Average Capital	72,00,000	73,00,000	80,00,000

Since the goodwill has been purchased, it is taken as a part of Capital employed.

2. Valuation of Goodwill

(i) Future Maintainable Profit	**31.3.2015**	**31.3.2016**	**31.3.2017**
Net Profit as given	8,40,000	12,40,000	16,40,000
Less: Opening Balance	(2,40,000)	(2,80,000)	(3,20,000)
Adjustment for Valuation of Opening Inventory	-	(4,00,000)	(4,00,000)
Add: Adjustment for Valuation of closing inventory	4,00,000	4,00,000	4,00,000
Goodwill written off	-	4,00,000	4,00,000
Transferred to General Reserve	4,00,000	4,00,000	4,00,000
Future Maintainable Profit	14,00,000	17,60,000	21,20,000
Less: 12.50% Normal Return	(9,00,000)	(9,12,500)	(10,00,000)
(ii) Super Profit	5,00,000	8,47,500	11,20,000

(i) **Average Super Profit** = Rs (5,00,000 + 8,47,500+11,20,000) ÷ 3 = Rs 8,22,500

(ii) **Value of Goodwill** at five years' purchase= Rs 8,22,500 × 5 = Rs 41,12,500.

(Answer: Goodwill: 5195.85; Value of Business: 12475.85/ 11392.5 on simple avg Or Goodwill – 4112.5 SP (Avg) – 822.50)

Q15. Timby Ltd. is in the business of making sports equipment. The Company operates from Thailand. To globalise its operations, Timby has identified Fine Toys Ltd. an Indian Company, as a potential takeover candidate. After due diligence of Fine Toys Ltd. the following information is available:

(a)

Cash Flow Forecasts										**(Rs in crore)**
Year	10	9	8	7	6	5	4	3	2	1
Fine Toys Ltd.	24	21	15	16	15	12	10	8	6	3
Timby Ltd.	108	70	55	60	52	44	32	30	20	16

(b) The net worth of Fine Toys Ltd. (Rs in lakhs) after considering certain adjustments suggested by the due diligence team reads as under:

Tangible		750
Inventories		145
Receivables		75
		970
Less:		
Trade Payables	165	
Bank Loans	250	(415)
Represented by equity shares of Rs 1,000 each		**555**

Talks for takeover have crystalized on the following:

1. Timby Ltd. will not be able to use Machinery worth Rs 75 lakhs which will be disposed of by them subsequent to take over. The expected realization will be Rs 50 lakhs.
2. The inventories and receivables are agreed for takeover at values of Rs 100 and Rs 50 lakhs respectively which is the price they will realize on disposal.
3. The liabilities of Fine Toys Ltd. will be discharged in full on take over alongwith an employee settlement of Rs 90 lakhs for the employees who are not interested in continuing under the new management.

4. Timby Ltd. will invest a sum of Rs 150 lakhs for upgrading the Plant of Fine Toys Ltd. on takeover. A further sum of Rs 50 lakhs will also be incurred in the second year to revamp the machine shop floor of Fine Toys Ltd.
5. The Anticipated Cash Flows (in Rs crore) post takeover are as follows:

Year	1	2	3	4	5	6	7	8	9	10
Cash Flows	18	24	36	44	60	80	96	100	140	200

You are required to advise the management the maximum price which they can pay per share of Fine Toys Ltd. if a discount factor of 20 per cent is considered appropriate.

Answer

Calculation of Maximum Price that can be quoted for takeover of Fine Toys Ltd.

	Rs in lakhs	Rs in lakhs
Present (Discounted) value of incremental cash flows (Refer Working Note)		7,845.02
Add: Proceeds from disposal of fixed assets	50.00	
Proceeds from disposal of inventories	100.00	
Receipts from Trade Receivables	50.00	200.00
		8,045.02
Less: Settlement of Trade Payables	165.00	
Bank Loans	250.00	
Employee settlement	90.00	
Renovation of Plant	150.00	
Revamp of machine shop floor (Rs 50 lakhs× 0.6944)*	34.72	(689.72)
Maximum value that can be offered		7,355.30
Maximum price per share of Fine Toys Ltd. (Rs 7,355.30 lakhs / 55,500 shares) Rs 13,252.79		

Working Note:

Present Value of Incremental Cash Flows

(Rs in lakhs)

Year	Cash flow after takeover	Cash flows before takeover	Incremental Cash flows	Discount factor @ 20%	Discounted Cash flows
1	1,800	1600	200	0.8333	166.66
2	2,400	2000	400	0.6944	277.76
3	3,600	3000	600	0.5787	347.22
4	4,400	3200	1200	0.4823	578.76
5	6,000	4400	1600	0.4019	643.04
6	8,000	5200	2800	0.3349	937.72
7	9,600	6000	3600	0.2791	1,004.76
8	10,000	5500	4500	0.2326	1,046.70
9	14,000	7000	7000	0.1938	1,356.60
10	20,000	10800	9200	0.1615	1,485.80
					7,845.02

BRAND VALUATION

Brand may be SELF GENERATED or ACQUIRED.

Valuation of Acquired Brand is given below:

1. Brand Value = Price paid to acquire such brand; or
2. Brand Value = Purchase Consideration – Net Assets taken over

Valuation of Self Generated Brand is given below:

1. ***Historical Cost Method***

   Brand Value = Actual Cost Incurred in Brand Building (Development + Marketing + Promotion Cost)

2. ***Potential Earning Model***

   Brand Value = Profit arising due to Brand / Capitalisation Factor

   How to Calculate Profit due to Brand?

	PAT	xxx
Less:	Expected Return due to unbranded Products	(xxx)
	(From Tangible and Intangible Assets other than Brand)	

Q16. From the Following, determine the possible value of brand as per potential earning model:

		Rs. In Lakhs
1	Profit after tax (PAT)	2500
2	Tangible Fixed Assets	10000
3	Identifiable intangible assets other than brand	1500
4	Weighted average cost of capital (%)	14%
5	Expected normal return on tangible assets	
	[weighted average cost (14%) + normal spread 4%]	18%
6	Appropriate capitalization factor for intangibles	25%

Answer

Calculation of possible value of brand

	Rs in lakhs
Profit after Tax	2,500
Less: Profit allocated to tangible assets [18% of Rs 10,000]	(1,800)
Profit allocated to intangible assets including brand	700
Capitalisation factor 25%	
Capitalised value of intangibles including brand [700/25×100]	2,800
Less: Identifiable intangibles other than brand	(1,500)
Brand value	1,300

Q17. Zed Ltd. is a FMCG player in the range of Men's cosmetics and deals in both Branded and Unbranded products. The Branded products are sold under brand of 'Zed' and are full outsourced from third party manufacturers. The Company's unbranded products are manufactured at its own manufacturing units. The earnings for the last three years (Lakhs Rs.) are furnished below:

	Year 1	**Year 2**	**Year 3**
Earnings before interest and Tax from Sale of Products	5100	7500	9900
Other Income – Royalty from partial use of Zed Brand	190	135	225
Tangible Fixed Assets employed	9000	10800	13500
Returns (Before interest and Tax) on cost of tangible assets	14%	12%	14%
Spread over return	2%	3%	3%

The average annual fund's used in the company's operations is Rs. 5200 lakhs of which Rs. 2800 lakhs is in respect of the branded business. The company's tax rate is 33.33% and has an average cost of funds of 17% after considering tax shelter on cost of borrowed funds. You are required to determine the value of Brand Zed considering a capitalization rate of 20%. **(November – 2013, 8 Marks)**

(Answer: Value of Brand – 19490 by Weighted avg. or 17170 by Simple avg.)

Solution:

1. **Calculation of EBIT on unbranded product (Rs In lakhs)**

	Year 1	**Year 2**	**Year 3**
Tangible Fixed Assets	9,000	10,800	13,500
Return on cost +spread (5%)	16	15	17
Absolute value of the above	1,440	1,620	2,295

EBIT from sale of unbranded products	1,440	1,620	2,295

2. **Calculation of Average earnings after tax on Branded Products (Rs In Lakhs)**

	Year 1	Year 2	Year 3
Total EBIT	5,100	7,500	9,900
Less: EBIT in respect of unbranded products	1,440	1,620	2,295
Add: Brand Royalty	90	135	225
EBIT from ZED Branded products	3,750	6,015	7,830
Average EBIT from Branded sold [(3750+6015+7830)/3]			5,865
Less : Tax @ 33.33%			1,955
Average post tax earnings from Branded Goods (including tax shelter on interest)			3,910

3. **Net Earnings from Brand (Rs Lakh)**

= Average post tax earnings from Branded Goods less cost of funds used in Branded operations

= Average post tax earnings from Branded goods = 3,910

Less: Cost of funds used in Branded operations = 2,800 x 17% 476

Net earnings from brand 3,434

Brand Value = Net Earnings from Brand x Capitalisation Rate =

= 3,434 x 100/20 = 17,170

Value of the ZED Brands is ` 17,170 lakh

Q18.

Agile Limited is a manufacturer-cum-dealer of 'R Tuff' brand of trousers. With passage of time, its brand has been well accepted in the market. The company has been approached by a foreign company engaged in the same trade to enter as partner in its business. Agile, in order to negotiate the deal wants to get its brand valued. The following information based on market research is available:

(i) Garment industry of which Agile is a constituent, is expected to grow by 9% per annum during the next five years. The present market size of the industry is Rs 7,500 crores.

(ii) There are other brands both national and international in the market. The existence of duplicate brands is unavoidable. The share of such players is estimated to be 63% of the total industry market. The market share of other national brands will increase @ 0.25% year on year basis in the next 5 years. The share of international brands is expected to grow 1.5 times of national brands. But the existence of duplicate brands is to fall by 2.5% over the period of next 5 years, spread equally.

(iii) The expected foreign partner needs the production line of the company to be re-engineered which will lead to an increase in the yield of the company by 3% after one year over the present yield of 10% followed thereafter by further increase of 5% year on year.

Following the market oriented approach, determine the brand value to be used for negotiation with the foreign company, considering the discount factor for 1st five years as 0.909; 0.826; 0.751; 0.683 and 0.621 (Monetary values in crores to be rounded off to nearest 2 decimal places).

Answer

Market Share of Agile Ltd.

Calculation of last year's market share = 100% –63% = 37%

Increase or decrease in market share of other players [0.25+(.25 x 150%)-2.5/5] = 0.125% i.e. increase in others' market share every year over the period of 5 years. Hence, market share of Agile Ltd. is expected to decrease by 0.125% every year over the period of 5 years, from the current level of 37%.

Brand Valuation under Market Approach

Year	Market Size (Rs in Crores)	Market Share of Agile Ltd.	Market Share (Rs in Crores)	Expected Profit (Rs in Crores)	Discount Factor	Discounted Cash Flow (Rs in Crores)
1	7500 x 109% = 8,175	36.875%	3014.53	@ 10% = 301.45	0.909	274.02
2	8,175 x 109% = 8910.75	36.75%	3274.70	@ 13% = 425.71	0.826	351.64
3	8,910.75x 109% = 9712.72	36.625%	3557.28	@18% = 640.31	0.751	480.87
4	9,712.72 x 109% = 10,586.86	36.5%	3864.20	@23% = 888.77	0.683	607.03
5	10,586.86 x 109% = 11,539.68	36.375%	4197.56	@28% = 1,175.32	0.621	729.87
Brand Value						2,443.43

Brand Value of Agile Ltd. under Market Oriented Approach is Rs 2,443.43 crores.

Important Notes:

CORPORATE RESTRUCTURING

Part – 1 Amalgamation Of Companies

Q19. (PM)

A Ltd. agreed to absorb B Ltd. on 31st March 1999, whose balance sheet stood as follows:

Equity & Liabilities:	
Shareholders Fund:	
Share Capital 80,000 shares of Rs. 10 each	800,000
Reserves & Surplus:	
General Reserve	100,000
Non-Current Liabilities:	
Secured Loan	-
Unsecured Loan	-
Current Liabilities:	
Sundry Creditors	100,000
	1,000,000
Assets:	
Non-Current Assets:	
Fixed Assets	700,000
Investments	-
Current Assets:	
Stock in trade	100,000
Sundry Debtors	200,000
	1,000,000

The consideration was agreed to be paid as follows:

(a) A payment in cash of Rs. 5 per share in B Ltd. and the issue of shares of Rs. 10 each in A Ltd., on the basis of 2 Equity Shares (valued at Rs. 15) and one 10% cum. Preference share (valued at Rs. 10) for every five shares held in B Ltd.

The whole of the share capital consists of shareholdings in exact multiple of five except the following holding:

Chopra	116
Karki	76
Amar Singh	72
Malhotra	28
Other individuals	8 (Eight members holding one share each)
	300

It was agreed that A Ltd. will pay in cash for fractional shares equivalent at agreed value of shares in B Ltd. i.e. Rs. 65 for five shares of Rs. 50 paid.

Prepare a statement showing the purchase consideration receivable in share and cash.

Solution:

Purchase Consideration

	Rs
31,994 Equity shares @ Rs 15 each	4,79,910
15,997 Preference shares @ Rs 10 each	1,59,970
Cash on 79,985 shares (i.e 80,000 – 15) of B Ltd.@ Rs 5 each	3,99,925
	10,39,805
Add: Cash for fractional shares (W.N. 3)	195
	10,40,000

Working Notes:

1. Schedule showing fractional shares

Holding of Shares		Exchangeable in multiple of five	Exchange in Equity shares	Exchange in preference shares	Non exchangeable shares
A	116	115	46	23	1
B	76	75	30	15	1
C	72	70	28	14	2
D	28	25	10	5	3
Others	8	-	-	-	8
	300	285	114	57	15

2. Shares Exchangeable: Equity Shares in A Ltd.

	No. of shares		No. of shares
(i) 80,000 – 300	79,700	2/5 thereof	31,880
(ii) 300 – 15	285	2/5 thereof	114
	79,985		31,994

Shares Exchangeable: Preference Shares in A Ltd.

	No. of shares		No. of shares
(i) 80,000 – 300	79,700	1/5 thereof	15,940
(ii) 300 – 15	285	1/5 thereof	57
	79,985		15,997

3. There are 15 shares (W.N.1) in B Ltd. which are not capable of exchange into equity and preference shares of A Ltd. They will be paid cash = 15 × 10 × 65 / 50 = 195

Accounting under Purchase Method

Q20. (PM)

T. Ltd. and V. Ltd. propose to amalgamate. Their summarized balance sheets as at 31st March, 2016 were as follows:

Liabilities	T. Ltd.	V. Ltd.	Assets	T. Ltd.	V. Ltd.
	Rs	Rs		Rs	Rs
Share capital:			Fixed assets		
Equity shares of Rs 10 each	15,00,000	6,00,000	Less: Depreciation	12,00,000	3,00,000

General reserve	6,00,000	60,000	Investments (fetching interest @ 6%)	3,00,000	-
Profit & Loss A/c	3,00,000	90,000	Inventory	6,00,000	3,90,000
Trade payables	3,00,000	1,50,000	Trade receivables	5,10,000	1,80,000
			Cash and bank balances	90,000	30,000
	27,00,000	**9,00,000**		**27,00,000**	**9,00,000**

Their net profits (after taxation) were as follows:

Year	T. Ltd.	V. Ltd.
2013-2014	3,90,000	1,35,000
2014-2015	3,75,000	1,20,000
2015-2016	4,50,000	1,68,000

Normal trading profit may be considered as 15% on closing capital invested. Goodwill may be taken as 4 years' purchase of average super profits. The inventory of T. Ltd. and V. Ltd. are to be taken at Rs 6,12,000 and Rs 4,26,000 respectively for the purpose of amalgamation. W. Ltd. is formed for the purpose of amalgamation of two companies. Assume tax @ 40%.

(a) Suggest a scheme of capitalization of W. Ltd. and ratio of exchange of shares; and

(b) Draft the opening balance sheet of W. Ltd.

Answer

(a) Scheme of capitalization of W. Ltd. and ratio of exchange of shares Computation of Net Assets of amalgamating companies

	T. Ltd.	V. Ltd.
	Rs	Rs
Goodwill (W.N.2)	3,22,080	1,29,840
Fixed Assets	12,00,000	3,00,000
6% investments (Non-trade)	3,00,000	-
Inventory	6,12,000	4,26,000
Trade receivables	5,10,000	1,80,000
Cash and Bank Balances	90,000	30,000
	30,34,080	10,65,840
Less: Trade payables	(3,00,000)	(1,50,000)
Provision for tax	4,800	14,400
Net Assets	27,29,280	9,01,440
No. of Equity shares	1,50,000	60,000
Intrinsic value of a share	Rs 18.1952	Rs 15.024
No of shares to be issued by W. Ltd to		
T. Ltd (1,50,000 x 18.1952/10)	2,72,928 shares	
V. Ltd (60,000 x 15.024/10)		90,144 shares

In total 2,72,928 + 90,144 i.e. 3,63,072 shares will be issued by W. Ltd.

Ratio of exchange of shares will be as follows:

1. Holders of 1,50,000 equity shares of T Ltd. will get 2,72,928 shares in W. Ltd.
2. Similarly, holders of 60,000 equity shares of V Ltd. will get 90,144 shares in W. Ltd.

(b) Opening Balance Sheet of W. Ltd.

Particulars	Note No.	(Rs)
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
Share Capital	1	36,30,720
(2) **Current Liabilities**		
Trade payables [3,00,000 + 1,50,000]		4,50,000
Provision for tax (4,800 + 14,400)		19,200
Total		40,99,920
II. Assets		
(1) **Non-current assets**		
(a) Fixed assets		
i. Tangible assets	2	15,00,000
ii. Intangible assets	3	4,51,920
(b) Non-current investments	4	3,00,000
(2) **Current assets**		
(a) Inventories [6,12,000+ 4,26,000]		10,38,000
(b) Trade receivables [5,10,000 + 1,80,000]		6,90,000
(c) Cash and cash equivalents [90,000 + 30,000]		1,20,000
Total		40,99,920

Notes to Accounts

		(Rs)
1.	Share Capital	
Equity share capital		
3,63,840 Equity shares of Rs 10 each		36,38,400
(Issued for consideration other than cash, pursuant to scheme of amalgamation)		
2.	Tangible Assets	
Other Fixed Assets (Rs 12,00,000+Rs 3,00,000)		15,00,000
3.	Intangible assets	
Goodwill (W.N.2) (Rs 3,22,080 +Rs 1,29,840)		4,51,920
4.	Non-current investments	
6%Investments		3,00,000

Working Notes:

1. Calculation of closing trading capital employed on the basis of net assets

	T. Ltd. Rs	V. Ltd. Rs
Fixed Assets	12,00,000	3,00,000
Inventory	6,12,000	4,26,000
Trade receivables	5,10,000	1,80,000
Cash and Bank Balances	90,000	30,000
	24,12,000	9,36,000

Less: Trade payables	(3,00,000)	(1,50,000)
Tax provision on appreciation in inventory	(4,800)	(14,400)
Net Assets	21,07,200	7,71,600

2. Calculation of value of goodwill

		T. Ltd. Rs	V. Ltd. Rs
(i)	Average Trading Profit		
2013-2014		3,90,000	1,35,000
2014-2015		3,75,000	1,20,000
2015-2016		4,50,000	1,68,000
Profit after tax		12,15,000	4,23,000
Profit before tax @ 40%		20,25,000	7,05,000
Add: Under valuation of closing inventory		12,000	36,000
		20,37,000	7,41,000
Average of 3 years' profit before tax		6,79,000	2,47,000
Less: Income from non-trade investments (Rs 3,00,000 x 6%)		(18,000)	-
Average profit before tax		6,61,000	2,47,000
Less: 40% tax		(2,64,400)	(98,800)
Average profit after tax		3,96,600	1,48,200
(ii)	Super Profits		
Average trading profit		3,96,600	1,48,200
Less: Normal Profit			
T. Ltd. Rs 21,07,200 x 15%		(3,16,080)	
V. Ltd Rs 7,71,600 x 15%			(1,15,740)
Super Profit		80,520	32,460
(iii)	Value of goodwill at 4 year s' purchase of super profits	3,22,080	1,29,840

Note: It is assumed that investments are made before 2013-2014.

Q21. (PM)

The summarised Balance Sheets of R Ltd. and P Ltd. for the year ending on 31.3.2016 are as under:

	R Ltd.	P Ltd.		R Ltd.	P Ltd.
	Rs	Rs		Rs	Rs
Equity share Capital (in shares of Rs 10 each)	24,00,000	12,00,000	Fixed Assets	55,00,000	27,00,000
8% Preference Share Capital (in shares of Rs 10 each)	8,00,000	-	Current Assets	25,00,000	23,00,000
10% Preference Share Capital (in shares of Rs 10 each)	-	4,00,000			
Reserves	30,00,000	24,00,000			
Current Liabilities	18,00,000	10,00,000			
	80,00,000	**50,00,000**		**80,00,000**	**50,00,000**

The following information is provided:

		R Ltd.	P Ltd.
		Rs	Rs
(1)	Profit before tax	10,64,000	4,80,000
(b)	Taxation	4,00,000	2,00,000
(c)	Preference dividend	64,000	40,000
(d)	Equity dividend	2,88,000	1,92,000

1. The equity shares of both the companies are quoted in the market. Both the companies are carrying on similar manufacturing operations.
2. R Ltd. proposes to absorb P Ltd. as on 31.3.2016. The terms of absorption are as under:
   (a) Preference shareholders of P Ltd. will receive 8% preference shares of R Ltd. sufficient to increase the income of preference shareholders of P Ltd. by 10%.
   (b) The equity shareholders of P Ltd. will receive equity shares of R Ltd. on the following basis:
      (i) The equity shares of P Ltd. will be valued by applying to the earnings per share of P Ltd. 75% of price earnings ratio of R Ltd. based on the results of 2015-2016 of both the companies.
      (ii) The market price of equity shares of R Ltd. is 40 per share.
      (iii) The number of shares to be issued to the equity shareholders of P Ltd. will be based on the above market value.
      (iv) In addition to equity shares, 8% preference shares of R Ltd. will be issued to **the equity shareholders** of P Ltd. **to make up for the loss in income arising from the above exchange of shares based on the dividends** for the year 2015-2016.
   (a) The assets and liabilities of P Ltd. as on 31.3.2016 are revalued by professional valuer as under:

	Increased by Rs	Decreased by Rs
Fixed Assets	1,00,000	-
Current Assets	-	2,00,000
Current Liabilities	-	40,000

For the next two years, no increase in the rate of equity dividend is expected.

You are required to:

(i) Set out in detail the purchase consideration.

(ii) Give the Balance Sheet as on 31.3.2016 after absorption.

Note: Journal entries are not required.

Answer

(i) Computation of Purchase Consideration

		Rs
(a)	Preference Shareholders	
Current income of preference shareholders of P Ltd.		40,000
Add: 10% increase thereof		4,000
		44,000
Preference shares to be issued = 44,000 × 100 ÷ 8		5,50,000
(b)	Equity Shareholders	
(1) Issue of Equity Shares		
Profit before tax of R Ltd.		10,64,000
Less: Tax		(4,00,000)

	6,64,000
Less: Preference dividend	(64,000)
Profit available for equity shareholders of R Ltd.	6,00,000

Basic EPS = Earnings available for Shareholders / Average no. of shares

Earnings per share (EPS) = 6,00,000 ÷ 2,40,000 = Rs 2.50

PE Ratio = Market Price / EPS

Price earnings ratio (P/E) = 40/2.50 =16

EPS of P Ltd.

	Rs
Profit before tax	4,80,000
Less: Tax	(2,00,000)
Profit after tax	2,80,000
Less: Preference dividend	(40,000)
Profit available for equity shareholders	2,40,000

EPS = 2,40,000 /1,20,000 = Rs 2

Valuation of equity shares of P Ltd.

= 1,20,000 shares × (Rs 2 × 16 × 0.75 i.e. Rs 24) = Rs 28,80,000

Number of equity shares to be issued = 28,80,000 / 40 = 72,000

	Rs
(1) Equity Share Capital	7,20,000
Securities Premium	21,60,000
28,80,000	
(2) Issue of Preference Shares to make up loss to equity shareholders	Rs
Current equity dividend	1,92,000
Less: Expected equity dividend from R Ltd. i.e. in proportion of the existing dividend policy (Rs 7,20,000×2,88,000/24,00,000)	(86,400)
Loss in income	1,05,600
(i) 8% Preference Shares to be issued = 1,05,600 / 0.08 = Rs 13,20,000	
Total Purchase Consideration:	Rs
Preference shares to be issued 5,50,000	
13,20,000	18,70,000
Equity shares to be issued (at premium)	28,80,000
	47,50,000

(ii) R Ltd.

Balance Sheet as at 31st March, 2016 (after absorption)

Particulars	**Note No.**	**Amount (Rs)**
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital	1	57,90,000
(b) Reserves and Surplus	2	51,60,000
(2) **Current Liabilities**	3	27,60,000
Total		1,37,10,000
II. Assets		

(1) **Non-current assets**		
(a) Fixed assets		
i. Tangible assets	4	83,00,000
ii. Intangible assets	5	8,10,000
(2) **Current assets**	6	46,00,000
Total		1,37,10,000

Notes to Accounts

		(Rs)	(Rs)
1.	Share Capital		
3,12,000 Equity Shares of Rs 10 each (of the above shares, 72,000 Equity shares are allotted as fully paid up for consideration other than cash)		31,20,000	
2,67,000 8% Preference Shares of Rs 10 each (of the above, 1,87,000 are allotted as fully paid up for consideration other than cash)		26,70,000	57,90,000
2.	Reserves and surplus		
Reserves (As per last Balance Sheet)		30,00,000	
Securities Premium		21,60,000	51,60,000
3.	Current Liabilities		
As per last balance sheet		18,00,000	
Taken over on absorption of P Ltd. Rs (10,00,000-40,000)		9,60,000	27,60,000
4.	Tangible Assets		
As per last Balance Sheet		55,00,000	
Taken over on absorption of P Ltd.		28,00,000	83,00,000
5.	Intangible assets		
Goodwill (See Working Note)		8,10,000	
6.	Current Assets		
As per last Balance Sheet		25,00,000	
Taken over on absorption of P Ltd. Rs (23,00,000-2,00,000)		21,00,000	46,00,000

Working Note:

Calculation of Goodwill on Absorption

	Rs	
Purchase consideration		47,50,000
Fixed assets taken over [27,00,000 + 1,00,000]	28,00,000	
Current assets taken over [23,00,000 – 2,00,000]	21,00,000	
49,00,000		
Less: Current liabilities [10,00,000 – 40,000]	(9,60,000)	
Net assets taken over		(39,40,000)
Goodwill		8,10,000

(Ans.: P.C. 47,50,000; Goodwill 8,10,000; Balance Sheet Total 1,09,50,000/1,37,10,000)

AMALGAMATION IN THE NATURE OF MERGAR

Q22.

Long Ltd. and Short Ltd. were amalgamated on and from 1st April, 1999. A new company Moderate Ltd. was formed to take over the business of the existing companies. The balance sheets of Long Ltd. and Short Ltd as on 31st March, 1999 are given below:

Equity & Liabilities	**Long Ltd.**	**Short Ltd.**
Shareholders Fund:		
Share Capital:		
Equity shares of Rs. 100 each	850	725
14% Pref. Shares of Rs. 100 each	320	175
Reserves and Surplus:		
Revaluation reserve	125	80
General Reserve	240	160
Investment Allowance Reserve	50	30
Profit &Loss A/c	75	52
Non-Current Liabilities:		
13% debentures (Rs. 100 each)	50	28
Unsecured Loan:		
Public deposits	25	-
Current Liabilities:		
Sundry Creditors	145	75
Bill Payable	20	
	19,00	**13,25**
Non Current Assets:	**Long Ltd.**	**Short Ltd.**
Fixed assets:		
Land & Building	460	275
Plant & Machinery	325	210
Investments	75	50
Current Assets:		
Stock	325	269
Sundry Debtors	305	270
Bills receivable	25	-
Cash and Bank	385	251
	19,00	**13,25**

Other information:

1. 13% Debenture holders of Long Ltd. and Short Ltd. are discharged by Moderate Ltd. by issuing such number of its 15% Debentures of Rs. 100 each so as to maintain the same amount of interest.

2. Preference shareholders of the two companies are issued equivalent number of 15% preference shares of Moderate Ltd. at a price of Rs. 125 per share (face value Rs. 100).
3. Moderate Ltd. will issue 4 equity shares for each equity share of Long Ltd. and 3 equity shares for each equity share of Short Ltd. The shares are to be issued @ Rs. 35 each, having a face value of Rs. 10 per share.
4. Investment allowance reserve is to be maintained for two more years.

Prepare the balance sheet of Moderate Ltd. as on 1st April, 1999 after the amalgamation has been carried out on the basis of the following assumption:

(a) Amalgamation is in the nature of merger.

(b) Amalgamation is in the nature of purchase.

(Ans : Balance Sheet Total (i) 32.25 (ii) 33.05; P.C. Long Ltd. 1,590; Short Ltd. 980)

AMALGAMATION – INTER COMPANY HOLDINGS, CROSS HOLDINGS, COMPLEX HOLDINGS:

Q23.		**Old Co.**	**New Co.**
No. of Shares		40,000	50,000
Holding of	Old Co.	-	5,000
	New Co.	4,000	-
Intrinsic Value		20	15

Calculate Purchase Consideration.

(Ans.: Purchase Consideration Rs. 7,40,000/-; Payment to be discharged Rs. 6,40,000/-.)

Q24. (PM – Two Transferor companies holding shares in each other)

AB Ltd. and MB Ltd. decide to amalgamate and to form a new company AM Ltd. The following are their summarised balance sheets as at 31.3.2017: (Rs)

Liabilities	AB Ltd.	MB Ltd.	Assets	AB Ltd.	MB Ltd.
Share Capital			Fixed Assets	7,50,000	2,00,000
(Rs 100) each	10,00,000	6,00,000	Investments:		
General Reserve	1,00,000	50,000	1,500 Shares in MB	3,50,000	–
Investment Allowance			4,000 Shares in AB	–	5,00,000
Reserve	40,000	30,000			
12% Debentures			Current Assets	4,00,000	1,00,000
(Rs 100 each)	3,00,000	1,00,000			
Trade payables	60,000	20,000		________	_______

				—	—
	15,00,000	8,00,000		15,00,000	8,00,000

Calculate the amount of purchase consideration for AB Ltd. and MB Ltd. and draw up the balance sheet of AM Ltd. after considering the following:

(a) Assume amalgamation is in the nature of purchase.

(b) Fixed assets of AB Ltd. are to be reduced by Rs 50,000 and that of MB Ltd. are to be taken at Rs 3,00,000.

(c) 12% debenture holders of AB Ltd. and MB Ltd. are discharged by AM Ltd. by issuing such number of its 15% debentures of RS 100 each so as to maintain the same amount of interest.

(d) Shares of AM Ltd. are of Rs 100 each.

Also show, how the investment allowance reserve will be treated in the Financial Statement assuming the Reserve will be maintained for 3 years.

Answer

Calculation of Purchase consideration

(i) Value of Net Assets of AB Ltd. and MB Ltd. as on 31st March, 2017

	AB Ltd.		**MB Ltd.**	
	(Rs)		**(Rs)**	
Assets taken over:				
Fixed Assets	7,00,000			3,00,000
Current Assets	4,00,000	11,00,000	1,00,000	4,00,000
Less: Liabilities taken over:				
Debentures (WN)	2,40,000			80,000
Trade payables	60,000	(3,00,000)	20,000	(1,00,000)
8,00,000			3,00,000	

(ii) Value of Shares of AB Ltd. and MB Ltd.

AB Ltd. holds 1,500 shares in MB Ltd. i.e. 1/4th of the shares of MB Ltd.

The value of shares of AB Ltd. is Rs 8,00,000 plus 1/4 of the value of the shares of MB Ltd.

MB Ltd. holds 4,000 shares in AB Ltd. i.e. 2/5th of the shares of AB Ltd.

Similarly, the value of shares of MB Ltd. is Rs 3,00,000 plus 2/5 of the value of shares of AB Ltd.

Let 'a' denote the value of shares of AB Ltd. and 'm' denote the value of shares of MB Ltd. then

a = 8,00,000 + 1/4 m; and

m = 3,00,000 + 2/5 a.

Substituting the value of m,

a = 8,00,000 + 1/4 (3,00,000 + 2/5 a)

a = 8,00,000 + 75,000 + 1/10 a

9/10 a = 8,75,000

a = 9,72,222

m = 3,00,000 + 2/5 (9,72,222)

m = 6,88,889

(iii) Amount of Purchase Consideration

	AB Ltd.	MB Ltd.
	Rs	Rs
Total value of shares (as determined above)	9,72,222	6,88,889
Less: Internal investments:		
2/5 for shares held by MB Ltd.		(3,88,889)
1/4 for shares held by AB Ltd.	________	(1,72,222)
Amount due to outsiders	5,83,333	5,16,667

Purchase Consideration will be satisfied by AM Ltd. as follows:

	AB Ltd.	MB Ltd.
	Rs	Rs
In shares (of Rs 100 each)	5,83,300	5,16,600
In cash	33	67

(iv) Net Amount of Goodwill/Capital Reserve

	Rs	Rs
Total Purchase Consideration		
AB Ltd.	5,83,333	
MB Ltd.	5,16,667	11,00,000
Less: Net Assets taken over		
AB Ltd.	8,00,000	
MB Ltd.	3,00,000	(11,00,000)
Nil		

(Alternatively, the calculations may be made separately for both the companies)

Balance Sheet of AM Ltd. as at 31st March, 2017

Particulars	Note No.	Amount (Rs)
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital	1	10,99,900
(b) Reserves and Surplus	2	Nil
(2) **Non-Current Liabilities**		
Long-term borrowings	3	3,20,000
(3) **Current Liabilities**		
Trade payables		80,000
Total		14,99,900
II. Assets		
(1) **Non-current assets**		
(a) Fixed assets		10,00,000
(2) **Current assets**	4	4,99,900
Total		14,99,900

Notes to Accounts

		(Rs)	(Rs)
1.	Share Capital		
10,999 shares of Rs 100 each (All the above shares are allotted as fully paid- up for consideration other than cash)			10,99,900

2.	Reserves and surplus		
Investment Allowance Reserve		70,000	
Amalgamation Adjustment Reserve		(70,000)	Nil
3.	Long Term Borrowings		
15% Debentures (W.N.)			3,20,000
4.	Current assets [4,00,000 + 1,00,000]	5,00,000	
Less: Purchase consideration paid in cash Rs (33+67)		(100)	4,99,900

Working Note:

Calculation of Debentures to be issued

	AB Ltd.	MB Ltd.
12% Debentures	3,00,000	1,00,000
Interest on Debentures @ 12 % (a)	36,000	12,000
AM Ltd. Debentures rate of interest (b)	15 %	15 %
Debenture Value to earn above calculated interest (a/b)	2,40,000	80,000

Q25. (PM)

The following are the summarized Balance Sheets of X Ltd. and Y Ltd. as on 31stMarch, 2017:

	Amount in Rs	
	X Ltd.	**Y Ltd.**
Assets		
Fixed Assets	7,00,000	2,50,000
Inventory	2,40,000	3,20,000
Trade receivables	4,20,000	2,10,000
Cash at Bank	1,10,000	40,000
Investments in:		
6,000 shares of Y Ltd.	80,000	-
5,000 shares of X Ltd.	-	80,000
	15,50,000	**9,00,000**
Liabilities		
Share Capital:		
Equity shares of Rs 10 each	6,00,000	3,00,000
10% preference shares of Rs 10 each	2,00,000	1,00,000
Reserve and Surplus	3,00,000	2,00,000
12% Debentures	2,00,000	1,50,000
Trade payables	2,50,000	1,50,000
	15,50,000	**9,00,000**

Details of Trade payables and Trade receivables:

	X Ltd.	Y Ltd.
Trade payables		
Bills Payable	30,000	25,000
Sundry creditors	2,20,000	1,25,000
	2,50,000	**1,50,000**
Trade receivables		
Debtors	3,60,000	1,90,000

Bills Receivables	60,000	20,000
	4,20,000	**2,10,000**

Fixed assets of both the companies are to be revalued at 15% above book values and inventory and debtors are to be taken over at 5% less than their book values. Both the companies are to pay 10% equity dividends, preference dividends having been paid already.

After the above transactions are given effect to, X Ltd. will absorb Y Ltd. on the following terms:

(i) 8 Equity shares of Rs 10 each will be issued by X Ltd. at par against 6 shares of Y Ltd.

(ii) 10% preference shares of Y Ltd. will be paid off at 10% discount by issue of 10% preference shares of Rs 100 each of X Ltd. at par.

(iii) 12% Debenture holders of Y Ltd. are to be paid off at a 8% premium by 12% debentures in X Ltd. issued at a discount of 10%.

(iv) Rs 30,000 to be paid by X Ltd. to Y Ltd. for liquidation expenses.

(v) Creditors of Y Ltd. include Rs 10,000 due to X Ltd.

Prepare:

(a) A statement of purchase consideration payable by X Ltd.

(b) A Balance Sheet of X Ltd. after its absorption of Y Ltd.

Answer

Total No. of shares of X Ltd. = 6,00,000/10 = 60,000 shares
X Ltd's shares held by Y Ltd. = 5,000 shares
Total No. of shares of Y Ltd. = 3,00,000/10 = 30,000 shares
Y Ltd's shares held by X Ltd. = 6,000 shares
Hence, X Ltd. hold's 1/5th (6,000/30,000) of Y Ltd.'s total shares

(a) Statement of Purchase Consideration payable by X Ltd.

i. **For Equity Shareholders**

8 Equity Shares of X Ltd. for every 6 Equity Shares of Y Ltd.

30,000 shares 6 / 8 x =	40,000 shares
Less:1/5th Share of X Ltd.	(8,000) shares
Balance for outsiders	32,000 shares
Less: 5,000 Shares of X Ltd. already with Y Ltd.	(5,000) shares
Shares to be issued	27,000 shares
Value of 27,000 equity shares at Rs 10	Rs 2,70,000

ii. **For Preference Shareholders**

Preference Share Capital of Y Ltd.	Rs 1,00,000
Less: 10% Discount	Rs 10,000
X Ltd.'s Preference shares to be issued	Rs 90,000

Total Purchase Consideration

Particulars	Numbers	Amount
Equity Shares @ Rs 10 each	27,000	Rs 2,70,000
Preference Shares @ Rs 100 each	900	Rs 90,000
Total Purchase Consideration		Rs 3,60,000

(b) Balance Sheet of X Ltd. after its absorption of Y Ltd.

Particulars	Note No.	Rs
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital	1	11,60,000

(b) Reserves and Surplus	2	3,57,000
(2) **Non-Current Liabilities**		
Long-term borrowings	3	3,80,000
(3) **Current Liabilities**		
Trade payables	4	3,90,000
Total		22,88,000
II. Assets		
(1) **Non-current assets**		
(a) Fixed assets [7,00,000 X 115 % + 2,87,500]		10,92,500
(2) **Current assets**		
(a) Inventories (2,40,000 + 3,04,000)		5,44,000
(b) Trade receivables	5	6,10,500
(c) Cash and cash equivalents	6	41,000
Total		22,88,000

Notes to Accounts

		Rs	Rs
1.	Share Capital		
Equity share capital			
87,000 (60,000 + 27,000) Equity shares of Rs 10 each, fully paid up (Out of the above, 27,000 equity shares have been issued for consideration other than cash)		8,70,000	
20,000 10% Preference shares of Rs 10 each		2,00,000	
900 10% Preference shares of Rs 100 each		90,000	11,60,000
2.	Reserves and Surplus		
Revaluation Reserve [15 % of Rs 7,00,000]		1,05,000	
Capital Reserve (W. N.1)		25,000	
Other Reserves (W.N.4)		2,46,000	
Discount on issue of Debentures [W.N. 5, Calculation (C)]		(18,000)	3,57,000
3.	Long Term Borrowings		
Secured (assumed)			
12% Debentures Existing Add: Issued to Y Ltd. [W.N. 5, Calculation (B)]		2,00,000 1,80,000	3,80,000
4.	Trade payables		
Creditors (2,20,000 + 1,25,000 – 10,000)		3,35,000	
Bills Payable (30,000 + 25,000)		55,000	3,90,000
5.	Trade receivables		
Debtors (3,60,000 + 1,80,500 – 10,000)		5,30,500	
Bills Receivable (60,000 + 20,000)		80,000	6,10,500
6.	Cash & cash equivalents		
Cash at Bank (W.N. 3)			41,000

Working Notes:

1. Calculation of Capital Reserve

Net Assets taken over from Y Ltd.	Rs

Fixed Assets (Rs 2,50,000 × 115%)		2,87,500
Inventory (Rs 3,20,000 x 95%)		3,04,000
Debtors (Rs 1,90,000 x 95%)		1,80,500
Bills Receivable		20,000
Cash at Bank (W.N. 2)		15,000
Total Assets (A)		8,07,000
Liabilities taken over:		
Debentures [W.N. 5, Calculation (A)]		1,62,000
Creditors		1,25,000
Bills Payable		25,000
Total Liabilities	(B)	3,12,000
Net Asset taken over	(A – B)	4,95,000
Less: Investment cancelled (i.e. 5,000 shares held in × Ltd.)		(80,000)
		4,15,000
Purchase Consideration		(3,60,000)
Capital Reserve		55,000
Less: Liquidation expenses reimbursed to Y Ltd.		(30,000)
Capital Reserve		25,000

2. Cash taken over from Y Ltd.

	Rs
Cash balance given in Balance Sheet of Y Ltd.	40,000
Add: Dividend received from X Ltd. (5,000 shares × Rs 1)	5,000
	45,000
Less: Dividend paid (30,000 shares × Rs 1)	(30,000)
	15,000

3. Cash balance in Balance Sheet (after absorption)

	Rs
Cash balance given in Balance Sheet of X Ltd.	1,10,000
Add: Cash taken over from Y Ltd. (W.N. 2)	15,000
	1,25,000
Less: Dividend paid Rs 60,000	
Expenses on liquidation RS 30,000	(90,000)
	35,000
Add: Dividend from Y Ltd.	6,000
	41,000

4. Other Reserves in the Balance Sheet (after absorption)

	Rs
Reserves given in the Balance Sheet of X Ltd.	3,00,000
Add: Dividend from Y Ltd. [6,000 shares X Rs 1)	6,000
	3,06,000
Less: Dividend declared [60,000 shares X Rs 1)	(60,000)
	2,46,000

5. Debenture Holders Payment

Debenture Holders of Y Ltd.	Rs 1,50,000
Add: Premium @ 8 %	Rs 12,000

Value of Debenture Holder Liability taken over by X Ltd. (A)	Rs 1,62,000
Issue Price of X Ltd. Debentures @ 10 % discount [(A) / 90 %] (B)	Rs 1,80,000
Discount on Issue of Debentures (C)	Rs 18,000

6. Inter-company transactions

Creditors of Y Ltd. include Rs 10,000 due to X Ltd.

Therefore, journal entry in the books of X Ltd. will be

Creditors A/c	Dr.	10,000	
To Debtors A/c			10,000

Q26. (PM)

The following are the Balance Sheets of Big Ltd. and Small Ltd. as at 31.3.2017:

(Rs in lakhs)

	Big Ltd.	Small Ltd.		Big Ltd.	Small Ltd.
	Rs	Rs		Rs	Rs
Share Capital	40	15	Sundry Assets (including cost of shares)	56	20
Profit & Loss A/c	7.5	--	Goodwill	4	5
Sundry Creditors	12.5	12.5	Profit and Loss A/c	--	2.5
	60.0	27.5		60.0	27.5

Additional Information:

(ii) The two companies agree to amalgamate and form a new company, Medium Ltd.

(iii) Big Ltd. holds 10,000 shares in Small Ltd. acquired at a cost of Rs 2,50,000 and Small Ltd. holds 5,000 shares in Big Ltd. acquired at a cost of Rs 7,00,000.

(iv) The shares of Big Ltd. are of Rs 100 and are fully paid and the shares of Small Ltd. are of Rs 50 each on which Rs. 30 has been paid-up.

(v) It is agreed that the goodwill of Big Ltd. would be valued at Rs 1,50,000 and that of Small Ltd. at Rs 2,50,000.

(vi) The shares which each company holds in the other are to be valued at book value having regard to the goodwill valuation decided as given in (iv).

(vii) The new shares are to be of a nominal value of Rs 50 each credited as Rs 25 paid.

You are required to:

(ii) Prepare the Balance Sheet of Medium Ltd., as at 31st March, 2017 after giving effect to the above transactions; and

(iii) Prepare a statement showing the shareholdings in the new company attributable to the shareholders of the merged companies.

Answer

(i) Balance Sheet of Medium Ltd. as on 31st March, 2017

Particulars	Note No.	(Rs)
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
Share Capital	1	45,50,000
(2) **Current Liabilities**		
Trade Payables		25,00,000

Total		70,50,000
II. Assets		
(1) **Non-current assets**		
Fixed assets		
Intangible assets	2	4,00,000
(2) **Current assets** (Rs 53,50,000+ Rs 13,00,000)		66,50,000*
Total		70,50,000

Notes to Accounts:

		(Rs in crores)
1.	**Share Capital**	
1,82,000 shares of Rs 50 each, Rs 25 paid up		45,50,000
[Issued for consideration other than cash]		
2.	**Intangible Assets**	
Goodwill (Rs 1,50,000 + Rs 2,50,000)		4,00,000

(ii) Statement of Shareholding in Medium Ltd.

	Big Ltd. Rs	Small Ltd. Rs
Total value of Assets	44,20,513	8,52,564
Less: Pertaining to shares held by the other company	5,52,564	1,70,513
	38,67,949	6,82,051
Rounded off Shares of new company (at Rs 25 per share)	38,67,950 1,54,718	6,82,050 27,282
Total purchase consideration to be paid to Big Ltd and Small Ltd. (Rs 38,67,950 +Rs 6,82,050)		Rs 45,50,000
Number of shares in Big Ltd. (40,00,000/100) Number of shares in Small Ltd. (15,00,000/30) Holding of Small Ltd. in Big Ltd. (5,000/40,000) Holding of Big Ltd. in Small Ltd. (10,000/50,000) Number of shares held by outsiders in Big Ltd. (40,000 – 5,000) =		40,000 shares 50,000 shares 1/8 1/5 35,000
Number of shares held by outsiders in Small Ltd. (50,000 – 10,000)		40,000

❖ Sundry assets are assumed to be current assets.

Working Note:

Calculation of Book Value of Shares

	Big Ltd	Small Ltd.
	Rs	Rs
Goodwill	1,50,000	2,50,000
Sundry Assets other than shares in other company		
(56,00,000 – 2,50,000) (20,00,000 – 7,00,000)	53,50,000	13,00,000
	55,00,000	15,50,000
Less: Sundry Creditors	12,50,000	12,50,000
	42,50,000	3,00,000

If "x" is the Book Value of Assets of Big Ltd and "y" of Small Ltd.

x = 42,50,000 + 1 / 5 y

y = 3,00,000 + 1 / 8 x

x = 42,50,000 + 1 / 5 (3,00,000 + 1 / 8 x)

= 42,50,000 + 60,000 + 1 / 40 x
= 43,10,000 39x40
x = 39/40 x = 43,10,000
x = 44,20,513 (approx.)
y = 3,00,000 +) 44,20,513(81
= 3,00,000 + 5,52,564 = Rs 8,52,564 (approx.)
Book Value of one share of Big Ltd. = 44,20,513 / 40,000 = Rs 110.513 (approx.)
Book Value of one share of Small Ltd. = 8,52,564 / 50,000 = Rs17.05 (approx.)

SPECIAL QEUSTIONS:

Q27. (PM)

The summarized Balance sheets of X Ltd. and its subsidiary Y Ltd. as at 31.3.2016 were as follows:

Liabilities	X Ltd. Rs	Y Ltd. Rs	Assets	X Ltd. Rs	Y Ltd. Rs
Share capital	50,00,000	10,00,000	Fixed assets	60,00,000	18,00,000
(Share of Rs 10 each)			Investment in Y Ltd. (60,000 shares)	6,00,000	---
General reserves	50,00,000	20,00,000	Trade receivables	35,00,000	5,00,000
Profit and Loss account	20,00,000	15,00,000	Inventories	30,00,000	25,00,000
Secured loan	20,00,000	2,50,000	Cash and bank	39,00,000	2,00,000
Current liabilities	30,00,000	2,50,000			
	1,70,00,000	50,00,000		1,70,00,000	50,00,000

X Ltd. holds 60% of the paid-up capital of Y Ltd. and the balance is held by a foreign company.

A memorandum of understanding has been entered into with the foreign company by X Ltd. to the following effect:

(i) The shares held by the foreign company will be sold to X Ltd. at a price per share to be calculated by capitalizing the yield at 15%. Yield, for this purpose, would mean 50% of the average of pre-tax profits for the last 3 years, which were Rs 12 lakhs, 18 lakhs and 24 lakhs respectively. (Average tax rate was 40%).

(ii) The actual cost of shares to the foreign company was Rs 4,40,000 only. Gains accruing to the foreign company are taxable at 20%. The tax payable will be deducted from the sale proceeds and paid to government by X. 50% of the consideration (after payment of tax) will be remitted to the foreign company by X Ltd. and also any cash for fractional shares allotted.

(iii) For the balance of consideration, X Ltd. would issue its shares at their intrinsic value.

It was also decided that X Ltd. would absorb Y Ltd. Simultaneously by writing down the fixed assets of Y Ltd. by 10%. The Balance Sheet figures included a sum of Rs 1,00,000 due by Y Ltd. to X Ltd. and inventory of X Ltd. included inventory of Rs 1,50,000 purchased from Y Ltd., who sold them at cost plus 20%.

The entire arrangement was approved and put through by all concern effective from 1.4.2016.

You are required to prepare a Balance Sheet after absorption of Y Ltd., in the books of X Ltd. Workings should form part of your answer.

Answer

X Ltd.Balance Sheet as at 1st April, 2016

Particulars	Note No.	Amount (Rs)
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital	1	53,35,220
(b) Reserves and Surplus	2	89,63,764
(2) **Non-Current Liabilities**		
Long-term borrowings	3	22,50,000
(3) **Current Liabilities**	4	31,50,000
Total		1,96,98,984
II. Assets		
(1) **Non-current assets**		
(a) Fixed assets		
Tangible assets	5	76,20,000
(2) **Current assets**		
(a) Inventories	6	54,75,000
(b) Trade receivables	7	39,00,000
(c) Cash and cash equivalents		27,03,984
Total		1,96,98,984

Notes to Accounts

		Rs	Rs
1.	Share Capital		
5,33,522 shares of Rs 10 each (Out of the above 33,522 shares of Rs 10 each issued for consideration other than cash)			53,35,220
2.	Reserves and surplus		
General Reserve		50,00,000	
Capital Reserve 13,20,000			
Less: unrealized profit on inventory (Rs 25,000) Profit and Loss Account		12,95,000 20,00,000	
Securities Premium (Rs 33,522×19.95)		6,68,764	89,63,764
3.	Long Term Borrowings		
Secured Loans (Rs 20,00,000 + Rs 2,50,000)			22,50,000
4.	Current Liabilities		

(Rs 30,00,000 + Rs 2,50,000)		32,50,000	
Less: Mutual owing		(1,00,000)	31,50,000
5.	Tangible Assets		
Fixed Assets		78,00,000	
Less : Revaluation loss		(1,80,000)	76,20,000
6.	Inventories (Rs 30,00,000+Rs 25,00,000)		55,00,000
Less: Unrealised profit on inventory		(25,000)	54,75,000
7.	Trade receivables		
Trade receivables (Rs 35,00,000+Rs 5,00,000)		40,00,000	
Less: Mutual owings		(1,00,000)	39,00,000

Working Notes:

(1) Yield of Y Ltd.

Average of Pre Tax Profit = 12 + 18 + 24 / 3 = Rs 18 lakhs

Yield = 18 × 50 / 100 = Rs 9 lakhs

(2) Price per share of Y Ltd:-

Capitalized value of yield of Y Ltd. 9 lakhs × 100 / 15 = Rs 60 lakhs

No. of shares = 1,00,000

Price per share = 60 lakhs /1 lakhs = Rs 60 per share

(3) Purchase consideration for 40% of share capital of Y Ltd.

= 1,00,000 x 60 x 40 / 100 = Rs 24,000

(4) Calculation of intrinsic value of shares of X Ltd.

	Rs	
Total Assets excluding Investments in Y Ltd.		1,64,00,000
Value of Investment 60,000 × Rs 60		36,00,000
		2,00,00,000
Less: Loading on Stock		(25,000)
Less: Outside Liabilities:		
Secured Loan	20,00,000	
Current Liabilities	30,00,000	(50,00,000)
Net Assets		1,49,75,000

Intrinsic value per share = Net Assets / No. of Shares = Rs 1,50,000 / 5,00,000 = Rs 29.95 per shares

❖ By setting the trend, weighted average profit can also be calculated.

(5) Discharge of purchase consideration by X Ltd.

		Equity share capital Rs	Cash Rs	Total Rs
(i)	Payment of Tax (Rs 24 Lakh - Rs 4.40 Lakh) x = 20 / 100	---	3,92,000	3,92,000
(ii)	Issue of shares to foreign company			
	[50% of (24 Lakh – 3.92 Lakh) = 10.04 lakhs			
	No. of shares issued by X Ltd.			

	10,04,000 / 29.05 = 33,522.5375655626 shares			
	Value of shares capital = 33,522 × Rs 29.95 =	10,03,984	---	10,03,984
(iii)	Cash Payment [50% of (Rs 24 Lakh – Rs 3.92 Lakh) = 10.04 lakhs	---	10,04,000	10,04,000
(iv)	Cash for fractional shares = 0.5375626 × Rs 29.95	---	16	16
	Total	10,03,984	13,96,016	24,00,000

(6) Calculation for Goodwill/Capital Reserve to X Ltd.

		Rs
Total of assets as per Balance Sheet of Y Ltd.		50,00,000
Less: 10% Reduction in the value of Fixed Assets (10 × 18,00,000 / 100)		(1,80,000)
		48,20,000
Less: Secured Loan	2,50,000	
Current Liabilities	2,50,000	(5,00,000)
Net Assets		43,20,000
Less: Purchase consideration (outside shareholders)		(24,00,000)
		19,20,000
Less: Investment in Y Ltd. as per Balance Sheet of X Ltd.		(6,00,000)
Capital Reserve		13,20,000

(7) Cash and Bank Balance of X Ltd. after acquisition of shares

	Rs
Opening Balance (X Ltd.)	39,00,000
Cash and Bank Balance of Y Ltd.	2,00,000
	41,00,000
Less: Remittance to the foreign company	(10,04,016)
	30,95,984
Less: T.D.S. paid to Government	(3,92,000)
	27,03,984

(8) Unrealized profit included in inventory of X Ltd. =Rs 1,50,000x20/120= Rs 25,000

Q28 (PM)

The following was the abridged Balance Sheet of X Co. Ltd, as at 31st March, 2016:

Liabilities	Rs	Assets	Rs
Capital: Authorized: 10,000 Equity shares of Rs 100 each	10,00,000	Plant and machinery at depreciated value	8,60,000
		Land	7,00,000
Issued and paid up: 8,000 Equity shares of Rs 100 each, fully paid up	8,00,000	*Current assets* Trade receivables Patents, trademarks and copyrights	 8,00,000 6,00,000

<u>Reserves and surplus:</u> General reserve - 5,00,000 Securities premium - 4,00,000 Profit and loss - 3,60,000	12,60,000		
11% Debentures secured against the assets of the Co.	5,00,000		
Trade payables	4,00,000		
	29,60,000		**29,60,000**

The Company ran two distinct departments utilizing the trademarks and copyrights owned and generated by it. The assets and liabilities of one of the departments as on the date of Balance Sheet were:

	Rs.
Plant and machinery	4,00,000
Land (used for business)	2,00,000
Current assets	2,00,000
Trademarks and copyrights	3,50,000
	11,50,000
Trade payables	2,50,000
Net Assets	**9,00,000**

Due to managerial constraints, X is unable to develop this department. An overseas buyer is interested to acquire this department and after due diligence, offers a consideration of Rs 20,00,000 to the company for transfer of business. The buyer offered to discharge the purchase consideration immediately after 31st March, 2016, in the following manner:

(i) Issue of equity shares of the buyer's company for Rs 10,00,000 nominal value at a premium of 20% over the face value; and

(ii) Payment of the balance consideration in £ Sterling. The exchange rate agreed upon is Rs 80 per £ Sterling. This amount will be retained in London, till the actual takeover of the business is done by the buyer.

(a) Expenses to put through the transaction come to Rs 8,00,000 initially to be incurred by X but to be shared equally by the parties.

(b) The balance value of trademarks, copyrights and patents left with X does not enjoy any market value and has to be written off.

(c) The value of the balance of land in X's possession will be taken at its market value in the books of account. Such a value, determined by an approved valuer, is 200 percent of the book value.

(d) The parties agree that the date of legal ownership of the transferred business shall be 31st March, 2016, though certain formalities may have to be gone through and agree that the actual transfer to the buyer will be affected before 30th April, 2016.

X Co. Ltd to carry on the business in the normal course and account for the profits of the transferred department to the foreign buyer. X made a net profit of Rs 2,40,000 from the whole business for April, 2016; 40 percent of the net profit related to the business of the transferred department.

(e) The shares of the overseas buyer's company were quoted on the London Stock Exchange and on 30th April, 2016 were quoted at 95 percent of their face value.

(f) The cash received by X at London was remitted by it to its Indian banking account on 30th April 2016 when the rupee sterling rate was Rs 75 per UK sterling pound.

Draw the Balance Sheet of X Co. Ltd. as at 30th April, 2016, after the transfer of the business to the overseas buyer.

Answer

Balance Sheet of X Co. Ltd. as at 30th April, 2016 (after demerger)

Particulars	Note No.	(Rs)
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital	1	8,00,000
(b) Reserves and Surplus	2	20,54,000
(2) **Non-Current Liabilities**		
Long-term borrowings	3	5,00,000
(3) **Current Liabilities**		
Trade payables		1,50,000
Total		**35,04,000**
II. Assets		
(1) Non-current assets		
Fixed assets		
Tangible assets	4	14,60,000
(2) Current assets		
(a) Trade receivables (8,00,000-2,00,000)		6,00,000
(b) Current investment		9,50,000
(c) Cash and cash equivalents (W.N.2)		4,94,000
Total		**35,04,000**

Notes to Accounts

		Rs	Rs
1.	Share Capital		
Authorised share capital:			
10,000 Equity shares of Rs 100 each		10,00,000	
Issued share capital:			
8,000 Equity shares of Rs 100 each			8,00,000
2.	Reserves and surplus		
Revaluation reserve (W.N.6)		5,00,000	
General reserve		5,00,000	
Capital reserve (W.N.3)		11,00,000	
Securities Premium		4,00,000	
Profit and Loss Account (W.N.1)		(4,46,000)	20,54,000
3.	Long-term Borrowings		
Secured borrowings			

11% Debentures secured against the assets of the Co.		5,00,000
4. Tangible Assets		
Plant & Machinery at depreciated value (8,60,000-4,00,000)	4,60,000	
Land (W.N.6)	10,00,000	14,60,000

Working Notes:

1. Computation of Profit and Loss Account as on 30th April, 2016

		Rs
Balance as on 31st March, 2016		3,60,000
Add: Profit earned during the month of April, 2016 (W.N.4)		1,44,000
		5,04,000
Less: Expenses on sale of department (share of X Co.) (Rs 8,00,000 x 50%)	4,00,000	
Patents, trademarks and copyrights written off (W.N.5)	2,50,000	
Diminution in the value of investment (W.N.7)	2,50,000	
Loss due to on foreign exchange translation difference (W.N.8)	50,000	(9,50,000)
		(4,46,000)

2. Cash and bank

		Rs
Cash received from Overseas buyer on 30th April, 2016 (£ 10,000 x Rs 75)		7,50,000
Add: Cash reimbursed by Overseas buyer (Rs 8,00,000x50%)		4,00,000
Cash profit earned during the month of April, 2016 by X Co. Ltd. (See Note)		2,40,000
		13,90,000
Less: Expenses on sale of department to overseas buyer	8,00,000	
Share of profit (for April, 2016) paid to Overseas buyer (W.N.4)	96,000	(8,96,000)
		4,94,000

3. Calculation of gain on sale of department and discharge of purchase consideration.

	Rs
Purchase consideration	20,00,000
Less: Net assets sold	9,00,000
Gain on sale of department transferred to capital reserve	11,00,000
Purchase consideration	20,00,000
Less: Discharged by issue of Overseas Buyer's Equity shares of Rs 10,00,000 at 20% premium	12,00,000
Balance discharged in cash i.e. (8,00,000/80) = £ 10,000	8,00,000

4. Profit earned during the month of April, 2016

	Rs
Total profit earned by X Co. Ltd. during the month of April, 2016	2,40,000
Less: 40% Profit of the sold department	96,000
Profit of X Co. Ltd. on the retained department	1,44,000

5. Patents, trademarks and copyrights written off

	Rs
Patents, trademarks and copyrights as per balance sheet of X Co. Ltd.	6,00,000
Less: Patents, trademarks and copyrights taken over by Overseas buyer	(3,50,000)
Patents, trademarks and copyrights written off (charged to Profit and Loss Account)	2,50,000

6. Land

	Rs
Land as per balance sheet of X Co. Ltd.	7,00,000
Less: Land taken over by Overseas buyer	(2,00,000)
Book value of land retained by X Co. Ltd.	5,00,000
Revalued value (200% of book value)	10,00,000
Revaluation reserve (10,00,000-5,00,000)	5,00,000

7. Diminution in the market value of equity shares of Overseas Buyer

	Rs
Nominal value of shares	10,00,000
Issued at 20% Premium	12,00,000
Market value of shares on 30th April, 2016 is 95% of nominal value (10,00,000 x 95%)	9,50,000
Diminution charged to Profit and Loss Account	2,50,000

8. Loss due to foreign exchange translation difference

	Rs
Cash payment by overseas buyer £ 10,000 due on 31st March, 2016 @ Rs 80 per £	8,00,000
Exchange rate on 30th April, 2016 is Rs 75 per £ Less: Amount remitted in Indian Currency (£ 10,000 x Rs 75)	(7,50,000)
Loss on foreign exchange translation transferred to Profit and Loss Account	50,000

Note:

1. The above solution has been given on the assumption that X Co. Ltd intends to hold investment in shares of overseas buyer as temporary investment. Therefore, its carrying value has been shown in the balance sheet at market value and reduction to market value has been included in the profit and loss account. In case it is assumed as long term investment, then investment in shares of Overseas buyer will be shown at cost i.e. Rs 12,00,000 and Profit and Loss account balance will be Rs 9,04,000. The Balance Sheet total will be Rs 37,54,000.
2. It is also assumed that the profit earned during the month of April, 2016 is entirely the cash profit and also the amount of current assets and current liabilities of X Co. Ltd. has been same as on 31.3.2016.

Q29. (PM)

Small Ltd. and Little Ltd., two companies in the field of speciality chemicals, decided to go in for a follow on Public Offer after completion of an amalgamation of their businesses. As per agreed terms initially a new company Big Ltd. will be incorporated on 1st January, 2017 with an authorized capital of Rs 2 crore comprised of 20 lakh equity shares of Rs 10 each. The holding company would acquire the entire equity shareholding of Small Ltd. & Little Ltd. and in turn would issue its shares to the outside holders of these shares. It is also agreed that the consideration would be a multiple of the average P/E ratio for the period 1st January, 2016 to 31st March, 2016 times the rectified profits of each company, subject to necessary adjustments for complying with the terms of the share issue.

The following information is supplied to you:

	Small Ltd.	Little Ltd.
Ordinary Shares of Rs 10 each (Nos.)	40 lakhs	20 lakhs
10% Preference shares of Rs 100 each (Nos.)	2 lakhs	Nil
10% Preference shares of Rs 10 each (Nos.)	Nil	2 lakhs
5% debentures of Rs 10 each (Nos.)	4 lakhs	4 lakhs
Investments Held		
(a) 4 lakh ordinary shares in Small Ltd.	-	Rs 40 lakhs
(b) 2 lakh ordinary shares in Little Ltd.	Rs 20 lakhs	-
Profit before Interest& Tax (PBIT) after considering impact of Inter-company Transactions and Holdings.	Rs 50 lakhs	Rs 25 lakhs
Average P/E ratio January, 2016 to March, 2016	10	8

The following additional information is also furnished to you in respect of adjustments required to the profit figure as given above:

1. The profits of the respective companies would be adjusted for half the value of contingent liabilities as on 31st March, 2016.
2. Trade receivables of Small Ltd. include an irrecoverable amount of Rs 2 lakh against which Rs 1 lakh was recovered but kept in Advance account.
3. Little Ltd. had omitted to provide for increased FOREX liability of US$ 10,000 on loan availed in financial year 2015-2016 for purchase of Machinery. The machinery was acquired on 1st January, 2016 and put to use in financial year 2016-2017. The additional liability arose due to change in exchange rates and is arrived at in conformity with prevailing provisions of AS 11. The exchange rate is US $ 1 = INR 50.
4. Small Ltd. has omitted to invoice a sale that took place on 31st March, 2016 of goods costing Rs 2,50,000 at a mark-up of 15 per cent instead the goods were considered as part of closing inventory.
5. Closing Inventory of Rs 45 lakhs of Little Ltd. as on 31st March, 2016 stands undervalued by 10 per cent.
6. Contingent liabilities of Small Ltd. and Little Ltd. as on 31st March, 2016 stands at Rs 5 lakhs and Rs 10 lakhs respectively.

The terms of the share issue are as under:

(i) Shares in Big Ltd. will be issued at a premium of Rs 13 per share for all external shareholders of Small Ltd. The Premium will be Rs 15 per share for shares in Big Ltd. issued to all external shareholders of Little Ltd.

(ii) No shares in Big Ltd. will be issued in lieu of the investments (intercompany holdings) of both companies. Instead the shares so held shall be transferred to Big Ltd. at the close of the financial year ended 31st March, 2017 at Par Value consideration payable on date of transfer.

(iii) Big Ltd. would in addition to the issue of shares to outside shareholders of Small Ltd. and Little Ltd. make a preferential allotment on 31st March, 2017 of 2 lakhs ordinary shares at a premium of Rs 28 per share to Virgin Capital Ltd. (VCL). These shares will not be eligible for any dividends declared or paid till that date.

(iv) Big Ltd. will go in for a 18 per cent unsecured Bank overdraft facility to meet incorporation costs of Rs 16 lakhs and towards management expenses till 31st March, 2017 estimated at Rs 14 lakhs. The overdraft is expected to be availed on 1st February, 2017 and closed on 31st March, 2017 out of the proceeds of the preferential allotment.

(v) It is agreed that interim dividends will be paid on 31.03.2017 for the period January, 2017 to March, 2017 by Big Ltd. at 2 per cent; Small Ltd. at 3 per cent and Little Ltd. at 2.5 per cent. Ignore Dividend Distribution tax.

(vi) The prevailing Income Tax Rate is 25 per cent.

You are required to compute the number of shares to be issued to the shareholders of each of the companies and prepare the projected Profit and Loss Account for the period from 1st January, 2017 to 31.03.2017 of Big Ltd. and its Balance Sheet as on 31st March, 2017.

Answer

Computation of number of shares issued

Calculation of Rectified Profits and Purchase consideration

	Rs	Rs
Small Ltd.		
Given profits		50,00,000
Less: Irrecoverable Trade receivables	1,00,000	
50% Contingent Liability	2,50,000	(3,50,000)
		46,50,000
Add: Profit on omitted sale (15% of Rs 2,50,000)		37,500
		46,87,500
Less: Debenture interest (4,00,000 x Rs 10 x 5 %)		(2,00,000)
		44,87,500
Less: Income Tax @ 25%		(11,21,875)
Profits after Tax (PAT)		**33,65,625**
Less: Preference Dividend (10% of Rs 2,00,00,000)		(20,00,000)
Rectified Profits		**13,65,625**
Average PE ratio = 10		
Total consideration for all equity shareholders (Average PE ratio × Profit)		1,36,56,250
Less:10% thereof for shareholders of Little Ltd. [As Little Ltd. holds 4 lakhs out of 40 lakhs shares of Small Ltd.]		(13,65,625)
Balance available for other shareholders of Small Ltd. [A]		**12290625**
Little Ltd.		
Given profits		25,00,000
Less: Increase in FOREX liability (US$10,000 × 50) *	5,00,000	
50% Contingent Liability	5,00,000	(10,00,000)

		15,00,000
Add: Undervaluation of inventory (45,00,000×10/90)		5,00,000
		20,00,000
Less: Debenture interest (4,00,000 × Rs 10 × 5%)		(2,00,000)
		18,00,000
Less: Income Tax @ 25%		(4,50,000)
Profits after Tax (PAT)		13,50,000
Less: Preference Dividend (10% of Rs 20,00,000)		(2,00,000)
Rectified Profits		**11,50,000**
Average PE ratio		8
Total consideration for all equity shareholders (Average PE ratio × Profit)		92,00,000
Less:10% thereof for shareholders of Small Ltd. [As Small Ltd. holds 2 lakhs out of 20 lakhs shares of Little Ltd.]		(9,20,000)
Balance available for other shareholders of Little Ltd. [B]		**82,80,000**

Statement showing Disposal of Purchase Consideration

	Small Ltd.	**Little Ltd.**	**Total**
	Rs	**Rs**	**Rs**
Purchase Consideration	1,22,90,625 [A] above	82,80,000 [B] above	2,05,70,625
Number of shares [Purchase consideration/(Face Value + Securities Premium)]	5,34,375	3,31,200	8,65,575
Share Capital	53,43,750	33,12,000	86,55,750
Securities Premium	69,46,875	49,68,000	1,19,14,875
Purchase Consideration	1,22,90,625	82,80,000	2,05,70,625

❖ As per para 46 and 46A of AS 11 as per the Companies (Accounting Standards) Rules, 2006, the Companies have the option to treat the exchange difference on long-term foreign currency monetary items i.e. they can be added to or deducted from the cost of the asset. It is assumed, that this option has not been exercised, hence the exchange difference been taken to profit and loss. Other alternative is also possible.

Projected Statement of Profit and Loss of Big Ltd. for the period 1st January, 2017 to 31st March, 2017

Particulars	**Note No.**	**Rs**
I. Revenue from operations		___
II. Other income	5	17,00,000
III. Total Revenue(I+II)		17,00,000
IV. Expenses:		
Employee benefits expense	7	14,00,000
Finance costs	6	90,000
Other expenses	8	16,00,000
V. Total expenses		30,90,000
VI. Loss for the period (V - III)		(13,90,000)

Projected Balance Sheet of Big Ltd. as on 31st March, 2017

Particulars	Note No.	(Rs)
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital	1	1,06,55,750
(b) Reserves and Surplus	2	1,59,51,760
Total		**2,66,07,510**
II. Assets		
(1) **Non-current assets**		
Non-current investments	3	2,65,70,625
(2) **Current assets**		
Cash and cash equivalents	4	36,885
Total		**2,66,07,510**

Notes to Accounts

		(Rs)	(Rs)
1.	Share Capital		
Authorised			
20 lakhs shares of Rs 10 each		2,00,00,000	
Issued & Paid up			
10,65,575 shares of Rs 10 each (out of the above 8,65,575 shares have been issued for consideration other than cash)		1,06,55,750	1,06,55,750
2.	Reserves and surplus		
Securities Premium (Rs 1,19,14,875 + 56,00,000)			1,75,14,875
Loss for the period		(13,90,000)	
Less: Dividend (2% of Rs 86,55,750)		(1,73,115)	(15,63,115)
Balance of Profit and Loss Account carried forward			1,59,51,760
3.	Non-current investments		
Shares in Subsidiaries (W.N. 4)			2,65,70,625
4.	Cash and cash equivalents		
Cash at Bank (W.N. 3)			36,885
5.	Other income		
Dividends received from Subsidiaries (Rs 12,00,000 + 5,00,000)			17,00,000
6. Finance costs			
Interest on Bank O/D			90,000
7.	Employee benefits expenses		
Management expenses			14,00,000
8.	Other expenses		
Preliminary expenses*			16,00,000

❖ As per para 56 of AS 26, 'Intangible Assets', preliminary expenses are to be recognized as expenses as and when they are incurred.

Working Notes:

1. Shares issued by Big Ltd. to Virgin capital Ltd. (VCL)

Number of shares issued	2,00,000
Face Value of Share Capital @ ` 10 each	Rs 20,00,000
Securities Premium @ ` 28 each	Rs 56,00,000
Total cash received from VCL	Rs 76,00,000

2. Overdraft of Big Ltd. as on 31.3.2017

	Rs
Towards Incorporation expenses i.e. preliminary expenses	16,00,000
Towards Management expenses	14,00,000
Total Bank Overdraft availed	30,00,000
Interest @ 18% p.a. for 2 months	90,000

3. Bank balance of Big Ltd. as on 31.3.2017

Bank Account of Big Ltd.

		Rs			Rs
01.02.2017	To Overdraft	30,00,000	01.02.2017	By Incorporation expenses	16,00,000
31.03.2017	To VCL	76,00,000	31.03.2017	By Management expenses	14,00,000
31.03.2017	To Dividend Small	12,00,000*	31.03.2017	By Interest on Overdraft	90,000
	Little	5,00,000†	31.03.2017	By Overdraft	30,00,000
			31.03.2017	By Dividend paid	1,73,115‡
			31.03.2017	By Shares in Small Ltd. bought from Little Ltd.	40,00,000
			31.03.2017	By Shares in Little Ltd. bought from Small Ltd.	20,00,000
				By Balance c/d (Bal. fig.)	36,885
		1,23,00,000			1,23,00,000

*(40,00,000 x 10) x 3% = 12,00,000.

† (20,00,000 x 10) x 2.5% = 5,00,000.

‡ [(5,34,375 + 3,31,200) x 10] x 2% = 1,73,115.

4. Investments of Big Ltd. in Projected Balance Sheet

	Rs
Purchase consideration paid for acquiring shares of outside holders of-	
Small Ltd	1,22,90,625
Little Ltd.	82,80,000
Consideration paid in cash for acquiring cross holdings	
From Small Ltd. (shares of Little Ltd.)	20,00,000
From Little Ltd. (shares of Small Ltd.)	40,00,000
	2,65,70,625

Q30. (PM)

The following are the summarized Balance Sheets of Andrew Ltd. and Barry Ltd., as at 31.12.2016:

Andrew Ltd.

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

Barry Ltd.

Liabilities	Amount (Rs '000)	Assets	Amount (Rs '000)
Share capital		Fixed assets	6,800
1,00,000 Equity shares of Rs 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 Charlie Ltd., is formed to take over their businesses. The following information is given:

i. All Current assets of two companies, except pledged inventory are taken over by Charlie Ltd. The realisable value of all current assets are 80% of book values in case of Andrew Ltd. and 70% for Barry Ltd. Fixed assets are taken over at book value.

ii. The break-up of Current liabilities is as follows:

	Andrew Ltd. Rs	Barry Ltd. Rs
Statutory liabilities (including Rs 22 lakhs in case of Andrew 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.

iii. Secured loans include Rs 16,00,000 accrued interest in case of Barry Ltd.

iv. 2,00,000 equity shares of Rs 10 each are allotted by Charlie Ltd. at par **against cash payment** of entire face value to the shareholders of Andrew Ltd. and Barry Ltd. in the ratio of shares held by them in Andrew Ltd. and Barry Ltd.

v. Preference shareholders are issued Equity shares worth Rs 2,00,000 in lieu of present holdings.

vi. Secured loan payables agree to continue the balance amount of their loans to Charlie Ltd. after adjusting value of pledged security in case of Andrew Ltd. and after waiving 50% of interest due in the case of Barry Ltd.

vii. Unsecured loans are taken over by Charlie Ltd. at 25% of Loan amounts.

viii. Employees are issued fully paid Equity shares in Charlie Ltd. in full settlement of their dues.

ix. Statutory liabilities are taken over by Charlie Ltd. at full values and trade payables are taken over at 80% of the book value.

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

Answer

Balance sheet of Charlie Ltd. as at 31st December, 2016

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

Notes to Accounts

			(Rs 000)
1.	Share Capital		
Issued, subscribed & Paid up:			
7,00,000 equity shares of Rs 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 (Rs 1,280 + Rs 7,200) – W.N. 2		8,480	
Unsecured Loans (25% of Rs 8,600)		2,150	10,630

3.	Trade Payables (W.N.1)		
Andrew Ltd.		4,000	
Barry Ltd.		1,440	5,440
4.	Tangible Assets		
Fixed Assets (Rs 3,400 + Rs 6,800)			10,200
5.	Intangible assets		
Goodwill (W.N.4)			9,470
6.	Other Current Assets		
Andrew Ltd.		2,880	
Barry Ltd.		6,720	9,600
7.	Other Current liabilities		
Andrew Ltd.		7,200	
Barry Ltd.		1,000	8,200

Working Notes:

1. Value of trade payables taken over by Charlie Ltd. (Rs '000)

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

2. Value of total liabilities taken over by Charlie Ltd.

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

3. Assets taken over by Charlie Ltd. (` '000)

	Andrew Ltd. Rs	**Barry Ltd. Rs**
Fixed Assets	3,400	6,800
Current Assets 80% and 70% respectively of book value	2,880	6,720
	6,280	13,520

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

Liabilities taken over (W.N. 2)	17,630	11,440
Equity shares to be issued to Preference Shareholders	200	-
A	17,830	11,440
Less: Total assets taken over (W.N. 3) B	(6,280)	(13,520)

A-B	11,550	(2,080)
Goodwill		Capital Reserve
Net Goodwill	9,470	

5. Equity shares issued by Charlie 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	20,000	5,00,000
			7,00,000
Value of shares (Rs 10 x 7,00,000)		Rs 70 lakhs	

PART 2 – DEMERGER

Q31: (PM)

The summarized Balance Sheet of Z Ltd. as at 31st March, 2016 is given below. In it, the respective shares of the company's two divisions namely S Division and W Division in the various assets and liabilities have also been shown.

(Rs in crores)

	S Division	W Division	Total
Fixed Assets:			
Cost	875	249	
Less: Depreciation	(360)	(81)	
Written-down value	515	168	683
Investments	-	97	97
Net Current assets:			
Current Assets	445	585	
Less: Current Liabilities	(270)	(93)	
	175	492	667
			1,447
Financed by:			
Loan funds	-	15	417
Own funds:			
Equity share capital: Shares of Rs 10 each			345
Reserves and surplus			685
			1,447

Loan funds included, inter alia, Bank Loans of Rs 15 crores specifically taken for W Division and Debentures of the paid up value of Rs 125 crores redeemable at any time between 1st October, 2015 and 30th September, 2016.

On 1st April, 2016 the company sold all of its investments for Rs 102 crores and redeemed all the debentures at par, the cash transactions being recorded in the Bank Account pertaining to S Division.
Then a new company named Y Ltd. was incorporated with an authorized capital of Rs 900 crores divided into shares of Rs 10 each. All the assets and liabilities pertaining to W Division were transferred to the newly formed company; Y Ltd. allotting to Z Ltd.'s shareholders its **two** fully paid equity shares of Rs. 10 each **at par** for **every fully paid** equity share of Rs 10 each held in Z Ltd. as discharge of consideration for the division taken over.

Y Ltd. recorded in its books the fixed assets at Rs 218 crores and all other assets and liabilities at the same values at which they appeared in the books of Z Ltd.
You are required to:
(i) Show the journal entries in the books of Z Ltd.
(ii) Prepare Z Ltd.'s Balance Sheet immediately after the demerger and the initial Balance Sheet of Y Ltd.
(iii) Calculate the intrinsic value of one share of Z Ltd. immediately before the demerger and immediately after the demerger; and
(iv) Calculate the gain, if any, per share to the shareholders of Z Ltd. arising out of the demerger.

Answer

(i) Journal Entries in Z Ltd.'s books (Rs in crores)

	Dr. Amount	Cr. Amount
Bank Account (Current Assets) Dr.	102	
To Investments		97
To Profit and Loss Account (Reserves and Surplus)		5
(Sale of investments at a profit of Rs 5 crores)		
Debentures (Loan Funds) Dr.	125	
To Bank Account (Current Assets)		125
(Redemption of debentures at par)		
Current Liabilities Dr.	93	
Bank Loan (Loan Funds) Dr.	15	
Provision for Depreciation Dr.	81	
Reserves and Surplus (Loss on Demerger) Dr.	645	
To Fixed Assets		249
To Current Assets		585
(Assets and liabilities pertaining to W Division taken out of the books on transfer of the division to Y Ltd.)		

(ii)

(a) Z Ltd.'s Balance Sheet after demerger

Particulars	Note No.	(Rs in crores)
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital		345

(b) Reserve and Surplus	1	45
(2) **Non-Current Liabilities**		
Long-term borrowings	2	277
(3) **Current Liabilities**		270
Total		937
II. Assets		
(1) **Non-current assets**		
Fixed assets		
Tangible assets		515
(2) **Current assets**	3	422
Total		937

Notes to Accounts:

	(Rs in crores)
1. Reserves and Surplus	
Balance as on 31st March, 2016	685
Add: Profit on sale of investments	5
	690
Less: Loss on demerger	(645)
Balance shown in balance sheet after demerger (gain)	45
2. Loan Funds	
Balance as on 31st March, 2016	417
Less: Bank Loan transferred to Y Ltd. 15	
Debentures redeemed 125	(140)
Balance shown in balance sheet after demerger	277
3. Current Assets	
Balance as on 31st March, 2016	445
Add: Cash received from sale of investments	102
	547
Less: Cash paid to redeem debentures	(125)
Balance in balance sheet after demerger	422

(b) Initial Balance Sheet of Y Ltd.

Particulars	**Note No.**	**(Rs in crores)**
I. **Equity and Liabilities**		
(1) **Shareholder's Funds**		
(a) Share Capital	1	690
(b) Reserves and Surplus	2	5
(2) **Non-Current Liabilities**		
Long-term borrowings	3	15
(3) **Current Liabilities**		93
Total		803
II. Assets		
(1) **Non-current assets**		
Fixed assets (Revalued)		218
(2) **Current assets**		585
Total		803

Notes to Accounts:

1. Share Capital

	(Rs in crores)
Authorised capital	
90 crores Equity shares of Rs 10 each	900
Issued and subscribed capital	
69 crores Equity shares of Rs 10 each (issued for consideration other than cash)	690

2. Reserves and Surplus

		(Rs in crores)
Capital Reserve		
Purchase consideration		690
Less: Assets transferred*	710	
Loan funds transferred	(15)	(695)
Capital reserve		5

* The fixed assets have been recorded at 218 crores instead of 168 crores as in the books of Z Ltd before demerger. Therefore, Y Ltd. makes a capital profit of 5 crores whereas Z Ltd is having a capital gain of 45 crores.

3. Long-term borrowing

Loan Funds	15

(iii) Calculation of intrinsic value of one share of Z Ltd.

Particulars	Before demerger (Division S and W)	After demerger (Division S)
Fixed Assets	683	515
Net Current Assets	(667-125+102) 644	(175-125+102) 152
Total Assets	1,327	667
Less: Loan Funds	(292)	(277)
	(417-125)	(417-125-15)
Net Asset Value	1,035	390
No. of share	34.5	34.5
Intrinsic Value per share	Rs 30/Share	Rs 11.30/Share

Intrinsic Value of one share = Rs 390/34.5 crores = Rs 11.30 per share

(iv) Gain per share to Shareholders:

After demerger, for every share in Z Ltd. the shareholder holds 2 shares in Y Ltd.

	Rs
Value of one share in Z Ltd.	11.30
Value of two shares in Y Ltd. Value per share = (Net Assets / No. of shares i.e.695/69 = Rs 10.07× 2)	20.14
	31.44
Less: Value of one share before demerger	(30.00)
Gain per share	1.44

The gain per share amounting Rs 1.44 is due to appreciation in the value of fixed assets by Y Ltd.

PART 3 – SALE OF UNITS

Q32: (PM)

Ksha Ltd. and Yaa Ltd. are two companies. On 31st March, 2016 their summarised Balance Sheets were as under:

(Rs in crores)

	Ksha Ltd.		**Yaa Ltd.**	
	Rs	**Rs**	**Rs**	**Rs**
Sources of funds:				
Share Capital:				
Authorised:		500		500
Issued: Equity shares of Rs 10 each fully paid up		300		200
Reserves and surplus:				
Capital reserves	40		20	
Revenue reserves	700		425	
Surplus	10	750	5	450
Owners' funds		1,050		650
Loan funds		250		350
		1,300		**1,000**
Fund employed in:				
Fixed assets:				
Cost	1,000		700	
Less: Depreciation	(400)	600	(300)	400
Net current assets:				
Current assets	2,000		1,500	
Less: Current liabilities	(1,300)	700	(900)	600
		1,300		**1,000**

Ksha Ltd. has 2 divisions, very profitable division A and loss making division B.
Yaa Ltd. similarly has 2 divisions, very profitable division C and loss making division D.

The two companies decided to reorganize. Necessary approvals from trade payables and members and sanction by High Court have been obtained to the following scheme:

1. Division B of Ksha Ltd. which has fixed assets costing Rs 400 crores (written down value Rs 160 crores), Current assets Rs 900 crores, Current liabilities Rs 750 crores and loan funds of Rs 200 crores is to be transferred at Rs 125 crores to Yaa Ltd.
2. Division D of Yaa Ltd. which has fixed assets costing Rs 500 crores (depreciation Rs 200 crores), Current assets Rs 800 crores, Current liabilities Rs 700 crores, and loan funds Rs 250 crores is to be transferred at Rs 140 crores to Ksha Ltd.

3. The difference in the two considerations is to be treated as loan carrying interest at 15% per annum.
4. The directors of each of the companies revalued the fixed assets taken over as follows:

(i) Division of D of Yaa Ltd. taken over: Rs 325 crores.
(ii) Division B of Ksha Ltd. taken over: Rs 200 crores.

All the other assets and liabilities are recorded at the balance sheet values.

(a) The directors of both the companies ask you to prepare the balance sheets after reconstruction (showing the corresponding figures before reconstruction).

(b) Master Richie Rich, who owns 50,000 equity shares of Ksha Ltd. and 30,000 equity shares of Yaa Ltd. wants to know whether he has gained or lost in terms of net asset value of equity shares on the above reorganizations.

Answer

(a) Ksha Ltd. Balance Sheet as at 31st March, 2016

Particulars	Note No.	After reconstruction (Rs in crores)	Before reconstruction (Rs in crores)
I. Equity and Liabilities			
(1) **Shareholder's Funds**			
(a) Share Capital	1	300	300
(b) Reserve and Surplus	2	800	750
(2) **Non-Current Liabilities**			
Long-term borrowings	3	315	250
(3) **Current Liabilities**		1,250	1,300
Total		2,665	2,600
II. Assets			
(1) **Non-current assets**			
(a) Fixed assets			
Tangible assets	4	765	600
(2) **Current assets**		1,900	2,000
Total		2,665	2,600

Notes to Accounts

Particulars	After reconstruction (Rs in Crores)		Before reconstruction (Rs in Crores)	
1. Share Capital				
Authorised:				
50 crores equity shares of Rs 10 each Issued and subscribed:		500		500
30 crores equity shares of Rs 10 each fully paid up		300		300
2. Reserves and surplus				
Capital reserves	40		40	
Add: Capital profit on reconstruction [WN 1(ii & iii)]	50		-	
Revenue reserves			700	700
Surplus	10	800	10	750
3. Long term Borrowings				
Yaa Ltd. (Interest @ 15% p.a.) [WN 1(i)]	15			

Others	300	315		250
4. **Fixed assets**				
Gross block	925		1,000	
Less: Depreciation	(160)		(400)	
Net block		765		600

Yaa Ltd. Balance Sheet as at 31st March, 2016

Particulars	Note No.	After reconstruction (Rs in Crores)	Before reconstruction (Rs in Crores)
I. Equity and Liabilities			
(1) **Shareholder's Funds**			
(a) Share Capital	1	200	200
(b) Reserves and Surplus	2	465	450
(2) **Non-Current Liabilities**			
Long-term borrowings		300	350
(3) **Current Liabilities**		950	900
Total		1,915	1,900
II. Assets			
(1) **Non-current assets**			
Fixed assets			
Tangible assets	3	300	400
Long term loans and advances	4	15	-
(2) **Current assets**			
Other current assets		1,600	1,500
Total		1,915	1,900

Notes to Accounts

Particulars	After reconstruction (Rs in crores)		Before reconstruction (Rs in crores)	
1. **Share Capital**				
Authorized:				
50 crores equity shares of Rs 10 each		500		500
Issued and subscribed:				
20 crores equity shares of Rs 10 each fully paid up		200		200
2. **Reserves and surplus**				
Capital reserves	20		20	
Add: Capital profit on reconstruction [WN 1(ii)]	15	35	-	20
Revenue reserves		425		425
Surplus		5		5
		465		450
3. **Tangible assets:**				
Gross block	400		700	
Less: Depreciation	(100)		(300)	
Net block		300		400

4.	Long-term loans and advances				
Loan to Ksha Ltd.[WN 2(i)]			15		----

(b) Net asset value of Master Riche Rich's holdings

	Pre-reorganisation	Post-reorganisation	Change (Gain)
	(Rs)	(Rs)	(Rs)
Net asset value of one equity share:			
(Refer to working notes)			
Ksha Ltd.	35.00	36.67	1.67
Yaa Ltd.	32.50	33.25	0.75
Net asset value of equity shares owned by Master Riche Rich			
Ksha Ltd. (50,000 shares)	17,50,000	18,33,500	83,500
Yaa Ltd. (30,000 shares)	9,75,000	9,97,500	22,500
	27,25,000	28,31,000	1,06,000

Master Riche Rich has gained in terms of net asset value of his holdings as indicated in the last column.

Working Notes:

3. Ksha Ltd. (Rs in crores)

	Pre-re-organisation figures	Sale of division B	Purchase of division D of Yaa Ltd.	Post-re-organisation figures
	(a)	(b)	(c)	(d) = (a) – (b) + (c)
(i) Fixed assets:				
Cost	1,000	400	325	925
Depreciation	(400)	(240)	-	(160)
Written down value (I)	600	160	325	765
Current assets	2,000	900	800	1,900
Current liabilities	(1,300)	(750)	(700)	(1,250)
Net current assets (II)	700	150	100	650
Funds employed [(I) + (II)]	1,300	310	425	1,415
Loan funds:				
Others (III)	(250)	(200)	(250)	(300)
Yaa Ltd. (balance payable on transfers of divisions i.e. Rs 140 – Rs 125) (IV)				(15)
Net worth (I + II – III – IV)	1,050	110	175	1,100

Calculation of Profit/(Loss) on Division sale and purchase

(ii)	Sale of division B	(Rs in crores)
Transfer price		125
Cost of the division (Rs 160 + Rs 150 – Rs 200)		(110)
Capital Profit		15
(iii)	Purchase of division D of Yaa Ltd.	
Agreed value of assets less liabilities taken over Rs (325 +		175

800-700 – 250)	
Less: Transfer price	(140)
Capital Profit	35
(iv) Pre-reorganisation net worth	1,050
Add: Capital profit on	
Sale 15	
Acquisition 35	50
Post-reorganisation net worth	1,100

No. of equity shares — 30 crores

Net asset value of equity share: — Rs

Pre-reorganisation — 1,050/30 = 35.00

Post-reorganisation — 1,100/30 = 36.67 (rounded off)

4. Yaa Ltd.

(i) (Rs in crores)

	Pre-re-organisation figures	**Sale of division D**	**Purchase of division B of Ksha Ltd.**	**Post-re-organisation figures**
	(a)	**(b)**	**(c)**	**(d) = (a) – (b) + (c)**
Fixed assets:				
Cost	700	500	200	400
Depreciation	(300)	(200)	–	(100)
Written down value (I)	400	300	200	300
Current assets	1,500	800	900	1,600
Current liabilities	(900)	(700)	(750)	(950)
Net current assets (II)	600	100	150	650
Funds employed [(I) + (II)]	1,000	400	350	950
Loan funds-others (III)	(350)	(250)	(200)	(300)
650		150	150	650
Ksha Ltd. (balance on account of transfers of divisions) (IV)	-	-	-	15
Net worth (I + II – III + IV)	650	150	150	

(ii) (Rs in crores)

	Purchase of division B of Ksha Ltd.		**Sale of division D**
Value of assets less liabilities			
(Value to Yaa Ltd.) (200 + 900 – 750 – 200)	150	(300 + 800 – 700 – 250)	150
Less: Transfer Price		(125)	(140)
Capital Profit/(Capital Loss)		25	(10)

(i) (Rs in crores)

Pre-reorganisation net worth		650
Add: Capital profit - on acquisition	25	
- Sale	(10)	15
Post-reorganisation net worth		665

No. of equity shares 20 crores

Net asset value of equity share: Rs

Pre-reorganisation 650/20 = 32.50

Post-reorganisation 665/20 = 33.25

Important Notes:

CONSOLIDATION OF FINANCIAL STATEMENTS OF GROUP COMPANIES

Basics, Cost of Control, AOP, Minority Interest

Q33. **Balance Sheet 31-3-2012**

Equity & Liabilities	**H**	**S**
Share capital	1,50,000	1,00,000
Profit & Loss a/c	40,000	30,000
Current Liabilities:		
Creditors	30,000	20,000
	2,20,000	**1,50,000**
Assets	**H**	**S**
Non Current Assets:		
Fixed assets	1,00,000	60,000
Investment in Subsidy. 80% share	50,000	
Current Assets	70,000	90,000
	2,20,000	**1,50,000**

H Ltd. had purchased 80% share of S Ltd. on 31.3.12 Prepare consolidated Balance sheet.

(Answer: COC: 54000 and MI: 26000)

Q34. **Balance Sheet 31.3.2012**

Equity & Liabilities	**H**	**S**
Shareholder Funds:		
Share capital	2,00,000	1,00,000
Profit & Loss a/c	70,000	30,000
Current Liabilities:		
Creditors	60,000	20,000
	3,30,000	**1,50,000**
	H	**S**
Non Current Assets:		
Fixed Assets	1,00,000	1,20,000
Investment 60%	1,90,000	-
Current Assets	40,000	30,000
	3,30,000	**1,50,000**

H Ltd Purchases investment on on 1-4-2011 when Balance in Profit & Loss a/c of S Ltd. was Rs. 18,000. Prepare consolidated Balance Sheet.

(Answer: Goodwill: 119200 and MI: 52000)

Q35. Assume same Balance Sheet as in question 2, but with following information. Investment were purchased by H Ltd. in S Ltd. on 1.10.03 Balance in Profit and Loss Account of S Ltd. was 26,000 on 1.4.03. **(Answer: Goodwill 13,400 and Min Int. 30,000)**

ABNORMAL ITEMS

Q36.

Balance Sheet 31.3.2010

Equity & Liabilities	**H**	**S**
Shareholder Funds:		
Share capital	400,000	300,000
Profit & Loss a/c	100,000	80,000
General reserve	200,000	50,000
Capital reserve	100,000	50,000
Current Liabilities:		
Creditors	50,000	20,000
	850,000	**500,000**
Non Current Assets:		
Fixed Assets	500,000	300,000
Investment in 80% shares	200,000	-
Current Assets	150,000	200,000
	850,000	**500,000**

H Ltd. had acquired shares of S Ltd. on 1/8/09. Balance of S Ltd. reserves on. 1/4/09.

Profit & Loss a/c	20,000
General reserve	14,000
Capital reserve.	26,000

There were abnormal items on certain dates.

Date	**Item**	**Amount**
1-11-09	Abnormal loss	2000
1-7-09	Abnormal gain	3000

Prepare Consolidated Balance Sheet.

(Answer: CR: 122134, MI: 96000, BS Total: 1150000)

BONUS DISTRIBUTION

Q37.

Balance Sheet 31.3.2012

Equity & Liabilities	**H**	**S**
Shareholder Funds:		
Share Capital	4,00,000	1,00,000
Profit and Loss A/c	5,00,000	3,00,000
Current Liabilities:		

Creditors	70,000	2,00,000
	9,70,000	**6,00,000**
Assets *Non-Current Assets:* Fixed Assets Investments in S Ltd. *Current Assets*	 6,00,000 70,000 3,00,000	 4,00,000 - 2,00,000
	9,70,000	**6,00,000**

H Ltd. purchased 6,000 shares of S Ltd. on 1-7-2011. Balance in Profit & Loss A/c of S Limited on 1.4.2011 was Rs. 1,00,000. There was Abnormal Loss Rs. 12,000 on 1-11-2011 at S Limited. S Ltd. distributed bonus in ratio of 1:2 whose entry has not been passed by S Ltd. Prepare Consolidated Balance Sheet

(Ans: CR – 81,800/-; MI – 1,60,000/- and BS Total – 15,00,000/-)

Q38. A Ltd. acquired 8,000 shares of Rs. 100 each in B Ltd. on 30th September, 1991. The Summarized Balance Sheet of the two companies as on 31st March 1992 were as follows:

	A Ltd	**B Ltd.**
Equity & Liabilities:	**Rs.**	**Rs.**
Shareholder Funds:		
Share Capital		
30,000 shares of Rs. 100 each	30,00,000	-
10,000 shares of Rs. 100 each	-	10,00,000
Capital Reserves	-	5,50,000
General Reserves	3.00,000	50,000
Profit and Loss Account	3,82,000	1,80,000
Non-Current Liabilities		
Loans from B Ltd	21,000	-
Current Liabilities:		
Bills Payable (including Rs. 5,000 to A Ltd.)	-	17,000
Creditors	1,79,000	70,000
	38,82,000	**18,67,000**
Non Current Assets:	**A Ltd.**	**B Ltd.**
Fixed Assets	15,00,000	14,47,000
Investment in B Ltd. at cost	17,00,000	-
Current Assets:		
Stock in hand	4,00,000	2,00,000
Loans to A Ltd.	-	20,000
Bills Recevb. (Including 5,000 from B Ltd.)	12,000	-
Debtors	2,50,000	1,80,000
Cash and Bank Balance	20,000	20,000
	38,82,000	**18,67,000**

Note: On the balance sheet of A Ltd.: There is a contingent liability for bills discounted of Rs. 6,000

You are given the following information:

1. B Ltd. made a bonus issue on 31st march, 1992 of one share for every two shares held, reducing the capital reserve equivalently but the accounting effect to this has not been given in the above Balance Sheet.
2. Interest receivable for the year (Rs.1,000) in respect of the loan due by A Ltd. to B Ltd. has not been credited in the books of B Ltd.
3. The credit balance in the Profit and Loss Account of B Ltd. as on 1-4-1991 was Rs. 21,000.
4. The Director decided on the date of acquisition that the fixed assets of B Ltd. were over-valued and should be written down by Rs. 50,000. Consequential adjustments on depreciation are to be ignored.

Prepare the consolidated Balance Sheet as at 31 st march, 1992 showing your working.

(Ans.: Minority Intt. 3,46,200 Goodwill 3,79,200 and BS Total: 43,53,200)

DIVIDENDS DISTRIBUTION

Q39. Calculate Cost of Control and Minority interest

Investments Purchased (75%) on 1-7-2010		Rs. 5,00,000
Share capital of S Ltd.	31-3-2012	Rs. 10,00,000
Balance is Profit & Loss A/c	1-4-2010	Rs.4,00,000
Balance is Profit & Loss A/c	31-3-2012	Rs.7,50,000

Dividend Paid by S limited

On	Type	Amount
01-08-2010	Final Dividend	10,000
01-01-2011	Interim Dividend	18,000
01-05-2011	Final Dividend	24,000
01-10-2011	Interim Dividend	12,000

All Dividends received were credited by H Ltd. in its P&L a/c

(Ans: Capital Reserve 5,88,813/- and Minority Interest 4,37,500)

DIVIDEND WITH BONUS

Q40.

Balance Sheet as on 31-3-2011

Equity & Liabilities	**H**	**S**
Shareholder Funds:		
Share Capital	10,00,000	4,00,000
Profit & Loss A/c	5,00,000	3,00,000
Current Liabilities:		
Creditor	5,00,000	5,00,000
	20,00,000	**12,00,000**
Non-Current Assets:	**H**	**S**
Fixed Assets	7,50,000	6,50,000
Investments in Shares	5,00,000	-
Current Assets	7,50,00	5,50,000
	20,00,000	**12,00,000**

H Ltd. had purchased shares of S Ltd. on 1-10-2010. H Ltd. held 30,000 shares of S Ltd. on 31-3-2011. Balance in Profit & Loss A/c of S Ltd. on 1-4-2010 was Rs. 2,00,000.

1. Abnormal Loss Rs. 20,000 on 1-5-2010.
2. S Ltd, distributed dividend of 10% on 1-1-2011 for the year 2009-2010. H Ltd. credited its Profit & Loss A/c for receipt of dividend.
3. On 31-3-2011 S Ltd. declared & distributed Bonus 1:4, whose entry is yet to be passed by S Ltd. Prepare Consolidated Balance Sheet.
(Ans: Goodwill 1,04,000/- and Min. Int. 2,80,000/-)

Q41. A Ltd. acquired 70% equity shares of B Ltd. on 01.04.2008 at cost of Rs. 10,00,000 when B Ltd. had an equity share capital of Rs. 10,00,000 and reserves and surplus of Rs. 80,000. In the four consecutive years, B Ltd. fared badly and suffered losses of Rs. 2,50,000, Rs. 4,00,000, Rs. 5,00,000 and Rs. 1,20,000 respectively. Thereafter in 2012-13, B Ltd. experienced turnaround and registered an anuual profit of Rs. 50,000. In the next two years i.e. 2013-14 and 2014-15, B Ltd. recorded annual profits of Rs. 1,00,000 and Rs. 1,50,000 respectively. Show the Minority Interests and Cost of Control at the end of each year for the purpose of Consolidation. **(RTP – May 2015)**

(Answer: COC – 2,44,000 and MI – 3,24,000; 2,49,000, 1,29,000; Nil; Nil, Nil, Nil, 33,000)

Note:
Para 26 of AS 21: Losses applicable to Minority in Consolidated Financial Statements may exceed the Minority Interest in the equity/net worth of the subsidiary. The excess and any further losses applicable to minority are adjusted against majority interest except to the extent the minority has binding obligation to, and is able to make good the losses. If

subsidiary subsequently reports profits, then all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered.

Q42. On 31st March, 2004 the Balance Sheets of H Ltd. and its subsidiary S Ltd, stood as follows: **(In Lakhs)**

Equity & Liabilities	**H Ltd.**	**S Ltd.**
Shareholder Funds:		
Authorized Share Capital	**15,000**	**6,000**
Issued shares of Rs.10 each	12,000	4,800
General Reserve	2,784	1,380
Profit and Loss A/c	2,715	1,620
Current Liabilities:		
Bills Payable	372	160
Sundry Creditors	1,461	854
Provision for Taxation	855	394
Proposed Dividend	1,200	-
	21,387	**9,208**
ASSETS:		
Non-Current Assets:		
Land and Building	2,718	-
Plant and Machinery	4,905	4,900
Furniture and Fittings	1,845	586
Investments in shares in S Ltd.	3,000	-
Current Assets:		
Stock	3,949	1,956
Debtors	2,600	1,363
Cash and Bank balances	1,490	204
Bills Receivable	360	199
Sundry Advances	520	-
	21,387	**9,208**

The following information is also provided to you:

(a) H Ltd. purchased 180 lakh shares in S Ltd. on 1st April, 2003 when the balances to General Reserve and Profit and Loss Account of S Ltd. stood at Rs. 3,000 lakh and 1,200 lakh respectively.

(b) On 4th July, 2003 S Ltd. declared & paid a dividend @ 20% for the year ended 31st March, 2003. H Ltd. credited the dividend received by it to its Profit and Loss Account.

(c) On 1st January, 2004 S Ltd. issued 3 fully paid-up shares for every 5 shares held as bonus shares out of balances to its general reserve as on 31st March, 2003.

(d) On 31st March, 2004 all the bills payable in S Ltd.'s balance sheet were acceptances in favour of H Ltd. But on that date, H. Ltd. held only Rs.45 lakh of these acceptances in hand, the rest having been endorsed in favour of its creditors.

(e) On 31st March, 2004 S Ltd.'s stock included goods which it had purchased for Rs.100 lakh from H Ltd. which made a profit @ 25% on cost.

Prepare a Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 2004 bearing in mind the requirements of AS 21. **(May 2004, Marks 16)**

(Ans.: Capital reserve Rs.1,320; Minority Interest Rs.3120)

Updation of Accounts

Q43. (ICAI MODULE)

Consider the following summarised balance sheets:

	A Ltd. 31.3.20X2	B Ltd. 31.12.20X1		ALtd. 31.3.20X2	B Ltd. 31.12.20X1
	Rs	Rs		Rs	Rs
Share Capital (Shares of Rs 10 each)	10,00,000	5,00,000	Fixed Assets	6,50,000	4,05,000
Reserves and Surplus	4,50,000	2,05,000	Investment: 40,000 Shares in B Ltd.	8,00,000	—
Secured Loan: 13% Debentures (Rs 100 each)	—	3,00,000	1,000 Debentures In B Ltd.	1,50,000	—
Current Liabilities:			Current Assets:		
Trade payables	3,80,000	80,000	Inventory	2,00,000	3,50,000

Other liabilities	2,00,000	40,000	Trade Receivables	1,50,000	2,65,000
			Cash and Bank	80000	105000
	20,30,000	**11,25,000**		**20,30,000**	**11,25,000**

On 5th January 20X2, certain inventory of B Ltd. costing Rs 20,000 were completely destroyed by fire. The insurance company paid 75% of the claim.
On 20th January, 20X2, A Ltd. sold goods to B Ltd. costing Rs 1,50,000 at an invoice price of cost plus 20%.
50% of those goods were resold by B Ltd. to A Ltd. within 31st March, 20X2 (these were then sold by A Ltd. to a third party before 31st March, 20X2). As on 31st March, 20X2, B Ltd. owes Rs 60,000 to A Ltd. in respect of those goods. Pre-acquisition profits of B Ltd. were Rs 75,000. Prepare consolidated balance sheet as on 31st March, 20X2 after making necessary adjustments in the balance sheet of B Ltd.

Solution:

Consolidated Balance Sheet of A Ltd. and its subsidiary B Ltd.
As on 31st March, 20X2

Particulars	Note No.	(Rs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		10,00,000
(b) Reserves and Surplus (W.N.5.)		5,09,000
(2) Minority Interest (W.N 3.)		1,46,000
(3) Non-current liabilities		
(a) Long term borrowings	1	2,00,000
(4) Current Liabilities		
(a) Trade Payables	2	4,60,000
(b) Other current liabilities (Rs 2,00,000 + Rs 40,000)		2,40,000
Total		**25,55,000**
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
(i) Tangible assets	3	10,55,000
(ii) Intangible assets	4	3,40,000
(2) Current assets		
(a) Inventories	5	6,05,000
(b) Trade receivables	6	3,55,000
(c) Cash & Cash equivalents	7	2,00,000
Total		**25,55,000**

Notes to Accounts

			Rs
1.	**Long Term Borrowings**		

	Secured loans		
	13% Debentures (Rs 100 each)		2,00,000
2.	**Trade Payables**		
	A Ltd.	3,80,000	
	B Ltd.(W.N 1)	1,40,000	
	5,20,000		
	Less : Mutual indebtedness	(60,000)	4,60,000
3.	**Tangible Assets**		
	A Ltd.	6,50,000	
	B Ltd.	4,05,000	10,55,000
4.	**Intangible assets**		
	Goodwill (W.N 2)	3,40,000	
5.	**Inventories**		
	A Ltd.	2,00,000	
	B Ltd. [WN 1	4,20,000	
	6,20,000		
	Less : Unrealised profit [90,000 X 20/120]	(15,000)	6,05,000
6	**Trade Receivables**		
	A Ltd.	1,50,000	
	B Ltd.	2,65,000	
	4,15,000		
	Less : Mutual indebtedness	(60,000)	3,55,000
7	**Cash & Cash equivalents**		
	A Ltd.	80,000	
	B Ltd.[W.N 1]	1,20,000	2,00,000

Working Notes:

1. Adjustments to be made in the balance sheet items of B Ltd.:

Assets side	**Rs**
Inventories:	
As given on 31.12.20X1	3,50,000
Add : Unsold Inventory out of goods purchased from A Ltd.	90,000
	4,40,000
Less: Loss of Inventory by fire	(20,000)
	4,20,000
Cash & Bank balance:	
As given on 31.12.20X1	1,05,000
Add: Insurance claim received [20,000 × 75 %]	15,000
	1,20,000
Liabilities side:	
Trade payables:	
As given on 31.12.20X1	80,000
Add: Owings to A Ltd. on 31.3.20X2	60,000
	1,40,000

Reserves and Surplus:	
As given on 31.12.20X1	2,05,000
Less: Abnormal Loss on goods destroyed [20,000 – 15,000]	(5,000)
	2,00,000
Add: Profit from sale of goods purchased from A Ltd.	30,000
	2,30,000

2. **Goodwill / capital reserve on consolidation:**

	Rs	Rs
Amount paid for 40,000 Shares	8,00,000	
Less: Nominal value of proportionate share capital	4,00,000	
Share of pre-acquisition profits (80% of Rs 75,000)	60,000	(4,60,000)
Goodwill		3,40,000

3. **Minority Interest: 10,000 / 50,000 shares = 20%**

	Rs
Paid up value of 10,000 shares	1,00,000
Add: 20% of Reserves & Surplus of B Ltd. (20% of Rs 2,30,000)	46,000
	1,46,000

4. **Profit /Loss on Debentures acquired**

	Rs
Amount paid for 1,000 Debentures	1,50,000
Less: Nominal value of proportionate 13% debentures	(1,00,000)
Loss charged to Profit and Loss Account	50,000

5. **Reserves and Surplus of A Ltd.**

Balance as on 31.3.20X2	4,50,000
Add: Share of revenue reserves of B Ltd.	
([80% of Rs 1,55,000 (2,30,000 – 75,000)]	1,24,000
	5,74,000
Less: Unrealised profit on Inventory 1/6 × Rs90,000	(15,000)
Loss on elimination of debentures acquired	(50,000)
	5,09,000

Q44. (ICAI MODULE)

Consider the following summarized balance sheets of subsidiary B Ltd.:

	20X1 Rs	20X2 Rs		20X1 Rs	20X2 Rs
Share-Capital			**Fixed Assets**		
Issued & subscribed			Cost	3,20,000	3,20,000
5,000 equity shares			Less: Accumulated		

of Rs 100 each	5,00,000	5,00,000	depreciation	(48,000)	(96,000)
Reserves & Surplus			Net Value	**2,72,000**	**2,24,000**
Revenue reserves	2,86,000	7,14,000	Investments		
Current Liabilities & Provisions:			at cost	—	4,00,000
			Current Assets:		
Trade Payables	4,90,000	4,94,000	Inventory	5,97,000	7,42,000
Bank overdraft	—	1,70,000	Trade Receivables	5,94,000	8,91,000
Provision for taxation	3,10,000	4,30,000	Prepaid Expenses	72,000	48,000
			Cash at Bank	51,000	3,000
	15,86,000	**23,08,000**		**15,86,000**	**23,08,000**

Consider also the following information:

(a) B Ltd. is a subsidiary of A Ltd. Both the companies follow calendar year as the accounting year.

(b) A Ltd. Values its inventory on LIFO basis while B Ltd. used FIFO basis. To bring B Ltd.'s values in line with those of A Ltd. its value of inventory is required to be reduced by Rs 12,000 at the end of 20X1 and Rs 34,000 at the end of 20X2.

(c) Both the companies use straight-line method of depreciation. However, A Ltd. charges depreciation @ 10%.

(d) B Ltd. deducts 1% from Trade Receivables as a general provision against doubtful debts.

(e) Prepaid expenses in B Ltd. include advertising expenditure carried forward of Rs 60,000 in 20X1 and Rs 30,000 in 20X2, being part of initial advertising expenditure of Rs 90,000 in 20X1 which is being written off over three years. Similar amount of advertising expenditure of A Ltd. has been fully written off in 20X1.

Restate the balance sheet of B Ltd. as on 31st December, 20X2 after considering the above information, for the purpose of consolidation. Such restatement is necessary to make the accounting policies adopted by A Ltd. and B Ltd. Uniform.

Solution:

Adjusted revenue reserves of B Ltd.

	Rs	Rs
Revenue reserves as given		7,14,000
Add: Depreciation over charged (Rs 16,000 × 2)	32,000	—
Provision for doubtful debts [8,91,000 / 99 X 1]	9,000	41,000
		7,55,000
Less: Reduction in value of Inventory	34,000	
Advertising expenditure to be written off	30,000	(64,000)
Adjusted revenue reserve		6,91,000

Restated Balance Sheet of B Ltd.
as at 31st December, 20X2

Particulars	Note No.	Rs
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		5,00,000
(b) Reserves and Surplus	1	6,91,000
(2) Current Liabilities		
(a) Short term borrowings	2	1,70,000
(b) Trade Payables		4,94,000
(c) Short-term provision	3	4,30,000
Total		**22,85,000**
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
Tangible assets	4	2,56,000
(b) Non-current Investment		4,00,000
(2) Current assets		
(a) Inventories		7,08,000
(b) Trade Receivables		9,00,000
(c) Cash & Cash Equivalents		3,000
(d) Other current assets	5	18,000
Total		**22,85,000**

Notes to Accounts

1.	**Reserves and Surplus**		
	Revenue Reserve		6,91,000
2.	**Short term borrowings**		
	Bank overdraft		1,70,000
3.	**Short-term provision**		
	Provision for taxation		4,30,000
4.	**Tangible Assets**		
	Cost	3,20,000	
	Less: Depreciation to date	(64,000)	2,56,000
5.	**Other current assets**		
	Prepaid expenses		18,000

Unit – 2 (AS – 21)

Multiple Acquisition of Shares and Disposal of Shares in Single Subsidiary

Q45. H Ltd. acquired shares of S Ltd. as follows:

Date	No. of shares	%	Amount
1/1/2000	8000	40%	120,000
1/4/2001	3000	15%	40,000
1/4/2002	3000	15%	42,000

Every year on 31st May, Subsidiary Co. pays dividend of 10% for previous year. Shares of S Ltd. are of Rs.10/- each. Profit & loss of subsidiary is as follows:

Balance on 1/1/2000	100,000
Add profit for year 2000	60,000
	1,60,000
Less dividend paid in year 2000	20,000
Balance as on 1/1/01	**140,000**
Add Profit for the year 2001	90,000
Less: Dividend paid in year 2001	20,000
	2,10,000
Add profit for the year 2002	1,20,000
Less Dividend paid in year 2002	20,000
Balance on 31/12/2002	**3,10,000**

(Ans: Cost of Control Rs. 38,375; M/1 Rs 1,53,000 and Cons. P&L – 1,16,625)

Q46. (ICAI MODULE)

'HIM' Limited is a company carrying on the business of beauty products and is having a subsidiary 'SIM' Limited. Their Balance-sheets as on 31st March 20X1 were as under:

Equity and Liabilities	HIM Limited (Rs)	SIM Limited (Rs)
Shareholders' Funds		
Share Capital	25,00,000	5,80,000
Reserves and Surplus		
General Reserves	2,00,000	1,20,000
Profit and Loss Account	3,12,500	2,05,000
Current Liabilities		

Trade Payable	4,55,000	2,35,500
Bills Payable	28,000	83,000
Total	**34,95,500**	**12,23,500**
Assets		
Non-Current Assets		
Fixed Assets	21,70,000	6,25,000
Investments		
4060 Shares in SIM Limited	5,10,000	-
Current Assets		
Inventories	4,80,000	3,19,200
Trade Receivable	1,80,000	1,64,000
Bills Receivable	68,000	1,00,000
Cash and Bank Balance	87,500	15,300
Total	**34,95,500**	**12,23,500**

HIM Limited has also given the following information:

(i) HIM Limited has acquired the shares in SIM Limited in two lots on two different dates. The relevant information at the time of acquisition of shares was as under:

No. of shares acquired	**Balance in General Reserve**	**Balance in Profit and Loss Account**
1st acquisition 3480	80,000	25,000
2nd acquisition 580	85,000	1,02,000

(ii) Bills Receivable of HIM Limited includes Rs 15,000 being acceptance from SIM Limited.

(iii) Both the companies have declared dividends of 10% on 31st March 20X1, but it has not been provided in the books of account.

(iv) SIM Limited's inventory includes stock of Rs 1,45,000 purchased from HIM Limited. HIM Limited sells goods at mark up of 25% on its cost.

Prepare the Consolidated Balance Sheet of HIM Limited along with 'Notes to accounts'.

Solution

Consolidated Balance Sheet of Him Ltd. and its subsidiary Sim Ltd. as on 31st March, 20X1

Particulars	*Note No.*	*Amount*
I. Equity and Liabilities		
(1) Shareholder's Funds		
Share Capital	1	25,00,000
Reserves and Surplus	2	3,79,300
(2) Minority Interest (W.N.2)		2,54,100
(3) Current Liabilities		
Trade payable	3	7,86,500
Other current liability	4	2,67,400
Total		41,87,300
II. Assets		

(1) Fixed Assets		
Tangible assets (21,70,000 + 6,25,000)	5	27,95,000
Intangible assets	6	22,300
(2) Current assets		
Inventories	7	7,70,200
Trade Receivables	8	4,97,000
Cash and Cash equivalents (87,500+15,300)	9	1,02,800
Total		41,87,300

Notes to Accounts

			Rs
1.	**Share Capital** Authorised, Issued, Subscribed and Paid up 25,000 Equity shares of Rs 100 each		25,00,000
2.	**Reserves and Surplus**		
	General Reserve (W.N.4)	2,27,500	
	Profit & Loss Account (W.N.4)	1,51,800	3,79,300
3.	**Trade payables**		
	Trade Payables		
	Him Ltd.	4,55,000	
	Sim Ltd.	2,35,500	6,90,500
	Bills payable		
	Him Ltd.	28,000	
	Sim Ltd. 83,000		
	Less: Mutual owings (15,000)	68,000	96,000
			7,86,500
4.	**Other current liability**		
	Dividend payable		
	Him Ltd.	2,50,000	
	Minority Interest	17,400	2,67,400
5.	**Tangible assets**		
	Him Ltd.	21,70,000	
	Sim Ltd.	6,25,000	27,95,000
6.	**Intangible assets**		
	Goodwill (W.N.3)	22,300	
7.	**Inventories**		
	Him Ltd.	4,80,000	
	Sim Ltd.	3,19,200	
		7,99,200	
	Less: Unrealised profit	(29,000)	7,70,200
8.	**Trade Receivables**		
	Trade Receivables		
	Him Ltd.	1,80,000	
	Sim Ltd.	1,64,000	3,44,000

	Bills Receivable		
	Him Ltd. 68,000		
	Less: Mutual owings (15,000)	53,000	
	Sim Ltd.	1,00,000	1,53,000
			4,97,000
9.	**Cash and Cash equivalents**		
	Him Ltd.	87,500	
	Sim Ltd.	15,300	1,02,800

Working Notes:

1. **Analysis of Profits**

	Pre-acquisition Profits	**Post-acquisition**	
		General Reserve	**Profit & Loss Account**
	Rs	**Rs**	**Rs**
General Reserve	80,000	40,000	
Profit & Loss Account	25,000		1,80,000
For Lot 1 (A)	1,05,000	40,000	1,80,000
Pre-acquisition for Lot 2			
General Reserve (85,000 – 80,000)		5,000	
Profit & Loss Account (1,02,000-25,000)			77,000
Post-acquisition for Lot 2		35,000	1,03,000
Him Ltd. (70%) of (A)	73,500	28,000	1,26,000
Adjustment of pre-acquisition General Reserve for Lot 2 (10%)	500	(500)	
Adjustment of pre-acquisition Profit & Loss Account for Lot 2 (10%)	7,700		(7,700)
Him Ltd.	81,700	27,500	1,18,300
Minority Interest (30%) of (A)	31,500	12,000	54,000

2. **Minority Interest**

	Rs
Share Capital (30%)	1,74,000
Add: Share of pre-acquisition profit of Sim Ltd.	31,500
Share of post-acquisition General Reserve	12,000
Share of post-acquisition Profit & Loss Account	54,000
	2,71,500
Less: Share of Dividend declared and payable	(17,400)
	2,54,100

3. Cost of Control/Goodwill

	Rs
Cost of investments	5,10,000
Less: Share capital (70%)	(4,06,000)
Share of pre-acquisition profit	(81,700)
Goodwill	22,300

4. Consolidated General Reserve & Profit and Loss Account

	General Reserve Rs	Profit and Loss Rs
Him Ltd.	2,00,000	3,12,500
Less: Dividend declared by Him Ltd.		(2,50,000)
Less: Unrealised profit		(29,000)
	2,00,000	33,500
Add: Share in post-acquisition item of Sim Ltd.	27,500	1,18,300
	2,27,500	1,51,800

Q47. From the following Summarized Balance Sheet of X Ltd. and its subsidiary Y Ltd., prepare a consolidated Balance Sheet as on 31st December, 1999.

Equity & Liabilities:	**X Ltd.**	**Y Ltd.**
Shareholder Funds:	Rs.	Rs.
Share Capital		
Equity Shares of Rs. 10 each	100,000	20,000
Profit on sale of Shares	3,000	-
Profit & Loss a/c Brought forward	6,000	7,200
Profit for the year	2,000	4,800
	1,11,000	**32,000**
Non-Current Assets:	**X Ltd.**	**Y Ltd.**
	Rs.	Rs
Sundry Assets	93,000	32,000
Shares in Y Ltd. 1,200 shares at Rs.15 each	18,000	-
	1,11,000	**32,000**

X Ltd. bought in earlier years 1,600 equity shares in Y Ltd. @ 15 when the Profit and Loss Account balance in Y Ltd. was Rs. 4,400. X Ltd. sold 400 shares @ Rs.22.50, credited the difference between the sale proceeds and cost to "Profit on sale of investment account" on 30th June, 1999 and crediting the balance to the investment account. Profit during the year accrued uniformly.

(Ans: Godwill 3,360/-; Min Intt. 12,800/-)

Q48.

H Ltd. acquired 20% shares in S Ltd. on 1-7-20X1 for Rs 50 million, then another 20% on 1-10-20X1 for Rs 60 million and finally, another 20% on 1-11-20X1 for Rs 80 million. S Ltd.

became subsidiary of H Ltd. on and from 1-11-20X1. Balance of Reserve of S Ltd. as on 1-4-20X1 (Rs in million) 60.

Summarised Balance Sheets of H Ltd. and S Ltd. as on 31-3-20X2

		Rs in Million
	H Ltd.	**S Ltd.**
Equity Share Capital	500	200
General Reserve	400	120
Profit & Loss A/c	10	12
Sources	**910**	**332**
Fixed Assets		
Gross Block	800	350
Less: Accumulated Depreciation	(100)	(30)
Net Block	700	320
Investments	190	
Current Assets	20	12
Applications	**910**	**332**

Solution:

In this case goodwill paid in acquiring cost of control should be computed step by step basis:

Rs in million					
Goodwill	**1-7-20X1**	**1-10-20X1**	**1-11-20X1**	**Total**	**Minority Interest**
Cost of investments (A)	50	60	80	190	
Book Value of Investments:					
Equity Share Capital	40 (200 x 20%)	40 (200 x 20%)	40 (200 x 20%)	120.00	80 (200-120)
General Reserve 1-4-20X1	12 (60 x 20%)	12 (60 x 20%)	12 (60 x 20%)	36.00	24 (60-36)
Pre-acquisition profit of 20X1-20X2 WN 1	3.6	7.2	8.40	19.20	
(B)	55.6	59.2	60.40	175.20	
Cost of Control (A-B)	5.60	0.80	19.60	14.80	
40% of post-acquisition reserve and profit					28.80
					132.80

Consolidated Profit & Loss a/c			
Balance of P&L A/c of H Ltd.			10
Share of current reserve [72 x 60 % - 19.2]			24
			34

Working Note:

Total Profit from 1-4-20X1 to 31-03-20X2 = 120 + 12 – 60 = 72 Million

Acquisition Date	**Pre-acquisition Period**	**Pre-acquisition Duration [A]**	**% Holding [B]**	**Profit amount 72 x [A]/12 X [B]**
1-7-20X1	1-4-20X1 to 1-7-20X1	3 Months	20	3.6
1-10-20X1	1-4-20X1 to 1-10-20X1	6 Months	20	7.2
1-11-20X1	1-4-20X1 to 1-11-20X1	7 Months	20	8.4

Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 20X2

Particular	**Note No.**	**(Rs in million)**
I. Equity and Liability		
(1) Shareholder's Fund		
(a) Share Capital		500.00
(b) Reserves and surplus	1	434.00
(2) Minority Interest		132.80
Total		1,066.80
II. Assets		
(1) Non-current assets		
(a) Fixed assets		
(i) Tangible Assets	2	1,020.00
(ii) Intangible Assets		14.80
(2) Current Assets (20+12)		32.00
Total		1,066.80

Notes to Accounts

Notes to Accounts		**(` in million)**
1.Reserves and Surplus		
General reserve	400	
Profit and Loss A/c [As calculated above]	34	434.00
2.Tangible assets		
Gross Block		1,150.0
Less: Accumulated Depreciation		(130.0)
Net Block		1,020.0

Q49. A Ltd. had acquired 80% shares in the B Ltd. for Rs 15 lakhs. The net assets of B Ltd. on that day are Rs 22 lakhs. During the year, A Ltd. sold the investment for Rs 30 lakhs and net assets of B Ltd. on the date of disposal was Rs 35 lakhs. Calculate the profit or loss on disposal of this investment to be recognized in the Financial Statements of A Ltd.

Solution:

A Ltd. had acquired 80% shares in the B Ltd. for Rs 15 lakhs. The net assets of B Ltd. on that day are Rs 22 lakhs. During the year, A Ltd. sold the investment for Rs 30 lakhs and net assets of B Ltd. on the date of disposal was Rs 35 lakhs. Calculate the profit or loss on disposal of this investment to be recognized in the Financial Statements of A Ltd.

Calculation of Profit/Loss on disposal of investment in subsidiary

Particulars	**Rs**
Proceeds from the sale of Investment	30,00,000
Less: A Ltd.'s share in net assets of B Ltd. (W.N.1)	(28,00,000)
	2,00,000
Add: Capital Reserve at the time of acquisition of shares in B Ltd. (W.N.2)	2,60,000
Profit on sale of investment	4,60,000

Working Notes:

1. A Ltd.'s share in net assets of B Ltd.

	Rs
Net Assets of B Ltd. on the date of disposal	35,00,000
Less: Minority Interest (20% of ` 35 lakhs)	(7,00,000)
A Ltd.'s share in the net assets of B Ltd.	28,00,000

2. Capital Reserve at time of acquisition of shares in B Ltd.

	Rs
A Ltd.'s share in the net assets of B Ltd. on the date of acquisition (80% of Rs 22 lakhs)	17,60,000
Less: Cost of investment	(15,00,000)
Capital Reserve at time of acquisition of shares in B Ltd.	2,60,000

UNIT – 3

AS 27 – INTEREST IN JOINT VENTURES

Q50.

Balance Sheet 31-3-2011

Equity & Liabilities	**H**	**S**	**J**
Shareholder Funds:			
Share Capital	4.00	2.00	1.00
Reserves	1.00	0.50	0.50
Profit & Loss A/c	1.00	1.20	0.80
Current Liabilities:			
Creditor	3.00	0.80	1.10
	9.00	**4.50**	**3.40**
	H	**S**	**J**
Non-Current Assets:			
Fixed Assets	2.00	1.50	1.20
Investments in 80% S	3.00	---	---
40% shares in J	1.50	---	---
Current Assets:	2.50	3.00	2.20
	9.00	**4.50**	**3.40**

1. H Ltd. has a Joint Venture with B Ltd. for control of J Ltd.

2. Where Investments were purchased in S Ltd. and J Ltd.

Profit were as follows:	**S**	**J**
Reserve	.20	.30
Profit & Loss A/c	.75	.25

Prepare Consolidated Balance Sheet

(Answer: Balance Sheet: 11.88)

Q51.

Air Ltd., a listed company, entered into an expansion programme on 1st October, 2009. On that date purchased from Bag Ltd. its investments in two Private Limited Companies. The purchase was of:

(a) The entire share capital of Cold Ltd. and

(b) 50% of the share capital of Dry Ltd.

Both the investments were previously owned by Bag Ltd. After acquisition by Air Limited, Dry Ltd. was to be run by Air Ltd. and Bag Ltd. as a jointly controlled entity.

Air Ltd. makes its financial statements up 30th September each year. The terms of acquisition were.

Cold Ltd.

The total consideration was based on price earnings ratio (P/E) of 12 applied to the reported profit of Rs. 20 lakhs of Cold Ltd. for the year 30 September, 2009. The consideration was settled by Air Ltd. issuing 8% debentures for Rs. 140 lakhs (at par) and the balance by a new issue of Rs. 1 equity shares, based on its market value of Rs.2.50 each.

Dry Ltd.

The market value of Dry Ltd. on first October, 2009 was mutually agreed as Rs.375 lakhs. Air Ltd. satisfied its share of 50% of this amount by issuing 75 lakhs Rs.1 equity shares (market value Rs. 2.50 each) to Bag Ltd.

Air Ltd. has not recorded in its books the acquisition of the above investments or the discharge of the consideration.

The summarized statements of financial position of the three entities at 30th September, 2010 are:

			Rs. thousands
Equity & Liabilities	**Air Ltd.**	**Cold**	**Dry Ltd.**
Shareholder Funds:			
Equity capital: Rs. 1 Each	10,000	20,000	25,000
Retained earnings	20,800	15,000	4,500
Current Liabilities:			
Trade and other payables	17,120	5,270	14,100

Overdraft	1,540	-	-
Provision for taxes	5,640	2,400	760
	55,100	**42,670**	**44,360**
Non-Current Assets:			
Tangible Assets	34,260	27,000	21,060
Current Assets:			
Inventories	9,640	7,200	18,640
Debtors	11,200	5,060	4,620
Cash	-	3,410	40
Total Assets	**55,100**	**42,670**	**44,360**

The following information is relevant.

(a) The book values of the net assets of Cold Ltd. and Dry Ltd. on the date of acquisition were considered to be a reasonable approximation to their fair values.

(b) The current profits of Cold Ltd. and Dry Ltd. for the year ended 30th September, 2010 were Rs. 80 lakhs and Rs. 20 lakhs respectively. No dividends were paid by any of the companies during the year.

(c) Dry Ltd. the jointly controlled entity is to be accounted for using proportional consolidation, in accordance with AS-27 "Interests in joint venture".

(d) Goodwill in respect of the acquisition of Dry Ltd. has been impaired by Rs10 lakhs at 30th September, 2010. Gain on acquisition, if any will be separately accounted.

Prepare the consolidated Balance Sheet of Air Ltd. and its subsidiaries as at 30th September, 2010.

(November 2010 New Course; 16 Marks)

Solution:

Consolidated Balance Sheet of Air Ltd. with its Subsidiary Cold Ltd. and Jointly controlled Dry Ltd. as on 30th Sep, 2010

Particulars	Note No.	(Rs in thousands)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	21,500
(b) Reserves and Surplus	2	49,050
(2) Non-Current Liabilities		
Long-term borrowings	3	15,540
(3) Current Liabilities		

(a) Trade Payables Rs (17,120 + 5,270 + 7,050)		29,440
(b) Short-term provisions	4	8,420
Total		1,23,950
II. Assets		
(1) Non-current assets		
Fixed assets		
(a) Tangibles assets Rs (34,260+27,000+10,530)		71,790
(b) Intangible assets (W.N.6)		4,000
(2) Current assets		
(a) Inventories Rs (9,640 + 7,200 + 9,320)		26,160
(b) Trade receivables Rs (11,200+5,060+2,310)		18,570
(c) Cash and cash equivalents	5	3,430
Total		1,23,950

Notes to Accounts

			Rs in thousands
1.	Share Capital		
Equity Capital Rs (10,000 + 4,000 + 7,500)			
(Out of the above 11,500 thousand shares have been issued for consideration other than cash)		21,500	
2.	Reserves and Surplus		
Retained Earnings (W.N.4)		28,800	
Capital Reserve (W.N.5)		3,000	
Securities Premium		17,250	49,050
3.	Long Term Borrowings		
8% Debentures		14,000	
Overdraft		1,540	15,540
4.	Short-term provisions		
Provision for taxes Rs (5,640 + 2,400 + 380)		8,420	
5.	Cash and cash equivalents		
Cash Rs (3,410 + 20)		3,430	

Working Notes:

1. **Purchase consideration paid to Cold Ltd.**

   Earnings per share for the year 30th Sep, 2009
   = 20,00,000/2,00,00,000 = Rs 0.10 per share
   Market price per share = Rs 0.10 x 12 (i.e. P/E ratio) = Rs 1.20 per share
   Purchase consideration = Rs 1.20 x 2,00,00,000 shares= Rs 2,40,00,000
   Purchase consideration to be paid as under:

8% Debentures	Rs 1,40,00,000
Equity Shares (40,00,000 shares of Rs 2.50 each)	Rs 1,00,00,000
	Rs 2,40,00,000

   Purchase consideration paid to Cold Ltd. will be Rs 24,000 thousands.

2. **Consideration paid to Dry Ltd.** (Rs in thousands)

   Total market value (as given) 37,500
   50% Shares acquired by Air Ltd.(75,00,000 shares @ Rs 2.50 each) 18,750

3. **Analysis of retained earnings of Cold Ltd. as on 30th Sep, 2017**

   (Rs in thousands)

Retained earnings given in balance sheet on 31.3.2017	15,000
Less: Current profits for the year ended 31.3.2017 (Post acquisition)	(8,000)
Pre acquisition retained earnings	7,000

Air Ltd. has 100% share in pre and post acquisition profits of Cold Ltd.

4. Retained Earnings in the Consolidated Balance Sheet

	Rs in thousands
Balance in Air Ltd. balance sheet	20,800
Add: Share in post acquisition profits of Cold Ltd.	8,000
Add: Share in post acquisition profits of Dry Ltd. (joint venture)	1,000
	29,800
Less: Goodwill (written off)	(1,000)
	28,800

5. Capital Reserve

	Rs in thousands
Amount Paid	24,000
Less: Paid up value of shares 20,000	
Pre-acquisition profit 7,000	(27,000)
Capital Reserve	3,000

6. Goodwill

	Rs in thousands
Amount paid for shares of Dry Ltd (Rs 37,500 x 50%)	18,750
Less: Paid up value of shares (Rs 25,000x 50%)	(12,500)
Pre-acquisition profit (Rs 2,500 x 50%)	(1,250)
Goodwill	5,000
Less: Impairment (Written off)	(1,000)
	4,000

TRANSACTIONS BETWEEN JOINT VENTURE AND VENTURER IN CASE OF JCA/JCO

Q52. Journalise assuming JV of JCO nature between A and B in ratio of 1:1

1. A & B Jointly Purchased machine Rs.1,00,000
2. A Sold machine of Rs.70,000 to JV for Rs.1,10,000
3. B Sold Machine of Rs.1,60,000 To JV for Rs.2,00,000
4. A Sold Machine of Rs.1,00,000 to JV for Rs.90,000
5. B Sold Machine of Rs.2,00,000 to JV for Rs. 150,000
6. Machine of Book Value Rs. 1,00,000 to Joint Venture was sold to A for Rs.1,20,000

ASSOCIATE – AS 23

Q53. **Balance Sheet 31-3-2011**

Shareholder Funds:	**H**	**S**	**A**
Share Capital	10.00	3.00	2.00
Reserves	1.00	2.00	0.50
Profit & Loss A/c	1.00	1.00	0.50
Current Liabilities:			
Liability	2.00	0.50	2.20
	14.00	**6.50**	**5.20**
	H	**S**	**A**
Non-Current Assets:			
Fixed Assets	7.00	6.00	5.00
Investments in 80% S	4.00	-	
30% of A	2.00	-	-
Current Assets:	1.00	0.50	0.20
	14.00	**6.50**	**5.20**

H Ltd. had acquired shares in S & A on 1-4-2010 when Balances were:

	S	**A**
Reserves	1.50	.30
Profit & Loss A/c	.20	.20

Q54. (ICAI)

A Ltd. acquired 40% share in B Ltd. on April 01, 20X1 for Rs 10 lacs. On that date B Ltd. had 1,00,000 equity shares of Rs 10 each fully paid and accumulated profits of Rs 2,00,000.

During the year 20X1-20X2, B Ltd. suffered a loss of Rs 10,00,000.

During 20X2-20X3 loss of Rs 12,50,000 and during 20X3-20X4 again a loss of Rs 5,00,000. Show the extract of consolidated balance sheet of A Ltd. on all the four dates recording the above events.

Solution

Calculation of Goodwill/Capital Reserve under Equity Method

Particulars	Rs
Equity Shares	10,00,000
Reserves & Surplus	2,00,000
Net Assets	12,00,000
40% of Net Asset	4,80,000
Less: Cost of Investment	(10,00,000)
Goodwill	5,20,000

Consolidated Balance Sheet (Extract) as on April 01, 20X1

Assets	Rs	Rs
Investment in B Ltd.	4,80,000	
Add: Goodwill	5,20,000	10,00,000

Calculation of Carrying Amount of Investment in the year ended on 20X1-20X2

Particulars	Rs
Investment in B Ltd.	4,80,000
Add: Goodwill	5,20,000
Cost of Investment	10,00,000
Less: Loss for the year (10,00,000 x 40%)	(4,00,000)
Carrying Amount of Investment	6,00,000

Consolidated Balance Sheet (Extract) as on March 31, 20X2

Assets	Rs	Rs
Investment in B Ltd.	80,000	
Add: Goodwill	5,20,000	6,00,000

Calculation of Carrying Amount of Investment in the year ended on 20X2-20X3.

Particulars	Rs
Carrying Amount of Investment	6,00,000
Less: Loss for the year (12,50,000 x 40%)	(5,00,000)
Carrying Amount of Investment	1,00,000

Consolidated Balance Sheet (Extract) as on March 31, 20X3

Assets	Rs	Rs
Investment in B Ltd.	-	-
Add: Goodwill	1,00,000	1,00,000

Calculation of Carrying Amount of Investment in the year ended on 20X3-20X4

Particulars	Rs
Carrying Amount of Investment	1,00,000
Less: Loss for the year (5,00,000 x 40%)	(2,00,000)
Carrying Amount of Investment	(1,00,000)

Consolidated Balance Sheet (Extract) as on March 31, 20X4

Assets	Rs	Rs

Investment in B Ltd.		-

Q55. Eagle Ltd. had acquired 51% in Sparrow Ltd. for Rs. 75.80 lakhs on 1st April, 2010. On the date of the acquisition Sparrow's Assets stood at Rs. 196 lakhs and liabilities at Rs. 16 lakhs. The net asset position of Sparrow Ltd. as on 31st March, 2011 and 30th Sep 2011 were Rs. 280 lakhs and Rs. 395 lakhs respectively, the increase resulting from profits during the period.

On 1st October, 2011 25.5% holdings were sold for Rs. 125 lakhs. You are required explain the nature of the relationship between the two companies on the relevant dates and the accounting adjustments that are necessary as a result of any change in the relationship. The profit arising on part sale of investment, carrying value of the portion unsold and goodwill/capital reserve that arises on change in nature of the investment may also be worked out by you.

(November 2011, 8 marks)

Solution:

Sparrow Ltd. became a subsidiary of Eagle Ltd. on 1st April 20X0 when 51% thereof was acquired. The holding-subsidiary relationship continued till 30th September 20X1 and from 1st October, 20X1 the relationship between the two companies will change to Associate. As per para 24 of AS 21, "Consolidated Financial Statements", **the carrying value of the investment at the date it ceases to be subsidiary is regarded as cost thereafter.** Accordingly, if the nature of the investee changes to that of an associate, the carrying amount of the investment in Consolidated Financial Statements of the investor, as on date it ceases to be a subsidiary, would be considered as cost of investment in the associate.

Goodwill or capital reserve arising on account of the change in the nature of the investment will be computed as on the date of such change. Accordingly, when a part of the investment takes the form of an investment in an associate, the results of operations of the subsidiary will be included in the consolidated statement of Profit and Loss for the period from the beginning of the period until it ceased to be a subsidiary.

Ascertainment of Gain or Loss
on the Disposal of the Part of the Investment in Sparrow Ltd.

		Rs
Proceeds received on sale of 25.5% holdings in Sparrow Ltd.		1,25,00,000
Net Assets of sparrow Ltd. on the date of disposal	3,95,00,000	
Less: Minority's interest in Sparrow Ltd. on the date of disposal	(1,93,55,000)	
Share of Eagle Ltd. in Net Assets	2,01,45,000	
Less: Capital reserve on acquisition (Refer W.N.)	(16,00,000)	

Total value of investment in consolidated financial statements of Eagle Ltd.	1,85,45,000	
Less: Carrying Value of investment disposed off		92,72,500
Profit on sale of 25.5% of investment		32,27,500

Carrying Value of the Investment retained in the Consolidated Financial Statements

		Rs
Total value of investment in consolidated financial statements of Eagle Ltd.	1,85,45,000	
Less: Carrying value of investment disposed off	(92,72,500)	
Carrying Value of the investment retained in consolidated financial statements including capital reserve		92,72,500
This amount of Rs 92,72,500 would be used to apply the equity method of accounting as specified in AS 23		

Goodwill / Capital Reserve arising on the Carrying Value of Unsold Portion of the Investment

	Rs
Carrying value of 25.5% holdings in Sparrow Ltd. as on 1st October, 20X1	92,72,500
Less: Share in value of equity of Sparrow Ltd., as at date of investment when subsidiary relationship is transformed to an associate (3,95,00,000 x 25.5%)	(1,00,72,500)
Capital reserve arising on such investment under Equity method as per AS 23	(8,00,000)

Working Note:

Calculation of Goodwill/Capital Reserve on the Date of Acquisition of Shares in Sparrow Ltd.

	Rs
Net Assets on Acquisition date (Rs 1,96,00,000 - Rs 16,00,000)	1,80,00,000
51% thereof	91,80,000
Less: Cost of investment	(75,80,000)
Capital reserve on acquisition	16,00,000

Q56. A Ltd acquired 30% Equity share Capital of B Ltd a cost of Rs. 4,50,000. The comparative balance sheets of B Ltd. on the date of acquisition and year end are given below:

Balance Sheet of B Ltd.

Equity & Liabilities	**Begining**	**Year end**
Shareholder Funds:	Rs.	Rs.
Share Capital	10,00,000	10,00,000
General Reserve	2,00,000	3,30,000
Securities Premium	1,00,000	1,00,000
Current Liabilities:		
Current Liabilities	1,50,000	2,10,000
Proposed Dividend	-	50,000
	14,50,000	**16,90,000**
Assets	**Beginning**	**Year end**
Non-Current Assets:	Rs.	Rs.
Fixed Assets	6,00,000	7,00,000
Investment	3,50,000	4,80,000
Current Assets	5,00,000	5,10,000
	14,50,000	**16,90,000**

There was no revaluation of asset by B Ltd. during the year. Current Assets of B Ltd. at year-end include stock costing Rs60,000 purchased from A Ltd. which sells at cost + 20%. Show the investment in associates in the consolidated balance sheet to be prepared by A Ltd. in the beginning and at year-end. **(RTP Nov. 05)**

Ans.:

Calculation of Goodwill/Capital Reserve

Share capital of B Ltd.	10,00,000
General Reserve of B Ltd.	2,00,000
Securities Premium of B Ltd.	1,00,000
Total Equity of B Ltd.	**13,00,000**
% holding of A Ltd.	30%
Share of A Ltd.	3,90,000
Cost of Acquisition	4,50,000
Goodwill	**60,000**

Calculation of share of profit earned during the year

	Rs.
Increase in General Reserve	1,30,000
Proposed dividend	50,000
Total profit for the year	**1,80,000**
Share of A Ltd. (30%)	54,000

Calculation of Unrealised profit on stock

	Rs.	
Cost of stock to B Ltd.	60,000	
Unrealised profit of A Ltd. (20/120)	10,000	
Share of A Ltd. in unrealized profit (30%)		3,000

Consolidated Balance Sheet of A Ltd. (Beginning)

Liabilities	Amount	Assets	Amount
		Investment in B Ltd. (including Goodwill Rs.60,000)	4,50,000

Consolidated Balance Sheet of A Ltd. (Year end)

Liabilities	Amount	Assets	Amount
		Investment in B Ltd.	
		(Including Goodwill 60,000)	4,50,000
		Add: Share of profit (current year)	54,000
		Less: Unrealised profit on stock	3,000
			501000

UNIT - 4

Consolidation of Two or More Subsidiary

Same Date Acquisitions:

Q57.

From the following summarized Balance Sheets of a group of companies and the other information provided, draw up the consolidated Balance Sheet as on 31.3.2017. Figures given are in Rs Lakhs:

Balance Sheets as on 31.3.2017

	X	Y	Z		X	Y	Z
Shares capital (in shares of Rs 100 each)	300	200	100	Fixed Assets less depreciation	130	150	100
Reserves	50	40	30	Cost of investment in Y Ltd.	180	-	-
Profit and loss balance	60	50	40	Cost of investment in Z Ltd.	40	-	-
Trade payables	40	10	15	Cost of investment in Z Ltd.	-	80	-
Y Ltd. balance	-	-	15	Inventory	50	20	20
Z Ltd. balance	50	-	-	Trade receivables	70	20	40
				Z Ltd. balance	-	10	-
				X Ltd. balance	-	-	30
	___	___	___	Cash and bank balance	30	20	10
	500	300	200		500	300	200

X Ltd. holds 1,60,000 shares and 30,000 shares respectively in Y Ltd. and Z Ltd.; Y Ltd. holds 60,000 shares in Z Ltd. These investments were made on 1.7.2016 on which date the provision was as follows:

	Y Ltd.	Z Ltd.
Reserves	20	10
Profit and loss account	30	16

In December, 2016 Y Ltd. invoiced goods to X Ltd. for Rs 40 lakhs at cost plus 25%. The closing inventory of X Ltd. includes such goods valued at Rs 5 lakhs.

Z Ltd. sold to Y Ltd. an equipment costing Rs 24 lakhs at a profit of 25% on selling price on 1.1.2017. Depreciation at 10% per annum was provided by Y Ltd. on this equipment.

X Ltd. declared dividend at 10% on 31.3.2017.

Details of Trade payables and Trade receivables:

	X	Y	Z
Trade payables			
Bills Payable	10	-	5
Sundry creditors	30	10	10
	40	10	15

Trade receivables			
Debtors	70	10	20
Bills Receivables	-	10	20
	70	20	40

Bills payables of Z Ltd. represent acceptances given to Y Ltd. out of which Y Ltd. had discounted bills worth Rs 3 lakhs.

Trade receivables of X Ltd. include Rs 5 lakhs being the amount due from Y Ltd.

Answer

Consolidated Balance Sheet of X Ltd. and its subsidiaries Y Ltd. and Z Ltd. as at 31st March, 2017

Particulars	Note No.	(Rs in Lacs)
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital		300.00
(b) Reserves and Surplus	1	151.90
(2) **Minority Interest (W.N 4)**		79.30
(3) **Current Liabilities**		
(a) Trade payables	2	58.00
(b) Other current liabilities	3	55.00
Total		644.20
II. Assets		
(1) **Non-current assets**		
Fixed assets		
Tangible assets	4	372.20
(2) **Current assets**		
(a) Inventories	5	89.00
(b) Trade receivables	6	123.00
(c) Cash and cash equivalents	7	60.00
Total		644.20

Notes to Accounts

		(Rs in lacs)	(Rs in lacs)
1.	Reserves and Surplus		
Capital Reserve [W.N. 3]		13.40	
Other Reserves [W.N. 7]		81.60	
Profit and Loss Account [W.N. 6]		56.90	151.90
2.	Trade payables		
X Ltd. Rs 40.00			
Y Ltd. Rs 10.00			
Z Ltd. Rs 15.00		65.00	
Less: Mutual indebtedness Rs (5.00)			
Less :Mutual indebtedness [5-3] Rs (2.00)		(7.00)	58.00
3.	Other current liabilities		
(a) Current Account Balances			
X Ltd. Rs 50.00			
Z Ltd. Rs 15.00			

Rs 65.00		
Less: Mutual indebtedness (Rs 10+ 30) (Rs 40.00)	25.00	
(b) Dividend payable	30.00	55.00
4. Tangible assets		
Fixed Assets		
X Ltd.	130.00	
Y Ltd.	150.00	
Z Ltd.	100.00	
380.00		
Less: Unrealised profit [W.N. 5]	(7.80)	372.20
5. Inventories		
X Ltd.	50.00	
Y Ltd.	20.00	
Z Ltd.	20.00	
90.00		
Less: Unrealised profit [5 x 25 / 125]	(1.00)	89.00
6. Trade receivables		
X Ltd. Rs 70.00		
Y Ltd. Rs 20.00		
Z Ltd. Rs 40.00	130.00	
Less: Mutual indebtedness ` (5.00)		
Less: Mutual indebtedness ` (2.00)	(7.00)	123.00
7. Cash and Cash Equivalents		
X Ltd. Rs 30.00		
Y Ltd. Rs 20.00		
Z Ltd. Rs 10.00	60.00	

Working Notes:

Shareholding Pattern

	Y Ltd.	**Z Ltd.**
Total Shares	2 lakh shares	1 lakh shares
X Ltd's holding	1.6 lakh shares [80 %]	.3 lakhs [30%]
Y Ltd's holding	NA	.6 lakhs [60%]
Minority Holding	.4 lakh shares (20 %)	.1 lakh shares (10%)

(Rs in lakhs)

	Capital Profit	**Revenue Reserve**	**Revenue profit**
(1) Analysis of Profits of Z Ltd.			
Reserves on 1.7.2016	10.00		
Profit and Loss A/c on 1.7.2016	16.00		
Increase in Reserves		20.00	
Increase in Profit	______	______	24.00
	26.00	20.00	24.00
Less: Minority Interest (10%)	(2.60)	(2.00)	(2.40)
	23.40	18.00	21.60

Share of X Ltd. [30%]	7.80	6.00	7.20
Share of Y Ltd. [60%]	15.60	12.00	14.40
(2) Analysis of Profits of Y Ltd.			
Reserves on 1.7.2016	20.00		
Profit and Loss A/c on 1.7.2016	30.00		
Increase in Reserves		20.00	
Increase in Profit	______	______	20.00
	50.00	20.00	20.00
Share in Z Ltd. [WN 1]	______	12.00	14.40
	50.00	32.00	34.40
Less: Minority Interest (20%)	(10.00)	(6.40)	(6.88)
Share of X Ltd.[80%]	40.00	25.60	27.52
(3) Cost of Control			
Investments in Y Ltd.			180.00
Investments in Z Ltd.			120.00
			300.00
Less: Paid up value of investments			
in Y Ltd.	(160.00)		
in Z Ltd.	(90.00)	(250.00)	
Capital Profit			
in Y Ltd. [WN 1]	(40.00)		
in Z Ltd. [WN 2]	(23.40)	(63.40)	(313.40)
Capital Reserve			13.40
(4) Minority Interest	Y Ltd.	Z Ltd.	
Share Capital	40.00	10.00	
Capital Profit	10.00	2.60	
Revenue Reserves	6.40	2.00	
Revenue Profits	6.88	2.40	
	63.28	17.00	
Less: Unrealised profit on inventory (20% of 1)	(.20)		
Unrealised profit on equipment (10% of Rs 7.8)	______	(0.78)	
	63.08	16.22	
(5) Unrealised Profit on equipment sale			
Cost	24.00		
Profit [25 % on selling price]	8.00		
Selling Price	32.00		
Unrealised profit = [8 – (8 × 10 / 100 × 3 / 12)] = 8.00 – 0.20 = 7.80			
(6) Profit and Loss Account – X Ltd.			
Balance	60.00		
Less: Dividend	(30.00)		
	30.00		
Share in Y Ltd.	27.52		
Share in Z Ltd.	7.20		
64.72			

Less: Unrealised profit on equipment (90% of 7.8)	(7.02)		
	57.70		
Less: Unrealised profit on inventory (5 × 25 / 125 × 80%)	(0.80)		
	56.90		
(7)			
X Ltd.	50.00		
Share in Y Ltd. [WN 2]	25.60		
Share in Z Ltd. [WN 1]	6.00		
	81.60		

Q58. (Homework)

The Balance Sheets of three companies Sun Ltd., Moon Ltd. and Light Ltd. as at 31 st March, 2010 are given below:

	Sun Ltd.	**Moon Ltd.**	**Light Ltd.**
Equity & Liabilities:			
Shareholder Funds:			
Share Capital (of Rs.10 each)	1,50,000	1,00,000	60,000
Reserves	50,000	40,000	30,000
Profit and Loss A/c.	60,000	50,000	40,000
Current Liabilities:			
Sundry Creditors	30,000	35,000	25,000
Sun Ltd.	-	10,000	8,000
	2,90,000	**2,35,000**	**1,63,000**
Assets:			
Non Current Assets:			
Fixed Assets	70,000	1,20,000	1,03,000
Investments (at Cost)			
Shares in Moon Ltd.	90,000	---	---
Shares in Light Ltd.	40,000	---	---
Shares in Light Ltd.	-	50,000	-
Current Assets:			
Stock-in-Trade	40,000	30,000	20,000
Debtors	20,000	25,000	30,000
Due from Moon Ltd.	12,000	-	-
Due from Light Ltd.	8000		- -
Cash in Hand	10,000	10,000	10,000
	2,90,000	**2,35,000**	**1,63,000**

(a) Sun Ltd. held 8,000 shares of Moon Ltd. and 1,800 shares of Light Ltd.

(b) Moon Ltd. held 3,600 shares of Light Ltd.

(c) All investments were made on 1st July, 2009.

(d) The following balances were there on 1st July, 2009:

	Moon Ltd.	Light Ltd.
Reserves	25,000	15,000
Profit and Loss A/c	20,000	25,000

(e) Moon Ltd. invoiced goods to Sun Ltd. for Rs. 40,000 as cost plus 25% in December, 2009. The Closing stock of Sun Ltd. includes such goods valued at Rs. 5,000

(f) Light Ltd. sold to Moon Ltd. an equipment costing Rs. 24,000 at a profit of 25% on selling price on 1st Jan, 2010. Depreciation at 10% per annum was provided by Moon Ltd. on this equipment.

(g) Sun Ltd. proposes dividend at 10%

Prepare the Consolidated Balance Sheet of the group as at 31st March, 2010. Working should be part of the answer.

(Answer: CR – 26,000; MI – 52,680; BS – 4,81,200; Cons. R&S – 1,88,520)

Solution: (Suggested solution of ICAI)

Consolidated Balance Sheet of Sun Ltd. and its subsidiaries Moon Ltd. and Light Ltd. as at 31st March, 2017

Particulars	Note No.	(Rs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1,50,000
(b) Reserves and Surplus	2	1,73,516
(2) Minority Interest		52,684
(3) Current Liabilities		
(a) Trade Payables	3	90,000
(b) Other current liabilities	4	15,000
Total		4,81,200
II. Assets		
(1) Non-current assets		
Fixed assets	5	2,85,200
(2) Current assets		
(a) Inventories	6	89,000
(b) Trade receivables	7	75,000
(c) Cash and cash equivalents	8	32,000
Total		4,81,200

Notes to Accounts

		Rs	
1.	Reserves and Surplus		
Capital Reserve (W.N.3)		26,000	
Other Reserves (W.N.7)		73,700	
Profit and Loss Account (W. N. 6)		73,816	1,73,516

2.	Minority interest		
Moon Ltd. (W. N. 4)		40,464	
Light Ltd. (W.N.4)		12,220	52,684
3.	Trade Payables		
	Sun Ltd.	30,000	
	Moon Ltd.	35,000	
	Light Ltd.	25,000	90,000
4.	Other current liabilities		
	Dividend	15,000	
5.	Fixed Assets		
Sun Ltd.		70,000	
Moon Ltd. Rs 1,20,000			
Less: Unrealised Profit (W.N.5) Rs (7,800)		1,12,200	
Light Ltd.		1,03,000	2,85,200
6.	Inventories		
	Sun Ltd. Rs 40,000		
	Less: Unrealised Profit Rs (1,000)	39,000	
	Moon Ltd.	30,000	
	Light Ltd.	20,000	89,000
7.	Trade Receivables		
	Sun Ltd.	20,000	
	Moon Ltd.	25,000	
	Light Ltd.	30,000	75,000
8.	Cash and cash equivalents		
Cash in hand			
	Sun Ltd. Rs 10,000		
	Moon Ltd. Rs 10,000		
Light Ltd. Rs 10,000		30,000	
Cash in transit (W.N.8)		2,000	32,000

Working Notes:

1. Analysis of Profits of Light Ltd.

	Pre-acquisition	Post-acquisition	
	Capital Profit Rs	Revenue Reserves Rs	Revenue Profits Rs
Reserves on 1.7.2016	15,000	-	-
Profit and Loss A/c on 1.7.2016	25,000	-	-
Increase in Reserves	-	15,000	-
Increase in Profit	-	-	15,000
	40,000	15,000	15,000
Less: Minority Interest (10%)	(4,000)	(1,500)	(1,500)
	36,000	13,500	13,500
Share of Sun Ltd.	12,000	4,500	4,500
Share of Moon Ltd.	24,000	9,000	9,000

2. Analysis of Profits of Moon Ltd.*

	Pre-acquisition	Post-acquisition

	Capital Profit Rs	Revenue Reserves Rs	Revenue Profits Rs
Reserves on 1.7.2016	25,000	-	-
Profit and Loss A/c on 1.7.2016	20,000	-	-
Increase in Reserves	-	15,000	-
Increase in Profit	-	-	30,000
	45,000	15,000	30,000
Add: Share in Light Ltd. (post acquisition)	-	9,000	9,000
Less: Unrealised profit on equipment (60% of 7,800)		(4,680)	
	45,000	24,000	34,320
Less: Minority Interest (20%)	(9,000)	(4,800)	(6,864)
Share of Sun Ltd.	36,000	19,200	27,456

∗ Treatment of capital profit of sub-subsidiary company i.e. Light Ltd. has been done by applying direct approach.

3. Cost of Control

	Rs	
Investment in Moon Ltd.		90,000
Investment in Light Ltd. Rs by Moon Ltd. 50,000 by Sun Ltd. 40,000		90,000 1,80,000
Less: Paid up value of shares		
in Moon Ltd. 80,000		
in Light Ltd. 54,000	1,34,000	
Capital Profit of Sun Ltd.		
in Moon Ltd. 36,000		
in Light Ltd. 12,000	48,000	
Capital profit of Moon Ltd. in Light Ltd.	24,000	(2,06,000)
Capital Reserve		26,000

4. Minority Interest

	Moon Ltd. Rs	Light Ltd. Rs
Share Capital	20,000	6,000
Capital Profit	9,000	4,000
Revenue Reserves	4,800	1,500
Revenue Profits	6,864	1,500
	40,664	13,000
Less: Unrealised Profit on Inventory 20% of (Rs 5,000 x 25/125)	(200)	
Unrealised Profit on Equipment (10% of Rs 7,800)		(780)
	40,464	12,220

5. Unrealised Profit on Equipment Sale

	Rs

Selling price of the equipment (24,000 × 100 / 75)	32,000
Less: Cost price of the equipment	(24,000)
Profit on sale	8,000
Unrealised profit = [8,000-(8,000 x 10 /100 × 3 / 12)] = Rs 7,800	

6. **Profit and Loss Account – Sun Ltd.**

	Rs
Balance as per separate Balance Sheet	60,000
Less: Dividend	(15,000)
	45,000
Add: Share in Moon Ltd.	27,456
Share in Light Ltd.	4,500
	76,956
Less: Unrealised profit on Equipment (30% of 7,800)	(2,340)
	74,616
Less: Unrealised profit on Inventory () 255,000xx80%125	(800)
	73,816

7. **Other Reserves – Sun Ltd.**

	Rs
Balance as per separate Balance Sheet	50,000
Share in Moon Ltd.	19,200
Share in Light Ltd.	4,500
	73,700

8. **Cash in Transit**

	Rs
Due to Sun Ltd. from Moon Ltd.	12,000
Less: Due by Moon Ltd.	(10,000)
	2,000

Q59.

The balance sheet of three companies Anand Ltd., Bajaj Ltd. and Charan Ltd. as on 31st December 2001 are given below:

Equity & Liabilities	**Aanad Ltd.**	**Bajaj Ltd.**	**Charan Ltd.**
Shareholder Funds:			
Share Capital (100 each)	1,50,000	1,00,000	60,000
Reserves	20,000	10,000	7,500
Profit & Loss A/c	50.000	30,000	25,000
Current Liabilities:			
Sundry Creditors	20,000	25,000	15,000
Anand Ltd.	-	10,000	8,000
Total	**2,40,000**	**1,75,000**	**1,15,500**
Non-Current Assets:			
Goodwill	20,000	15,000	10,000
Fixed Assets	70,000	50,000	60,000

Shares in Bajaj Ltd. (750 shares)	90,000	-	-
in Charan Ltd (100 shares)	15,000	-	
in Charan Ltd (350 shares)		52,000	
Current Assets:			
Due from Bajaj Ltd.	12,000	-	
Charan Ltd.	8,000	-	-
Current Assets	25,000	58,000	45,500
	2,40,000	**1,75,000**	**1,15,500**

All shares were acquired on 1st July, 2001. On 1st January, 2001, the balance were:

	Anand Ltd.	**Bajaj Ltd.**	**Charan Ltd.**
Reserves	10,000	10,000	5,000
Profit & Loss Account	5,000	(Dr.) 5,000	3,000

Profits during 2001 were earned evenly over the year.

In August 2001 each company declared and paid an interim dividend of 10% p.a. for six months. Anand Ltd. and Bajaj Ltd. have credited their Profit & Loss Account with the dividends received. During 2001, Charan Ltd. fabricated a machine costing Rs.10,000 which is sold to Bajaj Ltd. for Rs. 12,000. Bajaj Ltd then sold the machine to Anand Ltd., for Rs. 13,000, the transactions being completed on 31 st December 2001.

Prepare the consolidated Balance Sheet of the Group as on 31st December, 2001

(Ans.: Goodwill 47,593; Min. Intt. 58,650; Con P&L 65,688, BS 3,55,093)

Different Date Acquisitions

Q60.

The following are the summarized Balance Sheets of Ram Ltd., Shyam Ltd. and Tom Ltd. as on 31.03.2017:

Particulars	**Rs in'000**		
	Ram Ltd.	**Shyam Ltd.**	**Tom Ltd.**
Liabilities			
Equity Share Capital (Rs 100 each)	8,000	4,000	1,600
General Reserve	1,600	280	-
Profit and Loss Account	1,360	960	-
Current Liabilities	1,280	3,000	1,120
Total	**12,240**	**8,240**	**2,720**
Assets			
Investments:			
32,000, shares in Shyam Ltd.	4,800	-	-
4,000, shares in Tom Ltd.	200	-	-
12,000, shares in Tom Ltd.	-	720	-
Profit and Loss Account	-	-	640
Current Assets	7,240	7,520	2,080
Total	12,240	8,240	2,720

From the following information, prepare consolidated Balance Sheet of Ram Ltd. and its subsidiaries as on 31.03.2017:

(i) Shyam Ltd. has advanced Rs 8,00,000 to Tom Ltd.

(ii) Current Liabilities of Ram Ltd. includes Rs 4,00,000 due to Tom Ltd.

(iii) Shyam Ltd. and Tom Ltd. have not paid any dividend.

(iv) Ram Ltd. acquired its investments on 01.04.2016 from Shyam Ltd. and then amount standing to credit of General Reserve and Profit and Loss account were Rs 2,80,000 and Rs 5,20,000 respectively.

(v) Ram Ltd. acquired investments in Tom Ltd. on 01.04.2016, when the debit balance in Profit and Loss account in books of Tom Ltd. was Rs 4,80,000.

(vi) Shyam Ltd. acquired its investments in Tom Ltd. on 01.04.2014 and then the debit balance in Profit and Loss account was Rs 1,60,000.

(vii) Shyam Ltd.'s inventory includes inventory worth Rs 4,80,000 which was invoiced by Ram Ltd. at 20% above cost.

(Answer: Goodwill – 712; MI – 976; BS – 16272)

Solution:

Consolidated Balance Sheet of Ram Ltd. and its subsidiaries Shyam Ltd and Tom Ltd. As on 31.3.2017

Particulars	Note No.	(Rs in '000s)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		8,000
(b) Reserves and Surplus	1	3,096
(2) Minority Interest (W.N.7)		952
(3) Current Liabilities	2	4,200
Total		16,248
II. Assets		
(1) Non-current assets		
Fixed assets		
Intangible assets	3	688
(2) Current assets	4	15,560
Total		16,248

Notes to Accounts

		Rs in '000s	
1.	Reserves and Surplus		
General Reserve		1,600	
Profit & Loss (W.N.6)		1,496	3,096
2.	Current Liabilities		
	Ram Ltd.	1,280	
	Shyam Ltd.	3,000	
	Tom Ltd.	1,120	
		5,400	
Less: Mutual Owings		(1,200)	4,200
3.	Intangible assets		
Goodwill (W. N. 5)		688	

4.	Current Assets		
	Ram Ltd.	7,240	
	Shyam Ltd.	7,520	
	Tom Ltd.	2,080	
		16,840	
Less: Mutual Owings		(1,200)	
		15,640	
Less: Unrealised Profit		(80)	15,560

Working Notes:

Shareholding Pattern

	Shyam Ltd.	**Tom Ltd.**
	40,000 shares	16,000 shares
Held by Ram Ltd.	32,000 shares (80%)	4,000 shares (25%)
Held by Shyam Ltd.	NA	12,000 shares (75%)
Minority Interest	8,000 shares (20%)	NIL

1. General Reserve and Profit and Loss Account of Shyam Ltd.

General Reserve Account of Shyam Ltd.

		Rs '000			**Rs '000**
31.3.15	To Balance c/d	280	1.4.14	By Balance b/d	280

Draft Profit and Loss Account of Shyam Ltd.

		Rs '000			**Rs '000**
31.3.15	To Balance c/d	960 960	1.4.14	By Balance b/d By Profit earned during the year (Bal. Fig.)	520 440 960

2. Draft Profit and Loss Account of Tom Ltd.

		Rs '000			**Rs '000**
1.4.12	To Balance b/d	160 160	31.3.13	By Balance c/d	160 160
1.4.13	To Balance b/d	160	31.3.14	By Balance c/d	480
To Loss incurred during the year (Bal. Fig.)		320 480			480
1.4.14	To Balance b/d	480	31.3.15	By Balance c/d	640
To Loss incurred during the year (Bal. Fig.)		160 640			640

3. Analysis of Profits of Tom Ltd.

		Capital Profits Rs '000	**Revenue Profits Rs '000**
(i)	**From the viewpoint of Shyam Ltd.**		
Debit Balance in Profit and Loss Account as on 1.4.2014		(160)	
Loss incurred between 1.4.2014 to 31.3.2017 [(320 + 160)– Refer W.N. 2]			(480)
		(160)	(480)
Share of Shyam Ltd.-75% [carried forward to W. N. 4]		(120)	(360)

(ii) From the view point of Ram Ltd.		
Debit Balance of Profit and Loss Account as on 1.4.14	(480)	
Loss during the year 2016-2017 [WN 2]		(160)
	(480)	(160)
Share of Ram Ltd. (25%)	(120)	(40)

4. **Analysis of Profits of Shyam Ltd. (From the viewpoint of Ram Ltd.)**

	Capital Profits Rs '000	Revenue Profits Rs '000
General Reserve as on 1.4.2016	280	
Profit and Loss Account Balance as on 1.4.2016	520	
Profit earned during 2016-2017 (W.N.1)		440
Brought forward Shyam Ltd.'s share of loss in Tom Ltd. [W. N. 3(i)]	(120)	(360)
Share of Shyam Ltd. in revenue loss of Tom Ltd. for the period 1.4.12 to 31.3.14 [75% of (360- 40)] being treated as capital loss from view point of Ram Ltd.	(240)	240
	440	320
Less:Share of Minority Interest (20%)	(88)	(64)
Balance taken to Ram Ltd. (80%)	352	256

5. **Cost of Control**

	Rs '000	
Investment by Ram Ltd. in	.	
Shyam Ltd.	4,800	
Tom Ltd.	200	
Investment by Shyam Ltd. in		
Tom Ltd.	720	5,720
Less: Paid up value of shares of:		
Shyam Ltd.	3,200	
Tom Ltd. (400 + 1,200)	1,600	
	4,800	
Capital loss of Ram Ltd. in Tom Ltd. [W.N. 3(ii)]	(120)	
Capital Profit of Ram Ltd. in Shyam Ltd. (W.N. 4)	352	(5,032)
Goodwill		688

6. **Consolidated Profit and Loss A/c of Ram Ltd.**

	Rs '000
Profit and Loss A/c Balance	1,360
Post-acquisition share of loss from Tom Ltd.	(40)
Post-acquisition share of profit from Shyam Ltd.	256
	1,576
Less: Unrealised Profit on Inventory (th of 480) 61	(80)
	1,496

7. **Minority Interest**

	Rs'000
Paid up value of shares in Shyam Ltd. (20% of 4,000)	800
Share of Capital Profit (W.N.4)	88
Share of Revenue Profit (W.N.4)	64
	952

Treatment of Proposed Dividend - Preference Shares:

This dividend whether declared or not (irrespective of declaration – Para 27 of AS 21), will be appropriated from AOP and distributed among Parent and Minority in the ratio of Preference Shares held.

AOP A/c Dr.

To CPL A/c (Parent's Share – Post Acquisition)

To COC A/c (Parent's Share – Pre Acquisition)

To Shot Term Provisions A/c (MI's share)

Q61.

Astha Ltd acquired 80% of both classes of shares in Birat Ltd. on 1.4.2007. The draft Balance sheets of two companies on 31st Mar 2008 were as follows:

		(Rs.000)
Equity & Liabilities:	**Astha Ltd.**	**Birat Ltd.**
Shareholder Funds:		
Share Capital:		
Equity Shares of Rs.10 each fully paid	3,000	600
14% Pref. Shares of Rs. 100 each fully paid	-	400
General Reserve	1,900	40
Profit & Loss a/c	1,600	720
Current Liabilities:		
Creditors	300	320
	6,800	**2,080**
Non-Current Assets:	**Astha Ltd.**	**Birat Ltd.**
Plant & Machinery	2,060	600
Furniture & Fixture	600	540
Investment Equity Shares of Birat Ltd	1,920	-
Preference Shares of Birat Ltd	320	-
Current Assets:		
Stock	680	404
Debtors	560	316
Cash at Bank	660	220

	6,800	**2,080**

Note: Contingent Liability - Astha Ltd: Claim for damages lodged by a contractor against the company pending in a law suit- Rs. 1,55,000.

Additional Information:

(i) General reserve balances of a Birat Ltd was the same as on 1.4.2007

(ii) The Balances in a profit and Loss A/c of Birat Ltd on 1.4.2007 was Rs. 3,20,000 out of which dividend of 16% p.a. on the Equity Capital of Rs, 6,00,000 was paid for the year 2006-07.

(iii) The dividend in respect of preference shares of Birat Ltd. for the year 2007-08 was still payable as on 31.3.2008

(iv) Astha Ltd. credited its profit and Loss a/c for the dividend received by it from Birat Ltd. for the year 2006-07.

(v) Sundry creditors of Astha Ltd included an amount of Rs. 1,20,000 for purchases from Birat Ltd on which the later company made a loss of Rs. 10,000.

(vi) Half of the above goods were still the closing stock of Astha Ltd as at 31.3.2008.

(vii) At the time of acquisition by Astha Ltd., while determining the price to be paid for the shares in Birat Ltd. it was considered that the value of Plant and machinery was to be increased by 25% and that of Furniture and Fixtures reduced to 80%. There was no transaction of purchase or sale of these assets during the year. The directors wish to give effect to these revaluations in the consolidated balance sheet.

(viii) The directors of Astha Ltd. are of opinion that disclosure of its Contingent liability will seriously prejudice the company's position in dispute with contractor.

Prepare consolidated Balance Sheet as at 31st Mar 2008, assuming the rate of the depreciation charged as 25% p.a and 10% p.a on Plant and Machinery and Furniture and Fixtures respectively. Workings should be part of the answer.

(May 2008, Marks 16)

(Ans: Goodwill – 1043200; Con. P&L – 1848800; MI – 350200 and BS – 7610200)

Q62. (PM)

The summarized Balance Sheets of Football Ltd. and its subsidiary Hockey Ltd. as on 31st March, 2017 are as under:

Liabilities	Football Ltd.	Hockey Ltd.	Assets	Football Ltd.	Hockey Ltd.
	Rs	Rs		Rs	Rs
Equity shares of Rs 10 each	48,00,000	20,00,000	Goodwill	4,50,000	3,00,000
10% Preference shares of Rs 10 each	7,00,000	3,80,000	Plant and machinery	12,00,000	5,00,000
			Motor vehicles	9,50,000	7,50,000
General reserve	5,50,000	4,20,000	Furniture and fittings	6,50,000	4,00,000
Profit and loss account	10,00,000	6,00,000			
Bank overdraft	1,20,000	70,000	Investments	26,00,000	4,50,000
Trade payables	4,30,000	6,40,000	Inventory	4,50,000	7,20,000
	-	-	Cash at bank	2,25,000	2,10,000
			Trade receivables	10,75,000	7,80,000
	76,00,000	**41,10,000**		**76,00,000**	**41,10,000**

Details of acquisition of shares by Football Ltd. are as under:

Nature of shares	No. of shares acquired	Date of acquisition	Cost of acquisition
			Rs.
Preference shares	14,250	1.4.2014	3,10,000
Equity shares	80,000	1.4.2015	9,50,000
Equity shares	70,000	1.4.2016	8,00,000

Other information:

(i) On 1.4.2016 profit and loss account and general reserve of Hockey Ltd. had credit balances of Rs 3,00,000 and Rs 2,00,000 respectively.

(ii) Dividend @ 10% was paid by Hockey Ltd. for the year 2015-2016 out of its profit and loss account balance as on 1.4.2016. Football Ltd. credited its share of dividend to its profit and loss account.

(iii) Hockey Ltd. allotted bonus shares out of general reserve at the rate of 1 share for every 10 shares held. Accounting thereof has not yet been made.

(iv) During the year 2016-2017 Football Ltd. purchased goods from Hockey Ltd. for Rs 1,00,000 at a sale price of Rs 1,20,000. 40% of these goods remained unsold at close of the year.

(v) On 1.4.2016 motor vehicles of Hockey Ltd. were overvalued by Rs 1,00,000. Applicable depreciation rate is 20%.

(vi) Dividends declared for the year 2016-2017 on 31.3.2017 in the holding and the subsidiary companies are 15% and 10% respectively.

(vii) Details of Trade payables and Trade receivables:

	Football Ltd.	Hockey Ltd.
Trade payables		
Bills Payable	–	1,60,000
Sundry creditors	4,30,000	4,80,000
	4,30,000	**6,40,000**

Trade receivables		
Debtors	9,30,000	7,80,000
Bills Receivables	1,45,000	-
	10,75,000	**7,80,000**

(viii) Bills receivable of Football Ltd. were drawn upon Hockey Ltd.

Prepare consolidated Balance Sheet as on 31st March, 2017.

Answer

Note: It is assumed that the preference shares given in the question are non-convertible in the nature.

Consolidated Balance Sheet of Football Ltd. and its subsidiary Hockey Ltd.as on 31st March, 2017

Particulars	**Note No.**	**(Rs)**
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	55,00,000
(b) Reserves and Surplus	2	12,24,750
(2) **Minority Interest (W.N.3)**		9,11,000
(3) **Current Liabilities**		
(a) Short term borrowings	3	1,90,000
(b) Trade payables	4	9,25,000
(c) Other current liabilities	5	8,63,750
Total		96,14,500
II. Assets		
(1) **Non-current assets**		
(a) Fixed assets		
i. Tangible assets	6	43,70,000
ii. Intangible assets	7	9,47,500
(b) Non-current investments	8	9,90,000
(2) **Current assets**		
(a) Inventories	9	11,62,000
(b) Trade receivables	10	17,10,000
(c) Cash and cash equivalents	11	4,35,000
Total		96,14,500

Notes to Accounts

	Rs.	**Rs.**
1. Share Capital		
Authorised, Issued and paid up capital		-
4,80,000, Equity shares of Rs 10 each	48,00,000	
70,000, 10% preference shares of Rs 10 each	7,00,000	55,00,000
2. Reserves and surplus		
General reserve – Football Ltd.		
Balance 5,50,000		
Add: Share in Hockey Ltd. [W.N. 1] 1,65,000	7,15,000	
Profit and loss account (W.N. 4)	5,09,750	12,24,750

3. Short term borrowings Bank Overdraft Football Ltd. Hockey Ltd.	 1,20,000 70,000	 1,90,000
4. Trade payables Football Ltd. Hockey Ltd. Less: Mutual debt	 4,30,000 6,40,000 (1,45,000)	 9,25,000
5. Other current liabilities Dividend payable Football Ltd. Equity Preference Hockey Ltd. Equity Preference	 7,20,000 70,000 50,000 23,750	 7,90,000 73,750 8,63,750
6. Tangible assets Plant and Machinery Football Ltd. Rs 12,00,000 Hockey Ltd. Rs 5,00,000 Motor Vehicles Football Ltd. Rs 9,50,000 Hockey Ltd. (Rs 7,50,000-1,00,000+ 20,000) Furniture & Fittings Football Ltd. Rs 6,50,000 Hockey Ltd. Rs 4,00,000	 17,00,000 16,20,000 10,50,000	 43,70,000
7. Intangible assets Goodwill Football Ltd. Hockey Ltd. Add: Goodwill on consolidation (W.N. 2)	 4,50,000 3,00,000 7,50,000 1,97,500	 9,47,500
8. Non-current investments Investments Football Ltd. (Rs 26,00,000 – 20,60,000) Hockey Ltd.	 5,40,000 4,50,000	 9,90,000
9. Inventories Inventory Football Ltd. Hockey Ltd. Less: Unrealised profit	 4,50,000 7,20,000 11,70,000 (8,000)	 11,62,000

10. Trade receivables		
Football Ltd.	10,75,000	
Hockey Ltd.	7,80,000	
Less: Mutual Debt	(1,45,000)	17,10,000
11. Cash and cash equivalents		
Cash at Bank		
Football Ltd.	2,25,000	
Hockey Ltd.	2,10,000	4,35,000

Working Notes:

(1)	**Analysis of Profits of Hockey Ltd.**		**Capital Profits**	**Revenue Reserve**	**Revenue Profit**
		Rs	**Rs**	**Rs**	**Rs**
(a)	General Reserve as on 1.4.2016	2,00,000			
Less: Bonus issue (1/10 of Rs 20,00,000)		(2,00,000)	–	–	
(b)	Addition to General Reserve during 2016-2017 (Rs 4,20,000 – Rs 2,00,000)			2,20,000	
(c)	Profit and Loss Account balance as on 1.4.2016	3,00,000			
Less: Dividend paid for the year 2015-2016		(2,00,000)	1,00,000		
(d)	Profit for the year 2016-2017 (Rs 6,00,000 – Rs 1,00,000)				5,00,000
(e)	Adjustment for over valuation of motor vehicles		(1,00,000)		
(f)	Adjustment of revenue profit due to overcharged depreciation (20% on Rs 1,00,000)				20,000
(g)	Preference dividend for the year 2016-2017 @ 10%				(38,000)
–				2,20,000	4,82,000
Football Ltd.'s share (3/4)				1,65,000	3,61,500
Minority Interest (1/4)				55,000	1,20,500
2,20,000					4,82,000
(2)	**Cost of Control**			**Rs**	**Rs**
Cost of investments in Hockey Ltd.					20,60,000
Less: Paid up value of equity shares (including bonus shares) [80,000 + 70,000 + (10% of 1,50,000)] × Rs 10				16,50,000	
Paid-up value of preference shares				1,42,500	
Pre-acquisition dividend*				70,000	(18,62,500)
Cost of control/Goodwill					1,97,500
(3)	**Minority Interest**				
Equity share capital [Rs 5,00,000 + Rs 50,000 (Bonus)]					5,50,000
Preference share capital (Rs 3,80,000 – Rs 1,42,500)					2,37,500
Share of revenue reserve [W.N. 1]					55,000
Share of revenue profit [W.N. 1]					1,20,500
Preference dividend					23,750

Less: Unrealised gain 8,000 x 1/4		(2,000)
		9,84,750
Less: Dividend payable		
Equity	50,000**	
Preference	23,750	73,750
		9,11,000
(4) **Profit and Loss Account – Football Ltd.**		
Balance	10,00,000	
Share in profit of Hockey Ltd. [W.N. 1]	3,61,500	
Share in preference dividend of Hockey Ltd.	14,250	
		13,75,750
Less: Pre-acquisition dividend credited to profit and loss account*	70,000	
Unrealised profit on inventory [(40% of Rs 20,000)x $\frac{3}{4}$]	6,000	
Equity dividend [48,00,000 x 15 %]	7,20,000	
Preference dividend [7,00,000 x 10 %]	70,000	(8,66,000)
		5,09,750

Note: No information has been given in the question regarding date of bonus issue by Hockey. It is also not mentioned whether the bonus shares are issued from pre-acquisition general reserve or post-acquisition general reserve. The above solution is given on the basis that Hockey Ltd. allotted bonus shares out of pre-acquisition general reserve.

* The dividend on 70,000 shares only (acquired on 1.4.2016) is a pre-acquisition dividend.

**It is assumed that bonus shares issued during the year 2016-17 are not entitled for dividend

Investment in Subsidiaries and Associate Co.

Q63.

The draft Balance Sheet of three companies, W, H, and O as at 31.3.2017 is as under:

	Rs in thousands		
Assets	**W**	**H**	**O**
Fixed assets	697	648	349
Investments			
1,60,000 shares in H	562	---	---
80,000 shares in O	184	---	---
Cash at bank	101	95	80
Trade receivables	386	321	251
Inventory	495	389	287
Total	**2,425**	**1,453**	**967**
Liabilities			
Share capital (Nominal value Rs 1 per share)	600	200	200
Reserves	1,050	850	478
Trade payables	375	253	189
Debentures	400	150	100
Total	**2,425**	**1,453**	**967**

You are given the following information:

(a) W purchased the shares in H on 13.10.2015 when the balance in reserves was Rs 500 thousands.

(b) The shares in O were purchased on 11.5.2015 when the balance in reserves was Rs 242 thousands.

(c) The following dividend have been declared but not accounted for before the accounting year end.

W	-	Rs 65 thousands
H	-	Rs 30 thousands
O	-	Rs 15 thousands

(d) Included in inventory figure of O is inventory valued at Rs 20 thousands which had been purchased from W at cost plus 25%.

(e) Goodwill in respect of the acquisition of H has been fully written off.

(f) On 31.3.2017 H made bonus issue of one share for every share held. This had not been accounted in the balance sheet as on 31.3.2017.

(g) Included in trade payables of W is Rs 18 thousands to O, which is included in trade receivables of O.

Prepare Consolidated Balance Sheet of W as at 31.3.2017.

Answer

Consolidated Balance Sheet of W and its subsidiary H as at 31st March, 2017

Particulars	Note No.	(Rs in thousands)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		600.00
(b) Reserves and Surplus (W.N.4)		1,355.80
(2) Minority Interest (W.N.3)		204.00
(3) Non-Current Liabilities		
Long-term borrowings	1	550.00
(4) Current Liabilities		
(a) Trade Payables (Rs 375+Rs 253)		628.00
(b) Other Current Liabilities	2	71.00
Total		3,408.80
II. Assets		
(1) Non-current assets		
(a) Fixed assets (Rs 697+ Rs 648)		1,345.00
(b) Non-current investment	3	270.80
(2) Current assets		
(a) Inventories (Rs 495 + Rs 389)		884.00
(b) Trade receivables (Rs 386 + Rs 321)		707.00
(c) Cash and cash equivalents	4	196.00
(d) Other current asset	5	6.00
Total		3,408.80

Notes to Accounts

		Rs in thousands	
1.	Long Term Borrowings		
Debentures (Rs 400 + Rs 150)			550.00
2.	Other current liabilities		
Dividend (W.N.6)			71.00
3.	Non-current investment		

Investment in Associate (W.N.5)	184.00	
(including goodwill Rs 7.20 thousand)		
Add: Accumulated reserves	86.80	270.80
4. Cash and cash equivalents		
Cash at Bank (Rs 101+ Rs95)		196.00
5. Other current asset		
Dividend receivable from O		6.00

Working Notes:

Shareholding Pattern

Total Shares of H Ltd. 2,00,000 Held by W Ltd. 1,60,000 i.e. 80%

Minority Interest 40,000 [20%]

1. Analysis of profits of H

	Rs in thousands	
	Pre acquisition profits	Post acquisition profits
Reserves on the date of acquisition	500	350
Less: Bonus issue*	(200)	-
	300	350
Less: Dividend declared on 31.3.2017	-	(30)
	300	320
Minority interest (20%)	60	64
W's share (80%)	240	256

2. Cost of control/Goodwill

	Rs in thousands	
Amount paid for investment		562
Less: Paid up value of shares including bonus (80% of 400)	320	
Share in pre-acquisition profits of H [WN 1]	240	(560)
Goodwill		2

* It is assumed that bonus issue had been made out of pre-acquisition reserves.

3. Minority Interest

	Rs in thousands
Paid up value of share including bonus issue (400 × 20%)	80
Share in pre acquisition profits of H [WN 1]	60
Share in post acquisition profits of H [WN 1]	64
	204

4. Consolidated Reserves

	Rs in thousands
Balance as per W's Balance Sheet	1,050.00
Add: Share in post-acquisition profits of H [WN 1]	256.00
Dividend from H	24.00
Share of profit from Associate O - 86.80	
Add: Dividend from O - 6.00	92.80 **1,422.80**
Less: Dividend payable - 65.00	

Goodwill written off - 2.00	(67.00)
	1,355.80

5. Investment in Associate O as on 31.03.2017 (As per AS 23)

	Rs in thousands	
Amount paid for investment		184.00
Less: Paid up value of shares	80.00	
Share in pre-acquisition reserves (40% of Rs 242)	96.8	(176.80)
Goodwill (Identified at the time of purchase)		7.20
Initial cost		184.00
Add: Increase in equity reserves [40% of Rs (478 –15 –242)]	88.40	
Less: Unrealised profit (20×25/125)×40%	(1.60)	86.80
Investment in Associate O as on 31.03.2017		270.80
Share of profit from Associate O Rs (270.80 – 184 + 6)		92.80

6. Dividend

	Rs in thousands
W	65
Minority Interest (Rs 30 – Rs 24)	6
	71

Important Notes:

Important Notes:

Important Notes:

Important Notes:

VALUE ADDED STATEMENT

Q64. (ICAI MODULE)

Value Added Ltd. furnishes the following Profit and Loss A/c:

Profit and Loss A/c for the year ended 31st March, 2007

Income	**Notes**	**Rs. ('000)**
Turnover	1	29,874
Other Income		1,040
		30,914
Expenditure		
Operating expenses	2	26,741
Interest on 8% Debenture		987
Interest on Cash Credit	3	151
Excise duty/GST		1,952
		29,831
Profit before depreciation		1,083
Less Depreciation		342
Profit before tax		741
Provision for tax	4	376
Profit after tax		365
Less Transfer to Fixed assets Replacement Reserve		65
		300
Less: Dividend paid		125
Retained Profit		175

Notes:

(1) Turnover is based on invoice value including GST/excise duty.

(2) Salaries, wages and other employee benefits amounting to Rs 14,761('000) are included in operating expenses.

(3) Cash Credit represents a temporary source of finance. It has not been considered as a part of capital.

(4) Transfer of Rs. 54('000) to the credit of deferred tax account is included in provision for tax.

Prepare value added statement for the year ended 31st March, 2007 and Reconcile total value added with profit before taxation.

(November 2007,- Marks 8)

Ans.: GVA = 16,831.

Q65. From the following Profit and Loss Account of Brightex Co. Ltd. prepare a gross value added statement for the year ended 31-12-1998:

Show also the reconciliation between gross value added and profit before taxation.

Profit & Loss Account for the year ended 31-12-1998

	Notes	(Rs. 000)	(Rs. 000)
Income:			
Sales			6,240
Other income			55
			6,295
Expenditure:			
Production and operational exp.	1	4,320	
Administration expenses	2	180	
Interest & other charges	3	624	
Depreciation		16	5,140
Profit before tax			**1,155**
Provision for tax			55
			1,100
Balance as per last balance sheet			60
Transferred to fixed assets replacement reserve		400	1,160
Dividend paid		160	560
Surplus carried to Balance Sheet			600

Notes

(1) **Production & operation:**

Consumption of raw materials	3,210
Consumption of stores	40
Local tax	8
Salaries to administrative staff	620
Other manufacture expenses	442
	4,320

(2) Administration expenses include salaries and commission to Directors — 5

(3) **Interest and other charges include:**

(a) Interest on bank overdraft (Overdraft is of temporary nature)	109
(b) Fixed loan from I.C.I.C.I.	51
(c) Working capital loan from I.F.C.I.	20
(d) GST amount to one-tenth of total value added by Manufacturing and trading activities	

(Ans.: Total Value Added 1,855)

Bonus Schemes based on Added Value

Q66. The Value added statement of Value Ltd. for the last 5 years are furnished below:

Year	**2007-08**	**2008-09**	**2009-10**	**2010-11**	**2011-12**
Sales	6,000	8,000	10,000	12,000	14,000
Less :					
Bought Out Goods and services:					
	2,960	4,400	5,800	7,200	8,400
Value added	**3,040**	**3,600**	**4,200**	**4,800**	**5,600**

Application Towards:					
To Pay Employees	1,368	1,584	1,680	1,968	2,240
To Directors Rem.	30	44	40	48	50
To Providers of Capital	250	336	440	512	630
To Government Tax	640	760	840	1,000	1,120
For Maint. & Expansion	752	876	1,200	1,272	1,560

The above employees cost includes Annual Incentives that were decided and paid after negotiations with labour unions as under:

	100	108	118	130	150

From 2012-13 onwards it was agreed to introduced value added incentive schemes (VAIS) that would enable employees to have the opportunity to earn better incentives in case of enhanced performances. The salient features of VAIS are as under:

(i) The **highest contribution** for the last 5 years shall be the target index.

(ii) 50% of the excess of actual contribution in 2012-13over target shall be paid to the employees as incentives.

(iii) CONTRIBUTION shall mean the value added for the year reduced by Employees costs before incentive and expressed as a percentage of Turnover for the year. The Result so obtained is to be rounded off to the nearest whole number.

The profit and loss account summary for the year 2012-13 is given below from which you are required to:

(I) Calculate the amount of incentive payable to the employees.

(II) Prepare statement of application of Value Added for the year 2012-13 after the payment of incentives.

Summarized Profit and Loss account of Value Ltd. for the year ended 31.03.2013

Sales		17,250
Less:		
Material Consumed	6,400	
Wages	1,200	

Production Salaries	400	
Production Expenses	1,600	
Depreciation on machinery	1,000	
Administrative Salaries	600	
Administrative Expenses	700	
Director Rem	60	
Administrative Deprecation	350	
Interest on debentures	80	
Advertisement and Sales promotion	600	
Salaries to sales team	125	
Selling Expenses	150	
Selling Deprecation	120	13,385
Profit Before Taxes		**3,865**
Taxes	1,190	
Dividends proposed	800	
Balance C/o		**1,875**

(November 2013 – 8 Marks)

(Answer: Target Index – 30%; Contribution – 32%, GVA – 7800, Incentive – 173)

Important Note:

ECONOMIC VALUE ADDED

Q67. (Q15 PM)

From the following information of Vinod Ltd., compute the economic value added:

(i)	Share capital	Rs. 2,000 lakhs
(ii)	Reserve and surplus	Rs. 4,000 lakhs
(iii)	Long-term debt	Rs. 400 lakhs
(iv)	Tax rate	30%
(iv)	Risk free rate	9%
(v)	Market rate of return	16%
(vi)	Interest	Rs.40 lakhs
(vii)	Beta factor	1.05
(viii)	Profit before interest and tax	Rs. 2,000 lakhs

(June 2009; Marks 8)

Ans. 391

Q68. (Q14 of PM)

Pilot Ltd. supplies the following information using which you are required to calculate the economic value added.

•	Financial Leverage	1.4 times
•	Capital (equity and debt)	
	Equity shares of Rs. 1,000 each	34,000 (number)
	Accumulated profit	Rs. 260 lakhs
	10 percent Debentures of Rs 10 each	80 lakhs (number)
•	Dividend expectations of equity shareholders	17.50%
•	Prevailing Corporate Tax rate	30%

(June 2009 Marks 6)

Ans. 35

Q69. You are given the following information about Ram Ltd.:

(i) Beta for the year 2010-11	1.05
(ii) Risk Free Rate	12%
(iii) Long Range Market Rate (based on BSE Sensex)	15.14%

(iv) Extracts from the liability side of Balance Sheet as at 31 st March, 2011.

	(Rs. in lakhs)
Equity	29,160
Reserves and surplus	43,740
Shareholder's fund	72,900
Loan funds	8,100
Total funds (long-term)	81,000

(v) Profit after tax Rs. 20,394.16 lakhs

(vi) Interest deducted from profit Rs. 487,00 lakhs

(viii) Effective tax rate (i.e. (Provision for Tax/PBT) x 100) 24.45%

Calculate Economic Value Added of Ram Ltd. as on 31 st March 2011.

[May 2012]

Ans.:

We know that EVA = NOPAT - Cost of Capital Employed

Where EVA = Economic Value Added

NOPAT = Net Operating Profit After Tax

Required calculation are as follows:

(i) NOPAT

Profit After Tax	Rs. 20,394.16 lakhs
Add Interest Net of Tax [Rs. 487 lakhs (1 -0.2445)]	Rs. 367.93 lakhs
NOPAT	Rs. 20,762.09 lakhs

(ii) Cost of Equity:

Cost of Equity = Risk free Rate + b [Market Rate - Risk Free Return]

= 12% + 1.05 x (15.14 -12.00)

= 12% + 3.30% = 15.30%

(iii) Cost of Debt

Cost of Debt $=\frac{487\times(1-0.2445)}{8,100}$ Rs. 100 = 4.54%

(iv) Weighted Average Cost of Capital (WACC)

	Amount (Rs. lakhs)	Weight	Cost	WACC%
Equity Debt	72,900	90	15.30	13.77
	8,100	10	4.54	0.454
	81,000	1.00		14,224

(v) Cost of Capital Employed = Rs. 81,000 × 14.224% = RS. 11,521.44 lakhs

(vi) EVA = NOPAT - Cost of Capital Employed

= Rs. 20,762.09 lakhs – Rs. 11,521.44 lakhs = Rs. 9,240.65 lakhs

Important Note:

MARKET VALUE ADDED

Q70. The Capital structure of W Ltd. whose shares are quoted on the NSE is as under –

Equity Shares of Rs. 100 each fully paid	Rs. 505 Lakhs
9% Convertible Pref. Shares of Rs. 10 each	Rs. 150 Lakhs
12% Secured Debentures of Rs. 10 each	5,00,000
Reserves	Rs. 101 Lakhs
Statutory Fund	Rs. 50,50,000

The statutory fund is compulsorily required to be invested in Government securities. The ordinary shares are quoted at a premium of 500%, Preference shares at Rs. 30 and debentures at par value.

You are required to ascertain the Marked Value added of the company and also give your assessement on the market value added as calculated by you.

(Answer: 2673.50) **(May 2014 – 4 Marks)**

HUMAN RESOURCE REPORTING

Q71:

From the following information in respect of Exe Ltd., calculate the total value of human capital by following Lev and Schwartz model:

Distribution of employees of Exe Ltd.

Age	Unskilled		Semi-skilled		Skilled	
	No	Av. Annual earnings	No.	Av. Annual earnings	No.	Av. Annual earnings
		(Rs'000)		(Rs '000)		(Rs'000)
30-39	70	3	50	3.5	30	5
40-49	20	4	15	5	15	6
50-54	10	5	10	6	5	7

Apply 15% discount factor.

Solution

The present value of earnings of each category of employees by applying 15% discount factor is ascertained as below:

(A) Unskilled employees:

Age group 30-39. Assume that all 70 employees are just 30 years old:

	Present value
	Rs
Rs 3,000 p.a. for next 10 years	15,057
Rs 4,000 p.a. for years 11 to 20	4,960
Rs 5,000 p.a. for years 21 to 25	1,025
	21,042

Age group 40-49. Assume that all 20 employees are just 40 years old:

Rs 4,000 p.a. for next 10 years	20,076
Rs 5,000 p.a. for years 11 to 15	4,140
	24,216

Age group 50-54: Assume that all 10 employees are just 50 years old:

` 5,000 p.a. for next 5 years	16,760

Similarly, present value of each employee under other categories will be calculated.

(B) Semi-skilled employees:

Age group 30-39

	Present value
	Rs
Rs 3,500 p.a. for next 10 years	17,567
Rs 5,000 p.a. for years 11 to 20	6,200
Rs 6,000 p.a. for years 21 to 25	1,230

Age group 40-49

Rs 5,000 p.a. for next 10 years	25,095
Rs 6,000 p.a. for years 11 to 15	4,968
	30,063

Age group 50-54

Rs 6,000 p.a. for next 5 years	20,112

(C) Skilled employees:
Age group 30-39

	Present value
	Rs
Rs 5,000 p.a. for next 10 years	25,095
Rs 6,000 p.a. for years 11 to 20	7,440
Rs 7,000 p.a. for years 21 to 25	1,435
	33,970

Age group 40-49

Rs 6,000 p.a. for next 10 years	30,114
Rs 7,000 p.a. for years 11 to 15	5,796
	35,910

Age group 50-54

Rs 7,000 p.a. for next 5 years	23,464

Total value of Human Capital

Age	**Unskilled**		**Semi-skilled**		**Skilled**		**Total**	
	No.	Av. Annual earnings	No.	Av. Annual earnings	No.	Av. Annual earnings	No.	Av. Annual earnings
		(Rs '000)		(Rs '000)		(Rs '000)		(Rs '000)
30-39	70	14,72,940	50	12,49,850	30	10,19,100	150	37,41,890
40-49	20	4,84,320	15	4,50,945	15	5,38,650	50	14,73,915
50-54	10	1,67,600	10	2,01,120	5	1,17,320	25	4,86,040
	100	21,24,860	75	19,01,915	50	16,75,070		57,01,845

Q72

From the following details, compute the total value of human resources of skilled and unskilled group of employees according to Lev and Schwartz (1971) model:

	Skilled	**Unskilled**
(i) Annual average earning of an employee till the retirement age.	60,000	40,000
(ii) Age of retirement	65 years	62 years
(iii) Discount rate	15%	15%

(iv) No. of employees in the group	30	40
(v) Average age	62 years	60 years

Solution

Value of Employees as per Lev and Schwartz method:

$$V = \sum_{t=\tau}^{T} \frac{I(t)}{(1+r)^{t-\tau}}$$

Where,

V = the human capital value of a person.

I(t) = the person's annual earnings up to retirement.

r = a discount rate specific to the person.

t = retirement age.

Value of Skilled Employees:

$$= \frac{60{,}000}{(1+0.15)^{65-62}} + \frac{60{,}000}{(1+0.15)^{65-63}} + \frac{60{,}000}{(1+0.15)^{65-64}}$$

$$= \frac{60{,}000}{(1+0.15)^{3}} + \frac{60{,}000}{(1+0.15)^{2}} + \frac{60{,}000}{(1+0.15)^{1}}$$

= Rs 39,450.97 + Rs 45,368.62 + Rs 52,173.91 = Rs 1,36,993.50

Total value of skilled employees is Rs 1,36,993.50 x 30 employees= Rs 41,09,805

Value of Unskilled Employees:

$$= \frac{40{,}000}{(1+0.15)^{62-60}} + \frac{40{,}000}{(1+0.15)^{62-61}}$$

$$= \frac{40{,}000}{(1+0.15)^{2}} + \frac{40{,}000}{(1+0.15)^{1}}$$

= Rs 30,245.74 + Rs 34,782.60 = Rs 65,028.34

Total value of unskilled employees = Rs 65,028.34 x 40 employees= Rs 26,01,133.60

Total value of human resources (skilled and unskilled)

= Rs 41,09,805 + Rs 26,01,133.60= Rs 67,10,938.60

Q73

The following information is supplied to you about Lookdown Ltd.

Capital & Reserves	
Equity Shares of Rs 100 each of which Rs 75 has been called up	5,00,000
Equity Shares in respect of which calls are in arrear @ 25 per share	Rs 1,00,000
General Reserve	Rs 10,00,000
Profit & Loss account (balance at beginning of the year)	(Rs 25,00,000)
Profit/(loss) for the year	(Rs 1,80,000)
Industry Average Profitability	12.50%
8% Debentures of Rs 10 each	8,00,000
Lookdown 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	Rs 4,00,000

Average Income tax rate on salaries after considering the impact of Rs 3 lakhs p.a. i.e., the exemption amount	25%
Provident Fund contribution by Employer per month	Rs 50,000
Profits over and above target expected by hiring Mr. X	10%

Required

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 @ Rs 50,000 per month and after deduction of Income-tax on salary.

Solution

Cost to Company in employing Mr. X

	Rs
Salary before tax Rs 4,00,000 x 12 = 48,00,000 / 0.75	64,00,000*
Add: Employee's PF contribution (50,000 x 12)	6,00,000
	70,00,000
Add: Employer's PF contribution (50,000 x 12)	6,00,000
	76,00,000
Equity Share Capital paid up (5,00,000 shares of Rs 75 each)	3,75,00,000
Less: Calls in arrears	(1,00,000)
	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	80,00,000
Capital base	4,37,20,000
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 Rs 76,00,000 is more than Rs 60,11,500.

Q74

Rose Limited provides you the following information on 31st March, 20X1:

Capital and Reserves	
Equity share capital of Rs 10 each of which Rs 8 has been called up	8,00,000 shares
Calls in arrears	Rs 1,00,000
General Reserve	Rs 7,50,000
50,000, 9% Debentures of ` 100 each	Rs 50,00,000
Profit/(loss) for the year	(Rs 2,50,000)
Industry Average Profitability rate	12.5%

The company is proposing to hire the service of Mr. Raman to turn around the company.

Required

You are required to determine the maximum salary that could be offered to him if it is expected that after his appointment, the profits of the company will increase by 10% over and above the target profit.

Solution

Calculation of Capital base

	Rs
Equity Share Capital paid up (8,00,000 shares of Rs 8 each)	64,00,000
Less: Calls in arrears	(1,00,000)
	63,00,000
General Reserve	7,50,000
Loss for the year	(2,50,000)
9% Debentures	50,00,000
Capital base	1,18,00,000
Target Profit 12.5% of capital base	14,75,000

Expected profits to be achieved by taking the services of Mr. Raman is Rs 16,22,500 (i.e. 14,75,000 + 10% of 14,75,000). Therefore, the maximum salary that can be paid to Mr. Raman will be Rs 16,22,500 p.a.

Important Notes:

Mutual Fund

Q75:

A Mutual fund raised 100 lakhs on 1st April, 2009 by issue of 10 lakh units of Rs. 10 per unit. The fund invested in several capital market instruments to build a portfolio of Rs. 90 lakhs. The initial expenses amounted to Rs. 7 lakhs. During April, 2009, the fund sold certain securities of cost Rs. 38 lakhs for Rs. 40 lakhs and purchased certain other securities for Rs. 28.20 lakhs. The fund management expenses for the month amounted to Rs. 4.50 lakhs of which Rs. 0.25 lakhs was in arrears. The dividend earned was Rs. 1.20 lakhs. 75% of the realised earnings were distributed. The market value of the portfolio on 30.04.2009 was Rs. 101.90 lakhs. Determine NAV per Unit.

(Answer: 11.10)

Q76:

On 1st April, 2016, Good Return Mutual Fund has the following assets and prices at 3.00 pm

Shares of	No. of Shares	Market price per share
A Ltd.	10000	18.50
B Ltd.	35000	384.40
C Ltd.	10000	263.60
D Ltd.	75000	575.60
E Ltd.	20000	27.65
No. of Units of Funds		5,00,000 units

(a) Calculate the Net Asset Value of Fund.

(b) Assuming Mr. Suresh send a cheque of Rs. 75,00,000 to the fund on 1st April, 2016 and Fund Manager purchases 15000 shares of C Ltd. and balance is held in Bank . What will be the new position of the Fund?

(c) Calculate the Net Asset Value of the Fund, if on 2nd April, 2016 at 3.00 pm the market price of shares is as follows:

Shares of	Rate per Share
A Ltd.	21.30
B Ltd.	417.00
C Ltd.	289.80
D Ltd.	512.20
E Ltd.	35.00

(Answer: 120 per unit, 120 per unit and 115.05 per unit)

Q77: (ICAI Module – Test your knowledge Q2)

On 1.4.2008, a mutual fund scheme has 18 lakh units of face value of Rs. 10 each was outstanding. The scheme earned Rs. 162 lakhs in 2008-09, out of which Rs.90 lakhs was earned in the first half of the year. On 30.9.2008, 2 lakh units were sold at a "NAV of Rs.70.

Pass Journal entries for sale of units and distribution of dividend at the end of 2008-09.

(Answer: DER – 5/- per unit; Dividend Distribution – 8.60/-)

Q78.

Sparrow Holdings is a SEBI Registered Mutual Fund which made its maiden N.F.O (New Fund Offer) on 10th April, 2016 at ` 10 face value per unit. Subscription was received for 90 lakhs units. An underwriting arrangement was also entered into with Affinity Capital Markets Ltd., that agreed to underwrite the entire NFO of 100 lakh units on a commission of 1.5%.

Out of the monies received ` 892.50 lakhs was invested in various capital market instruments. The marketing expenses for the N.F.O amounted to ` 11.25 lakhs. During the financial year ended March 2013 the Fund sold securities having cost of ` 127.25 lakh (FV ` 54.36 lakhs) for ` 141.25 lakhs. The fund in turn purchased securities for ` 130 lakhs. The management expenses of the fund are regulated by SEBI stipulations which state that the same shall not exceed 0.25% of the average funds invested during the year. The actual amount spent towards management expenses was ` 2.47 lakhs of which ` 47,000 was in arrear. The dividends earned on the investments held amounted to ` 2.51 lakhs of which a sum of ` 25,000 is yet to be collected. The fund distributed 80% of realized earnings. The closing market value of the portfolio was ` 1120.23 lakhs.

You are required to determine the closing per unit NAV of the fund.

Solution:

Particulars	**Amount**
Net Assets of Sparrow holding	
Closing cash balance (W.N.2)	79.99
Closing Market Value of Investments	1,120.23
Accrued Dividends (collectable)	0.25
	1,200.47
Less: Current Liabilities	
Outstanding Management Fee (payable)	(0.47)
Closing Net Assets (A)	1,200.00
Units outstanding (in lakhs) (B)	100.00
NAV per unit (A/B)	**12.00**

Working Notes:

		Rs. in Lakhs
Computation of opening cash balance		
Proceeds of NFO in full including underwriters commitment		1000.00
Less: Initial Purchase of Securities		(892.50)

		107.50
Less: Underwriting Commission	15.00	
Marketing Expenses	11.25	26.25
Opening Cash Balance		81.25
2. Computation of Closing cash balance		
Opening bank balance (W.N.1)		81.25
Add: Proceeds from sale of securities	141.25	
Dividends received on investment	2.26	143.51
		224.76
Less: Cost of Securities purchased	130.00	
Management Expenses (W.N.3)	1.76	
Capital Gains Distributed (141.25 – 127.25 x 80%0	11.20	
Dividends Distributed (2.26 x 80%)	1.81	(144.77)
Closing cash balance		79.99
3. Computation of Management Expenses Chargeable		
Actual Expense Incurred [A]		2.47
Opening Investment Made	892.50	
Closing Funds Invested (892.50 - 127.25 + 130)	895.25	
Total	1787.75	
Average Funds Invested (1,787.75/2)	893.875	
0.25% of Average Funds Invested [B]		2.23
Lower of A or B		2.23
Less: Amount unpaid		(0.47)
Management expenses paid		**1.76**

Q79.

Calculate the year-end NAV of the Mutual Fund scheme on the basis of the information given below:

(i) UTI launched a new Fund scheme for ` 6,000 crore.

(ii) Underwriting Commission is 1% of the fund shared equally by SBI, PNB, Syndicate Bank and UTI Bank.

(iii) The Fund was launched on 1.4.2016 with a face value of ` 1000 per unit.

(iv) Underwriting Commission was paid in full.

(vi) Management Expense was allowed by SEBI @ 1% of the Fund raised. However, during the year management expense was of ` 45 crore only. The management decided to defer the payment of ` 5 crore to the next financial year.

(vii) On 1.5.2016, the total fund received was invested after deduction of underwriting commission and ` 100 crore to meet the day to day management expenses. The investment fund received yielded 10% interest per annum. The interest was received for 3 quarters and the interest of last quarter is yet to be received. The interest realized in cash has

been distributed to the unit holders @ 80%. The financial year runs from April to March. The quarter starts from the date of investment i.e. 1.5.2016.

Solution:

Calculation of Net Asset Value of a fund

		Rs. In Crores
Total Assets:		
Investment (6,000 - 60 -100)	5840.00	
Add: Closing Cash Balance (Refer W.N.)	147.60	
Add: Interest for two months due to be received 5840 x 10% 2/12	97.33	6084.93
Less: Outstanding Management Expenses		(5.00)
Total value of the fund		**6079.93**

No. of units = 6000 / 1000 = 6 Cr Units

NAV per unit = 6079.93 crores / 6 Crore = Rs. 1013.32 per unit

Working Note:

Calculation of year-end cash/bank balance of the fund

		Rs. In Crores
Cash received during the year for the fund		
Sale of units		6,000
Add: Interest for 3 quarters on investment *5840 x 10% x 9/12*		438
		6,438
Less: Underwriting commission	60	
Management expenses paid in cash	40	
Investment	5840	
Dividend paid (438 x 80%)	350.40	(6290.40)
		147.60

Q80.

Ramesh Goyal 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 Ramesh Goyal 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 31.03.2017	1,900	3,000	Nil
NAV	10.40	10.10	9.80

Solution:

Calculation of effective yield on per annum basis in respect of three mutual fund schemes of Ramesh Goyal upto 31.03.2017

		X	Y	Z
1	Amount of Investment (Rs)	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 (Rs)	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 (Rs)	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 up to 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%)

Important Notes:

NON BANKING FINANCIAL COMPANIES

Q81:

XYZ Finance Ltd. is a non-banking finance company. It makes available to you the costs and market price of various investments held by it:

		(Rs. in lakhs)
Investments	**Cost**	**Market Price**
Equity shares:		
Scrip A	40.00	40.80
Scrip B	21.00	16.00
Scrip C	40.00	24.00
Scrip D	40.00	80.00
Scrip E	60.00	70.00
Scrip F	50.00	60.00
Scrip G	20.00	4.00
	271.00	**294.80**
Mutual Funds:		
MF1	26.00	16.00
MF2	20.00	14.00
MF3	4.00	6.00
	50.00	**36.00**
Government Securities:		
GV1	40.00	44.00
GV2	50.00	48.00
	90.00	**92.00**

You are required to answer following questions:

(i) Can the company adjust depreciation of a particular item of investment within a category?

(ii) What should be the value of investments?

(iii) Is it possible to offset depreciation investment in mutual funds against appreciation of value of investments in Equity Shares and Government Securities.

(Ans.: (i) Yes, Costs and Market price of current investments should be aggregated under each group.

(ii) Equity Shares	Rs.271.00
Mutual Funds	Rs.36.00
Government Securities	Rs.90.00

(iii) No)

Q82:

Provider Ltd. is a non-banking finance company who accepts public deposits and also deal in hire purchase business. It provides you with the following information regarding major hire purchase deals as on 31.3.2009:

Few machines were sold on hire purchase basis. The hire purchase price was set as Rs. 100 lakhs as against the cash price of Rs. 80 lakhs. The amount was payable as: (I) Rs. 20 lakhs down payment and balance in 5 equal instalments. The hire vendor collected 1st instalment as on 31.3.2010 but could not collect the second instalment, which was due on 313.2011. The company was finalizing accounts for the year 31.3.2011. Till 15.5.2011, the date on which the Board of Directors signed the accounts, the second instalment was not collected. Presume I.R.R. to be 10.42%. Required:

(i) What should be the principal outstanding as on 1.4.2010? Should the company recognise financial charge for the year 2010-11 as income?

(ii) What should be the net book value of assets as on 31.3.2011 so far as Provider Ltd. is concerned as per NBFC prudential norms requirement for provisioning?

(iii) What should be the amount of provision to be made as per prudential norms for NBFC laid down by RBI?

(Answer: 50.252; Yes – since it is PA; 48/-; Basic provision - 7.488, Additional – Nil)

Q83:

Peoples Financiers Ltd. is an NBFC providing Hire purchase solutions for acquiring consumer durables. The following information is extracted from its books for the year ended 31st March, 2014:

Assets Funded	**Interest overdue but recog. In P&L**		**Net Book Value of Assets O/s (Rs. Cr.)**
	Period overdue	**Interest Amount (Rs. Cr.)**	
LCD TV	Upto 12 months	480.00	20123.00
Washing Machine	For 24 months	102.00	2410.00
Refrigerators	For 30 months	50.50	1280.00
Air Conditioner	For 45 months	26.75	647.00

(Answer: Additional Provision – 1205.90/-)

Important Notes:

SHARE BASED PAYMENT & INDAS 102

Q84 –Share-based payment - Purchase of goods (ICAI Module)

Indian Inc. issued 995 shares in exchange for purchase of an office building. The title was transferred in the name of Indian Inc. on Feb 20X1 and shares were issued. Fair value of the office building was INR 2,00,000 and face value of each share of Indian Inc was INR 100.

Pass the journal entries?

Solution

1 February, 20X1	**INR**	
Office Building Dr.	2,00,000	
To Share capital (995 x 100)		99,500
To Securities premium (balance)		1,00,500
(Recognition of equity option and cash settlement option)		

Q85 – Share-based payment – Services (ICAI Module)

Reliance limited hired a maintenance company for its oil fields. The services will be settled by issuing 1,000 shares of Reliance. Period for which the service is to be provided is 1 April 20X1 to 1 July 20X1 and fair value of the service was estimated using market value of similar contracts for INR 1,00,000. Nominal value per share is INR 10.

Record the transactions?

Solution

Fair value of services	1,00,000
No. of months	3
Monthly expense	33,333.33

30-Apr-20X1	**INR**	
Repair & Maintenance Dr.	33,333.33	
To Share based payment reserve (equity)		33,333.33
(Recognition of Equity settled SBP using fair value of services rendered)		
31-May-20X1		
Repair & Maintenance Dr.	33,333.33	
To Share based payment reserve (equity)		33,333.33
(Recognition of Equity settled SBP using fair value of services rendered)		
30-Jun-20X1		
Repair & Maintenance Dr.	33,333.33	
To Share based payment reserve (equity)		33,333.33
(Recognition of Equity settled SBP using fair value of		

services rendered)		
1-Jul-20X1		
Share based payment reserve (equity) Dr.	1,00,000	
To Equity Shares (1000 x 10)		10,000
To Securities premium (balancing figure)		90,000

Q86 - Equity Settled Shared Based Payment- Service conditions (ICAI Module)

ABC Limited granted to its employees, share options with a fair value of INR 5,00,000 on 1 April 20X0, if they remain in the organization upto 31st March 20X3. On 31st March 20X1, ABC limited expects only 91% of the employees to remain in the employment. On 31st March 20X2, company expects only 89% of the employees to remain in the employment. However, only 82% of the employees remained in the organisation at the end of March, 20X3 and all of them exercised their options. Pass the Journal entries?

Solution

Period	Proportion	Fair value	To be vested	Cumulative expenses	Expenses
	a	b	c	d=bx c x a	e = d-previous period d
Period 1	1/3	5,00,000	91%	1,51,667	1,51,667
Period 2	2/3	5,00,000	89%	2,96,667	1,45,000
Period 3	3/3	5,00,000	82%	4,10,000	1,13,333
					4,10,000

Journal Entries

30-Jun-20X1		
Employee benefits expenses Dr.	1,51,667	
To Share based payment reserve (equity)		1,51,667
(1/3 of expected vested equity instruments value)		
30-Jun-20X2		
Employee benefits expenses Dr.	1,45,000	
To Share based payment reserve (equity)		1,45,000
(2/3 of expected vested equity instruments value)		
30-Jun-20X3		
Employee benefits expenses Dr.	1,13,333	
To Share based payment reserve (equity)		1,13,333
(Final vested equity instruments value)		
Share based payment reserve (equity) Dr.	4,10,000	
To Share Capital		4,10,000
(re-allocated and issued shares)		

Q87 - Cash Settled Shared Based Payment-Service conditions (ICAI Module)

XYZ issued 10,000 Share Appreciation Rights (SARs) that vest immediately to its employees on 1 April 20X0. The SARs will be settled in cash. At that date it is estimated, using an option pricing model, that the fair value of a SAR is INR 95. SAR can be exercised any time upto 31 March 20X3. At the end of period on 31 March 20X1 it is expected that 95% of total employees will exercise the option, 92% of total employees will exercise the option at the end of next year and finally 89% will be vested only at the end of the 3rd year. Fair Values at the end of each period have been given below:

Fair value of SAR	INR
31-Mar-20X1	112
31-Mar-20X2	109
31-Mar-20X3	114

Solution

Period	Fair value	To be vested	Cumulative	Expense
	a	b	c= a x b x 10,000	d= c-prev. period c
Start	95	100%	9,50,000	9,50,000
Period 1	112	95%	10,64,000	1,14,000
Period 2	109	92%	10,02,800	(61,200)
Period 3	114	89%	10,14,600	11,800
				10,14,600

Journal Entries

1-Apr-20X0		
Employee benefits expenses Dr.	9,50,000	
To Share based payment liability		9,50,000
(Fair value of the SAR recognized)		
31-Mar-20X1		
Employee benefits expenses Dr.	1,14,000	
To Share based payment liability		1,14,000
(Fair value of the SAR re-measured)		
31-Mar-20X2		
Share based payment liability Dr.	61,200	
To Employee benefits expenses		61,200
(Fair value of the SAR re-measured & reversed)		
31-Mar-20X3		
Employee benefits expenses Dr.	11,800	
To Share based payment liability		11,800
(Fair value of the SAR recognized)		
Share based payment liability Dr.	10,14,600	
To Cash		10,14,600
(Settlement of SAR)		

Q88 – Share-based payment - Cash & equity alternatives (ICAI Module)

Tata Industries issued share-based option to one of its key management personal which can be exercised either in cash or equity and it has following features:

Option I	**Period**	**INR**
No of cash settled shares		74,000
Service condition	3 years	
Option II		
No of equity settled shares		90,000
Conditions:		
Service	3 years	
Restriction to sell	2 years	
Fair values		
Equity price with a restriction of sale for 2 years		115
Fair value grant date		135
Fair value 20X0		138
20X1		140
20X2		147

Pass the Journal entries?

Solution

Fair value of Equity option components:		
Fair value of a share with restrictive clause		INR 115
No. of shares		90,000
Fair value (90,000 X 115)	A	INR 1,03,50,000
Fair value of a share at the date of grant		INR 135
No. of cash settled shares		74,000
Fair value (74,000 X 135)	B	INR 99,90,000
Fair value of equity component in compound instrument (A-B)		INR 3,60,000

Journal Entries

31/12/20X0	**INR**	
Employee benefit expenses Dr.	35,24,000	
To Share based payment reserve (equity) (3,60,000/3)		1,20,000
To Share based payment liability (138 x 74,000) / 3		34,04,000
(Recognition of equity option and cash settlement option)		
31/12/20X1		
Employee benefits expenses Dr.	36,22,667	
To Share based payment reserve (equity) (3,60,000/3)		1,20,000
To Share based payment liability (140 x 74,000) 2/3 - 34,04,000		35,02,667
(Recognition of equity option and cash settlement option)		

31/12/20X2		
Employee benefits expenses Dr.	40,91,333	
To Share based payment reserve (equity) (3,60,000/3)		1,20,000
To Share based payment liability		39,71,333
(147 x 74,000) 3/3 - (34,04,000 + 35,02,667) (Recognition of equity option and cash settlement option)		
Upon cash alternative chosen		
Share based payment liability (147 x 74,000) Dr.	1,08,78,000	
To Bank/ Cash		1,08,78,000
(Being settlement made in cash)		
Upon equity alternative chosen		
Share based payment liability (147 x 74,000) Dr.	1,08,78,000	
To Share capital		1,08,78,000
(Being settlement made in equity)		

Q89. - Equity settled – Non market conditions (Reversals) (ICAI Module)

ACC limited granted 10,000 share options to one of its managers. In order to get the options, the manager has to work for next 3 years in the organization and reduce the cost of production by 10% over the next 3 years.

Fair value of the option at grant date was INR 95
Cost reduction achieved-
Year 1 12% Achieved
Year 2 8% Not expected to vest in future
Year 3 10% Achieved
How the expenses would be recorded?

Solution

It is a non-market related condition. Hence the target to achieve cost reduction would be taken while estimating the number of options to be vested.

Year FV of the	**Options**	**Fair value**		**options vested**
Year 1	10,000	95	1/3	3,16,667
Year 2	10,000	95	0	(3,16,667)
Year 3 10,000 95	10,000	95	3/3	9,50,000

The condition to achieve 10% cost reduction each was not fulfilled in the year 2 and there was no expectation to vest this non-market condition in future as well and hence earlier expense amount was reversed in year 2. Since in the year 3 the non-market condition was again met, hence allsuch expense will be charged to Profit and Loss.

Q90 - Equity Settled – Market based conditions (ICAI Module)

Apple Limited has granted 10,000 share options to one of its directors for which he must work for next 3 years and the price of the share should increase by 20% over next 3 years.

The share price has moved as per below details -
Year 1 22%

Year 2	19%
Year 3	25%

At the grant date, the fair value of the option was INR 120.
How should we recognize the transaction?

Solution

The share price movement is a market based vesting condition hence its expectations are taken into consideration while calculating the fair value of the option.

Even if the required market condition as required is not fulfilled, there is no requirement to reverse the expense previously booked.

Irrespective of the outcome of the market prices (as it is already taken care of in the fair value of the option), each period an amount of (120 x 10,000)/3 = INR 4,00,000 will be charged to profit and loss.

MODIFICATIONS/REPRICING:

Repricing means decline in the exercise price of options, so as to make options more attractive. In such case:

1. **Calculate fair value as on the date of Repricing before the effect of modification**
2. **Calculate fair value on the date of repricing after the effect of modification**
3. **Calculate incentive due to repricing (1-2)**
4. **Such incentive should be written off over the remaining vesting period.**

Q91. At the beginning of year 1, an entity grants 100 share options to each of its 500 employees. Each grant is conditional upon the employee remaining in service over the next three years. The entity estimates that the fair value of each option is Rs. 15. On the basis of a weighted average probability, the entity estimates that 100 employees will leave during the three-year period and therefore forfeit their rights to the share options.

Suppose that 40 employees leave during year 1. Also suppose that by the end of year 1, the entity's share price has dropped, and the entity reprices its share options, and that the repriced share options vest at the end of year 3. The entity estimates that a further 70 employees will leave during years 2 and 3, and hence the-total expected employee departures over the three- year vesting period is 110 employees. During year 2, a further

35 employees leave, and the entity estimates that a further 30 employees will leave during year 3, to bring the total expected employee departures over the three-year vesting period to 105 employees: During year 3, a total of 28 employees leave, and hence a total of 103 employees ceased employment during the vesting period. For the remaining 397 employees, the share options vested at the end of year 3.

The entity estimates that, at the date of repricing, the fair value of each of the original share options granted (ie before taking into account the repricing) is Rs. 5 and that the fair value of each repriced share option is Rs. 8. Calculate option expense.

(Answer: Rs. 195000, 259250 260350)

Q92 - Cancellation- Equity Settled Share based payment (ICAI Module)

Anara Fertilizers Limited issued 2000 share options to its 10 directors for an exercise price of INR 100.The directors are required to stay with the company for next 3 years.

Fair value of the option estimated	INR 130
Expected no of Directors to vest the option	8

During the year 2, there was a crisis in the company and Management decided to cancel the scheme immediately. It was estimated further as below-

Fair value of option at the time of cancellation was INR 90
Market price of the share at the cancellation date was INR 99

There was a compensation which was paid to directors and only 9 directors were currently in employment. At the time of cancellation of such scheme, it was agreed to pay an amount of INR 95 per option to each of 9 directors.

How the cancellation would be recorded?

Solution

	Year 1	Year 2	
A)			
Expected directors to vest	8	9	
Fair value of option	130	130	
No. of options 2,000	2,000	2,000	
Total	20,80,000	23,40,000	
Expense weightage	1/3		Full, as it is cancelled
Expense for the year	6,93,333	16,46,667	Remaining amount since cancelled
B) Cancellation compensation			
No. of directors			9

Amount agreed to pay	95
No. of options/ director	2,000
Compensation amount (9 x 95 x 2,000)Also refer working notes 1 and	217,10,000

Working Notes:

1. Amount to be deducted from Equity

No. of directors	9
Fair value of option (at the date of cancellation)	90
No. of options/ director	2,000
Total	16,20,000

2. Amount transferred to Profit and Loss

Total cancellation compensation	17,10,000
Less: To deduct from Equity	(16,20,000)
Balance transferred to Profit and Loss	90,000

EXTRA QUESTIONS

GRADED VESTING

Q93. The following particulars in respect of stock options granted by a company are available:

Grant date	April 1,2006
Number of employees covered	400
Number of options granted per employee	60
Nominal value per share (Rs.)	100
Exercise price per share (Rs.)	125

Shares offered were put in three groups. Group I was for 20% of shares offered with vesting period one-year. Group II was for 40% of shares offered with vesting period two-years. Group III was for 40% of shares offered with vesting period three-years. Fair value of option per share on grant date was Rs.10 for Group 1, Rs.12.50 for Group II and Rs.14 for Group III

Position on 31/03/07

(a) Number of employees left = 40

(b) Estimate of number of employees to leave in 2007-08 = 36

(c) Estimate of number of employees to leave in 2008-09 = 34

(d) Number of employees exercising options in Group I = 350

Position on 31/03/08

(a) Number of employees left = 35

(b) Estimate of number of employees to leave in 2008-09 = 30

(c) Number of employees exercising options in Group II = 319

Position on 31/03/09

(a) Number of employees left = 28

(b) Number of employees at the end of last vesting period = 297

(c) Number of employees exercising options in Group III = 295

Options not exercised immediately on vesting, were forfeited.

Compute expenses to recognise in each year and show important accounts in books of the company.

(Ans.: 123080; 80700 and 33040)

Important Notes:

AS-4 Contingencies & Events occuring after the Balance Sheet Date	IND AS – 10 Events after the Reporting Period

Some important Case Studies:

CASE 94: While preparing its Final accounts for the year ended 31st March, 2011, a company made a provision for bad debts @ 5% of its total debtors. In the last week of feb, 2011 a debtor for Rs. 2 lakhs has suffered heavy losses due to earthquake; the loss was not covered by any insurance policy. In April 2011 the debtor became insolvent. Can the company provide for full loss arising out of insolvency of the debtor in the final accounts for the year ended 31st March, 2011?

Answer: According to AS 4 "Adjustment to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date.

In the above case, circumstances were existing on the balance sheet date and event of April (declaration of insolvency) only confirm the circumstances existing on the date of balance sheet i.e. 31.03.2011. In this case company should make full amount of provision for bad debts arising out of insolvency of the debtor for the year ended 31st March, 2011.

CASE 95: A company deals in petroleum products. The sale price of petrol is fixed by the government. After the balance sheet date, but before the finalization of accounts of the company, the government unexpectedly increased the petrol prices retrospectively. Can the company account for additional revenue at the close of the year? Discuss.

Answer: Company cannot account for the revenue at the close of the year because it is not an adjusting event as per AS 4, since there were no circumstances of price increase was persisting on the date of balance sheet. Hence mere disclosure is needed in this case. Further it cannot also be treated as prior period item in subsequent year as per AS 5 because there was no error or omission in preparation of FS of any earlier year or years.

CASE 96: Amitabh Ltd. entered into an agreement to sell its immovable property included in the balance sheet at Rs. 10 lacs to another company for Rs. 20 lacs. The agreement to sell was concluded on 28th Feb, 2011 and the sale deed was registered on 1st May, 2011. FS of the company are approved on 30th June,2011. Comment with reference to AS 4?

Answer: According to AS 4 "Adjustment to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date.

In this case, the sale of immovable property was carried out before the closure of the books of accounts. This is clearly an event occurring after the balance sheet date which requires an adjustment. Agreement to sell was effected before the balance sheet date and the registry was done after the balance sheet date but before the approval of accounts. So the adjustment for the sale of immovable property is necessary in the books of accounts for the year ended 31st March, 2011.

CASE: 97

In a company theft of cash of Rs. 1.80 lacs by the cashier in January 2011, was detected in May 2011. The accounts of the company were not yet approved by the Board of Directors of the company. Whether the theft of cash has to be adjusted in the accounts of the company for the year ended 31.03.2011. Decide.

CASE: 98

A company has filled a legal suit against the debtor from whom Rs. 15 lakh is recoverable as on 31.03.2012. The chances of recovery by way of legal suit are not good as per the legal opinion by the counsel in April, 2012. Can the company provide for full amount of Rs. 15 lakh as provision for doubtful debts? Discuss in brief.

CASE: 99

A major fire has damaged the assets in a factory of a Limited company on 5th April – five days after the year end and closure of accounts. The loss is estimated at 10 crores out of which 7 crores will be recoverable from the insurers. Explain briefly how the loss should be treated in the final accounts for the previous year.

CASE: 100

Neel Limited has its corporate office in Mumbai and sells its products to its stockists all over India. On 31st March, 2013, the company wants to recognize receipts of cheques bearing date 31st March, 2013 or before, as "Cheques in Hand" by reducing "Trade Receivables". The Cheques in Hand is shown in the Balance sheet as an item of Cash and Cash Equivalents. All the cheques are presented to the bank in the month of April 2013and are also realized in the same month in normal course. State with reasons, whether each of the following is an adjusting event and how this fact is to be disclosed by the company, with reference to the relevant accounting standard:

(a) Cheques collected by marketing personnel of the company from stockists on or before 31st March, 2013.
(b) Cheques sent by the stockists through courier on or before 31st March, 2013.

Important Notes:

ACCOUNTING STANDARD - 5

"NET PROFIT OR LOSS FOR THE PERIOD, PRIOR PERIOD ITEMS AND CHANGE IN ACCOUNTING POLICIES"

Some Important Case Studies:

Q101

A limited company created a provision for bad and doubtful debts at 2.5% on debtors in preparing the financial statements for the year 2010-11.

Subsequently on a review of the credit period allowed and financial capacity of customers, the company decided to increase the provision to 8% on debtors as on 31.3.2011. The accounts of the company were not approved by the Board of Directors till the date of decision. While applying the relevant accounting standard can this revision be considered as an Extraordinary item or Prior Period Item?

Q102

X co. Ltd. signed an agreement with its employees union for revision of wages in june, 2012. The wage revision is with retrospective effect from 1.4.2008. The arrears of wages upto 31.03.12 amounts to Rs. 80/- Lacs. Arrears wages for the period from 1.4.12 to 30.6.12 amounts to Rs. 7/- Lacs.

Decide whether a separate disclosure of arrear of wages is required.

Q103

Goods of Rs. 5,00,000/- were destroyed due to flood in September 2008. A claim was lodged with insurance company, but no entry was passed in the books for insurance claim.

In March, 2011, the claim was passed and the company received a payment of Rs. 3,50,000/- against the claim. Explain the treatment of such receipt in final accounts for the year ended 31st March, 2011.

Q104

Cost of a machine acquired on 01.04.09 was Rs. 5,00,000. The machine is expected to realize Rs. 50,000 at the end of its working life of 10 years. Straight line depreciation of Rs. 45,000 per year has been charged upto 2011-12. For and from 2012-13, the company switched over to 15% pa reducing balance method of depreciation in respect of machine. The new rate of depreciation is based on revised uselife life of 15 years. The New rate shall apply with restrospective effect from 01/04/2009. State how would you deal with the above in the annual accounts of the company for the year ended 31st march, 2013 in the light of AS 5?

AS – 7 CONSTRUCTION CONTRACTS

Q105

MOHIT LTD. has undertaken bridge construction contract to be constructed in 3 years. Initial contract revenue Rs.900 crores. Initial contract cost Rs.800 crores.

Particulars	Years		
	1st	2nd	3rd
Estimated contract cost	805	---	---
Increase in contract revenue	---	20	---
Estimated additional increase cost	---	15	---
Contract cost incurred upto	161	584	820

At the end of 2nd year cost incurred includes Rs.10 crores, for material stored at the sites to be used in 3rd year to complete the project.

Sol.: Amount of revenue, expenses and profit recognised in statement of P&L a/c in three years:

Particulars	Up to reporting Date	Recognised in earlier years	Recognised in C. Year
Year I:			
Revenue (900X20%)	180	---	180
Expenses	161	---	161
Profit	19	---	19
Year II:			
Revenue (920X70%)	644	180	464
Expenses (584 - 10)	574	161	413
Profit	70	19	51
Year III:			
Revenue (920X100%)	920	644	276
Expenses	820	574	246
Profit	100	70	30

WN:

Initial revenue agreed	900	900	900
Variation	---	20	20
Total contract value	900	920	920
Contract cost incurred upto the date of reporting	161	584[incl. 10 crores mat)	820
	805	820	820
Total estimated contract cost	20%	70%	100%

Stage of completion	(161/805 X 100)	(584-10/820 X 100]	(820/820 X 100)

Q106

A firm of contractors obtained a contract for construction of bridges across river Krishna. The following details are available for the year ended 31.3.04

Total Contract Price	1,000
Work Certified	500
Work not Certified	105
Estimated further Cost of Completion	495

Sol.:

Cost incurred up to the date	605
Cost incurred further cost	495
Total cost of contract	1100

Degree of Completion = 55% (605/1100). Turnover = 1000 X 55% = 550. Loss in C.Year = 550 – 605 = 55.

Provision to be created in current year for future loss:

Total cost	1100
Less: Total revenue	1000
Total loss	100
Less: C.Y. loss	55
Future loss	45

Q107

Chitram Movies undertook construction contract to construct sub-way for Rs.100 crores on 1.1.2004. It estimated construction cost initially at Rs.70 crores. Contract was estimated to be completed in three years. However, when starting the work it was found that there were rocks underground at construction site and cost shall increase by Rs.36 crores and the contract shall be completed in 3 years. The company wants to provide for expected loss of Rs.2 crores per year.

a. Is the treatment correct?

b. If work has not yet started but by technical survey it was known on 25.2.2004 that there was rock underneath at construction site. Company did not want to provide for any losses of Rs.6 crores for the year ended 31.3.2004, considering that when project work would start, the losses shall be provided for.

Sol.:

a. No, the stand of company is not correct. As per AS-7, when it is certain that total contract cost will exceed total contract revenue, the expected loss should be recognised as an expense immediately. Therefore expected loss of Rs.6crores, to be provided for the year ended 31.3.2004.

b. No, the argument of the company is not correct. Irrespective of whether or not work has commenced, the loss is to be provided for the year ended 3 1.03.2004.

GUIDANCE NOTE ON ACCOUNTING FOR REAL ESTATE TRANSACTIONS

Q108

Facts Details

Total saleable area 20,000 sqft
Land cost Rs. 300 lacs
Estimated construction and development cost Rs. 300 lacs
Total area sold 5000 sqft
Total sale agreement value Rs. 200 lacs
Amount realized Rs.50 lacs
Construction cost incurred including land cost Rs. 360 Lacs
Whether revenue to be recognised as threshold limit is achieved or not?

Solution

Percentage of completion for threshold limit is 20%
Area sold is 25% of total saleable area
Amount realized exceeds 10% of agreement value
Final answer – No revenue to be recognized as threshold limit not achieved

Q109

Facts Details

Total saleable area 20,000 sqft
Land cost Rs.300 lacs
Estimated construction and development cost Rs.300 lacs
Total area sold 5,000 sqft
Total sale agreement value Rs.200 lacs
Amount realized Rs.50 lacs
Cost incurred including land cost Rs.390 lacs
Compute profit.

Solution

Percentage of completion for threshold limit is 30%
Area sold is 25% of total saleable area
Amount realized exceeds 10% of agreement value
Revenue to be recognized at 65 % of Rs. 200 lacs i.e. Rs. 130 lacs
Cost [5000/20,000 x 390] Rs. 97.50 lacs
Work in progress = Rs. 292.50 lacs
Profit = Rs. 32.50 lacs

Important Notes:

AS – 10 (R) PROPERTY, PLANT & EQUIPMENT (PPE)	IND AS – 16 PROPERTY, PLANT & EQUIPMENT

Q110: (Change in estimate of useful life)

Entity A purchased an asset on 1st January 2013 for ` 1,00,000 and the asset had an estimated useful life of 10 years and a residual value of nil.

On 1st January 2017, the directors review the estimated life and decide that the asset will probably be useful for a further 4 years.

Calculate the amount of depreciation for each year, if company charges depreciation on Straight Line basis.

Solution

The entity has charged depreciation using the straight-line method at ` 10,000 per annum i.e (1,00,000/10 years).

On 1st January 2017, the asset's net book value is [1,00,000 – (10,000 x 4)] ` 60,000. The remaining useful life is 4 years.

The company should amend the annual provision for depreciation to charge the unamortised cost over the revised remaining life of four years.

Consequently, it should charge depreciation for the next 4 years at ` 15,000 per annum i.e. (60,000 / 4 years).

Q111 - Replacement Cost

Sun Ltd has acquired a heavy road trailer at a cost of ` 100,000 (with no breakdown of component parts). The estimated useful life is 10 years. At the end of the sixth year, the engine requires replacement, as further maintenance is uneconomical due to the off-road time required. The remainder of the vehicle is perfectly road worthy and is expected to last for the next four years. The cost of the new engine is ` 45,000. The discount rate assumed is 5%.

Whether the cost of new engine can be recognised as the asset, and if so, what treatment should be followed?

(Hint Answer: Revised Cost = (100,000 - 33,580 + 45,000) = 111,420)

Q112 - Deferred Payment Credit

On 1st April 20X1, an item of property is offered for sale at ` 10 million, with payment terms being three equal installments of ` 33,33,333 over a two years period (payments are made on 1st April 20X1, 31st March 20X2 and 31st March 20X3).

The property developer is offering a discount of 5 percent (i.e. ` 0.5 million) if payment is made in full at the time of completion of sale. Implicit interest rate of 5.36 percent p.a.

Show how the property will be recorded in accordance of Ind AS 16.

Q113 – Exchange of Assets

Pluto Ltd owns land and building which are carried in its balance sheet at an aggregate carrying amount of ` 10 million. The fair value of such asset is ` 15 million. It exchanges the land and building for a private jet, which has a fair value of ` 18 million, and pays additional 3 million in cash.

Show the necessary treatment as per Ind AS 16.

(Hint: Profit on Exchange – 5000; Private Jet recognize at 18000)

Q114: Accumulated depreciation at the date of revaluation

Jupiter Ltd. has an item of plant with an initial cost of ` 100,000. At the date of revaluation accumulated depreciation amounted to ` 55,000. The fair value of asset, by reference to transactions in similar assets, is assessed to be ` 65,000.

Find out the entries to be passed?

Solution

Method – I:

Accumulated depreciation	Dr.	55,000	
To Asset Cost			55,000
Asset Cost	Dr.	20,000	
To Revaluation reserve			20,000

The net result is that the asset has a carrying amount of ` 65,000 (100,000 – 55,000 + 20,000).

Method – II:

Carrying amount (100,000 – 55,000) =	45,000
Fair value (revalued amount)	65,000
Surplus	20,000
% of surplus (20,000/ 45,000)	44.44%

Entries to be Made:

Asset (1,00,000 x 44.44%)	Dr.	44,444	
To Accumulated Depreciation (55,000 x 44.44%)			24,444
To Surplus on Revaluation			20,000

Q115: Utilisation of Revaluation Surplus

An item of PPE was purchased for 9,00,000 on 1 April 20X1. It is estimated to have a useful life of 10 years and is depreciated on a straight line basis. On 1 April 20X3, the asset is revalued to` 9,60,000. The useful life remains unchanged at ten years.

Show the necessary treatment as per Ind AS 16.

Q116:

List price of machine	*80,00,000*
Import duty	*5,00,000*
Delivery fees	*1,00,000*
Electrical installation costs	*10,00,000*
Pre-production testing	*4,00,000*
Purchase of a five-year maintenance contract with vendor	*7,00,000*

In addition to the above information XYZ Ltd. was granted a trade discount of 10% on the initial list price of the asset and a settlement discount of 5%, if payment for the machine was received within one month of purchase. XYZ Ltd. paid for the plant on April 20, 20X1. At what cost the asset will be recognised?

(Hint: 92,00,000)

Important Notes:

ACCOUNTING STANDARD – 11(Revised)

"EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES"

Q117

Sunshine company Ltd. imported Raw Materials worth US Dollars 9,000 on 25th Feb, 2011, when the exchange rate was 44/- per US Dollars. The Transaction was recorded in the books at the above mentioned rate. The payment for the transaction was made on 10th April, 2011, when the exchange rate was 48/- per US Dollars. At the yearend 31st March, 2011, the rate of exchange was 49/- per US Dollar.

The Chief Accountant of company passed an entry on 31st March, 2011 adjusting the cost of raw material consumed for the difference between 48/- and 44/- per US Dollar. Discuss whether this treatment is justified as per the provisions of AS – 11 (Revised).

Q118

Patidar Ltd. borrowed US $ 5,00,000 on 31.12.2010 which will be repaid (settled) as on 30.06.11. Patidar Ltd. prepares its financial statements ending on 31.3.11. Rate of exchange between reporting currency (rupees) and foreign currency ($) on different dates are as under:

31.12.2010	1 US $ = Rs. 44.00
31.03.2011	1 US $ = Rs. 44.50
30.06.2011	1 US $ = Rs. 44.75.

(i) Calculate borrowings in reporting currency to be recognized in the books on above mentioned dates & also show journal entries for the same.

(ii) if borrowing was repaid on 28.02.11 on which date exchange rate was 1US $ = Rs. 44.20 than what entry should be passed?

Q119

S Ltd. purchased fixed assets costing Rs. 3,000 lacs on 01.01.2010 and the same was fully financed by foreign currency loan ($) payable in three equal installments. Exchange rates were 1US $ = Rs. 40.00 and 42.50 as on 01.01.2010 and 31.12.2010. First installment was paid on 31.12.2010. The entire difference in foreign exchange has been capitalized. You are required to state, whether the treatment made by S Ltd. is correct or not?

Q120

The following is the Trial Balance of TATA Ltd. as on 31st March, 2011 before subsequent recognition:

Particulars	Dr. Amt.	Cr. Amt.
Purchases	80,000	-
Debtors (Foreign currency) $ 2,000	60,000	-
Debtors (Indian currency)	25,000	-
Loan (long term F.C.) for financing Machine $ 3,000	-	1,00,000
Loan (long term F.C.) others $ 4,000	-	1,40,000
Machine	2,00,000	-
Sales		1,25,000
	3,65,000	**3,65,000**

Exchange rate as on 31.03.2011 is Rs. 50/- per US $. Apply Para 46 and Prepare Trial Balance thereafter.

Q121

A Ltd. has following information

Year	Exchange Diff on Short Term Foreign Currency Monetary Item	Exchange Diff on Long Term Foreign Currency Monetary Item Monetary Item (Dep Assets)	Exchange Diff on Long Term Foreign Currency Monetary Item Monetary Item (Other Items)
05-06	10,000	18,000	26,000
06-07	11,000	19,000	27,000
07-08	12,000	20,000	28,000
08-09	13,000	21,000	29,000
09-10	14,000	22,000	30,000
10-11	15,000	23,000	31,000
11-12	16,000	24,000	32,000
12-13	17,000	25,000	33,000

Apply Para 46. Depreciation rate 10%. WDV of Asset on 01/04/2006 is Rs. 10,00,000.

Important Notes:

ACCOUNTING STANDARD - 12
ACCOUNTING FOR GOVERNMENT GRANTS

CASE STUDIES:

Q122

AS-12 Govt. Grant (RTP Nov. 2012 and also in Practice Manual):

Gandhi Ltd. received a grant of 2,500/- lacs during the last accounting year (2010-11) from the govt. for walfare activities to be carried on by the company for its employees. The grant prescribed the conditions for its utilization. However, during the year 11-12, it was found that the conditions of grants were not complied with and the grant had to be refunded to the gov. in full. Elucidate the current accounting treatment, with reference to the provision of AS 12.

Q123

AS-12 Govt. Grant (Practice Manual):

Santosh Ltd. has received a grant of 8 Crores from the govt. for setting up a factory in backward area. Out of this grant, the company distributed 2 Crores as dividend. Also, Santosh Ltd. received land free of cost from the state govt. but it has not recorded the grant in its books as no money has been spent. In the light of AS 12 examine, whether the treatment of both the grants is correct.

Q124

AS-12 Govt. Grant (Practice Manual):

A Ltd. purchased a machinery for 40/- lacs (useful life 4 years and residual value 8/- lacs). Govt .grant received is 16/- lacs. After 2 years grant of 12/- lacs is to be refunded.
Show the journal entry to be passed at the time of refund of grant and also calculate the value of fixed asset, if:

(1) The grant is credited to the Machinery a/c
(2) The grant is credited to deferred grant a/c.

ACCOUNTING STANDARD – 15 (REVISED)

EMPLOYEE BENEFITS

DIFFERENCE BETWEEN DEFINED BENEFIT PLANS AND DEFINED CONTRIBUTION PLANS

Defined Contribution Plans (DCP)	Basis of Difference	Defined Benefit Plans (DBP)
Obligation is limited to the amount that it agrees to contribute	**Entity's Legal or Constructive Obligation**	Obligation is to provide agreed benefits to current and former employees (Obligation is not limited)
Contributions and Investment Returns	**How Much Post Employment Benefit is to be received by employee**	Agreed Benefits
Risk in substance on the Employee	**Actuarial Risk (Benefits will be more/less than expected)**	Risk in substance on the entity.
Risk in substance on the Employee.	**Investment Risk**	Risk in substance on the entity.

Q125. A lump sum gratuity, equal to 1% of final salary for each year of service, is payable on termination of service. The salary in year 1 is Rs. 10,000 and is assumed to increase at 7% (compound) each year resulting in Rs. 13,100 at the end of year 5. The discount rate used is 10% per annum. Shows how the obligation builds up for an employee who is expected to leave at the end of year 5, assuming that there are no changes in actuarial assumptions.

Ans.: (Amount in Rs.)

Year	**1**	**2**	**3**	**4**	**5**
Benefit attributed to:					
- prior year	0	131	262	393	524
- current year (1% of final salary)	131	131	131	131	131
- current and prior years	131	262	393	524	655
Opening Obligation	-	89	196	324	476
Interest at 10%	-	9	20	33	48
Current Service Cost (see note 2)	89	98	108	119	131

Closing Obligation (see note 1)	89	196	324	476	655

Note 1

Closing obligation

	Yr.1	Yr.2	Yr 3	Yr.4	Yr. 5
Gratuity attributable	131	262	393	524	655
Payable after (years)	4	3	2	1	0
Discounting factor	.683	.751	.826	.909	1
PV	89	196	324	476	655

Note 2

Current Service Cost

	Yr.1	Yr.2	Yr.3	Yr.4	Yr. 5
Gratuity of current year	131	131	131	131	131
Payable after (years)	4	3	2	1	0
Discounting factor	.683	.751	.826	.909	1
PV	89	98	108	119	131

Q126. The following data apply to X Ltd. defined benefit pension plan for the year ended 31.03.2009, calculate the actual return on Plan assets:

Benefits Paid	2,00,000
Employer contribution	2,80,000
Fair market value of plan assets on 31.03.2009	11,40,000
Fair market value of plan asset as on 31.03.2008	8,00,000

(Nov. 2009 New Course)

(Answer: Actual Return – 260000)

Q127. As on 1st April, 2014, the fair value of planned assets was Rs. 1,00,000 in respect of a pension plan of Zeleous Ltd. On 30th September, 2014, the plan paid out benefits of Rs. 19,000 and received contribution of Rs. 49,000. On 31st March, 2015, the fair value of plan assets was Rs. 1,50,000 and present value of the defined benefit obligation was Rs. 1,47,920. Actuarial losses on obligation for the year 2014-15 were Rs. 600.

On 1st April, 2014 the company made the following estimates, based on its market studies, understanding and prevailing prices:

Particulars	**%**
Interest and Dividend Income after tax payable by the fund	9.25
Realised and unrealised gains on plan assets (after tax)	2.00
Fund administration costs	-1.00
Expected rate of return	**10.25**

You are required to find expected and actual return on plan assets.

(Nov. 2015- 5 Marks)

(Answer: Expected Return on planned Assets – 11750; Actual Return – 20000)

Q128. An enterprise operates a pension plan that provides a pension of 2% on final salary for each year of service. The benefit will be vested after 5 years of service. On 1.1.2005, the enterprise improves the pension to 2.5% of the final salary for each year of service starting from 1.1.2001 at the date of improvement the Present Value of additional benefits for service from 1.1 .2001 to as follows:

Employees with more than 5 years of service at 1.1.2005	Rs. 2,00,000
Employees with less than 5 years of service	Rs. 1,20,000

(Average period until vesting = 3 years)
Suggest the accounting treatment.

Q129. An enterprise discontinues a business segment and the employees of this segment will earn no further benefits. This is curtailment without a settlement. Immediately before the curtailment the details were.

	Before Curtailment	**After Curtailment**
PV of obligation	1,000	900
FV of plan assets	820	820
Unrecognized past service cost	50	45

The curtailment reduces the obligation to Rs. 900 and URPSC to Rs.45. Suggest the accounting treatment.

Q130. P Ltd. has three business segments which are FMCG, Batteries and Sports Equipment. The Battery segment has been consistently underperforming and P Ltd. after several discussions with Labour unions have finally decided on closure of this segment. Under the agreement the employees of the Battery segment will earn no further benefit as the arrangement is a curtailment without settlement wherein the employees of the discontinued segment will continue to receive benefits for services rendered when the segment was functioning. As a result of the curtailment, the company's obligation that were arrived on the basis of actuarial valuations before the curtailment have come down. The following information is also furnished:

(i) The value of gross obligations before the curtailment calculated on actuarial basis was Rs. 4000 lakhs.
(ii) The value of unamortized past service costs is Rs. 100 lakhs.
(iii) The curtailment will bring down the gross obligations by Rs. 500 lakhs and P Ltd. anticipate a proportional decline in the value of unamortized past service costs also.
(iv) The fair value of the Plan Assets on date is estimated at Rs. 3250 lakhs.

You are required to calculated the gain from curtailment and also show the liability to be recognized in the Balance Sheet of P Ltd. after the Curtailment.

(Nov. 2013 – 5 Marks)

(Answer: Gain from Curtailment – 487.50 and Liability to be recognized in BS – 162.50)

Q131. A company furnishes the following details for its defined benefit plan on 1.4.2004

PV of obligation	1,00,000
FV of plan assets	1,00,000

	2004-05	**2005-06**	**2006-07**
Discount rate	10	9	8
Exp. Rate of return on Plan Assets	12	11.1	10.3
Current service cost	13,000	14,000	15,000
Benefits paid	15,000	18,000	19,000
Contributions paid	9,000	10,000	11,000
PV of Obligation on 31.03.	1,14,100	1,19,700	1,29,500
FV of Plan Assets on 31.03.	1,09,200	1,10,900	1,09,300

Expected average remaining working life of the employees is 10 years. In 2005-06 the plan was amended and the PV of additional benefit vested was Rs.5,000 and unvested was Rs.3,000. The remaining period till vesting was 3 years.

(Answer: Act. Gain/Loss on PVDBO – 6100 (L), 8669 (G) & 4224 (L)

Important Note:

ACCOUNTING STANDARD - 16
BORROWING COSTS

Q132:

XYZ Ltd. has taken a loan of USD 10,000 on 1.04.2003 for a specific project at an interest rate of 5% p.a., payable annually. On 1 April, 2003, the exchange rate between the currencies was Rs. 45 per \$. The exchange rate, as at March, 31st, 2004 is Rs. 48 per \$. The Corresponding amount could have been borrowed by XYZ Ltd. in local currency at an interest rate of 11% p.a. as on 1 April, 2003.

(Answer: 24000 + 25500 = 49500 BC)

Q133:

Assume the same questiong 2 above except interest rate in local currency borrowing is 13% instead of 11%.

(Answer: 24000 + 30000 = 54000 BC)

Q134:

The borrowings profile of Santra Pharmaceuticals Ltd. set up for the manufacture of antibiotics at Navi Mumbai is as under:

Date	Nature of borrowings	Amount borrowed	Purpose of Borrowings	Incidental Expenses
1/1/08	15% Demand Loan	60 Lakhs	Acquisition of Fixed Assets	8.33%
1/7/08	14.5% Term Loan	40 Lakhs	Acquisition of Plant & Machinery	5%
1/10/08	14% Bonds	50 Lakhs	Acquisition of Fixed Assets	8%

Fixed assets considered as Qualified as Under:

Sterling Manufacturing Shed	Rs. 10,00,000
Plant & Machinery (Total)	Rs. 90,00,000
Other Fixed Assets	Rs. 10,00,000

The project is completed on 1st January 2009 and is ready for commercial production. Show the capitalization of the borrowing cost.

Q135:

X Ltd. began Construction of a new building on 1st January, 2007. It obtained Rs. 1 lakhs special loan to finance the construction of the building on 1st January, 2007 at an interest rate of 10%. The company's outstanding two non specific loans were:

Amount	Rate
5,00,000	11%
9,00,000	13%

The expenditure that were made on the building project were as follows:

Janaury 2007	Rs. 2,00,000
April, 2007	Rs. 2,50,000
July, 2007	Rs. 4,50,000
December, 2007	Rs. 1,20,000

Building was completed by 31st December, 2007. Following the principles prescribed in AS – 16 Borrowing Cost. Calculate the amount of interest to be capitalized and pass one Journal Entry for capitalization of Cost and borrowing cost in respect of the building.

WIP A/c Dr. 1020000
To Bank A/c 10.20

Bulding A/c Dr. 1020000
To WP a/c 10.20

Interest a/c Dr 182000
To Loans a/c 182000

Building A/c Dr. 74216
To Interest a/c 74216

Profit and loss a/c dr. (182000-74216) = 107784
To Interest a/c 107784

Q136:
Calculate the amount of borrowing cost to be capitalized.

Particulars	**Amount**
Expenditure incurred till 31.03.2011	700000
Interest cost capitalised for FY 10-11	30000
Amount borrowed till 31.03.11 @ 15%	400000
Amount transferred to construction during 11-12	200000
Cash payment during 11-12 out of above	100000
Progress payments received	500000
New borrowings until 11-12 @ 15%	300000

EFFECTIVE INTEREST RATE METHOD:

Example: Martin Ltd. took a Loan of Rs. 10,00,000 on 01/04/2010 @ Interest rate of 10% pa for 5 years to be repaid in equal principal amount along with interest. Stamp duty charges incurred initially was Rs. 15000. Processing fees of Rs. 5000 was deducted by Bank. After 3 years Bank charged Rs. 9500 as renewal fees & on closure date bank charged Rs. 2500 for closure fees. Calculate Borrowing Cost for every year as per AS 16 and IND AS 23.

Important Note:

ACCOUNTING STANDARD - 17

SEGMENT REPORTING

Q137. An enterprise operates through segments, namely, A. B, C, D, E, F. G and H. The relevant information about these segments is given in the following table:

(Amount in Rs. '000)

	A	B	C	D	E	F	G	H	Total (Seg.)	Total (Entp.)
Seg. Revn										
(a) Ext		255	15	10	15	50	20	35	400	
(b) Inter-Seg	100	60	30	5	-	-	5	-	200	
(c) Total	100	315	45	15	15	50	25	35	600	400
Seg. Result	5	-90	15	-5	8	-5	5	7		
Seg. Assets	15	47	5	11	3	5	5	9	100	

Identify Reportable Segments

Q138. M/s XYZ Ltd. has three segments namely X, Y, Z. The total Assets of the Company are Rs. 10.00 crs. Segment X has Rs. 2.00 crs., segment Y has Rs. 3.00 crs. And segment Z has Rs. 5.00 crs. Deferred tax Assets included in the assets of each segments are X-Rs. O.50 ers., YRs. 0.40 crs. and Z-Rs. 0.30 crs. The accountant contends that all the three segments are reportable segments. Comment.

Q139. Prepare a segmental report for publication in Diversifiers Ltd. from the following details of the company's three divisions and the head office:

	Rs.(000)
Forging Shop Division	
Sales to Bright Bar Division	4,575
Other Domestic Sales	90
Export Sales	6,135
	10,800
Bright Bar Division	
Sales to Fitting Division	45
Export Sales to Rwanda	300
	345
Fitting Division	
Export Sales to Maldives	270

	Head Office	Divisions		
		Forging	Bright Bar	Fitting
Operating Profit or Loss before tax	-	240	30	-12
Reallocated cost from Head Office		72	36	36
Interest Costs		6	8	2
Fixed Assets	75	300	60	180
Net Current Assets	72	180	60	135
Long term Liabilities	57	30	15	180

[Advanced Accounting, May 2005, 8 marks]

Ans.:

Diversifiers Ltd.

Segment Report

	Divisions			Intersegment eliminations	Total
Particulars	**Forging Shop**	**Bright Bar**	**Fitting**		
Segment Revenue					
Domestic	90	-	-	-	90
Export	6135	300	270	-	6705
Total Ext. Sales	**6225**	**300**	**270**	**-**	**6795**
Inter Seg. Sales	4575	45	-	4620	-
Total Sales	**10800**	**345**	**270**	**4620**	6795
Segment Result	240	30	(12)	-	258
Head Office Expenses					(144)
Operating Profit					114
Interest					(16)
PBT					98
Assets & Liabilities					
Fixed Assets	300	60	180	-	540
Net Current Assets	180	60	135	-	375
Total Assets	480	120	315		915
Unallocated					147

Corporate Assets					(75+72)
Total assets					1062
Segment liabilities Unallocated corporate liabilities	30	15	180	-	225 57
Total liabilities					282

Geographical Marketwise Segment Revenue (Rs.000)

	Domestic	**Export (forging)**	**Export to Rwanda**	**Export to Maldives**	**Total**
External Sales	90	6135	300	270	6795

ACCOUNTING STANDARD – 19
LEASES

FINANCE LEASE

Q140. Fair value of Machine is Rs. 70,000

Years	Lease Rentals
0	20,000
1	38,000
2	25,000
3	23,000
4	6,000

Guaranteed residual value on lease was 5,000, Rate of interest 10%
Calculate value of Machine & Finance charges.

Q141. AS Ltd. Leased a machine to SB Ltd. on the following terms:
Fair value of the Machine is 4,00,000, Leas term is 5 years, Lease rental per annum would be Rs. 1,00,000, Guaranteed residual value is Rs. 20,000, Expected Residual value is Rs. 40,000 and Internal rate of return is 15%.
Depreciation is provided on straight line method at 10% pa. Ascertain unearned finance income. Necessary journal entries in the books of the Lessee in first year may be shown.
(November 2009, Old course)

Q142. S. Square P Ltd. has taken machinery on lease from S K ltd. The information is as under:

Lease term	= 4 years
Fair value at inception of lease	= Rs. 20,00,000
Lease rent	= Rs. 6,25,000 p.a. at the end of year
Guaranteed residual value	= Rs. 1,25,000
Expected residual value	= Rs. 3,75,000
Implicit interest rate	= 15%

Discounted rates are 0.8696, 07561, 06575, and 05718 respectively.
Calculate the value of the lease liability as per AS 19. **(November 2010: 4 Marks)**

Q143. Global Ltd. has initiated a lease for three years in respect of an equipment costing Rs. 1,50,000 with expected useful life of 4 years. The asset would revert to Global Ltd. under the leased agreement. The other information available in respect of lease agreement is:

(1) The unguaranteed residual value of the equipment after the expiry of the lease term is estimated at Rs. 20,000
(2) The implicit rate of interest is 10%
(3) The annual payments have been determined in such a way that the present value of the lease payment plus the residual value is equal to the cost of asset.

Ascertain in the hands of Global Ltd.

(i) The annual lease payments.
(ii) The unearned finance income
(iii) The segregation of finance income, and also
(iv) Show how necessary iterms will appear in its profit and loss account and balance sheet for the various years. **(May 2006, Marks 8)**

OPERATING LEASE

Q144. On April 1, 2002 ABC Ltd. leases equipment for 4 years to XYZ Ltd. The Cost of the equipment is Rs. 15,00,000 and has a useful life of 10 years (assume straight line method of depreciation). The lease payments to be made are as follows:

Year	Amount
1	1,00,000
2	1,50,000
3	1,75,000
4	2,00,000

The lease is classified as an operating lease. How would this lease be accounted for in the books of accounts of the Lessee and the Lessor?

SALE AND LEASE BACK TRANCTIONS:

Q145. A transferred to Bank a machine on sale and lease back basis:

Fair value of Machine	Rs. 1,50,000
Book value of Machine	Rs. 1,00,000
Selling price to bank	Rs. 1,30,000
Implicit rate of Interest	10%

Lease Rentals: 33,000; 21,000; 30,000; 28,000; 26,000; 24,000 and 22,000

Depreciation is on SLM basis and estimated life of machine is 7 years.

Consider sale and lease back was financial in nature.

Journalise for A

Q146. Journalise in each of the following cases assuming transaction is of sale and operating lease back:

Cases	Fair Value	Book Value	Sale Price
1	100000	100000	100000
2	100000	80000	100000
3	100000	120000	100000
4	100000	100000	120000
5	100000	80000	120000
6	100000	120000	120000
7	100000	100000	90000
8	100000	90000	80000
9	100000	70000	80000
10	100000	110000	80000

Important Notes:

ACCOUNTING STANDARD – 20

EARNINGS PER SHARE

Q147. Calculate Basic earnings per share for 10-11:-
Earnings attributable for Equity shareholders (10-11)- Rs. 10,00,000/-
Equity Shares opening Balance 1/4/2010: 16,500 shares of Rs. 10 each 7 paid up
Public Issue 1/7/2010: 10,000 shares of Rs. 10 each 6 paid up
Received calls on 1/10/2010: 16,400 shares Rs. 3 per share
Received calls on 1/11/2010: 10,000 shares Rs. 4 per share
(Answer: EPS - 49.56)

Q148. Calculate BEPS for the year 2005-06
Earnings attributable to Equity Shareholders for the year 2004-05- Rs10,00,000
Earnings attributable to Equity Shareholders for the year 2005-06- Rs. 12,00,000
Equity shares as on 1-4-04 - 10,000shares of Fv Rs. 10
Issued 5,000 and 3000 equity shares on 1-1-05 and 1-7-05 respectively and shares fully subscribed and paid up. 1:1 Bonus issue on 1-12-05
(Ans.: Rs. 88.89 & Rs. 34.04 and restated 34.18)

Q149. Calculate BEPS for the year 2005-06
Earnings attributable to Equity Shareholders for the year 2004-05– Rs. 10,00,000
Earnings attributable to Equity Shareholders for the year 2005-06 – Rs. 12,00,000
Equity share as on 1.4-04 -10,000 shares of FV 10/-
On 1-10-04, fresh issue of 5000 equity shares of FV Rs. 10 and Rs. 6 paid up.
On 1-7-05, issued 5000 equity shares of FV Rs.10 and received Rs. 4 per share.
On 1-11-05, issued 5000 bonus shares of face value Rs. 10
(Ans.: Rs. 8.70 per Re and Rs. 6.15)

Q150. X Co. Ltd. supplied the following information. You are required to compute the Basic EPS. (Accounting year 1.1.2002 - 31.12.2002)
Net Profit for the accounting years 2002 and 2003 is Rs. 20,00,000 and Rs.30,00,000
No. of shares outstanding prior to Right Issue 10,00,000 shares
Rights Issue: One new share for each Shares outstanding i.e., 2,50,000 shares
Terms of Right Issue Price: Rs. 20. Last date for exercise of rights is 31.3.2013
Fair Rate of one Equity Share immediately prior to exercise of right on 31.3.13 Rs. 25
(November 2004 - Final - Accounts, 8 Marks)
Ans.: Basic EPS for the current year Rs. 30,00,000 ÷ 11,97,917 = Rs. 2.50.
EPS for the previous year as originally reported Rs. 20,00,000 ÷10,00,000 = Rs. 2.00,
Adjusted EPS for the previous reporting period Rs. 20,00,000÷(10,00.000×1.042) =Rs. 1.92

Q151. From the Following information Calculate

Basic Earning per share 10-11

Basic Earning per share 11-12

Restated Basic Earning per share 10-11

Profit after Tax (10-11)	15,00,000
Profit after Tax (11-12)	20,00,000
1/4/2010	Opening Balance of 2,50,000 shares
1/7/2010	Public issue of 50,000 of Rs 10 each 7 paid up (issue price Rs. 27/)
1/10/2010	Call received Rs. 3/-
1/8/2011	Bonus issue of 70,000 shares of Rs. 10/- each 10/- paid up
1/9/2011	Right issue of 40,000 share of Rs. 10 each @ 70 each
	Fair Value before right Rs. 90/- each
On 1/4/2010	Company had 12% Preference share capital of Rs. 5,00,000
	Dividend Distribution Tax 10%

For company it is mandatory to transfer Rs. 2,00,000 to general reserve.

Profit after Taxes of both years are calculated before adjusting extraordinary loss of Rs. 30,000 (Tax Rate 30%)

(Ans: Ex-Right Price = 88.05/-; EPS = 4.98/-; 4.82/- and Restated EPS = 3.90/-)

AMALGAMATION IN NATURE OF PURCHASE

Q152. Calculate BEPS of A Ltd. from the following information:

Earnings attributable to Equity Shareholders for the year 2004-05 = Rs.10,00,000

Earnings attributable to Equity Shareholders for the year 2005-06 = Rs. 12,00,000

Equity shares as on 1-4-04 =10,000 shares of FV of Rs. 10

On 1-10-05 A Ltd. issued 10,000 shares as Purchase consideration for amalgamation in the nature of purchase to the shareholders of B Ltd. Earnings of B Ltd. for the year 2005-06 till 01.10.2005 are Rs. 3,60,000

(Ans.: Rs. 100 and Rs. 80)

AMALGAMATION IN NATURE OF MERGER

Q153. On June 30 200I, B Limited merged into A Limited. The amalgamation was accounted for in accordance with the pooling of interests method described in Accounting Standard (AS) 14 on 'Accounting for Amalgamations'.

The following is the relevant information for the year ended 31st March, 2002:

Particulars	**A Limited**	**B Limited**
Net profit (Rs)		
Until Merger	5,00,000	2,00,000

After Marger to year end (March 31,2002}	800,000	-

Number of shares (Rs. 10 each)

At the start of the year	6,000	4,000
On the date of merger	6,000	4,000
At year end (March 31,2002)	10,000	

Compute the EPS of A Ltd. at the year end, i.e. March 31, 2002

Ans. Basic EPS for A Limited for the year ended March 31, 20×2 would be Rs. 150 (Rs.1,500,000/10,000)

ABSOLUTE DIFFERENTIAL DIVIDEND RIGHTS

An enterprise should present basic and diluted earnings per share on the face of the statement of profit and loss for each class of equity shares.

Q154. Calculate BEPS

Earnings attributable to Equity Shareholders - 6,00,000

ESC I class - 3,00,000 (30,000 shares of Face Value Rs 10)

ESC II class - 4,00,000 (50,000 shares of Face Value Rs. 8)

ESC I class is entitled to 3% extra dividend in comparison to ESC II class.

Ans.: 8.74 for ESC I, 6.75 ESC II.

PROPORTIONATE DIFFERENTIAL DIVIDEND RIGHTS

Q155. XYZ Limited has the following different classes of equity shares of Rs.10 each, outstanding as at March 31, 2002, having disproportionate rights with respect to voting and dividends:

Number of shares	Rights as to share in net profit to the extent of capital
100,000 "A" class equity shares	Proportionate to capital
30,000 "B" class equity shares	In proportion of 3:2 with respect to "A" class shares
20,000 "C" class equity shares	In the proportion of 5:2 with respect to "A" class shares
40,000 "D" class equity shares	In the proportion of 3: 1 with respect to "A" class shares

Profit for the year ended March 31, 2002 was Rs. 8,00,000. As paragraph 8 of the Statement requires an enterprise to present basic and diluted earnings per share on the face of the statement of profit and loss for each class of equity shares that has a different right to share in the net profit for the period, the company calculates and discloses Basic EPS as follows:

The Company believes that net profit is to be shared in the ratio of 2:3:5:6, as derived from their rights to share net profit.

Class	Calculation	Net Profit (Rs)	No. of shares	Basic EPS (Rs)
Class A	Rs.800,000x2/16	100,000	100,000	1.00
Class B	Rs. 800,000x3/16	150,000	30,000	5.00
Class C	Rs. 800,000x5/16	250,000	20,000	8.33
Class D	Rs. 800,000x6/16	300,000	40,000	7.50

Is the calculation of EPS by the company correct?

DILUTED EARNINGS PER SHARE

How to Calculated DEPS – Following calculation is required:

1. Identify Potential Equity Shares first. (Whether any security which is pending for conversion is outstanding and resources thereof have been used in the business)

2. In case of Vested ESOPs, potential equity shares will be calculated as under:

   Total ESOP – {Exer. Price x No. of Option / Avg. Fair Value)

   In case of Unvested ESOPs – Potential equity shares will be Zero

3. Identify Dilutive potential equity shares by applying following steps:

(a) Calculate Incremental EPS for every single potential equity share

(b) Arrange IEPS in Increasing Order

(c) Apply Test for Dilution. Test each potential equity share on BEPS from continuing ordinary operations. If ratio EPS declines from preceding calculation then it is called Diluted EPS and if ratio increases from previous calculation then it is called Anti – Diluted EPS

- **Note:** Anti Diluted EPS shall not be presented in the Statement of P&L, in that case Diluted EPS shall be equal to BEPS

Q156. Test Potential Equity shares as dilutive or anti dilutive:

Earning for equity share holders	9,10,000
Wt. Avg of Equity Shares before effect of Potential Equity Shares	32,913
Share warrant	10,000

Convertible Debentures convertible in 716 number shares

(Savings in earnings net of Tax Rs. 20,000 if Interest is saved)

(BEPS – 27.65/-; DEPS – 21.21/-; Debenture is Anti Dilutive)

Q157. Calculate Basic & Diluted EPS

PBIT (10-11)	Rs. 10,00,000
Equity Share 1/4/2010	80,000 shares of Rs. 10 each
Public issue 1/7/2010	5000 shares of Rs. 10 each

Bonus issue 1/8/2010 6000 shares of Rs. 10 each

Right share 1/9/2010:7000 shares of Rs. 10 each @ Rs. 40 each fair value before right 50

It also had following instruments:

(a) 1/4/2010: 7% convertible debentures Rs.5,00,000 to be converted into 10,000 shares

(b) 1/7/2010: share warrant 15000 to be converted in to shares on 1/1/2011

PBIT includes extra ordinary income of Rs. 1,00,000 and Profit from discontinuing operations Rs. 60000. Income Tax Rate 30%.

(Answer: BEPS – 6.88 and BEPS – 5.09)

Q158. From the following information of Beta Ltd. calculate Earnings Per Share (EPS) in accordance with AS-20:

	31.03.08	**31.03.07**
1. Net profit before tax	3,00,000	1,00,000
2. Current tax	40,000	30,000
Tax relating to earlier years	24,000	(13,000)
Deferred tax	30,000	10,000
3. Profit after tax	2,06,000	73,000

4. Other information:

(a) Profit includes compensation from central Government towards loss on account of Earthquake in 2005 (non-taxable) 1,00,000 -

(b) 1,000 Outstanding convertible 6% Preference shares issued and paid on 30.9.06. Face value Rs. 100, Conversion ratio 15 equity shares for every preference share.

(c) 15% convertible debentures of Rs.1,000 each total face value Rs.1,00,000 to be converted into 10 Equity shares per debenture issued and paid on 30.6.06.

Total no. of Equity shares outstanding as on 31.3.08, 20,000 including bonus shares issued on 1.1.08 of 10,000 shares, face value Rs.100. (November 2008, Marks 8)

(Ans: 06-07: EPS- 7/- ; DEPS- 4.17/- and 07-08: EPS- 10/-; DEPS- 3.03/-; Restated BEPS and DEPS of 06-07: 3.50/- & 2.65/-)

Q159. Net profit for the year 2005 Rs. 12,00,000

W. Avg No. of equity shares outstanding during the year: 5,00,000 shares

Average fair value of one equity share during the year 2005: Rs. 20.00

Weighted average number of shares under option during the year: 1,00,000 shares

Exercise price for shares under option during the year 2005: Rs.15.00

Compute Basic and Diluted Earnings per Share.

Ans. Computation of earnings per share

	Earnings/shares	Shares	Earnings
Net profit for the year 2005	12,00,000		
W.Avg no. of shares during year		5,00,000	
Basic earnings per share			2.40
Number of shares under option		1,00,000	
No. of Shares that would have been issued at fair value (100,000 x 15.00) . 20.00		(75,000)	
Diluted earnings per share	12,00,000	5,25,000	2.29

Illustration 10

PQ Ltd. grants 100 stock options to each of its 1,000 employees on 1-4-2013, conditional upon the employee remaining in the company for 2 years. The fair value of the option is ₹ 18 on the grant date and the exercise price is ₹ 55 per share. The other information is given as under:

(i) The no. of employees expected to satisfy service condition are 930 in the 1st year and 850 in the 2nd year.

(ii) 40 employees left the company in the 1st year of service and 880 employees have actually completed 2 year vesting period.

(iii) The profit of the enterprise before amortization of the compensation cost on account of ESOPs is as follows:

(A) ₹ 18,50,000

(B) ₹ 22,00,000

(iv) The fair value of share for these years was ₹ 80 and ₹ 88 respectively.

(v) The company has 6 lakhs shares of ₹ 10 each outstanding at the end of both years.

Compute basic and diluted EPS for both the years (ignore the tax impacts).

Solution

Calculation of Basic & Diluted EPS

	2013-14	*2014-15*
Profit before amortization of ESOP cost	18,50,000	22,00,000
Less: ESOP cost amortised	(8,37,000)	(7,47,000)
Net profit for shareholders	10,13,000	14,53,000
No. of shares outstanding	6,00,000	6,00,000
Basic EPS	1.69	2.42
Potential equity	19,200	33,000
Total no. of equity shares	6,19,200	6,33,000
Diluted EPS	1.64	2.30

Working Notes:

1. Calculation of Potential Equity

		2013-2014	*2014-2015*
a.	Actual no. of employees	960	880
b.	Options granted per employee	100	100
c.	No. of options outstanding	96,000	88,000
d.	Unamortised ESOP cost per option (₹)	(₹ 18-18/2)9	0
e.	Exercise price (₹)	55	55
f.	Expected exercise price to be received (c x e) (₹)	52,80,000	48,40,000
g.	Unamortised ESOP cost (c x d) (₹)	8,64,000	0
h.	Total proceeds (₹)	61,44,000	48,40,000
i.	Fair value per share	80	88
j.	No. of shares issued for consideration (h/i)	76,800	55,000
k.	Potential Equity (c-j)	19,200	33,000

2. Calculation of ESOP cost to be amortised

	2013-2014	*2014-15*
Fair value of options per share	₹ 18	₹ 18
No. of options expected to vest under the scheme	(930 x 100) 93,000	(880 x 100) 88,000
Fair value of options	16,74,000	₹ 15,84,000
Value of options recognized as expenses	(₹ 16,74,000 / 2) 8,37,000	(₹ 15,84,000 – ₹ 8,37,000) 7,47,000

Important Notes:

ACCOUNTING STANDARD – 22

ACCOUNTING FOR TAXES ON INCOME

Q161. Following information is of X Ltd.

Sale	20,00,000
Cost of goods sold	11,00,000
Income from other (Bank Interest) sources	1,00,000
Salary	1,00,000
Provisions for Legal Damages	40,000
Interest to Bank (not yet paid)	30,000
Service Tax (not yet Paid)-	50,000

X Ltd purchased during the year one Machine for Scientific Research for Rs.120000 whose life is 3 years and is 100% tax deductible during the year

X Ltd also made contribution to national Laboratory Rs. 10000 on which weighted deduction of 125% is allowed.

Effective Rate of Tax 32.33%

Prepare Profit and Loss Account.

Q162. Ram Ltd. started its operations in 2000-2001 and gave you the following details:

Financial Year	AccountingIncome	Permanent Difference	Timing Difference	Tax Rate	Remarks
2000-2001	80,000	+10,000	+9000	30%	Reversible in 2003-2004
2001-2002	90,000	+2,000	+6000	35%	Reversible in 2002-2003
2002-2003	1,10,000	+6,000	-2000	40%	Reversible in 2003-2004
2003-2004	40,000	+12,000	Nil	50%	Nil

Tax rate for the next year are known in current year itself. Plus represents disallowance of expense in Income Tax.

Prepare necessary parts of Profit and Loss account, Balance Sheet in accordance with AS-22.

Q163. PQR Ltd.'s accounting ends on 31.03.2001. The company made a loss of Rs. 2,00,000 for the year ending 31.03.2001. For the year ending 31.03.2002 and 31.03.2003, it made profits of Rs. 1,00,000 and Rs. 1,20,000 respectively. It is assumed that the loss of a year can be carried forward for the eight years and tax rate is 40%. By the end of 31.03.2001, the company feels that there will be sufficient taxable income in the future years against which carry forward loss can be setoff. There is no difference between taxable income and accounting income expect that the carry forward loss is allowed in the years ending 2002 and 2003 for the tax purposes. Prepared a statement of Profit and Loss for the years ending 2001, 2002 and 2003. **(Nov. 2003)**

(Ans.: Loss 1,20,000, Profit 60,000 and 72,000)

Q164. Book Profit	Rs.10,00,000
Accounting Income	Rs.2,00,000
Regular Tax Rate	30%
Taxable Income	Rs.1,50,000

Difference between Accounting Income & Taxable Income is due to timing Difference

Mat Rate	18%

Prepare Extracts of Profit and Loss account and Balance Sheet.

Q165. Y Ltd. is a full tax free enterprise for the first ten years of its existence and is in the second year of its operation. Depreciation timing difference resulting in a tax liability in year 1 and 2 is Rs.200 lakhs and Rs. 400 lakhs respectively. From the third year it is expected that the timing difference would reverse each year by Rs.10 lakhs. Assuming tax rate of 40%, find out the deferred tax liability at the end of the second year and any charge to the Profit and Loss account. **4 Marks (May 2010 New Course)**

<u>DEPRECIATION</u>

Q166. ABC Ltd. prepares its accounts annually on 31st March. On 1st April' 2001, it purchases a machine at a cost of Rs. 1,50,000. The machine has a useful life of three years and an expected scrap value of zero. Although it is eligible for a 100% first year depreciation allowance for tax purposes, the straight-line method is considered appropriate for accounting purposes. ABC Ltd. has profits before depreciation and taxes of Rs. 2,00,000 each year and the corporate tax rate for 2002, 2003 and 2004 are 40%, 35% and 38% respectively. Show the profit and loss account and pass the journal entries as per Accounting Standard-22.

Ans.: Deferred Tax Liability Rs. 40,000 , Rs. 17,500 and Rs. Nil.

Q167. Company A has a block of assets with a written down value of Rs.100,000 on April 1, 20X I for tax purposes. The book value of the assets for accounting purposes is also Rs. 100,000. The assets are depreciated on written down value basis at 25 per cent per annum for both accounting and tax purposes. Of the entire block, assets costing Rs. 5,000 on April 1, 20XI, were sold for Rs. 10,000 on March 31, 20X3. Compute the deferred tax asset/liability assuming tax rate of 40 per cent. **(RTP Nov. 2014)**

Ans.: Depreciation for income tax purposes is computed on block of assets, rather than for individual assets. Further, as per section 50 of the Income tax Act, 1961, the entire sale consideration received on sale of fixed assets be reduced from the written down value of the relevant block. For example, if the block had a written down value of Rs. 10,000 and an asset costing Rs. 2,000 was sold for Rs. 3,000, the block would be reduced by Rs 3,000 rather than by Rs. 2,000. Conversely, if the asset had been sold for Rs. 1,000 the block would have been reduced by Rs. 1000 and not by Rs. 2,000.

It may be noted that Appendix 1 to AS 22 gives examples of timing differences. One of the examples is "Differences in method of calculation e.g. calculation of depreciation with reference to individual assets in the books but on block basis for tax purposes ... .

In view of the above, in the case of Company A in question, the following computations will be made:

20X1-X2

In this year, depreciation for both accounting and taxation purposes would be Rs. 25,000 (25 per cent of Rs. 100,000). Accordingly no timing difference arises on this account.

20X2-X3

Depreciation for the year would be Rs.18,750 (25 per cent of Rs. 75,000) as per the books of account, while for tax purposes it would be Rs. 16,250 as sale proceeds of Rs. 10,000 would be reduced from the block of assets prior to the computation of depreciation. Accordingly, the following timing differences arise:

Depreciation for tax purposes is Rs. 16,250 and for accounting purposes Rs. 18,750 giving rise to a timing difference of Rs. 2,500

Profit on sale of fixed asset amounting to Rs. 7,188 (Rs. 10000 – Rs. 2812 being the WDV of the asset as on 31st March 20X3) is recognised for accounting purposes. However, for tax purposes this income is not considered. This will result in a timing difference of Rs.7,188.

The net timing difference would be Rs. 4,688 by which the accounting income would exceed the taxable income, thus requiring creation of a deferred tax liability of Rs. 1,875 (4,688-0.4).

The difference of 74,688 would reverse in future years when depreciation for accounting purposes would be higher as compared to depreciation for tax purposes because depreciation for accounting purposes would be computed on a higher carrying amount of fixed assets as compared to carrying amount of those assets for tax purposes. Rs. 4,688 is also the difference between the accounting and tax. written down values of the assets as on March 31, 20X3 (i.e., assets for accounting purposes of Rs. 53,438 (75,000 - 18,750 - 2,812) less assets for tax purposes of Rs. 48,750 (75,000 - 10,000 - 16,250).

Q168. Ultra Ltd. has provided the following information:

Depreciation as per accounting records	Rs. 2,00,000
Depreciation as per tax records	Rs. 5,00,000
Unamortised preliminary expenses as per tax records	Rs. 30,000

There is adequate evidence of future profit sufficiency. How much deferred Tax asset/liability should be recognized as transition adjustment? Tax rate is 50%.

Ans.: Calculation of difference between taxable income and accounting income

Particulars	**Amount (Rs.)**
Excess depreciation as per tax (5,00,000 - 2,00,000)	3,00,000
Less: Expenses provided in taxable income	30,000
Timing difference	2,70,000

Tax expense is more than the current tax due to timing difference. Therefore deferred tax liability = 50%*2,70,000 = Rs. 1,35,000

Q169. From the following information given below you are required to computed Deferred Tax Assets and Deferred Tax Liability for Ramanujam Ltd. as on 31st March, 2014. The tax applicable is 35%.

(1) The company has charged Rs. 7,42,900 in the books of accounts while as per Income Tax Computation, the depreciation available for the company is Rs. 8,65,400.

(2) The Company has made provision for doubtful debts for Rs. 54,300 during the year.

(3) The company has debited share issue expenses of Rs. 6,23,500 which will be available for deduction under the income tax Act from the next year.

(4) The expenses of Rs. 7,84,500 has been charged to profit and loss account which are disallowed under the income tax act.

(5) The company has made donation of Rs. 2,00,000 which has been debited to Profit and loss account and only 50% thereof will be allowed as deduction as per Income Tax law. **(November 2014, 5 Marks)**

Important Note:

ACCOUNTING STANDARD – 25

INTERIM FINANCIALREPORTING

Q170. ABC India Ltd. has Rs.1,02,000 net income for the quarter ended 31st December, 2003 including the following items:

(a) Rs. 60,000 extraordinary gain received on July 30 2003, was allocated equally to the second, third and fourth quarter of financial year 20032004.

(b) Rs. 16,000 cumulative effect loss resulting from change in method of inventory valuation method was recognized on November 2, 2003. Out of this loss ?10,000 relates to the previous quarters.

Compute the profit as per AS-25 for the quarter ended 31st December, 2003 ofABC India Ltd.

Ans.: **ABC India Ltd.**

Statement showing computation of the correct amount of profit attributable for the quarter

(Amount Rs,)

Net income for the quarter as shown by the company	1,02,000
Extra ordinary gains should be recognized in the quarter in which it is accrued .Hence, allocation of Rs.20,000 for current quarter should be adjusted	(20,000)
Eflect of change in the method of inventory valuation pertaining to earlier period, to be adjusted	10,000
Net profit for the period	92,000

Q171. Kaveri Ltd. shows the net profit of Rs. 5,40,000 for quarter III after incorporating the following:

(i) Bad debt of Rs.30,000 incurred during the quarter. 50% of the bad debts have been deferred to next quarter.

(ii) Extra ordinary loss of Rs 28,000 incurred during the quarter has been fully recognized in this quarter.

(iii) Additional depreciation of Rs.36,000 of third quarter resulting from the change in the method of depreciation.

Do you agree with the treatment adopted by the company? If not find out the correct quarterly income as per AS 25.

Ans: In the above case the quarterly income has not been correctly stated. As per AS 25 the quarterly income should be adjusted and restated as follow:

Bad debt of Rs.30,000 have been incurred during the current quarter. Out of this, the company has deferred 50% i.e., Rs.15,000 to next quarter. This is not correct. Rs.1 5,000 therefore, should be deducted from Rs.5,40,000.

The treatment of extraordinary loss of Rs.28,000 being recognized in the same quarter and recognizing the additional depreciation of Rs. 36,000 in the same quarter is correct and in tune with AS 25. So, no adjustment required for these two items.

The company should report the quarterly income as Rs. 5,25,000 (i.e., Rs. 5,40,000 Rs. 15,000).

Q172. A Ltd. expects to receive dividend income of Rs.100 crores on its investments in the quarter October to December, 2005. It proposes to recogniseRs. 25 crores dividend income in interim financial statement of each quarter. Is this justified.

(RTR May 2006)

Ans.: As per para 36 of AS 25 revenues received seasonally/occasionally should be recognized as they occur and not be anticipated/deferred. Hence, entire 100 crores; to be recognized in October to December, 2005, quarterly statement.

Q173. On 30-6-2007, Asmitha Ltd. incurred Rs.2,00,000 net loss from disposal of a business segment. Also, on 30-7-2007, the company paid Rs.60,000 for property taxes assessed for the calendar year 2007. How the above transactions should be included in determination of net income of Asmitha Ltd. for the six months interim period ended on 30-9-2007. **[Financial Reporting, Nov. 2008, 5 marks]**

Ans.: As per AS 25, if an enterprise prepares and presents a complete set of financial statements in its interim financial report then, the form and content of those statements should conform to the requirements that are applicable to annual complete set of financial statements.

As on 30-9-2007, Asmitha Ltd., would report the entire Rs.2,00,000 loss an the disposal of its business segment since the loss was incurred during interim period. A cost charged as an expense in an annual period should be allocated to interim periods on accrual basis. Since Rs. 60,000 Property Tax payment relates to entire calendar year 2007, Rs. 30,000 would be reported as an expense for six months ended on 30th September, 2007 while remaining Rs. 30,000 would be reported as prepaid expenses.

GUIDANCE NOTE ON MEASUREMENT OF INCOME TAX FOR INTERIM FINANCIAL REPORTING

1. Calculate Actual Income upto current IFR and estimated Income for remaining interim period of CY along with bifurcation of Regular Income and Special Income (such as Capital gain).

2. Calculate Tax Expenses (Special Tax, Deferred Tax, and Normal Tax) on above actual/estimated Taxable Income for the entire yearwise.

3. Calculate weighted avg tax rate for different taxes separately.

Regular W. Avg. Tax Rate = Regular Tax / Regular Income x 100

Special W. Avg Tax Rate = Special Tax / Total Special Income x 100

(or we don't need to calculate Weighted avg. special tax, it is to be applied on specific basis)

Deferred Tax W. Avg Rate - Def. Tax / Regular Income x 100

4. Calculate tax expense for IFR based on actual income and WA tax rates.
5. Distribute Special Tax in the ratio of Special Income Ratio, distribute deferred tax and Normal Tax in the ratio of Normal Income Ratio.

QUESTIONS ON GUIDANCE NOTE

Q174. Calculate Tax Expense for Quarter 1 to 4 as per Guidance Note:

	Income	Base
Quarter-1	100,000	Actual
Quarter -2	150,000	Estimated
Quarter -3	1,90,000	Estimated
Quarter -4	2,10,000	Estimated

Income in Quarter -1 includes 20,000 capital gains which is taxable @ 15% Company estimates temporary Difference resulting in DTA of Rs. 50,000 at the end of year

Rate of Tax:

upto 200,000	-
next 200,000	20%

Balance	30%

Timing Difference are expected to result in liability.

ACCOUNTING STANDARD - 26
"INTANGIBLE ASSETS"

Q175:

M Ltd. launched a project for producing product A in Nov. 2008. The company incurred Rs. 30 Lacs towards research and development expense upto 31st March, 2010. Due to unfavorable conditions the management feels that it is not possible to manufacture and sold the product in the market for so many years. The management hence wants to differ the expenditure written off to future years. Advice the management as per the applicable Accounting Standard. **(Hint:**Charged to P&L A/c)

Q176:

Hera Ltd. has got the license to manufacture particular medicines for 10 years at a license fees of Rs. 200 lacs. Given below is the pattern of expected production and expected operation cash inflow:

Year	Production (in lacs)	Net operating Cash Inflows (in Rs. Lacs)
1	300	900
2	600	1800
3	650	2300
4	800	3200
5	800	3200
6	800	3200
7	800	3200
8	800	3200
9	800	3200
10	800	3200

Suggest the amortization method.

(**Hint:** Amortize in proportion of future economic benefits i.e. in proportion of Cash Inflows)

Q177:

On Jan. 2009, A Ltd. bought a Trademark from B Ltd. for Rs. 10 lacs. A Ltd. hired an independent consultant, who estimated the trademark's life to be 20 years. Its unamortized cost on B Ltd's records was Rs. 5 lacs. A Ltd. decided to amortize the trademark over the maximum period allowed. In A Ltd's Balance sheet as on 31st December 2009, what amount should be reported, as accumulated amortization?

(Hint: Intangibles are initially recognized at Cost)

Q178:

Fortune Ltd. is developing a new Teaching and Learning process. During the FY ending 31st march, 2009, the expenditure incurred was Rs. 50 lacs. This process made the criteria for recognition as an intangible asset on 1st Dec, 2008, expenditure incurred till this date was Rs. 22 lacs. Further expenditure incurred on the process for the FY ending 31st march, 2010 was Rs. 80 lacs. As at 31st March, 2010, the recoverable amount of know-how is estimated to be Rs. 72 lacs. You are required to calculate:

(i) Amount to be charged to P&L a/c for the year ending 31st march, 2009 and the carrying value as on 31st March, 2009.

(ii) Amount to be charged to P&L a/c and carrying value of intangible as on 31st March, 2010.

(Hint: For year ending 2009 – Rs. 22 lacs transferred to p&l and remaining capitalized as intangible. For year ending 2010 – impairment loss is Rs. 36 lacs and Carrying value is Rs. 72 lacs.)

Q179:

An Enterprise acquired patent right for 400/- lakhs. The product life cycle has been estimated to be 5 years and the amortization was decided in the ratio of estimated future cash flows which are as under:

Year	Estimate Future Cash Flows (Rs. In Lakhs)
1	200
2	200
3	200
4	100
5	100

After 3rd year it was ascertained that the patent would have an estimated balance future life of 3 years and the estimated cash flows after 5th year is expected to be Rs. 50 lakhs each year. Determine the amortization under AS – 26.

ACCOUNTING STANDARD - 28

IMPAIRMENT OF ASSETS

Q180. From the following details of an asset:

(a) Find out impairment loss

(b) Treatment of impairment loss

(c) Subsequent depreciation

Particulars of Assets	
Cost of asset	Rs. 56 lakhs
Useful life	10 years
Salvage value	Nil
Current carrying value	Rs. 27.30 lakhs
Useful life remaining	3 years
Recoverable amount	Rs. 12 lakhs
Upward revaluation done in last year	Rs. 14 lakhs

Q181. Ram Ltd. acquired plant on 1.4.95 for Rs. 50 lakhs having 10 years useful life and provides depreciation on straight line basis with nil residual value. On 1.4.2000, Ram Ltd. revalued the plant at Rs. 29 lakhs against book value of Rs. 25 lakhs and credited Rs. 4 lakhs to revaluation reserve. On 31.03.02 the plant was impaired and its recoverable amount on this date was Rs. 14 lakhs. Calculate the impairment loss and how this loss should be treated in accounts.

(Answer: CA as on 31.03.2002: Rs. 17.40/-; Imp Loss: 3.40/-; to be set off with RR of Rs. 2.40/-**)**

Q182. Fine Ltd. acquired a Machine on 1st April, 2009 for Rs. 14 Crores that had an estimated useful life of 7 years. The machine is depreciated on straight line basis and does not carry any residual value. On 1st April, 2013, carrying value of the machine was reassessed at Rs. 10.20 crore and the surplus arising out of the revaluation being credited to revaluation reserve. For the year ended 31st March, 2015, conditions indicating an impairment of the machine existed and the amount recoverable ascertained to be only Rs. 140 lacs.

You are required to calculate the loss on impairment of the machine and show how this loss to be treated in the books of Fine Ltd.

Fine Ltd. had followed the policy of writing down the revaluation surplus by the increased charge of depreciation resulting from the revaluation. **(Nov. 2015 – 5 Marks)**

(Answer:

Q183. Mohan Ltd. gives the following estimates of cash inflows relating to fixed asset on 31.03.2000. The discount rate is 15%.

Year	Cash Flows (Rs. in Lakhs)
2001	2000
2002	3000
2003	3000
2004	4000
2005	2000
Residual Value	500

Fixed asset was purchased on 1.1.98 for Rs. 20,000 lakhs. Useful life was 8 years. Residual value estimated Rs. 500 lakhs at the end of 8 years. Net selling price is Rs. 10,000 lakhs. Calculate on calendar year:

(a) Carrying amount at the end of 2000
(b) Value in use on 31.12.2000
(c) Recoverable amount on 31.12.2000
(d) Impairment loss to be recognized for the year ended 31.12.2000
(e) Revised carrying amount
(f) Depreciation for the calendar year 2001

(Answer: Value in use: Rs. 9513 lakhs, Carrying amount on 31.12.2000 – Rs. 12687 lakhs, Net selling price as given Rs. 10,000 lakhs, Recoverable amount is higher of 9513 and 10000; impairment loss- Rs. 2687 lakhs and depreciation charge for 2001 = 10000-500/5 = 1900)

Q184. A Ltd. gives following information

Asset	Carrying Amount	Cash generating unit
A	1,00,000	1
B	2,00,000	3
C	3,00,000	2
D	3,50,000	2
E	70,000	1
F	8,00,000	3
G	2,20,000	2
H	4,50,000	1
Goodwill X	90,000	Allocate in ratio 1:1:1
Goodwill Y	60,000	Unallocable
<u>Corporate:</u>		
Asset P	1,50,000	Allocate in ratio 3:2:1
Asset Q	2,00,000	Unallocable

Recoverable Amount of Cash generating Unit: 1 – 6,70,000; 2 – 8,40,000 and 3 – 10,30,000 Recoverable Amount of Entity: Case A – 25,50,000; Case B – 25,40,000. Calculate impairment loss.

Q185. A Ltd. acquired S Ltd. business on 31.03.2001 for Rs. 5000 lakhs. The details of acquisition are as under:

Fair value of identifiable assets	4000 lakhs
Goodwill (to be amortised in 5 years)	1000 lakhs

The anticipated useful life of acquired assets is 8 years. A Ltd. uses straight line method of depreciation with nil residual values is anticipated on 31.03.2003. A Ltd. estimated the significant decline in production due to changed government policies, the net selling price of identifiable asset is not determinable. The cash flow forecast based on recent financial budget for next 6 years after considering changed govt. policies are as follows, incremental financial cost is 10% which represent current market assessment of the time value of money.

Year	Cash flow	Year	Cash flow
2004	700	2007	500
2005	700	2008	500
2006	700	2009	500

Acquired business is a cash generating unit

Required:-

(a) Value in use

(b) Impairment loss

(c) Revised carrying amount assets on 31.03.2003

(Ans: Impairment loss Rs. 925 (Goodwill – 600 and 325 Other Assets); revised carrying amount Nil & 2674)

Q186. On 31.03.1999 A Ltd. acquired B Ltd. for Rs. 600 lakhs. B Ltd. has three cash generating unit X, Y and Z, net fair values of Rs. 240 lakhs. 160 lakhs and 80 lakhs respectively. A Ltd. recognize goodwill of Rs. 120 lakhs. For the accounting year ended 31.03.2003, X Unit incurred substantial losses and its recoverable amount is estimated to be Rs. 270 lakhs. Carrying amount of different cash generating units are as under:

X	260 Lakhs
Y	240 Lakhs
Z	160 Lakhs
Goodwill	24 Lakhs
Total	**684 Lakhs**

Calculate the impairment loss to be recognized in the financial statement if goodwill can be allocated on reasonable and consistent basis to cash generating unit.

(Answer: Impairment loss – Rs. 2 lakhs (272-270)

Q187. A Ltd., which is in business of manufacturing and export of its product. sometimes, back in 2000, the Govt. put the restriction on export of goods exported by A Ltd. Due to that restriction A Ltd. impaired its asset. A Ltd acquired at the end of 1996 Rs. 4000 Lakhs identifiable assets and paid Rs. 6000 lakhs balance is treated as goodwill. The useful life of the identifiable assets are 15 years and depreciated on straight line basis. When Govt. put the restriction at the of 2000, the company recognized the impairment loss by determining the recoverable amount of assets of Rs. 2720 lakhs. In 2002 Govt. lift the restriction imposed on the export and due to this favourable change A Ltd, estimate recoverable amount, which was estimated of Rs. 3420 lakhs.

Required:

A. Calculation and allocation of impairment loss in 2000

B. Reversal of an impairment loss and its allocation as per AS-28 in 2002

Ans. Impairment loss Rs.614; Reversal of Loss Rs.175.

Q188. Cost 1/4/2001 Rs. 10,00,000

Depreciation SLM life 10 year

On 31/3/2005 Recoverable Amount 3,00,000

On 311/3/2007 Recoverable Amount 2,20,000

Calculate Impairment Loss and its Reversal.

Q189. Aakash Limited is the owner of CGU (Cash Generating Unit) block of assets whose current carrying cost is Rs. 1,000 lacs. Current carrying cost of CGU block of assets as per Accounting and Tax records are after charging depreciation of the current year. The company after the detailed study by its technical team, has assessed the present value recoverable amount of this CGU block of assets at Rs. 550 lacs. The value of block of assets as per the Income Tax records is Rs. 800 lacs. The approving authority of the company has issued a signed statement confirming that impairment in the value of CGU is only a temporary phenomenon which is reversible in subsequent periods and also assuring virtual certainty of taxable incomes in the foreseeable future. You are required to show Deferred Tax workings as per Accounting Standards in force, given the tax rate of 30% plus 10% surcharge thereon. The depreciation rate for tax purpose is 15% and that as per books is 13.91%.

(Nov. 2015 – 4 Marks)

(Answer: DTL Reversed – 72.73 and DTA Created – 82.50)

Important Notes:

AS 18 - RELATED PARTY DISCLOSURES

Q190. (ICAI MODULE)

Identify the related parties in the following cases as per AS-18

A Ltd. holds 51% of B Ltd.

B Ltd holds 51% of O Ltd.

Z Ltd holds 49% of O Ltd.

Solution

Reporting entity- A Ltd.

- B Ltd. (subsidiary) is a related party

O Ltd. (subsidiary) is a related party

Reporting entity- B Ltd.

- A Ltd. (holding company) is a related party
- O Ltd. (subsidiary) is a related party

Reporting entity- O Ltd.

- A Ltd. (holding company) is a related party
- B Ltd. (holding company) is a related party
- Z Ltd. (investor/ investing party) is a related party

Reporting entity- Z Ltd.

- O Ltd. (associate) is a related party

Q191.

Mr. X has a 100% investment in A Limited. He is also a member of the key management personnel (KMP) of C Limited. B Limited has a 100% investment in C Limited.

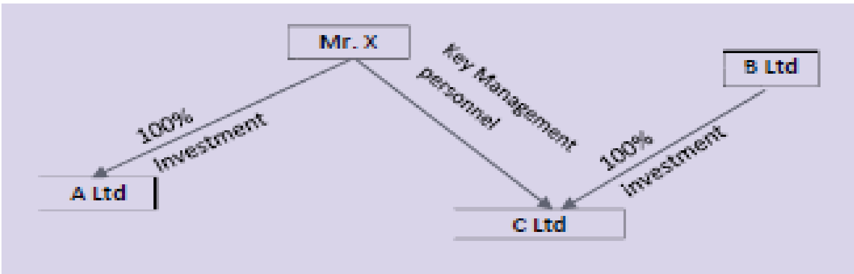
Required

(a) Examine related party relationships from the perspective of C Limited for A Limited.

(b) Examine related party relationships from the perspective of C Limited for A Limited if Mr. X is a KMP of B Limited and not C Limited.

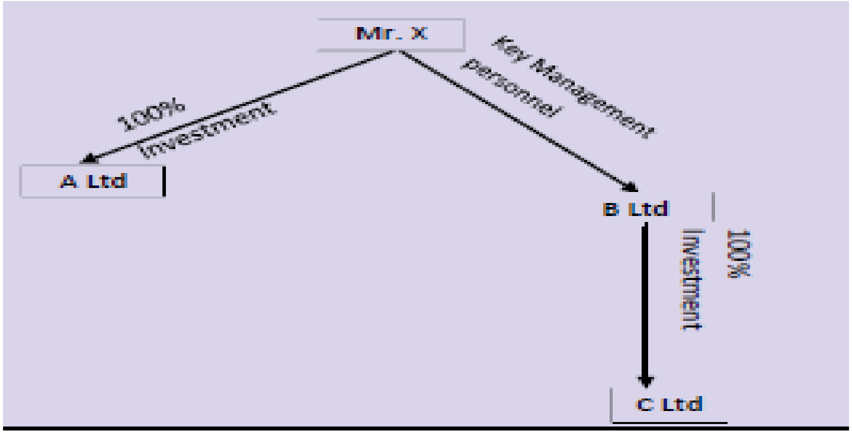
Solution

(a) A Limited is related to C Limited because Mr. X controls A Limited and is a member of KMP of C Limited.



(b) A Limited will not be related to C Limited, since Mr. X is not KMP in C Ltd. there is no relation of A Ltd. with C Ltd.

(But A Ltd. and B Ltd. are related parties by virtue of Mr. X)



Q192. (ICAI MODULE)

Narmada Ltd. sold goods for Rs 90 lakhs to Ganga Ltd. during financial year ended 31-3-2017. The Managing Director of Narmada Ltd. own 100% of Ganga Ltd. The sales were made to Ganga Ltd. at normal selling prices followed by Narmada Ltd. The Chief accountant of Narmada 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?

Solution

As per AS 18 'Related Party Disclosures', Enterprises over which a 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 and enterprise that have a member of key management in common with the reporting enterprise.

In the given case, Narmada Ltd. and Ganga 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 Narmada Ltd is wrong.

Q193.

Power Limited is a producer of electricity. Transmission Limited regularly purchases electricity from Power Limited. Power Limited whose financial year ends on March 31, 20X2, acquired 100% shareholding of Transmission Limited on July 15, 20X1. However, the entire shareholding is disposed of on March 21, 20X2. Power Limited and Transmission Limited had transactions when Transmission Limited was a subsidiary of Power Limited and also in the period when it was not a subsidiary of Power Limited.

Required

For which period, related party disclosure should Power Limited make in its financial statements for the year ended March 31, 20X2 with respect to transactions with Transmission Limited?

Solution

Power Limited should in its financial statements for the year ended March 31, 20X2 make related party disclosures for the period from July 15, 20X1 to March 21, 20X2 when Transmission Limited was its subsidiary.

ITEMS WHICH ARE SPECIFICALLY REQUIRED TO BE TRANSFER TO OTHER COMPREHENSIVE INCOME (OCI) as per INDAS:

Selective List:

RELEVANT INDAS	*PARTICULARS OF ITEMS*
INDAS 16 – PPE	Revaluation Profit of PPE – known as Revaluation Reserve
INDAS 19 – EMPLOYEE BENEFITS	Actuarial Gains and Losses on DBP and PLAN ASSETS
INDAS 21 – EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES	Exchange Difference on translation of Functional Currency To Presentation Currency – also called FCTR
INDAS 109 – FINANCIAL INSTRUMENTS	Financial Assets categorized under FVTOCI
INDAS 109 – FINANCIAL INSTRUMENTS	FV Gain/Losses under Cash Flow Hedge
INDAS 109 - FINANCIAL INSTRUMENTS	Equity Shares not Held For Trading – Option to designate as FVTOCI Parmanently
INDAS 109 - FINANCIAL INSTRUMENTS	Fair Value Gain or Loss on Net Investment in Foreign Operation and Derivative Instrument thereof
INDAS 103 – BUSINESS COMBINATIONS	NET ASSETS acquired less PURCHASE CONSIDERATION = OCI (CR)
INDAS 12 – INCOME TAXES	Current Tax & Deferred Tax is to be recognized in OCI or directly in Equity if the items on which CT & DT is calculated belongs to OCI