

## Paper 1: Financial Reporting

Self evaluation practice paper

Q1 is compulsory. Out of remaining six questions, answer **any five** questions.

Support your answer with working notes along with suitable assumptions, wherever necessary.

1. (a) Energy Ltd. sold certain goods to Power Ltd. on 15.03.2013 for ₹ 15,00,000 by virtue of an agreement entered into between them. On the same day, Power Ltd. entered into another agreement with Energy Ltd. to resell the same goods at ₹ 16,50,000 (including holding cost) on 16.06.2013. You are required to identify the nature of transaction between two parties.

Also prepare an abstract of balance sheet in the books of Energy Ltd. for the financial year ending 31.03.2013 as per the requirements of Revised Schedule VI. (5)

- (b) P Ltd. had purchased certain investments in 2011 for ₹ 20,00,000. However, these investments are no longer considered for holding purpose and hence been written down to ₹ 14,00,000. With reference to the relevant AS, explain how P Ltd. will recognize the permanent decline in the value of investments. If the company wishes to re-classify these investments as current investments, what treatment should be given for reclassification? (5)

- (c) Metro Constructions Ltd. was awarded a contract of construction of a bridge for ₹ 10 Lakhs on 1st April, 2007. The position of the contract on 31st March, 2012 and 31st March, 2013 was as under :

	₹ in Lakhs	
	As on 31.03.2012	As on 31.03.2013
Cost incurred up to date	5.50	9.00
Estimated further cost of completion	2.50	Nil

Total contract cost originally estimated was ₹ 8.00 Lakhs. While closing the books of accounts on 31.03.2013, the chief accountant calculated prior period expense as under :

	₹ in Lakhs	
Total cost of construction as on 31.03.2013	9.00	
Less :		
Cost incurred as on 31.03.2012	5.50	
Estimated additional cost during 2012-13	2.50	8.00
Excess cost treated as prior period expense		1.00

Calculate the amount of provision for foreseeable loss, which must be made and the proportion of total contract value to be recognized as turnover in the financial statements for the year ending 31st March, 2013.

Also comment on the treatment given by the chief accountant. (6)

- (d) X Ltd. borrowed ₹ 250 Lakhs on 01.04.2012 for construction of boiler plant @ 14 % p.a. The plant is expected to be completed in 5 years. The weighted average cost of capital is 18 % p.a. Company's accountant capitalized interest amounting to ₹ 45 Lakhs for the accounting period ending on 31.03.2013. Due to surplus funds out of the total borrowings, ₹ 13 Lakhs was earned and credited to Profit and loss A/c. Comment on the above treatment of accountant with reference to relevant accounting standard. (4)

2. The following is the balance sheet of GST Ltd. as on 31st March, 2012 :

Liabilities		₹ in Lakhs	
6,00,000 equity shares of ₹ 100 each	600	Land and building	200
2 Lakhs, 12% Preference shares of ₹ 100 each	200	Plant and machinery	300
15% debentures	200	Furniture and fixtures	50
Debenture interest	26	Inventory	150
Loan from ICICI Bank	74	Sundry debtors	70
Trade creditors	300	Cash and bank balance	130
		Preliminary Expenses	10
		Issue of debentures	5
		Profit and loss account	485
	<b>1,400</b>		<b>1,400</b>

GST Ltd. did not perform well and has suffered stringent losses during the last few years. However, the board of directors of the company have analyzed that the company can perform well and the financial and operational position can be recovered by proper financial restructuring and as per board's decision the following scheme of reconstruction has been devised:

- (i) Ordinary shares are to be reduced to ₹ 25/ share, fully paid up.
- (ii) Preference shares to be reduced with coupon rate of 10% and with equal number of shares of ₹ 50/ share, ₹ 50 paid up.
- (iii) Debenture holders have agreed to forego interest accrued to them. Besides this, they have agreed to accept new debentures carrying 10% interest.
- (iv) Creditors have agreed to forego 45% of their existing receivables and the balance outstanding to be converted into ordinary shares of ₹ 30/ share.
- (v) The company issues 5,00,000 ordinary shares at ₹ 30/ share to pay off the secured bank loan. The entire issued capital is required to be paid on application. The existing shareholders have agreed to subscribe to new shares issued by the company.
- (vi) During the course of re – construction, the company estimates that 10% of book debts amount will not be recovered.
- (vii) While land and building is to be revalued at ₹ 250 Lakhs, plant and machinery is to be written down to ₹ 46 Lakhs.

**Required:**

- 1) Evaluate the impact of financial re – construction. (6)
- 2) Prepare the new balance sheet as on 31st March, 2012 following Revised Schedule VI, assuming that the scheme of re – construction is implemented in letter and spirit. (10)

3. Big Ltd. purchased 8,000 equity shares of ₹ 100 each from Small Ltd. on 1st April, 2010. On that day, share capital of Small Ltd. was ₹ 10,00,000 and remained unchanged up to 31.03.2013.

Further transactions by Big Ltd :

On 01.04.2011 : Sale of 500 shares out of original investments

On 01.04.2012 : Purchase of 1,000 equity shares of Small Ltd.

Small Ltd. paid 15% dividend each year in the month of September. Profit and loss account balances in Small Ltd. and the investments of Big Ltd in Small Ltd. on different dates were as under:

As on	P & L a/c balance of Small Ltd.	Investments of Big Ltd. in Small Ltd.
1st April, 2010	₹ 5,00,000	₹ 12,80,000
31st March, 2011	₹ 6,20,000	₹ 12,80,000
31st March, 2012	₹ 7,20,000	₹ 11,90,000
31st March, 2013	₹ 8,00,000	₹ 14,00,000

The amounts shown as investments represent cost price as reduced by sale and increased by further purchase without making any adjustments for profit and loss on sale or dividend.

**You are required to:**

- A. Prepare "Investment in Shares in Small Ltd. Account" for the year 2010-11, 2011-12 and 2012-13 in the books of Big Ltd. (6)
- B. Prepare relevant statements to show the balances as on 31st March 2011, 2012 and 2013 for consolidated accounts in respect of: (10)
  - 1) Goodwill or Cost of Control
  - 2) Revenue Profit
  - 3) Capital Profit.

(Show detailed workings wherever necessary)

4. (a) Balance sheet of Goodwill Ltd. as on 31.03.2012 is given below:

Liabilities	₹	Assets	₹
Share Capital:		Fixed Assets	28,50,000
5,000 equity shares of ₹ 100 each, ₹ 100 paid-up	5,00,000	Investments:	
10,000 equity shares of ₹ 50 each, fully paid up	5,00,000	In subsidiaries	6,40,000
16,000 equity shares of ₹ 40 each, fully paid up	6,40,000	Non-trade investments	2,00,000
Share suspense	2,00,000	Current Assets:	
Reserves & Surplus:		Stock	5,00,000
General reserve	15,51,200	Debtors	10,00,000
P & L a/c	8,40,000	Cash in hand	2,40,200
15% Debentures	6,00,000	Prepaid expenses	42,500
Current Liabilities and provisions:		Cash at bank	2,50,000
Sundry creditors	2,00,000	Miscellaneous expenses:	
Tax provision	8,00,000	Preliminary expenses written off	1,08,500
	<b>58,31,200</b>		<b>58,31,200</b>

Further information:

- (i) Return on capital employed in similar business is 10%.
- (ii) Profit before tax (before deducting interest on 60% of debentures convertible on 1st April, 2013) for past five years were as under:
 

2007-08	₹ 5,00,000
2008-09	₹ 7,50,000
2009-10	₹ 4,30,000
2010-11	₹ 9,75,000
2011-12	₹ 12,32,000
- (iii) Non-trade investments earned @ 10% on an average.
- (iv) Rate of tax during 2011-12 was 30%, effective future tax rate will be 50%.
- (v) Expected future expenses are as follows:
 

Expenditure on annual research	₹ 2,90,000
Foreign currency loss (annualized)	₹ 35,000

**Required:**

- 1) Value the goodwill on the basis of 4 years purchase of weighted super profits. (6)
  - 2) Find out intrinsic value of different categories of equity shares. (6)
- (b) It is apparent from the books of G Ltd. that the trade payables are normally paid in 12 months. You are required to advise the company upon classification of these trade payables based on the reporting framework as provided in Revised Schedule VI of Companies Act, 1956. (4)
5. (a) Beloved Ltd issued ₹ 10,00,000, 6% convertible debentures (face value ₹ 100 per debenture) at par on 01.04.2010. The debentures are redeemable at premium of 10% on 31.03.2013 or at the debenture holders' discretion, they may be converted into ordinary shares. The prevailing market rate for debentures issued without conversion option is 10%.

P.V. factors:

End of year	10%
1	0.91
2	0.83
3	0.75

You are required to find out the equity and liability components. Also compute the debenture liability at the end of each year. (8)

- (b) Manjoo Ltd. granted 500 options to each of its 4,000 employees in 2007 at an exercise price of ₹ 50. The market price of options was also ₹ 50.

Fair value per option	: ₹ 15
Face value per share	: ₹ 10
Contractual life of options	: 6 years
Vesting period	: 3 years
Exercise period	: 3 years
Expected life	: 5 years

The expected annual forfeitures are estimated at 3%. However actual forfeitures in 2007 were 5%. Manjoo Ltd. expects that the actual forfeitures for rest of the 5 years would average only 3%. The company revised its estimated forfeiture @10% p.a. during the year 2008. Of the total employees, 2500 employees completed the 3 years vesting period. The position of remaining employees was as under:

Year end	No. of employees exercising their rights
2011	1000
2012	300

The rights of remaining employees expired unexercised at the end of 2012.

You are required to compute:

(8)

- Expense to be recognized each year.
- Amount to be recorded in Share Capital and Securities Premium account upon issue of shares.

6. (a) From the following information calculate:

- Gross Value Added and Net Value Added.
- Value added by manufacturing and trading activities.
- Value added per employee and average earnings per employee.
- Profit before tax.

Books of Future Ltd.

**Application of Value Added**  
for the year ended 31st March, 2013

	₹ '000	₹ '000	%
To pay employees		14,760	87.70
To pay providers of capital:			
Interest on 10% debentures	1,309		
Dividends	<u>125</u>	1,434	8.52
To pay government:			
Corporate tax	376		
Deferred tax	<u>54</u>	430	2.56
To provide for maintenance and expansion:			
Depreciation	342		
Fixed assets replacement reserve	- 311		
Retained profits	<u>175</u>	206	1.22

You are informed that 40 employees worked in Future Ltd. during the year 2012-13.

(8)

(b) A mutual fund company provides following information regarding its scheme:

Scheme name	: ABC
Scheme size	: ₹ 50 crores
Face value of units	: ₹ 10
Investments	: In shares
Market value of shares	: ₹ 75 crores

Compute NAV per unit of mutual fund. Also comment on your answer.

(4)

(c) AVTAAR Ltd's books of accounts furnishes following information:

(i) Equity share capital : 2,00,000 shares of ₹ 10 each.

(ii) Profits, dividends and retained earnings:

Year	Profit before tax (₹)	Dividend (₹)	Retained earnings (₹)
2010	9,00,000	2,15,000	2,35,000
2011	12,00,000	2,50,000	3,50,000
2012	8,00,000	2,96,000	1,03,500

(iii) The normal earnings of similar company in the industry in which AVTAAR Ltd. belongs is 12%. The normal rate of return expected by shareholders is 10%. Tax rate is 50% which is uniform since last three years.

Value the shares of company under earnings capitalization method.

(4)

7. Attempt **any four** of the following:

4 x 4 = (16)

(a) B Ltd. has set up its business in a designated backward area which entitles the company to receive from the Government of India a subsidy of 20% of cost of investment. Having fulfilled all the conditions under the scheme, the company on its investment of ₹ 50 crores in capital assets, received subsidy from the government in September, 2012. Company credits the subsidy in P & L account and thereby reduces the losses for the year ended 31<sup>st</sup> March, 2013.

Justify the treatment given by company in view of relevant AS.

(b) During the year 2012-13, a company develops a software product and incurs some expenses in line of development and production which are as follows:

R & D cost	49,200
Testing costs	15,000
Production masters for training materials	10,000
Cost of duplication of software training materials	28,000
Packing and labeling costs	17,500

Compute:

(i) Expense to be charged to P & L account.

(ii) Expense to be capitalized.

(c) Beta Ltd's financial statements shows following position as on 31st March, 2013:

PBT	₹ 430 Lakhs
15% debentures (₹ 100 each)	2 Lakhs
Shareholders funds	₹ 1800 Lakhs
Return to providers of funds	₹ 240 Lakhs
Co's net investments	₹ 590 Lakhs
Required rate of return	10%
Tax rate	40%

Calculate Economic Value Added.

- (d) J Ltd. wants to calculate the provision in respect of defined benefit scheme of gratuity for its employees for the interim period ending on 30th September, 2012. Suggest on what basis the company shall calculate the provision.
- (e) Compute the 'Net Assets' value of each category of equity shares of XML Ltd. from the following information:

**Abstract of balance sheet for the year ended 31st March, 2013**

	<u>Note No.</u>	<u>          `</u>
<b>Equity and Liabilities</b>		
(1) Shareholders' Funds:		
(a) Share Capital	1	7,40,000
(b) Reserves and Surplus		<u>2,50,000</u>
		9,90,000
 Notes to accounts:		
1) Share capital:		
5,000 equity shares of ` 100 each, ` 100 paid	5,00,000	
8,000 equity shares of ` 50 each, ` 30 paid	<u>2,40,000</u>	7,40,000

**Clarification regarding mistakes contained in "CA FINAL – FINANCIAL REPORTING Self Evaluation Practice Paper for NOV '13" uploaded on 22.08.2013**

It was observed that there were certain mistakes relating to some figures and values in 4 questions on account of typing error.

The same has been identified in this updated question paper and has been corrected and highlighted with grey color mark.

Members who have already downloaded the earlier practice paper are advised to take the notice in this regard.

**Solution for self evaluation practice paper**

Clarification: The solution and/ or hints given hereunder are suggested as per ICAI's publication and these solutions are recommendatory only. There can be more than one solution/ alternative answer for the same question/ problem.

P.T.O.

**Paper 1: Financial Reporting**  
**Self evaluation practice paper**  
**Hints/answers**

1. a) **Substance over form as per AS 1** : Transaction should be accounted for in accordance with actual happening and economic reality of the transactions and not by merely its legal form.

In the instant case, the transaction between Power Ltd. and Energy Ltd. should be accounted for as financing rather than sale considering the following facts:

1. Substance of the transaction is financing rather than sale.
2. Energy Ltd. has concurrently agreed to repurchase the same goods from Power Ltd. on 15th March, 2013 at a pre-determined re- selling price covering the purchase price and holding cost of Power Ltd.

Hence the resulting cash flow of ₹ 15,00,000 (advance received) from Power Ltd. , in the hands of Energy Ltd. cannot be considered as revenue as per AS 9 "Revenue Recognition".

**Disclosure in the balance sheet of Energy Ltd. as on 31st March, 2013 (an extract):**

	<u>₹ in Lakhs</u>	<u>₹ in Lakhs</u>
<b>I Equity and Liabilities</b>		
Current liabilities:		
a. <u>Short term borrowings</u>		
(i) Secured loans:		
Advance from Power Ltd.	15.00	
Add: Accrued finance charges [(16.50 – 15) x 0.5/3]	<u>0.25</u>	15.25
<b>II Assets</b>		
Current Assets		
a. <u>Short term Loans and Advances</u>		
Goods lying with Power Ltd. (under sale and repurchase agreement)		15.00

- b) **Reduction in carrying amount**

**Refer para 17 of AS 13**

P Ltd. should make provision of ₹ 6,00,000 for recognizing the diminution (i.e. to reduce the carrying amount) of long term investments to ₹ 14,00,000 in the financial statements.

Re-classification as current investments:

**Refer para 23 of AS 13**

(a) Book value/ original cost = ₹ 20,00,000

(b) Carrying amount = Amount written down after recognizing permanent decline = ₹ 14,00,000

Lower of (a) and (b) = ₹ 14,00,000

Hence, long term investments should be re-classified as current investments at carrying amount of ₹ 14,00,000.

- c) **Provision for foreseeable loss:**

**Refer para 35 of AS 7**

Since as on 31.03.2013 total contract cost is ₹ 9,00,000 and there is no expected further cost to be incurred in future, it has been assumed that the contract is completed on 31.03.2013.

Contract price	<u>10,00,000</u>
(-) Total contract cost as on 31.03.2013	<u>9,00,000</u>
Profit	<u><b>1,00,000</b></u>

Hence, there is no requirement of any provision for foreseeable loss as company is earning profit of ₹ 1,00,000.

Turnover : **Refer para 21 of AS 7**

Stage of completion of contract: 100%

Proportion to total contract value to be recognized as turnover = ₹ 10,00,000

**d) Refer para 10 of AS 16**

In the given case, the amount of ₹ 250 Lakhs was specifically borrowed for construction of boiler plant. Therefore, the treatment of X Ltd. is not correct and amount of borrowing cost to be capitalized for the financial year 2012-13 is calculated as under :

	<u>₹ in Lakhs</u>
Interest paid for 2012-13 (₹ 250 Lakhs x 14%)	35.00
Less : Income on temporary investments from specific borrowings	<u>13.00</u>
<b>Borrowing costs to be capitalized during 2012-13</b>	<b><u>22.00</u></b>

**2. Answer 1)**

Impact of financial restructuring :

**(i) Benefits to GST Ltd.**

	<u>₹ in Lakhs</u>
(a) <u>Reduction in liabilities payable</u>	
Reduction in equity share capital (6 lakh shares x ₹ 75/ share)	450
Reduction in preference share capital (2 lakh shares x ₹ 50/ share)	100
Waiver of O/s debenture interest	26
Waiver of trade creditors (₹ 300 Lakhs x 45%)	<u>135</u>
	711
(b) <u>Revaluation of assets</u>	
Appreciation of land and building (₹ 250 Lakhs - ₹ 200 Lakhs)	<u>50</u>
	<b>761</b>

**(ii) Amount of ₹ 7,61,00,000 utilized to write off losses, fictitious assets and over-valued assets**

	<u>₹ in Lakhs</u>
Writing off P&L a/c	485
Cost of issue of debentures	5
Preliminary expenses	10
Provision for bad and doubtful debts	7
Revaluation of Plant and machinery	<u>254</u>
	<b>761</b>

**Answer 2)**

**Balance Sheet of GST Ltd. as at \_\_\_\_\_**  
(after re-construction.)

	Note no.	₹ in lakhs
<b>I. Equity and Liabilities</b>		
(1) <b>Shareholder's Funds</b>		
a) Share Capital	1	400
(2) <b>Non-Current Liabilities</b>		
Long-term borrowings	2	200
(3) <b>Current Liabilities</b>		
a) Trade payables	3	165
<b>TOTAL</b>		<b>765</b>
<b>II. Assets</b>		
(1) <b>Non-current assets</b>		
a) Fixed Assets		
Tangible assets	4	346
(2) <b>Current assets</b>		
a) Inventories and trade receivables	5	213
b) Cash and cash equivalents	6	206
<b>TOTAL</b>		<b>765</b>

**Notes to accounts**

		₹ in lakhs	₹ in lakhs
1.	<b>Share Capital</b> Issued, subscribed and paid-up share capital: <b>Equity share capital</b> 6,00,000 equity shares of ₹ 25 each, fully paid up 5,00,000 equity shares of ₹ 30 each, fully paid up (of the above, 6,00,000 shares were issued for consideration other than cash) <b>Preference share capital</b> 2,00,000 10% preference shares of ₹ 50 each, fully paid up	150 150  100	400
2.	<b>Long term borrowings</b> 10% debentures		200
3.	<b>Trade payables</b> Sundry Creditors Less : liability waived off	300 135	165
4.	<b>Tangible assets</b> Land and building Add: Appreciation in value Plant and machinery Less : depreciation in value Furniture and fixtures	200 50 300 254 50	346
5.	<b>Inventories and trade receivables</b> Inventories Trade receivables: Sundry debtors Less : Provision for bad and doubtful debts	150  70 7	213
6.	<b>Cash and cash equivalents (WN 1)</b>		206

<b>WN 1) Calculation of closing cash and bank balance:</b>	<b>₹ in Lakhs</b>
Opening balance	130
Add: sale proceeds from issue of new equity shares	150
	280
Less: Payment of ICICI Bank loan	74
	<u><b>206</b></u>

**3. Answer A)**

**Investment in shares in Shares in Small Ltd. Account**

Year	Particulars	₹	Year	Particulars	₹
2010			2011		
April 1	To bank (8,000 shares)	12,80,000	March 31	By P & L a/c (Rectification for pre-acquisition dividend : ₹ 8,00,000 x 15/100	1,20,000
			March 31	By bal. c/d (8,000 shares)	11,60,000
		<b>12,80,000</b>			<b>12,80,000</b>
2011			April 1	By bank (sale proceeds of 500 shares = ₹ 12,80,000 – ₹ 11,90,000)	90,000
April 1	To bal. b/d (8,000 shares)	11,60,000	2012		
April 1	To P & L a/c [ Profit on sale ₹ 90,000 – (11,60,000 x 500/8,000)]	17,500	March 31	By bal. c/d (7,500 shares)	10,87,500
		<b>11,77,500</b>			<b>11,77,500</b>

2012 April 1	To bal. b/d (7,500 shares)	10,87,500	2013 March 31	By P & L A/c (Rectification regarding pre – acquisition dividend on 1,000 shares i.e. 1000 shares x ` 100 x 15%)	15,000
April 1	To bank (1,000 shares purchased)	2,10,000	March 31	By bal. c/d (8,500 shares)	12,82,500
2013 April 1	To bal. b/d	<b>12,97,500</b>			<b>12,97,500</b>
		12,82,500			

**Answer B)**

**WN 1) Capital Profits:**

Particulars	
<b>31st March, 2011:</b>	
Balance of P & L a/c as on 31.03.2010	5,00,000
Less : Dividend on ` 10,00,000 @ 15%	<u>1,50,000</u>
	<u>3,50,000</u>
Big Ltd's share = ` 3,50,000 x $\frac{8,000}{10,000}$ = 2,80,000	
<b>31st March, 2012:</b>	
As Big Ltd has sold 500 shares, its share of capital profits is reduced.	
Big Ltd's share = ` 3,50,000 x $\frac{7,500}{10,000}$ = 2,62,500	
<b>31st March, 2013:</b>	
Balance of P & L account as on 31.03.2012	7,00,000
Less : Dividend on ` 10,00,000 @ 15%	<u>1,50,000</u>
	<u>5,50,000</u>
Big Ltd's share in respect of 1,000 shares purchased on 01.04.2012 = ` 5,50,000 x $\frac{1,000}{10,000}$	55,000
Big Ltd's share of capital profits in respect of 7,500 shares purchased on 31.03.2010 as calculated above	<u>2,62,500</u>
<b>Total</b>	<b><u>3,17,500</u></b>

**WN 2) Goodwill or Cost of Control**

Particulars	31.03.2011	31.03.2012	31.03.2013
Correct cost of Investment as per WN 1)	11,60,000	10,87,500	12,82,500
Less : Paid up value of shares in hand	<u>8,00,000</u>	<u>7,50,000</u>	<u>8,50,000</u>
	3,60,000	3,37,500	4,32,500
Less : Big Ltd's share of capital profits as per WN 2)	<u>2,80,000</u>	<u>2,62,500</u>	<u>3,17,500</u>
<b>Goodwill or cost or control</b>	<b><u>80,000</u></b>	<b><u>75,000</u></b>	<b><u>1,15,000</u></b>

WN 3) **Revenue Profits**

Particulars	31.03.2011	31.03.2012
Balance of P & L account	6,20,000	7,00,000
Less : Capital profits		
Balance of P & L a/c as on 1st April, 2010 after deducting dividend for the year 2009-10 @ 15%	<u>3,50,000</u>	<u>3,50,000</u>
	2,70,000	3,50,000
Less : Minority interest		
20% on 31.03.2011	54,000	
25% on 31.03.2012		87,500
Big Ltd's share	<b>2,16,000</b>	<b>2,62,500</b>
<b>31st March, 2013</b>		
Balance of P & L account on 31.03.2013		8,00,000
Less Capital profits as mentioned above		<u>3,50,000</u>
		4,50,000
Less : Minority interest @ 15%		<u>67,500</u>
		3,82,500
<b>Less : Big Ltd's share in additional capital profits for shares acquired on 1.04.2012</b>		
Balance of P & L account as on 31.03.2012	7,00,000	
Less : Dividend for the year ended 31.03.2012 @ 15%	<u>1,50,000</u>	
	5,50,000	
Less : capital profits already taken into account above	<u>3,50,000</u>	
<b>Additional capital profit</b>	<b><u>2,00,000</u></b>	
Big Ltd's share = ` 2,00,000 x 10/100		<u>20,000</u>
<b>Total</b>		<b><u>3,62,500</u></b>

4. a) **Answer 1)**

**Goodwill = Super profits x No of years of purchase**

$$= ` 17,850 \times 4$$

$$= ` 71,400$$

**WORKING NOTES**

**WN 1) Capital employed:**

Particulars		
Total assets		58,31,200
Less: Preliminary expenses	1,08,500	
Non-trade investments	2,00,000	3,08,500
		55,22,700
Less: Outside liabilities:		
Sundry creditors	2,00,000	
Tax provision	8,00,000	
15% debentures( net of conversion)	2,40,000	12,40,000
Closing capital employed		42,82,700
Less: half of post tax profit for 2011-12		
Profit before tax	12,32,000	
Less: tax @ 30%	3,69,600	
	8,62,400	4,31,200
Average capital employed		38,51,500

**WN 2) Calculation of FMP**

Year	PBT	Weight	Product
2007-08	5,00,000	1	5,00,000
2008-09	7,50,000	2	15,00,000
2009-10	4,30,000	3	12,90,000
2010-11	9,75,000	4	39,00,000
2011-12	12,32,000	5	61,60,000
		15	1,33,50,000

$$\text{Weighted avg. profit} = \frac{1,33,50,000}{15} = ₹ 8,90,000$$

Average profit before tax	8,90,000
Less:	
Income from non-trade investments	20,000
R & D expenses	29,000
Expected increase in foreign currency liability	35,000
FMP before tax	8,06,000
Less : tax @ 50%	4,13,000
<b>FMP after tax</b>	<b>4,03,000</b>

**WN 3) Normal return and super profit**

$$\begin{aligned} \text{Normal return} &= \text{Capital employed} \times \text{NRR} \\ &= ₹ 38,51,500 \times 10\% \\ &= ₹ 3,85,150 \end{aligned}$$

$$\begin{aligned} \text{Super profit} &= \text{Expected profit} - \text{Normal profit} \\ &= ₹ (4,03,000 - 3,85,150) \\ &= ₹ 17,850 \end{aligned}$$

**Answer 2)****WN 4) Net assets available to equity shareholders**

Goodwill (as per Answer 1)	71,400
Sundry fixed assets	28,50,000
Investments (total)	8,40,000
Current assets (total)	20,32,700
	57,94,100
Less: outside liabilities	12,40,000
	<b>45,54,100</b>

**WN 5) Calculation of equivalent no of shares of ₹ 100 each**

	No. of shares
5,000 equity shares of ₹ 100 each, fully paid up	5000
10,000 equity shares of ₹ 50 each, fully paid up	5000
16,000 equity shares of ₹ 40 each, fully paid up	6400
Share suspense account (equivalent shares for ₹ 2,00,000)	2000
Shares for convertible debentures amounting to ₹ 3,60,000	3600
<b>Total</b>	<b>22,000</b>

**Valuation of equity shares:**

$$\begin{aligned} \text{For 5,000 equity shares} &= \frac{\text{Net assets available to equity shareholders}}{\text{No of shares}} \\ &= 45,54,100 / 22,000 = ₹ 207.00 \text{ per share} \end{aligned}$$

$$\text{For 10,000 equity shares} = 207 \times 0.5 = ₹ 103.50 \text{ per share}$$

$$\text{For 16,000 equity shares} = 207 \times 0.4 = ₹ 82.80 \text{ per share}$$

b)

**Operating cycle** : As per Revised Schedule VI "an operating cycle is the time between acquisition of assets for processing and their realization in cash or cash equivalents"

In the absence of information, the operating cycle of G Ltd is taken as 12 months (as presumed in general circumstances).

**Classification of trade payables:**

	Classification
<b>Based on operating cycle</b>	
Since trade payables are normally paid in 12 months (within the operating cycle period)	Current liabilities
However,	
If trade payables are not expected to be paid in 12 months or there is no enough evidence that it will be settled within 12 months from the end of last reporting date	Non-current liabilities

5. a) **Working Notes**

**WN 1) Value of equity and liability component:**

P.V. of debentures repayable after 3 years (10,00,000 x 110% x 0.75)	8,25,000
P.V. of interest = 10,00,000 x 6% x PVIFA (10%,3) i.e. 60,000 x 2.49	<u>1,49,000</u>
<b>Fair value of liability component</b>	<b><u>9,74,400</u></b>
<b>Equity component:</b>	
Fair value of instrument (issue proceeds)	10,00,000
Less: Liability component	<u>9,74,400</u>
	<b>25,600</b>

**WN 2) Debenture liability at the end of each year:**

PARTICULARS	31.3.2011	31.3.2011	31.3.2011
In beginning	9,74,400	10,11,840	10,53,024
Add Interest @ 10%	97,440	1,01,184	1,05,302
	<u>10,71,840</u>	<u>11,13,024</u>	<u>11,58,326</u>
Less : Interest @ 6%	60,000	60,000	60,000
<b>Carrying Amount</b>	<b><u>10,11,840</u></b>	<b><u>10,53,024</u></b>	<b><u>10,98,326**</u></b>

\*\* At the end of third year (i.e. on 31.03.2013), value of debt will be ₹ 11,00,000 [10,00,000 + 10% of 10,00,000 (premium)]. The difference of ₹ 1,674 (₹ 11,00,000 - 10,98,326) is due to the approximation of discounting factor @ 10%.

b) **Answer (i)**

**Calculation of expense to be recognized each year:**

**Year 2007:**

No. of options expected to vest = 500 x 4000 x 0.97 x 0.97 x 0.97 = **18,25,346 options**

Fair value = 18,25,346 x ₹ 15 = ₹ 2,73,80,190

**Expense recognized in 2007 = ₹ 2,73,80,190 x 1/3 = ₹ 91,26,730**

**Year 2008:**

Fair value of options revised in the year = 500 x 4000 x 0.90 x 0.90 x 0.90 x ₹ 15 = ₹ 2,18,70,000

Revised Cumulative Exp. in the year 2008 = ₹ 2,18,70,000 x 2/3 = ₹ 1,45,80,000

Less: Exp. already recognized in 2007

**Expense to be recognized in 2008**

₹ 91,26,730  
₹ 54,53,270

**Year 2009:**

No of options actually vested in 2009= 2500 x 500 = 12,50,000	
Fair value of options actually vested in 2009 = 12,50,000 x ` 15 = ` 1,87,50,000	
Less: Expense recognized till the year 2008	<u>        ` 1,45,80,000</u>
Balance amount to be recognized as expense in 2009	<u>        ` 41,70,000</u>

**Answer (ii)**

**Amount to be recorded in share capital and securities premium a/c upon issue of shares :**

Particulars	2011	2012
No of employees exercising option	1000	300
No of shares issued upon exercise of option @ 500 per share	5,00,000	1,50,000
Exercise price received @ ` 50 per share	` 2,50,00,000	` 75,00,000
Corresponding amount recognized in Employee Stock Option Outstanding A/c @ ` 15 per option	` 75,00,000	` 22,50,000
<b>Total consideration</b>	<b>` 3,25,00,000</b>	<b>` 97,50,000</b>
<b>Amount to be recorded in Share Capital A/c @ ` 10 per share</b>	<b>` 50,00,000</b>	<b>` 15,00,000</b>
<b>Amount to be recorded in Securities Premium A/c @ ` 55 per share (i.e. 65 – 10)</b>	<b>` 2,75,00,000</b>	<b>` 82,50,000</b>
	<b>` 3,25,00,000</b>	<b>` 97,50,000</b>

**6. a) WN 1) GVA & NVA**

Total application of value added  
 = 87.7 + 8.52 + 2.56 + 1.22 = 100 %  
 Since 100% of value added is applied, total of application of value added is Gross Value Added (GVA)  
 i.e. **GVA = 14760 + 1434 + 430 + 206 = ` 16,830 ('000)**

OR

$$\text{GVA} = \frac{14,760 \times 100}{87.70} = ` 16,830 ('000)$$

$$\text{Net value added (NVA)} = \text{GVA} - \text{depreciation} = 16830 - 342 = ` 16,488 ('000)$$

**WN 2) Value added by manufacturing and trading activities**

In the absence of information, it is assumed that Future Ltd. has no additional income other than sales receipts. Hence, **Value added by manufacturing and trading activities = ` 16,830 ('000)**

$$\text{WN 3) Value added per employee} = \frac{\text{Gross value added}}{\text{No of employees}} = \frac{` 16,830 ('000)}{40} = ` 4,20,750$$

$$\text{Average earnings per employee} = \frac{` 16,830 ('000)}{40} = ` 3,60,000$$

<b>WN 4) Calculation of PBT</b>	<u>        ` '000</u>	<u>        ` '000</u>
GVA		16,830
Less: Depreciation	342	
Employees earnings	14,760	
Interest on 10% deb.	<u>1,309</u>	<u>16,411</u>
<b>PBT</b>		<b><u>419</u></b>

**b)**

(a) Scheme size	` 50 crores
(b) F.V. of units	` 10
(c) No. of units [(a)/ (b)]	5,00,00,000
(d) Market value of investments	` 75,00,00,000
(e) NAV per unit =	<u>        ` 75,00,00,000</u> = ` 15
	5,00,00,000

Since NAV is the value of assets of each unit of scheme, we can say that each unit of ` 10 is worth ` 15. Thus in the given case, investors money has been appreciated as NAV is more than the face value.

c) **Calculation of Future Maintainable Profits (FMP) :**

Year	PBT (₹)	Profit after tax (₹)
2010	9,00,000	9,00,000 x 50% = 4,50,000
2011	12,00,000	12,00,000 x 50% = 6,00,000
2012	8,00,000	8,00,000 x 50% = 4,00,000
		<b>14,50,000</b>

$$\text{FMP} = 14,50,000 / 3 = ₹ 4,83,333 \text{ (Approx)}$$

$$\text{Value of AVTAAR Ltd (by capitalizing future maintainable profits)} = ₹ 4,83,333 / 12\% = ₹ 40,27,775$$

$$\text{Value per share} = \frac{\text{Value of company's business}}{\text{No of shares outstanding}} = \frac{₹ 40,27,775}{2,00,000} = ₹ 20.14 \text{ (rounded off)}$$

7.

a) **Refer para 10 of AS 12**

Treatment given by company is not appropriate. Grant of ₹ 10 crores (₹ 50 crores x 20%) should be treated as Capital Reserve.

B Ltd. shall not recognize ₹ 10 crores in the profit and loss account for the year ended 31.03.2013 and thereby reduce the losses, since the amount is not earned but it represents an incentive provided by Government without related cost.

b) **Refer para 44 of AS 26**

**Answer (i)** Costs incurred till technological feasibility/ asset recognition criteria is established would be charged as an expense

Hence R & D cost of ₹ 49,200 will be charged to P & L a/c.

**Answer (ii)** Costs incurred from the point of asset recognition criteria until the time when product costs are incurred are capitalized as software costs.

**Hence expense to be capitalized:**

Testing costs	15,000
Product masters for training material	<u>10,000</u>
	<b>25,000</b>

c) **Calculation of EVA based on Return on Net Assets (RONA) approach:**

$$\begin{aligned} \text{EVA} &= (\text{RONA} - \text{Required Minimum Return}) \times \text{net investments} \\ &= (12\% - 10\%) \times ₹ 590 \text{ Lakhs} \\ &= ₹ 11,80,000 \end{aligned}$$

**OR**

**Alternative answer if RONA = 13.80 %**

$$\begin{aligned} \text{EVA} &= (13.8\% - 10\%) \times ₹ 590 \text{ Lakhs} \\ &= ₹ 22,42,000 \end{aligned}$$

**WN 1) Net operating profit after tax (NOPAT)**

Return to providers of funds is also called NOPAT as post tax net operating results are available for Appropriation. Hence NOPAT = ₹ 240 Lakhs

**Alternative calculation, if NOPAT is not taken as return to providers of funds :**

Particulars	₹ in lakhs
PBT	430.00
Less : Tax @ 40%	172.00
Profit after tax (PAT)	258.00
Add: Interest adjusted for tax effect (2,00,000 x ₹ 100 x 15% x 60%)	18.00
<b>NOPAT</b>	<b>276.00</b>

**WN 2) Return on Net Worth (RONA)**

$$\text{RONA} = \frac{\text{NOPAT}}{\text{Capital employed}} = \frac{240}{2000} \text{ OR } \frac{276}{2000} = \mathbf{12\% \text{ or } 13.80\%}$$

[Capital employed = Shareholders funds + Debentures = 1800 + 200 = ` 2,000in lakhs]

- d) AS 25 suggests that provision in respect of defined benefit schemes like pension and gratuity for an interim period should be calculated based on the year-to - date basis by using the actuarially determined rates at the end of the prior financial year, adjusted for significant market fluctuations since that time and for significant curtailments, settlements or other significant one- time events.

**In the given case**, J Ltd. should calculate the provision in respect of defined benefit scheme of gratuity for its employees for the interim period as on 30.09.2012 on the basis of actuarially determined rate at 31.03.2012 subject to:

- a) Adjustment for fluctuations during the period 01.04.2012 to 30.09.2012, and
- b) Adjustments for significant curtailments, settlements and other one-time events..

e)

Net assets value of all shares = Shareholder's Funds = ` 9,90,000

$$\text{Value per rupee of paid up capital} = \frac{\text{Net assets value}}{\text{Paid-up capital}} = \frac{9,90,000}{7,40,000} = ` 1.338 \text{ (approx)}$$

Net assets value of :

$$\text{Shares of ` 100 paid up} = 1.338 \times 100 = ` \mathbf{133.80}$$

$$\text{Shares of ` 30 paid up} = 1.338 \times 30 = ` \mathbf{40.14}$$

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## Chapter wise weightage of marks

Sr. no.	Chapter	Question no.	Marks
1	Accounting Standards and Guidance Notes	1 7(a), (b) and (d)	20 <u>12</u> 32
3	Corporate Financial Reporting	4(b)	4
4	Accounting for Corporate Restructuring	2	16
5	Consolidated Financial Statements	3	16
6	Accounting and Reporting of Financial Instruments	5(a)	8
7	Share based payments	5(b)	8
8	Financial Reporting for Financial Institutions	6(b)	4
9	Valuation	4(a) 6(c) 7(e)	12 4 <u>4</u> 20
10	Development in Financial Reporting	6(a) 7(c)	8 <u>4</u> 12
<b>TOTAL</b>			<b>120</b>

### **Recommended reading for students appearing in NOV 13**

- **ACCOUNTING STANDARDS AND GUIDANCE NOTES** has much of importance as far as Paper 1 and Paper 2 are concerned.
- For chapters like holding company accounts and amalgamation, merger, demerger etc., Revised Schedule VI is made applicable for from NOV '12 examination onwards for questions covering preparation of balance sheet and profit and loss account. Looking to the hardship of students in attempting such questions, on an average it takes approximately 20 minutes each to attempt questions from these two chapters and since Revised Schedule VI is now mandatory, the time taken to complete such questions may go up to 30 minutes. Hence students are advised to revise and study such chapters on the basis of topics of small and considerable concepts as Institute may not ask all adjustments/ concepts under one roof since accuracy and knowledge of presenting answers with due care to Revised Schedule VI is also now under the observance of examiners and paper checkers while evaluating the answer sheet. Consequently, the length of questions from such chapters may get reasonably reduced.
- Students are advised to have in depth knowledge of Revised Schedule VI and to consider it as a separate chapter and not a context. Practice all practical aspect questions from past and current RTP's, MTP's, and module and practice manuals issued to Institute.  
**[Recommended read: Guidance Note on Revised Schedule VI issued by ICAI]**
- AS 30,31 and 32 : For these three standards, students are advised not to rush behind any additional reading materials or books of authors. Rather these standards are also covered in chapter 6 "Accounting and Reporting of Financial Instruments". Basic and fundamental knowledge for these standards is enough from the examination point of view.
- Chapter 8 and 10 plays a very significant role in boosting your marks especially under the circumstances where paper is more tricky and cornering. Do these chapters with maximum coverage and all small topics.

- Students must note that following materials/ reading books are important for examination :

Title	Reasons
Module I & II	Core conceptual knowledge, exceptional questions are often asked in exams directly from module.
Practice Manual	For developing presentation skills, average coverage of P.M. 40 marks in each attempt.
Past RTP (RTP for MAY 13 is a good example for cornering and concept based problems)	For gaining confidence in presenting cornering concepts and exceptional questions
Current RTP (RTP M'13, N'12, M'12, N'11 may have a big role for dot questions in NOV 13 question paper)	For better revision
MTP from BoS Knowledge Portal Series I : August 2013 <b>(will be available latest by first week of Oct,2013)</b> Series II : Sept 2013 <b>(may be available latest by third week of Oct,2013)</b>	For gaining confidence over accuracy and ability to solve paper under examination conditions
<b><i>On an average 70 - 80 marks paper is covered under aforesaid suggested reading materials.</i></b>	

## ***Last words***

*Financial Reporting can be said as the initiator for your examinations. When we start any new task, job or work, we expect the best to come out of it by doing worship and respecting LORD GANESHA as he is the initiator for our work. So if you crack this paper with 60 or 70 + marks, then it means that you have cleared half of your journey to the 1st group.*

***All the best, don't just wait for the next, do your best and GOD will do the rest.***