PAPER – 1 : FINANCIAL REPORTING

PART – I : RELEVANT AMENDMENTS, NOTIFICATIONS AND ANNOUNCEMENTS

A. Applicable for November, 2014 examination

(i) Schedule III to the Companies Act, 2013

Students may note that Schedule III to the Companies Act, 2013 (Revised Schedule VI to the Companies Act, 1956 discussed in the existing study material) gives general instructions for preparation of balance sheet and statement of profit and loss of a company. Schedule III to the Companies Act, 2013, also contains general instructions for preparation of consolidated financial statements, at its end in addition to Part I - Balance Sheet and Part II - Statement of Profit and Loss. Students are advised to go through complete Schedule III to the Companies Act, 2013 carefully for preparation of financial statements of companies including consolidated financial statements.

Students may refer Schedule III to the Companies Act, 2013 on the Institute's website www.icai.org>>Students>>Bos knowledge portal>>Final Course>>Paper 1 Financial Reporting>>Additional Reading Material>>Schedule III to the Companies Act, 2013.

However, for quick reference of students, the General Instructions for preparation of Consolidated Financial Statements are being reproduced hereunder:

GENERAL INSTRUCTIONS FOR THE PREPARATION OF CONSOLIDATED FINANCIAL STATEMENTS

1. Where a company is required to prepare Consolidated Financial Statements, i.e., consolidated balance sheet and consolidated statement of profit and loss, the company shall mutatis mutandis follow the requirements of Schedule III as applicable to a company in the preparation of balance sheet and statement of profit and loss. In addition, the consolidated financial statements shall disclose the information as per the requirements specified in the applicable Accounting Standards including the following:

    (i) Profit or loss attributable to "minority interest" and to owners of the parent in the statement of profit and loss shall be presented as allocation for the period.

    (ii) "Minority interests" in the balance sheet within equity shall be presented separately from the equity of the owners of the parent.

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2. In Consolidated Financial Statements, the following shall be disclosed by way of additional information:

Name of the entity in the	Net Assets, i.e., total assets minus total liabilities		Share in profit or loss	
	As % of consolidated net assets	Amount	As % of consolidated profit or loss	Amount
1	2	3	4	5
Parent Subsidiaries Indian 1. 2. 3. . . Foreign 1. 2. 3. . . Minority Interests in all subsidiaries Associates (Investment as per the equity method) Indian 1. 2. 3. . . Foreign 1. 2. 3. . . Joint Ventures (as per proportionate consolidation/investment as per the equity method) Indian 1. 2. 3. .				

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. Foreign 1. 2. 3. . .				
TOTAL				

3. All subsidiaries, associates and joint ventures (whether Indian or foreign) will be covered under consolidated financial statements.
4. An entity shall disclose the list of subsidiaries or associates or joint ventures which have not been consolidated in the consolidated financial statements along with the reasons of not consolidating.

(ii) Buy Back of Securities (Amendment) Regulations, 2013

In exercise of the powers conferred under section 30 of the Securities and Exchange Board of India Act, 1992 read with clause (f) of sub-section (2) of Section 77A of the Companies Act, 1956 SEBI made Securities and Exchange Board of India (Buy-back of Securities) (Amendment) Regulations, 2013 to amend the Securities and Exchange Board of India (Buy back of Securities) Regulations, 1998.

The important provisions of the new regulations (applicable for listed companies) are:

(i) No offer of buy-back for fifteen per cent or more of the paid up capital and free reserves of the company shall be made from the open market.

(ii) A company shall not make any offer of buyback within a period of one year reckoned from the date of closure of the preceding offer of buy-back, if any.

(iii) The company shall ensure that at least fifty per cent of the amount earmarked for buy-back is utilized for buying-back shares or other specified securities.

These new regulations can be downloaded from the link http://203.199.247.102/cms/sebi_data/ attachdocs/1375961931576.pdf

(iii) Securities and Exchange Board of India Mutual Funds (Amendment) Regulations, 2013

In exercise of the powers conferred by section 30 of the Securities and Exchange Board of India Act, 1992 (15 of 1992), the Board vide notification No. LAD-NRO/GN/2013-14/03/5652 dated April 16, 2013 had made amendment to the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996. These Regulations may be called as the Securities and Exchange Board of India (Mutual Funds) (Amendment) Regulations, 2013. The SEBI (Mutual Funds) (Amendment) Regulations, 2013 can be downloaded from the link http://www.sebi.gov.in/cms/sebi_data/attachdocs/1366172455558.pdf

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(iv) Securities and Exchange Board of India (Mutual Funds) (Third Amendment) Regulations, 2013

In exercise of the powers conferred by section 30, read with clause (c) of sub-section (2) of section 11 of the Securities and Exchange Board of India Act, 1992 (15 of 1992), the SEBI made new regulations to further amend the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996, namely Securities and Exchange Board of India (Mutual Funds) (Third Amendment) Regulations, 2013. These new regulations can be downloaded from the link http://203.199.247.102/cms/sebi_data/attachdocs/1376972189079.pdf.

(v) Securities and Exchange Board of India (Stock Brokers And Sub-Brokers) (Amendment) Regulations, 2013

In exercise of the powers conferred by section 30 of the Securities and Exchange Board of India Act, 1992 (15 of 1992), the Board vide notification No. LAD-NRO/GN/2013-14/01/8129 dated April 5, 2013 had made amendment to the Securities and Exchange Board of India (Stock Brokers and Sub-brokers) Regulations, 1992. These Regulations may be called as the Securities and Exchange Board of India (Stock Brokers and Sub-brokers) (Amendment) Regulations, 2013. The SEBI (Stock Brokers and Sub-brokers) (Amendment) Regulations, 2013 can be downloaded from the link http://www.sebi.gov.in/cms/sebi_data/attachdocs/1365161667044.pdf

(vi) Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) (Second Amendment) Regulations, 2013

SEBI has issued Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) (Second Amendment) Regulations, 2013 vide notification No. LAD-NRO/GN/2013-14/25/24775 dated 27th September, 2013. As per theses regulations, "clearing corporation, "clearing member" "proprietary trading member" “self-clearing member” and "stock broker” have been defined. These new regulations can be downloaded from the link http://www.sebi.gov.in/cms/sebi_data/attachdocs/1380282501004.pdf.

(vii) Application of AS 30, Financial Instruments: Recognition and Measurement, for the accounting periods ending on or before 31st March 2011 and from 1st April, 2011 onwards

1. Accounting Standard Board of ICAI has issued a clarification regarding applicability of AS 30 (dated 11th February, 2011). It is clarified that in respect of the financial statements or other financial information for the accounting periods commencing on or after 1st April 2009 and ending on or before 31st March 2011, the status of AS 30 would be as below:

   (i) To the extent of accounting treatments covered by any of the existing notified accounting standards (for eg. AS 11, AS 13 etc,) the existing accounting standards would continue to prevail over AS 30.

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(ii) In cases where a relevant regulatory authority has prescribed specific regulatory requirements (eg. Loan impairment, investment classification or accounting for securitizations by the RBI, etc), the prescribed regulatory requirements would continue to prevail over AS 30.

(iii) The preparers of the financial statements are encouraged to follow the principles enunciated in the accounting treatments contained in AS 30. The aforesaid is, however, subject to (i) and (ii) above.

2. From 1st April 2011 onwards,

(i) the entities to which converged Indian accounting standards will be applied as per the roadmap issued by MCA, the Indian Accounting Standard (Ind AS) 39, Financial Instruments; Recognition and Measurement , will apply.

(ii) for entities other than those covered under paragraph 2(i) above, the status of AS 30 will continue as clarified in paragraph 1 above.

3. The abovementioned clarifications would also be relevant to the existing AS 31, Financial Instruments: Presentation and AS 32, Financial Instruments: Disclosures as well as for Ind AS 32, Financial Instruments: Presentation and Ind AS 107, Financial Instruments: Disclosures, after 1st April 2011 onwards.

Note: Ind AS, have not been notified till date. AS 30, 31 and 32 have also not been notified. However, AS 30, 31 and 32 will presumed as encouraged to be followed by all the entities.

B. Not applicable for November, 2014 examination

Ind ASs issued by the Ministry of Corporate Affairs

The Ministry of Corporate Affairs (MCA) has hosted 35 converged Indian Accounting Standards (known as "Ind-AS'), without announcing the applicability date. The issuance of Ind-AS is a significant step towards the implementation of converged standards in India. The MCA will intimate the implementation date later. However, Ind ASs are not made applicable for November, 2014 examination.

PART – II : QUESTIONS AND ANSWERS

QUESTIONS

AS 2

1. (a) Calculate the value of raw materials and closing stock based on the following information:

Raw material X	
Closing balance	500 units

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	₹ Per unit
Cost price including excise duty	200
Excise duty (Cenvat credit is receivable on the excise duty paid)	10
Freight inward	20
Unloading charges	10
Replacement cost	150
Finished goods Y	
Closing Balance	1200 units
	₹ Per unit
Material consumed	220
Direct labour	60
Direct overhead	40

Total fixed overhead for the year was ₹ 2,00,000 on normal capacity of 20,000 units.

Calculate the value of the closing stock, when

(i) Net Realizable Value of the Finished Goods Y is ₹ 400.

(ii) Net Realizable Value of the Finished Goods Y is ₹ 300.

AS 3

(b) Money Ltd., a non financial company has the following entries in its Bank Account. It has sought your advice on the treatment of the same for preparing Cash Flow Statement.

(i) Loans and Advances given to the following and interest earned on them:

(1) to suppliers

(2) to employees

(3) to its subsidiaries companies

(ii) Investment made in subsidiary Smart Ltd. and dividend received

(iii) Dividend paid for the year

(iv) TDS on interest income earned on investments made

(v) TDS on interest earned on advance given to suppliers

(vi) Insurance claim received against loss of fixed asset by fire

Discuss in the context of AS 3 Cash Flow Statement.

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AS 4

(c) For seven companies whose financial year ended on 31st March, 2014, the financial statements were approved by their approving authority on 15th June, 2014.

During 2014-15, the following material events took place:

a. A Ltd. sold a major property which was included in the balance sheet at ₹ 1,00,000 and for which contracts had been exchanged on 15th March, 2014. The sale was completed on 15th May, 2014 at a price of ₹ 2,50,000.

b. On 30th April, 2014, a 100% subsidiary of B Ltd. declared a dividend of ₹ 3,00,000 in respect of its own shares for the year ended on 31st March, 2014.

c. On 31st May, 2014, the mail order activities of C Ltd. (a retail trading group) were shut down with closure costs amounting to ₹ 2.5 million.

d. On 1st July, 2014 the discovery of sand under D Ltd.'s major civil engineering contract site causes the cost of the contract to increase by 25% for which there would be no corresponding recovery from the customer.

e. A fire, on 2nd April, 2014, completely destroyed a manufacturing plant of E Ltd. It was expected that the loss of ₹ 10 million would be fully covered by the insurance company.

f. A claim for damage amounting to ₹ 8 million for breach of patent had been received by F Ltd. prior to the year-end. It is the director's opinion, backed by legal advice that the claim will ultimately prove to be baseless. But it is still estimated that it would involve a considerable expenditure on legal fees.

g. The change in foreign exchange rate of 8% between 1st April, 2014 and 1st June, 2014 has resulted in G Ltd.'s foreign assets being reduced by ₹ 1.3 million.

You are required to state with reasons, how each of the above items numbered (a) to (g) should be dealt with in the financial statement of the various companies for the year ended 31st March, 2014.

AS 5

2\. (a) Explain whether the following will constitute a change in accounting policy or not as per AS 5.

(i) Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement.

(ii) Management decided to pay pension to those employees who have retired after completing 5 years of service in the organistaion. Such employees will get pension of ₹ 20,000 per month. Earlier there was no such scheme of pension in the organization.

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AS 6

(b) On 01.04.2010 a machine was acquired at ₹ 4,00,000. The machine was expected to have a useful life of 10 years. The residual value was estimated at 10% of the original cost. At the end of the 3rd year, an attachment was made to the machine at a cost of ₹ 1,80,000 to enhance its capacity. The attachment was expected to have a useful life of 10 years and zero residual value. At the beginning of the 4th year, the original machine was revalued upwards by ₹ 90,000 and remaining useful life was reassessed at 9 years and residual value was reassessed at NIL value.

Find depreciation for the year 2013-14, if

(i) attachment retains its separate identity.

(ii) attachment becomes integral part of the machine.

AS 7

(c) M/s Highway Constructions undertook the construction of a highway on 01.04.2013. The contract was to be completed in 10 years. The contract price was estimated at ₹ 150 crores. Up to 31.03.2014 the company incurred ₹ 120 crores on the construction. The engineers involved in the project estimated that a further ₹ 45 crores would be incurred for completing the work.

What amount should be charged to revenue for the year 2013-14 as per the provisions of AS 7 'Construction Contracts'? Show the extract of the Profit & Loss Account in the books of M/s. Highway Constructions.

AS 9

3. (a) A Ltd. entered into a contract with B Ltd. to dispatch goods valuing ₹ 25,000 every month for 4 months upon receipt of entire payment. B Ltd. accordingly made the payment of ₹ 1,00,000 and A Ltd. started despatching the goods. In third month, due to a natural calamity, B Ltd. requested A Ltd. not to despatch goods until further notice though A Ltd. is holding the remaining goods worth ₹ 50,000 ready for despatch. A Ltd. accounted ₹ 50,000 as sales and transferred the balance to Advance Received against Sales. Comment upon the treatment of balance amount with reference to the provisions of Accounting Standard 9.

AS 10

(b) Amna Ltd. contracted with a supplier to purchase a specific machinery to be installed in Department A in two months time. Special foundations were required for the plant, which were to be prepared within this supply lead time. The cost of site preparation and laying foundations were ₹ 47,290. These activities were supervised by a technician during the entire period, who is employed for this purpose for ₹ 15,000 per month. Technician's services were given to Department A by Department B, which billed the services at ₹ 16,500 per month after adding 10% profit margin.

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The machine was purchased at ₹ 52,78,000. Sales tax was charged at 4% on the invoice, ₹ 18,590 transportation charges were incurred to bring the machine to the factory. An Architect was engaged at a fee of ₹ 10,000 to supervise machinery installation at the factory premises. Also, payment under the invoice was due in 3 months. However, the Company made the payment in 2nd month. The company operates on Bank Overdraft @ 11%.

Ascertain the amount at which the asset should be capitalized under AS 10.

AS 11

(c) Opportunity Ltd. purchased an equipment costing ₹ 24,00,000 lakhs on 1.4.2013 and the same was fully financed by foreign currency loan (US Dollars) payable in four annual equal installments. Exchange rates were 1 Dollar = ₹ 60.00 and ₹ 62.50 as on 1.4.2013 and 31.3.2014 respectively. First installment was paid on 31.3.2014. The entire difference in foreign exchange has been capitalized. You are required to state that how these transactions would be accounted for.

AS 12

4. (a) A Ltd. purchased a machinery for ₹ 40 lakhs. (Useful life 4 years and residual value ₹ 8 lakhs) Government grant received is ₹ 16 lakhs.

Show the Journal Entry to be passed at the time of refund of grant in the third year and the value of the fixed asset after refund of grant, when:

(1) the grant is credited to Fixed Asset A/c

(2) the grant is credited to Deferred Grant A/c.

AS 13

(b) ABC Ltd. wants to re-classify its investments in accordance with AS 13. Decide and state on the amount of transfer, based on the following information:

(1) A portion of current investments purchased for ₹ 20 lakhs, to be reclassified as long term investment, as the company has decided to retain them. The market value as on the date of Balance Sheet was ₹ 25 lakhs.

(2) Another portion of current investments purchased for ₹ 15 lakhs, to be reclassified as long term investments. The market value of these investments as on the date of balance sheet was ₹ 6.5 lakhs.

(3) Certain long term investments no longer considered for holding purposes, to be reclassified as current investments. The original cost of these was ₹ 18 lakhs but had been written down to ₹ 12 lakhs to recognize permanent decline as per AS 13.

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AS 15

(c) An employee Roshan has joined a company XYZ Ltd. in the year 2013. The annual emoluments of Roshan as decided is ₹ 14,90,210. The company also has a policy of giving a lump sum payment of 25% of the last drawn salary of the employee for each completed year of service if the employee retires after completing minimum 5 years of service. The salary of the Roshan is expected to grow @ 10% per annum.

The company has inducted Roshan in the beginning of the year and it is expected that he will complete the minimum five year term before retiring.

What is the amount the company should charge in its Profit and Loss account every year as cost for the Defined Benefit obligation? Also calculate the current service cost and the interest cost to be charged per year assuming a discount rate of 8%.

(P.V factor for 8% - 0.735, 0.794, 0.857, 0.926, 1)

AS 16

5. (a) Growth Ltd. has undertaken a project for expansion of capacity as per the following details:

	Plan (₹)	Actual (₹)
October, 2013	5,00,000	4,00,000
November, 2013	6,50,000	7,95,000
December, 2013	20,00,000	-
January, 2014	2,00,000	50,000
February, 2014	9,00,000	2,00,000
March, 2014	10,00,000	12,00,000

The company pays to its bank interest at a rate of 15% p.a., which is debited on a monthly basis. During the half yea, company had ₹ 20 lakhs overdraft up to 31st December, surplus cash in January and again overdraft of ₹ 14 lakhs from 1.2.2014 and ₹ 30 lakhs from 1.3.2014. The company had a strike during December and hence could not continue the work during said period. However, the substantial administrative work related to the project was continued. Onsite work was again commenced on 1st January and all the work were completed on 31st March. Assume that expenditure was incurred on 1st day of each month.

Calculate interest to be capitalized giving reason wherever necessary. Assume overdraft will be less, if there is no capital expenditure.

AS 19

(b) Lease Ltd. has initiated a lease for four years in respect of a vehicle costing ₹ 20,00,000 with expected useful life of 5 years. The asset would revert to the company under the lease agreement. The other information available in respect of lease agreement is:

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(1) The unguaranteed residual value of the equipment after the expiry of the lease term is estimated at ₹ 2,50,000.

(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 hand of Lease Ltd.

1. The annual lease payment.
2. The unearned finance income.
3. The segregation of finance income.

Note: (a) PV of residual value for 4th year @ 10% is 0.683.

(b) PV factor for 4 years @ 10% is 3.16987.

AS 20

6. (a) The following information is available in respect of Rise Ltd. for the accounting year 2012-13 and 2013 14:

Net profit for		₹
Year	2012-13	22,00,000
Year	2013-14	30,00,000

Number of shares outstanding prior to right issue 10,00,000 shares.

Right issue: One new share for each five shares outstanding i.e. 2,00,000 shares.

: Right issue price ₹ 25

: Last date to exercise right 31st July, 2013.

Fair value of one equity share immediately prior to exercise of rights on 31.07.2013 is ₹ 32.

You are required to compute:

(i) Basic earnings per share for the year 2012-13.

(ii) Restated basic earnings per share for the year 2012-13 for right issue.

(iii) Basic earnings per share for the year 2013-14.

AS 22

(b) What is the tax effect of sale of fixed assets, considering the block of assets approach followed in the Income-tax Act, 1961?

A company has a block of assets with a written down value of ₹ 1,00,000 on April 1, 2012 for tax purposes. The book value of the assets for accounting purposes

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is also ₹ 1,00,000. The assets are depreciated on written down value basis at 25 percent per annum for both accounting and tax purposes. Of the entire block, assets costing ₹ 5,000 on April 1, 2012, were sold for ₹ 10,000 on March 31, 2014. Compute the deferred tax asset/liability assuming tax rate of 40 per cent.

AS 23

(c) A Ltd. has a share capital of 50,000 shares @ ₹ 100 per share. H Ltd. acquired 15% shares in A Ltd. on 1.4.2013. It also acquired all the 5,000, 12% convertible debentures of ₹ 100 each of A Ltd. These debentures will be converted at par into equity shares of A Ltd. after 3 years. State whether A Ltd. is an Associate of H Ltd. or not with reasons?

AS 25

7. (a) On what basis, should the following be recognized and measured in the Interim Financial Statements

(i) Gratuity and other defined benefit schemes;

(ii) Year-end bonus;

(iii) Provisions;

(iv) Foreign currency translation gains and losses.

AS 26

(b) Religare Ltd. acquired a patent of a drug at a cost of ₹ 20,00,000 for a period of 4 years and the product life-cycle is also 4 years. The company capitalized the cost and started amortizing the asset at ₹ 5,00,000 per annum.

After one year, it was found that the product life-cycle may continue for another 5 years from then. The net cash flows from the product during these 5 years were expected to be ₹ 8,00,000, ₹ 12,00,000, ₹ 10,00,000, ₹ 12,50,000 and ₹ 7,50,000.

Find out the amortization of the patent for each of the years?

AS 28

8. (a) A publisher owns 150 magazine titles of which 70 were purchased and 80 were self-created. The price paid for a purchased magazine title is recognised as an intangible asset. The costs of creating magazine titles and maintaining the existing titles are recognised as an expense when incurred. Cash inflows from direct sales and advertising are identifiable for each magazine title. Titles are managed by customer segments. The level of advertising income for a magazine title depends on the range of titles in the customer segment to which the magazine title relates. Management has a policy to abandon old titles before the end of their economic lives and replace them immediately with new titles for the same customer segment.

What is the cash-generating unit?

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AS 29

(b) A company, incorporated under Section 8 of the Companies Act, 2013, have main objective to promote the trade by organizing trade fairs / exhibitions. When company was organizing the trade fair and exhibitions it decided to charge 5% contingency charges for the participants/outside agencies on the income received from them by the company, while in the case of fairs organized by outside agencies, 5% contingency charges are levied separately in the invoice, the contingency charges in respect of fairs organized by the company itself are inbuilt in the space rent charged from the participants. Both are credited to Income and Expenditure Account of the company.

The intention of levying these charges is to meet any unforeseen liability, which may arise in future. The instances of such unforeseen liabilities could be on account of injury/loss of life to visitors/ exhibitors, etc., due to fire, terrorist attack, stampede, natural calamities and other public and third party liability. The chances of occurrence of these events are high because of large crowds visit the fair. The decision to levy 5% contingency charges was based on assessment only as actual liability on this account cannot be estimated.

The following accounting treatment and disclosure was made by the company in its financial statements:

1. 5% contingency charges are treated as income and matching provision for the same is also being made in accounts.
2. A suitable disclosure to this effect is also made in the notes forming part of accounts.

Required:

(i) Whether creation of provision for contingencies under the facts and circumstances of the case is in conformity with AS 29.

(ii) If the answer of (i) is "No" then what should be the treatment of the provision which is already created in the balance sheet.

IFRS vis a vis AS applicable in India

9. Explain the treatment of the following items with reference to Existing Accounting Standards (as applicable in India) vis-a-vis IFRS.

(1) Statement of Cash Flows

(2) Accounting Policies, Changes in Accounting Estimates and Errors.

Corporate Financial Reporting

10. (a) On the basis of available information, show how these items will appear in the Balance Sheet of a Corporate Entity by preparing appropriate notes to accounts which comply with the requirements of the Schedule III to the Companies Act, 2013:

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Loan Fund	Schedule No.	As at 31st March 2014 (₹)
(a) Secured Loans	1	15,11,220
(b) Unsecured loans - Short term loan from Bank		1,24,190
		16,35,410
Schedule 1: Secured Loans		
Term loans from		
Bank		7,45,120
Others		7,66,100
		15,11,220
Other Information:		
Current maturities of long-term loan from bank		1,15,000
Current maturities of long-term loan from other parties		80,940

Note: There was no interest accrued/due as at the end of the year.

(b) Vasudha Ltd. provides following information:

Raw Material stock holding period : 3.5 months

Work-in-progress holding period : 1 month

Finished goods holding period : 4.5 months

Debtors collection period : 6 months

You are required to compute the operating cycle of Vasudha Ltd. What would happen if the trade payables of the company are paid in 14 months. Whether such trade payables are classified as current or non-current liability?

(c) The management of Kshitij Ltd. contends that the work in progress is not valued because it is difficult to ascertain the same in view of the multiple processes involved. They opine that the value of opening and closing work in progress would be more or less the same. Accordingly, the management had not separately disclosed the work in progress in its financial statements. Comment in line with the Schedule III to the Companies Act, 2013.

Accounting for Corporate Restructuring

11. As part of its expansion strategy A Ltd. has decided to amalgamate its business with that of B Ltd. and new company AB Ltd. being incorporated on the 1st December, 2013 having an authorized equity capital of 2 crore shares of ₹ 10 each. AB Ltd. shall in turn acquire the entire ownership of A Ltd. and B Ltd. in consideration for issuing its equity at 25% premium on 1st January, 2014. It is also agreed that the consideration shall be based on

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the product of the profits available to equity shareholders of each entity, times it PE multiple. The preference shareholders & debenture holders are to be satisfied by the issue of similar instruments in AB Ltd. on 1st January, 2014 in lieu of their existing holdings. Accordingly the relevant information is supplied to you as under:

	A Ltd.	*B Ltd.*
Paid up Equity shares of ₹ 10 class (Nos.)	3 Lakhs	1.2 Lakhs
8% Preference Shares ₹ 10 paid (Nos.)		1 Lakh
5% Redeemable Debentures 2019-20 of ₹ 10 each (Nos.)		0.8 Lakh
Profits before Interest & Taxation (₹)	6,00,000	4,40,000
Price to Earnings Multiple	15	10

To augment the cash retention level of AB Ltd. it is decided that on 1st January, 2014 AB Ltd. shall collect full share application money from the issue of 20,00,000 equity shares @ 40% premium under Private Placement. The allotment of the shares will be made on 31st March, 2014 and such shares shall qualify for dividend from 2014-15 only.

AB Ltd. shall also avail a 12.50% TOD of 15 lakhs to meet its preliminary expenses and cost of working which amount to ₹ 12 lakhs and ₹ 2 lakhs respectively. The TOD will be availed on 1st February, 2014 and closed on 31st March, 2014. Preliminary expenditure is tax deductible @ 20% each year.

Due to an accounting omission the opening inventory of B Ltd. of 5 lakhs (actual value) & the closing stock of A Ltd. of 2.20 lakh was understated & overstated by 5% and 10% respectively.

The dividend schedule proposed is that all companies would pay interim dividend for equity, for the period from 1st January, 2014 to 31st March, 2014. The rates of dividend being A Ltd. @ 5%, B Ltd. @ 2% and AB Ltd. @ 3.5%. The preference shareholders & debentureholders dues for the post take over period are discharged on 31st March, 2014.

It is proposed that in the period January-March 2014, AB Ltd. would carry out trade in futures that would generate an absolute post tax return of 18% by using the funds generated from the Private Placement. The trades would be squared off on 31st March, 2014. Proceeds from such transactions are not liable to withholding taxes.

You are required to prepare a projected Profit & Loss A/c for the period ended 31st March, 2014 and a Balance Sheet on that date for AB Ltd.

The corporate tax rate for the company is 40%.

Consolidated Financial Statements of Holding Companies

12. (a) Following are the summarized Balance Sheets of A Ltd., B. Ltd. & C Ltd., as on 31.3.2014:

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Liabilities	*A Ltd.*	*B Ltd.*	*C Ltd.*	*Assets*	*A Ltd.*	*B Ltd.*	*C Ltd.*
	₹	₹	₹		₹	₹	₹
Share capital of ₹ 10 each	5,00,000	3,00,000	2,00,000	Fixed Assets Investment	2,00,000	1,50,000	1,20,000
General Reserves	80,000	60,000	50,000	24,000 Shares in			
Profit & Loss A/c	1,00,000	80,000	60,000	B Ltd.	2,50,000		
Sundry Creditors B Ltd. Balance	70,000	20,000	30,000 40,000	6,000 Shares in C Ltd.	80,000		
C Ltd. Balance	1,20,000			12,000 shares in C Ltd.		1,60,000	
				Stock in trade	1,00,000	60,000	60,000
				Debtors	1,50,000	40,000	80,000
				C Ltd. Balance		30,000	
				A Ltd. Balance			90,000
				Cash and Bank Balance	90,000	20,000	30,000
	8,70,000	4,60,000	3,80,000		8,70,000	4,60,000	3,80,000

Other Information:

(a) All the investments were made on 1.8.2013 on which date the provisions were as follows:

	B Ltd. (₹)	*C Ltd. (₹)*
General Reserves	30,000	15,000
Profit & Loss Account	50,000	25,000

(b) In December 2013, B Ltd. invoiced goods to A Ltd. for ₹ 80,000 at cost plus 25%. The closing stock of A Ltd. includes such goods valued at ₹ 10,000.

(c) C Ltd. sold to B Ltd. a machinery costing ₹ 27,000 at a profit of 25% on selling price on 31.12.2013. Depreciation at 10% per annum was provided by B Ltd. on this equipment.

(d) Debtors of A Ltd. include ₹ 12,000 being the amount due from B Ltd.

(e) A Ltd. proposed dividend at 10%.

You are required to prepare the Consolidated Balance Sheet of the Group as on 31.3.2014 as per Schedule III to the Companies Act, 2013.

Joint Venture in Consolidated Balance Sheet

(b) The summarized consolidated balance sheets of M Ltd. and its subsidiary N Ltd. and balance sheet of joint venture entity C Ltd. as on 31.3.2014 are as follows:

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Liabilities	*M Ltd. (CBS) (₹)*	*C Ltd. (₹)*
Share capital :		
Shares of ₹ 100 each	6,00,000	2,00,000
General reserve	2,00,000	--
Profit and loss account	80,000	--
6% Debentures	-	1,50,000
Trade creditors	75,000	67,500
	9,55,000	4,17,500
Assets		
Fixed Assets	4,50,000	1,50,000
Stock-in-trade	1,40,000	60,000
Debtors	80,000	45,000
6% Debentures of C Ltd. acquired at par	90,000	-
Shares of C Ltd. (1,500 shares @ ₹ 80 each)	1,20,000	-
Cash at bank	75,000	12,500
Profit and loss A/c	-	1,50,000
	9,55,000	4,17,500

M Ltd., acquired the shares on 1st August, 2013. The Profit and Loss account of C Ltd., showed a debit balance of ₹ 2,25,000 on 1.4.2013. During June 2013, goods costing ₹ 9,000 were destroyed against which the insurer paid only ₹ 3,000. Trade creditors of C Ltd., include ₹ 30,000 for goods supplied by M Ltd., on which M Ltd., made a profit of ₹ 3,000. Half of the goods were still in stock on 31.3.2014.

Prepare a consolidated balance sheet incorporating the Joint Venture entity operations using proportionate consolidation method.

Financial Instruments

13. Liberal Ltd. granted ₹ 18,00,000 loan to its employees on April 1, 2013 at a concessional interest rate of 5% per annum. Loan is to be repaid in six equal annual instalments along with interest. Market rate of interest for such loan is 10% per annum. Following the principles of recognition and measurement as laid down in AS 30, calculate the value of loan initially to be recognized and amortised cost for all the subsequent years. The present value of ₹ 1 receivable at the end of each year based on discount factor of 10% can be taken as:

Year end	1	0.9090
	2	0.8263
	3	0.7512
	4	0.6829

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	5	0.6208
	6	0.5644

Share Based Payments

14. At the beginning of year 1, an enterprise grants 100 stock options to each of its 500 employees. The grant is conditional upon the employee remaining in service over the next three years. The enterprise estimates that the fair value of each option is ₹ 15. The enterprise estimates that 100 employees will leave during the three-year period and therefore forfeit their rights to the stock options.

    40 employees left during year 1. By the end of year 1, the share price of the enterprise has dropped, and the enterprise reprices its stock options, and that the repriced stock options will vest at the end of year 3. The enterprise estimates that further 70 employees will leave during years 2 and 3.

    During year 2, further 35 employees left, and the enterprise estimates that further 30 employees will leave during year 3. During year 3, 28 employees left. The stock options vested at the end of year 3 to the remaining employees.

    The enterprise estimates that, at the date of repricing, the fair value of each of the original stock options granted (i.e., before taking into account the repricing) is ₹ 5 and that the fair value of each repriced stock option is ₹ 8.

    Calculate the amount to be recognised towards employees services received in years 1-3.

Mutual Fund

15. (a) Calculate the NAV of a Mutual Fund Scheme from the information given below:

    At the beginning of the year:

    Number of units outstanding 1 Crore units of ₹ 10 each

    Investment at cost ₹ 10 crores (Market Value ₹ 16 crores)

    Outstanding Liabilities ₹ 5 crores

    Other Information:

    (1) Additional 20 lakhs units were sold during the year at ₹ 24.

    (2) No additional investments were made during the year and as at the year end, 50% of the investment at year beginning were quoted at 80% of the book value.

    (3) 10% of the investments had witnessed a permanent fall of 10% below cost.

    (4) The balance investments were quoted at ₹ 13.60 crores.

    (5) Outstanding liabilities towards custodian charges, salaries and commission etc. applicable to the scheme were 1 crore.

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NBFC

(b) Rental Limited is a non-banking finance company. It accepts public deposit and also deals in hire purchase business. It provides you with the following information regarding major hire purchase deals as on 31-03-2012. Few machines were sold on hire purchase basis. The hire purchase price was set as ₹ 100 lakhs as against the cash price of ₹ 80 lakhs. The amount was payable as ₹ 20 lakhs down payment and balance in 5 equal instalments. The hire vendor collected first instalment as on 31-03-2013, but could not collect the second instalment which was due on 31-03-2014. The company was finalising accounts for the year ending 31-03-2014. Till 15-05-2014, the date on which the Board of Directors signed the accounts, the second instalment was not collected. Presume IRR to be 10.42%.

Required :

(i) What should be the principal outstanding on 1-4-2013? Should the company recognize finance charge for the year 2013-14 as income?

(ii) What should be the net book value of assets as on 31-03-14 so far Rental 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 the RBI?

Valuation of Goodwill

16. Apex Ltd. gives the following information about past profits:

Year	*Profits (₹ in '000s)*
2009-10	21,70
2010-11	22,50
2011-12	23,70
2012-13	24,50
2013-14	21,10

On scrutiny it is found (i) that upto 2011-12, Apex Ltd. followed FIFO method of stock valuation and thereafter adopted LIFO method, (ii) that upto 2012-13, it followed straight line depreciation and thereafter adopted written down value method.

Given below are the details of stock valuation:

(₹ in '000s)

Year	*Opening Stock*		*Closing Stock*	
	FIFO	*LIFO*	*FIFO*	*LIFO*
2009-10	40,00	39,80	46,00	41,20

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2010-11	46,00	41,20	49,20	47,90
2011-12	49,20	47,90	38,90	39,10
2012-13	38,90	39,10	42,00	38,50
2013-14	42,00	38,50	45,00	43,10

Straight line and written down value depreciation were as follows:

Year	*Straight Line (₹ '000)*	*W.D.V. (₹ '000)*
2009-10	12,10	17,00
2010-11	14,15	18,10
2011-12	15,00	19,25
2012-13	16,70	19,60
2013-14	18,00	19,40

Determine future maintainable profits that can be used for valuation of goodwill.

Valuation of Shares

17. Following is the Balance Sheet of Survey Ltd. as on 31st March, 2014:

Liabilities	*₹*	*Assets*	*₹*
50,000 equity shares of ₹ 10 each	5,00,000	Building	3,50,000
2,500, 12% Preference shares of ₹ 100 each	2,50,000	Plant and Machinery	4,30,000
Profit & Loss A/c	2,20,000	Patents	80,000
15% Debentures	1,20,000	Sundry debtors	2,00,000
General Reserve	1,80,000	Stock in trade	2,90,000
Creditors	1,50,000	Cash at Bank	70,000
	14,20,000		14,20,000

Buildings & Plant and Machinery were acquired many years ago and should be considered as worth of ₹ 5,00,000 and ₹ 6,30,000 respectively.

The Profits for the last five years were as follows:

Year	*Profit (before tax) ₹*
2009-10	1,80,000
2010-11	2,50,000
2011-12	60,000
2012-13	3,00,000
2013-14	3,50,000

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The company paid a remuneration of ₹ 50,000 p.a. to the managerial personnel, but in future it will be paying ₹ 75,000, the increase having been sanctioned by the Government. During 2011-12, there was a prolonged strike, resulting in low profits. There has been no substantial change in the capital employed. The company has paid a dividend of 12 percent on equity shares consistently and proposes to stick to this rate in the foreseeable future. In the class of business to which the company belongs, the dividend rates have been fluctuating and the asset backing of an equity share is about 2 times. Equity shares with an average dividend of 15% sell at par. The company is anxious to provide funds for replacement of assets when due, for which it is proposed to make 20% provision on PAT. Assume future tax rate to be 40%. Calculate the value of an equity share of Survey Ltd. on yield basis.

Valuation of Brand

18. From the following information, determine the possible value of brand as per potential earning model:

	Particulars	*₹ in lakhs*
(i)	Profit After Tax (PAT)	2,500
(ii)	Tangible Fixed Assets	10,000
(iii)	Identifiable intangible other than brand	1,500
(iv)	Weighted average cost of capital (%)	14%
(v)	Expected normal return on tangible assets [weighted average cost (14%) + normal spread 4%]	18%
(vi)	Appropriate capitalization factor for intangibles	25%

Value Added Statement

19. From the following Profit & Loss Account of Yash Ltd. prepare Gross Value Added Statement and show the reconciliation between Gross Value Added and Profit before Taxation.

Profit and Loss Account for the year ended 31st March, 2014

Particulars		*Notes*	*(₹ in '000s)*
Sales less return			21,350
Trading profit		1	1,920
Less: Depreciation	302		
Interest	140	2	(442)
Add: Other income			80
Profit before tax			1,558
Provision for tax		3	(688)

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Profit after tax			870
Less: Extraordinary items		4	(15)
			855
Less: Proposed dividend			(340)
Retained profit			515

Notes:

1.	Trading profit is arrived at after charging the following:		(₹ in '000s)
	Salaries, wages etc. to employees		3685
	Director's remuneration		360
	Audit fees		220
	Hire of equipment		290
2.	Interest figure is ascertained as below		
	Interest paid on bank loans and overdrafts	160	
	Interest received	(20)	140
3.	Extraordinary items:		
	Surplus on sale of properties	20	
	Loss of Goods by fire	(35)	(15)
4.	The charge for taxation include a transfer of ₹ 1,48,000 to the credit of deferred tax account		

Economic Value Added

20. (a) The following information (as of 31-03-2014) is supplied to you by ABC Ltd.:

			(₹ in crores)
(i)	Profit after tax (PAT)		205.90
(ii)	Interest		4.85
(iii)	Equity Share Capital	40.00	
	Accumulated surplus	700.00	
	Shareholders fund	740.00	
	Loans (Long term)	37.00	
	Total long term funds		777.00
(iv)	Market capitalization		2,892.00

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Additional information:			
(a)	Risk free rate		12.00 percent
(b)	Long Term Market Rate (Based on BSE Sensex)		15.50 percent
(c)	Effective tax rate for the company		25.00 percent
(d)	Beta (β) for last few years		
	Year		
	1	0.48	
	2	0.52	
	3	0.60	
	4	1.10	
	5	0.99	

Using the above data you are requested to calculate the Economic Value Added of M/s. ABC Ltd. as on 31st March, 2014.

Human Resource Accounting

(b) From the following details, compute according to Lev and Schwartz (1971) model, the value of human resources of skilled employees group.

(i)	Annual average earning of an employee till the retirement age	₹ 1,00,000
(ii)	Age of Retirement	65 years
(iii)	Discount rate	15%
(iv)	No. of employees in the group	20
(v)	Average age	62 years

SUGGESTED ANSWERS / HINTS

1. (a) Statement showing valuation of Raw Material and Finished Goods at cost

Raw Material X	₹
Cost Price	200
Less: CENVAT credit	(10)
	190
Add: Freight Inward	20
Unloading charges	10
Cost	220

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Finished goods Y	₹
Materials consumed	220
Direct labour	60
Direct overhead	40
Fixed overheads (2,00,000/20,000)	10
Cost	330

(i) When Net Realisable Value (NRV) of the Finished Goods Y is ₹ 400

NRV is greater than the cost of Finished Goods Y i.e. ₹ 330

Hence, Raw Material and Finished Goods will be valued at cost

Accordingly, value of closing stock will be:

	Qty	*Rate*	*Amount (₹)*
Raw Material X	500	220	1,10,000
Finished Goods Y	1,200	330	3,96,000
Total cost of closing stock			5,06,000

(ii) When Net Realisable Value of the Finished Goods Y is ₹ 300

NRV is less than the cost of Finished Goods Y i.e. ₹ 330

Hence, Raw Material is to be valued at replacement cost and Finished Goods are to be valued at NRV.

Accordingly, value of closing stock will be:

	Qty	*Rate*	*Amount (₹)*
Raw Material X	500	150	75,000
Finished Goods Y	1,200	300	3,60,000
Total cost of closing stock			4,35,000

Note: It has been assumed that Raw Material X is used for production of Finished Goods Y.

(b) Treatment as per AS 3 'Cash Flow Statement'

(i) Loans and advances given and interest earned

(1) to suppliers — Cash flows from operating activities

(2) to employees — Cash flows from operating activities

(3) to its subsidiary companies — Cash flows from investing activities

(ii) Investment made in subsidiary company and dividend received

Cash flows from investing activities

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(iii) Dividend paid for the year

Cash flows from financing activities

(iv) TDS on interest income earned on investments made

Cash flows from investing activities

(v) TDS on interest earned on advance given to suppliers

Cash flows from operating activities

(vi) Insurance claim received against loss of fixed asset by fire

Extraordinary item to be shown under a separate heading as 'Cash inflow from operating activities'.

(c) Treatment as per AS 4 'Contingencies and Events Occurring After the Balance Sheet Date'

(a)	A Ltd.	The sale of property should be treated as an adjusting event since contracts had been exchanged prior to the year-end. The effect of the sale would be reflected in the financial statements ended on 31.3.2014 and the profit on sale of property ₹ 1,50,000 would be treated as an extraordinary item.
(b)	B Ltd.	The declaration of dividend on 30th April, 2014 of ₹ 3,00,000 would be treated as a non-adjusting event in the financial statements of 2013-14. This is because, the dividend has been declared after the balance sheet date and no conditions existed on the balance sheet date for such declaration of dividend. Further as per AS 9, right to receive dividend is established when it is declared and not before that.
(c)	C Ltd.	A closure not anticipated at the year-end would be treated as a non-adjusting event. Memorandum disclosure would be required for closure of mail order activities since non disclosure would affect user's understanding of the financial statements.
(d)	D Ltd.	The event took place after the financial statements were approved by the approving authority and is thus outside the purview of AS 4. However, in view of its significance of the transaction, the directors may consider publishing a separate financial statement/additional statement for the attention of the members in general meeting.
(e)	E Ltd.	The event is a non adjusting event since it occurred after the year-end and does not relate to the conditions existing at the year-end. However, it is necessary to consider the validity of the going concern assumption having regard to the extent of insurance cover. Also, since it is said that the loss would be fully recovered by the insurance company, the fact should be

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		disclosed by way of a note to the financial statements.
(f)	F Ltd.	On the basis of evidence provided, the claim against the company will not succeed. Thus, ₹ 8 million should not be provided in the account, but should be disclosed by means of a contingent liability with full details of the facts as per AS 9. Provision should be made for legal fee expected to be incurred to the extent that they are not expected to be recovered.
(g)	G Ltd.	The change in exchange rates is a non adjusting event since it does not relate to the conditions existing at the balance sheet date. However, they may be of such significance that they may require a disclosure in the report of the approving authority to enable users of financial statements to make proper evaluations and decisions.

2. (a) As per para 31 of AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy.

(i) Accordingly, introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is not a change in an accounting policy.

(ii) Similarly, the adoption of a new accounting policy for events or transactions which did not occur previously or that were immaterial will not be treated as a change in an accounting policy.

(b) 1. Depreciation of Original Machine

	₹
Original cost of Machine as on 01.04.2010	4,00,000
Less: Residual Value @ 10%	(40,000)
Depreciable Value (a)	3,60,000
Useful life is 10 years	
Depreciation per year	36,000
Depreciation for 3 years (36,000 x 3) (b)	1,08,000
Written down value at the end of 3 years (as on 31.03.2013) [4,00,000 – 1,08,000]	2,92,000
Add: Revaluation	90,000
Total book value after revaluation	3,82,000
Remaining useful life was reassessed as 9 years	
Depreciation per year from 2013-14	42,444

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2. Depreciation of Attachment ₹

Original cost of Attachment as on 01.04.2013	1,80,000
Useful life is 10 years	
Depreciation per year from 2013-14	18,000

Depreciation for the year 2013-14

(i) When Attachment retains its separate identity:

Depreciation of Original Machine	₹ 42,444
Depreciation of Attachment	₹ 18,000
Total Depreciation for 2013-14	₹ 60,444

(ii) Attachment becomes integral part of the Machine:

As per para 9 of AS 6 'Depreciation Accounting', any addition or extension to an existing asset which is of a capital nature and which becomes an integral part of the existing asset is depreciated over the remaining useful life of that asset. Accordingly,

Total value of Machine as on 01.04.2013

Original Machine at revalued cost (W.N.1)	₹ 3,82,000
Cost of attachment	₹ 1,80,000
	₹ 5,62,000
Remaining useful life of Original Machine	9 years
Depreciation for 2013-14	₹ 62,444

(c) Statement showing amount to be charged to revenue

	(₹ in crores)
Cost of construction incurred upto 31.03.2014	120
Add: Estimated future cost	45
Total estimated cost of construction	165
Degree of completion (120/165 x 100)	72.73%
Revenue recognized (72.73% of 150)	109 (approx)
Total Foreseeable loss (165 – 150)	15
Less: Loss for current year (120 – 109)	(11)
Expense loss to be provided for	4

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Profit and Loss Account (Extract)

	(₹ in crores)		(₹ in crores)
To Construction Costs	120	By Contract Price	109
To Provision for loss	4	By Net loss	15
	124		124

3. **(a)** As per para 11 of AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

In the given case, transfer of property in goods results in or coincides with the transfer of significant risks and rewards and ownership to the buyer. Also, the sale price has been recovered by the seller. Hence, the sale is complete. However, delivery has been postponed at buyer's request. Merely postponement of delivery at buyers request shall not postpone the recognition of sale. Therefore, A Ltd. should recognize the entire sale of ₹ 1,00,000 (₹ 25,000 x 4) and no part of the same should be treated as Advance Receipt against Sales.

(b) Calculation of Cost of Fixed Asset (i.e. Machine) as per AS 10

Particulars		₹
Purchase price	Given	52,78,000
Add: Sales tax at 4%	₹ 52,78,000 x 4%	2,11,120
Site preparation cost	Given	47,290
Technician's salary	Specific/Attributable overheads for 2 months [See Note (ii)]	30,000
Initial delivery cost	Transportation	18,590
Professional fee for installation	Architect's fee	10,000
Total cost of asset		55,95,000

Note:

(i) Interest on bank overdraft for earlier payment of invoice is not relevant under AS 10.

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(ii) Internally booked profits should be eliminated in arriving the cost of fixed assets as per para 10 of AS 10 'Accounting for Fixed Assets'.

(iii) It has been assumed that the purchase price of ₹ 52,78,000 excludes amount of sales tax.

(c) As per para 13 of AS 11 (Revised 2003) 'The Effects of Changes in Foreign Exchange Rates', exchange differences arising on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, should be recognized as income or expenses in the period in which they arise. Thus, exchange differences arising on repayment of liabilities incurred for the purpose of acquiring fixed assets will be recognized as income or expense.

Calculation of Exchange Difference:

Foreign currency loan =	₹ 24,00,000/60 = 40,000 US Dollars
Exchange difference =	40,000 US Dollars × (62.50-60.00) = ₹ 1,00,000
(including exchange loss on payment of first instalment)	

Therefore, entire loss due to exchange differences amounting ₹ 1,00,000 should be charged to profit and loss account for the year.

Note: The above answer has been given on the basis that the company has not availed the option for capilisation of exchange difference as per para 46/ 46A of AS 11.

However, as per para 46A of the standard, the exchange differences arising on reporting of long term foreign currency monetary items at rates different from those at which they were initially recorded during the period, in so far as they relate to the acquisition of a depreciable capital asset, can be added to or deducted from the cost of the asset and shall be depreciated over the balance life of the asset.

Accordingly, in case Opportunity Ltd. opts for capitalizing the exchange difference, then the entire amount of exchange difference of ₹ 1,00,000 will be capitalsied to 'Equipment account'. This capitalized exchange difference will be depreciated over the useful life of the asset.

Cost of the asset on the reporting date

Initial cost of Equipment	₹ 24,00,000
Add: Exchange difference as on 31.3.2014	₹ 1,00,000
Total cost on the reporting date	₹ 25,00,000

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4. (a) In the books of A Ltd.

Journal Entries (at the time of refund of grant)

(1) If the grant is credited to Fixed Asset Account:

		₹	₹
I	Fixed Asset A/c Dr.	16 lakhs	
	To Bank A/c		16 lakhs
	(Being grant refunded)		

II The balance of fixed assets after charging depreciation for two years was ₹ 16 lakhs (W.N.1) and after refund of grant it will become (₹ 16 lakhs + ₹ 16 lakhs) = 32 lakhs on which depreciation of ₹ 12 lakhs p.a [(32 lakhs – 8 lakhs)/2] = will be charged for remaining two years.

(2) If the grant is credited to Deferred Grant Account:

As per para 14 of AS 12 'Accounting for Government Grants,' income from Deferred Grant Account is allocated to Profit and Loss account usually over the periods and in the proportions in which depreciation on related assets is charged. Accordingly, in the first two years (₹ 16 lakhs /4 years) = ₹ 4 lakhs p.a. x 2 years = ₹ 8 lakhs were credited to Profit and Loss Account and ₹ 8 lakhs was the balance of Deferred Grant Account after two years.

Therefore, on refund in the 3rd year, following entry will be passed:

		₹	₹
I	Deferred Grant A/c Dr.	8 lakhs	
	Profit & Loss A/c Dr.	8 lakhs	
	To Bank A/c		16 lakhs
	(Being Government grant refunded)		

II Deferred grant account will become Nil. The fixed assets will continue to be shown in the books at ₹ 24 lakhs (W.N.2) and depreciation will continue to be charged at ₹ 8 lakhs per annum for the remaining two years.

Working Notes:

1. Balance of Fixed Assets after two years but before refund (under first alternative)

Fixed assets initially recorded in the books = ₹ 40 lakhs – ₹ 16 lakhs = ₹ 24 lakhs

Depreciation p.a. = (₹ 24 lakhs – ₹ 8 lakhs)/4 years = ₹ 4 lakhs per year

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Value of fixed assets after two years but before refund of grant

= ₹ 24 lakhs – (₹ 4 lakhs x 2 years) = ₹ 16 lakhs

2. **Balance of Fixed Assets after two years but before refund (under second alternative)**

Fixed assets initially recorded in the books = ₹ 40 lakhs

Depreciation p.a. = (₹ 40 lakhs – ₹ 8 lakhs)/4 years = ₹ 8 lakhs per year

Book value of fixed assets after two years = ₹ 40 lakhs – (₹ 8 lakhs x 2 years)

= ₹ 24 lakhs.

(b) As per AS 13, where investments are reclassified from current to long-term, transfers are made at the lower of cost and fair value at the date of transfer.

(1) In the first case, the market value of the investment is ₹ 25 lakhs, which is higher than its cost i.e. ₹ 20 lakhs. Therefore, the transfer to long term investments should be carried at cost i.e. ₹ 20 lakhs.

(2) In the second case, the market value of the investment is ₹ 6.5 lakhs, which is lower than its cost i.e. ₹ 15 lakhs. Therefore, the transfer to long term investments should be carried in the books at the market value i.e. ₹ 6.5 lakhs. The loss of ₹ 8.5 lakhs should be charged to profit and loss account.

As per AS 13, where long-term investments are re-classified as current investments, transfers are made at the lower of cost and carrying amount at the date of transfer.

(3) In the third case, the book value of the investment is ₹ 12 lakhs, which is lower than its cost i.e. ₹ 18 lakhs. Here, the transfer should be at carrying amount and hence this re-classified current investment should be carried at ₹ 12 lakhs.

(c) Calculation of Defined Benefit Obligation

Expected last drawn salary = ₹ 14,90,210 x 110% x 110% x 110% x 110% x 110%

= ₹ 24,00,000

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

Amount of ₹ 6,00,000 will be charged to Profit and Loss Account of the company every year as cost for Defined Benefit Obligation.

Calculation of Current Service Cost

Year	*Equal apportioned amount of DBO [i.e. ₹ 30,00,000/5 years]*	*Discounting @ 8% PV factor*	*Current service cost (Present Value)*
a	*b*	*c*	*d = b x c*
1	6,00,000	0.735 (4 Years)	4,41,000

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2	6,00,000	0.794 (3 Years)	4,76,400
3	6,00,000	0.857 (2 Years)	5,14,200
4	6,00,000	0.926 (1 Year)	5,55,600
5	6,00,000	1 (0 Year)	6,00,000

Calculation of Interest Cost to be charged per year

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

*Due to approximations used in calculation, this figure is adjusted accordingly.

5. (a) Growth Ltd.

Month	*Actual Expenditure (₹)*	*Interest capitalized (₹)*	*Cumulative amount (₹)*
October, 2013	4,00,000	5,000	4,05,000
November, 2013	7,95,000	15,000	12,15,000
December, 2013	-	15,188	12,30,188
January, 2014	50,000	-	12,80,188
February,2014	2,00,000	17,500	14,97,688
March, 2014	12,00,000	33,721	27,31,409
	26,45,000	86,409	

Note:

1. As per para 18 of AS 16, 'Borrowing Cost', capitalisation of borrowing costs is not normally suspended during a period when substantial technical and administrative work is being carried out. Therefore, the interest for that period i.e. for the month of December has also been capitalized.
2. During January, the company did not incur any interest as there was surplus cash in January. Therefore, no amount should be capitalized during January as per para 14(b) of AS 16.

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3. During February, actual overdraft (borrowings) was ₹ 14 lakhs only. Hence, interest of ₹ 17,500 on ₹ 14,00,000 has been calculated even though actual expenditure on project exceed ₹ 14 lakhs.

(b) (1) Calculation of annual lease payment

	₹
Cost of the equipment	20,00,000
Unguaranteed residual value	2,50,000
PV of residual value for 4th year @ 10% (₹ 2,50,000 x 0.683)	1,70,750
Fair value to be recovered from lease payment (₹ 20,00,000 - ₹ 1,70,750)	18,29,250
PV factor for 4 years @ 10%	3.16987
Annual lease payment (₹ 18,29,250 / 3.16987)	5,77,074

(2) **Unearned Finance Income**

	₹
Total lease payments (₹ 5,77,074 x 4)	23,08,296
Add: Residual value	2,50,000
Gross investment	25,58,296
Less: Present value of investment (₹ 18,29,250 + 1,70,750)	(20,00,000)
Unearned Finance Income	5,58,296

(3) **Segregation of Finance Income**

Year	*Lease rentals (₹)*	*Finance charge @ 10% on outstanding amount of the year (₹)*	*Repayment (₹)*	*Outstanding Amount (₹)*
0	-	-	-	20,00,000
1	5,77,074	2,00,000	3,77,074	16,22,926
2	5,77,074	1,62,293	4,14,781	12,08,145
3	5,77,074	1,20,814	4,56,260	7,51,885
4	8,27,074*	75,189	7,51,885	-
	25,58,296	5,58,296	20,00,000	

* ₹ 5,77,074 + ₹ 2,50,000 = ₹ 8,27,074.

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6. (a) **Computation of basic earnings per share**

	Year 2012-13 (₹)	*Year 2013-14 (₹)*
EPS for the year 2012-13 as originally reported = Net profit for the year attributable to equity share holders / weighted average number of equity shares outstanding during the year = ₹ 22,00,000/10,00,000 shares	2.20	
EPS for the year 2012-13 restated for the right issue = ₹ 22,00,000 / (10,00,000 x 1.04)	2.12	
EPS for the year 2013-14 (including effect of right issue) = ₹ 30,00,000 / {(10,00,000 x 1.04 x 4/12) + (12,00,000 x 8/12)}		2.62

Working Notes:

1. Computation of theoretical ex-rights fair value per share = (fair value of all outstanding shares immediately prior to exercise of rights + Total value received from exercise of rights) / (number of shares outstanding prior to exercise + number of shares issued on the exercise)

   = (₹ 32 x 10,00,000 + ₹ 25 x 2,00,000) / (10,00,000 + 2,00,000)
   = ₹ 30.83

2. Computation of adjustment factor

   = Fair value per share prior to exercise of rights / Theoretical ex-right value per share

   = ₹ 32/₹ 30.83

   = 1.04 (approx.)

(b) In the case of a company, the following computations will be made:

2012-13

In this year, depreciation for both accounting and taxation purposes would be ₹ 25,000 (25 per cent of ₹ 1,00,000). Accordingly, no timing difference arises on this account.

2013-14

Depreciation for the year would be ₹ 18,750 (25 percent of ₹ 75,000) as per the books of account, while for tax purposes it would be ₹ 16,250 as sale proceeds of

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₹ 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 ₹ 16,250 and for accounting purposes ₹ 18,750 giving rise to a timing difference of ₹ 2,500.
- Profit on sale of fixed asset amounting to ₹ 7,188 (₹ 10,000 - ₹ 2,812 being the WDV of the asset as on 31st March, 2014) is recognized for accounting purposes. However, for tax purposes this income is not considered. This will result in a timing difference of ₹ 7,188.

The net timing difference would be ₹ 4,688 (₹ 7,188 – ₹ 2,500) by which the accounting income would exceed the taxable income, thus requiring creation of a deferred tax liability of ₹ 1,875 (4,688 X 0.4).

The difference of ₹ 4,688 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 higher carrying amount of fixed assets as compared to carrying amount of those assets for tax purposes.

(c) As per para 3 of AS 23 'Accounting for Investments in Associates in Consolidated Financial Statements', an associate is an enterprise in which the investor has significant influence and which is neither a subsidiary nor a joint venture of the investor.

Standard further explains in para 4 that as regards share ownership, if an investor holds, directly or indirectly through subsidiary (ies), 20% or more of the voting power of the investee, it is presumed that the investor has significant influence, unless it can be clearly demonstrated that this is not the case. Conversely, if the investor holds, directly or indirectly through subsidiary (ies), less than 20% of the voting power of the investee, it is presumed that the investor does not have significant influence, unless such influence can be clearly demonstrated.

Further as per an explanation to para 4 of the standard, for the purpose of classification of associate, the potential equity shares of the investee held by the investor will not be taken into account for determining the voting power of the investor. In other words the voting power should be determined on the basis of the current outstanding securities with voting rights.

As per the information given in the question, H Ltd. presently holds indirectly 22.7% shares (with and without voting rights) (Refer W.N.) in A Ltd. However, the current outstanding securities with voting rights in A Ltd. is only 15% and the remaining holding is on account of potential equity shares. Since potential equity shares do not have voting rights they will not be taken into consideration while determining the significant influence of H Ltd. on A Ltd. Hence, A Ltd. is not an associate of H Ltd.

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Working Note:

Calculation of percentage of holding of shares after conversion

	₹
Current holding is 15% i.e. 7,500 shares of ₹ 100 each	7,50,000
Potential equity shares i.e. 5,000 shares of ₹ 100 each	5,00,000
	12,50,000

Total share capital of A Ltd. after conversion of debentures into equity shares will be

= ₹ 50,00,000 + ₹ 5,00,000 = ₹ 55,00,000

Percentage of holding = ₹ (12,50,000/55,00,000) x 100 = 22.7% approx.

7. (a) As illustrated in AS 25, 'Interim Financial Reporting',

(i) Provisions in respect of gratuity and other defined benefit schemes for an interim period are calculated on a year-to-date basis 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.

(ii) A bonus is anticipated for interim reporting purposes if, and only if,

1. the bonus is a legal obligation or an obligation arising from past practice for which the enterprise has no realistic alternative but to make the payment, and
2. a reliable estimate of the obligation can be made.

(iii) The enterprise should apply the same criteria for recognizing and measuring a provision at interim date as it would apply at the end of its financial year or as per the preceding annual financial statements.

(iv) Foreign currency translation gains and losses are measured for interim financial reporting by the same principles as at financial year end in accordance with the principles as stated in AS 11 'The Effects of Changes in Foreign Exchange Rates'.

(b) As per para 78 of AS 26 'Intangibles Assets', the amortisation period and the amortisation method should be reviewed at least at each financial year end. If the expected useful life of the asset is significantly different from previous estimates, the amortisation period should be changed accordingly. If there has been a significant change in the expected pattern of economic benefits from the asset, the amortisation method should be changed to reflect the changed pattern.

Accordingly, Religare Ltd. amortized ₹ 5,00,000 per annum for the first year. The remaining carrying cost of ₹ 15,00,000 (₹ 20,00,000 – ₹ 5,00,000) will be amortized

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during next 5 years on the basis of net cash flows arising from the sale of the product. The amortization may be calculated as follows:

Year	*Net Cash flows (₹)*	*Amortization basis*	*Amortizarion Amount (₹)*
1	-	₹ 20,00,000/4 years	5,00,000
2	8,00,000	0.160	2,40,000
3	12,00,000	0.240	3,60,000
4	10,00,000	0.200	3,00,000
5	12,50,000	0.250	3,75,000
6	7,50,000	0.150	2,25,000
	50,00,000	1.000	20,00,000

8. (a) It is likely that the recoverable amount of an individual magazine title can be assessed. Even though the level of advertising income for a title is influenced, to a certain extent, by the other titles in the customer segment, cash inflows from direct sales and advertising are identifiable for each title. In addition, although titles are managed by customer segments, decisions to abandon titles are made on an individual title basis.

Therefore, it is likely that individual magazine titles generate cash inflows that are largely independent one from another and that each magazine title is a separate cash-generating unit.

(b) (i) Para 14 of AS 29 "Provisions, Contingent Liabilities and Contingent Assets" states that a provision should be recognised when (a) An enterprise has a present obligation as a result of a past event and (b) It is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and (c) A reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision should be recognised.

From the above, it is clear that in the contingencies considered by the company, neither a present obligation exists as a result of past event, nor a reliable estimate can be made of the amount of the obligation. Accordingly, a provision cannot be recognised for such contingencies under the facts and circumstances of the case.

(ii) "Provision" is the amount retained by the way of providing for any known liability. Since the contingencies stipulated by the company are not known at the balance sheet date, the provision in this regard cannot be created. Therefore, the provision so created by the company shall be treated as a 'Reserve'.

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9. Treatment with reference to Existing Indian Accounting Standards vis-a-vis IFRS

Topic	*Existing Indian Accounting Standards*	*IFRS*
Statement of Cash flows	Mandatory for listed companies and those companies which fall in the category of Level - I corporate entities.	Mandatory for all entities preparing their financial statements in accordance with IFRS as it is a component of a complete set of financial statements.
	AS 3 permits use of "Direct" or "Indirect" method. However, SEBI mandates listed companies to present cash flows from operating activities in a cash flow statement according to the "indirect method" only.	Cash flow from operating activities may be presented using either direct or indirect method. However, IAS 7 encourages entities to report cash flows from operating activities using direct method.
	There is no specific guidance on treatment of bank overdraft by AS 3. In general, bank overdrafts are treated as financing activities in cash flow statement. However, demand deposits with bank are treated as cash.	Bank borrowings are normally treated as part of financing activities. However, bank overdrafts that are repayable on demand and that form an integral part of an entity's cash management are treated as cash equivalents under IAS 7.
	As per AS 3, interest and dividend paid are treated as cash outflow under financing activities and interest and dividend received are treated as cash inflow from investing activities. AS 3 does not provide any option with regard to classification of interest paid or received.	Under IAS 7, interest and dividend, whether received or paid, may be classified as operating or financing activities dependent upon classification which reflects the economic nature of transactions and in a manner consistent from period to period.
	In AS 3, the cash flows associated with extraordinary items may be classified as arising from operating, investing or financing activities as appropriate and will be disclosed separately.	IFRS does not classify any item as extraordinary item. Hence, no provision related to cash flows from extra-ordinary item has been discussed in IAS 7.

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Accounting Policies, Changes in Accounting Estimates and Errors	AS 5 allows a change in an accounting policy in three instances i.e. (a) If the adoption of a different accounting policy is required by statute; or (b) For compliance with an accounting standard; or (c) If it is considered that the change would result in a more appropriate presentation of the financial statements of the enterprise. AS 5 allows change in an accounting policy in case the change is required by the Statute.	As per IAS 8, an entity can change its accounting policy in two instances i.e. if the change: (a) Is required by an IFRS; or (b) Results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows. IAS 8 does not permit an entity to change an accounting policy even if it is required by the statute.
	This standard is silent that whether a change in accounting policy to be accounted for either retrospectively or prospectively. Any change in an accounting policy, which has a material effect, should be disclosed. Where the effect of such change is not ascertainable wholly or in part, the fact should be indicated.	If an entity changes an accounting policy voluntarily, it needs to apply the change retrospectively. When a change in an accounting policy is applied retrospectively, an entity should adjust the opening balance of each affected component of equity for the earliest prior period presented and disclose the comparative amounts for each prior period presented.
	AS 5 deals with "Prior period items" which basically cover income and expenses only. AS 5 does not consider fraud as an error i.e. errors are unintentional mistakes which may arise due to several reasons.	IAS 8 uses the term "Prior period errors" which covers all items in the financial statements including assets and liabilities. As per IAS 8, errors also include fraud within its scope. Standard says errors may be intentional or unintentional.

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	Since AS 5 does not deal with intentional errors, no such disclosures are discussed in it.	IAS 8 requires disclosure if financial statements do not comply with IFRSs i.e. if they contain either material errors or immaterial errors made **intentionally** to achieve a particular presentation of an entity's financial position, financial performance or cash flows.
	Prior period items are included in the Statement of Profit or Loss of the current period i.e. the period in which the error is discovered. Such errors are separately disclosed in the statement of profit and loss in a manner that the impact on current profit or loss can be perceived. There is no requirement of restating the comparatives of the prior periods.	As per IAS 8, material prior period errors shall be corrected retrospectively in the first set of financial statements authorised for issue after their discovery by: (a) Restating the comparative amounts for the prior period(s) presented in which the error occurred; or (b) If the error occurred before the earliest prior period presented, restating the opening balances of assets, liabilities and equity for the earliest prior period presented.

10. (a) Balance Sheet of a Corporate Entity (An Extract) as on 31st March, 2014

Particulars	*Note No.*	*Amount*
Non-Current Liabilities		
Long term borrowings	1	13,15,280
Current liabilities		
Short term borrowing	2	1,24,190
Other current liabilities	3	1,95,940
		16,35,410

Notes to Accounts

1.	Long term Borrowing	₹
	Term loans – secured	
	- from bank	7,45,120
	- from other parties	7,66,100

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		15,11,220
	Less: Shown in current maturities of long-term loans	(1,95,940)
		13,15,280
2.	Short-term borrowings (Unsecured-payable on demand)	1,24,190
	- from bank	
3.	Other current liabilities	
	Current maturities of long-term loans	
	From bank	1,15,000
	From others	80,940
		1,95,940

(b) According to Schedule III to the Companies Act, 2013 "An operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents".

Accordingly, operating cycle of Vasudha Ltd. will be computed as:

Raw material stock holding period + Work-in-progress holding period + Finished goods holding period + Debtors collection period

= 3.5 months + 1 month + 4.5 months + 6 months = 15 months

Further, a liability shall be classified as current when it is expected to be settled in the Company's normal operating cycle.

Since the operating cycle of Vasudha Ltd. is 15 months, trade payables expected to be paid in 14 months should be treated as a current liability.

(c) Schedule III to the Companies Act, 2013 does not require work-in-progress to be disclosed in the Statement of Profit and Loss. Thus, amounts for which work-in-progress have been completed at the beginning and at the end of the accounting period may not be disclosed. Therefore, the non-disclosure in the financial statements by the company may not amount to violation of the Schedule III to the Companies Act, 2013 if the differences between opening and closing WIP are not material.

11. Projected Profit & Loss Account of AB Ltd. for the period ended 31st March, 2014

Particulars		₹	*Particulars*		₹
To	Working capital expenses	2,00,000	By	Profits from Futures Trading	84,00,000
To	Interest on TOD	31,250	By	Dividends received	1,74,000
To	Debenture interest	10,000			

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		₹		₹
To	Provision for tax @ 40% on pre-tax profit - ₹ 81,58,750	32,63,500		
To	Profit after tax	50,69,250		
		85,74,000		85,74,000
To	Dividends (Equity & Preference)	2,06,760	By Profit for the year after tax	50,69,250
To	Profit transferred to Balance Sheet	48,62,490		
		50,69,250		50,69,250

Projected Balance Sheet of AB Ltd. as at 31-3-2014

Liabilities	₹	*Assets*	₹
Authorised share capital		Investments in Subsidiaries	
2 crore Equity shares of ₹ 10 each	20,00,00,000	In Equity shares at cost	66,70,000
Issued, subscribed & paid up		In preference shares at cost	10,00,000
25,33,600 Shares of ₹ 10 each (of the above 5,33,600 shares issued for consideration other than cash)	2,53,36,000	5% Red. Deb 2019-20 of ₹ 10	8,00,000
Preference Shares		Current Assets, Loans	
1 lakh 8% Preference Shares ₹ 10 paid	10,00,000	& Advances	
Reserves & Surplus		Bank Balance	3,49,25,990
Securities Premium Account (93,34,000 – 12,00,000)	81,34,000		
Profit & Loss Account	48,62,490		
Secured loan			
5% Red. Debentures 2019-20 of ₹ 10 each	8,00,000		
Current Liabilities & Provisions			
Provision for taxation	32,63,500		
	4,33,95,990		4,33,95,990

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Note:

1. Dividend received is exempted income and is not subject to tax in the hands of recipient. It is assumed that rate of dividend given in the question is net of tax.
2. Dividend distributed by AB Ltd. is subject to dividend distribution tax, if not net of tax.
3. As per the Companies Act, 2013, the balance of securities premium account can be used for writing off the preliminary expenses. As the company is having sufficient balance in the securities premium account, the amount of preliminary expenses is adjusted from the balance of securities premium account. As per para 56 of AS 26, when an expenditure is incurred to provide future economic benefits to an enterprise, but no intangible asset or other asset is acquired or created that can be recognized, then such an expenditure is recognized as an expense when it is incurred. However, whenever there is conflict in the treatment of a particular item as per Law / Statue & Accounting Standards then the Law / Statue will prevail. Accordingly, the above question has been solved by setting off the preliminary expenses from Securities Premium A/c. In this case it will be treated as permanent difference. Hence no DTA/DTL will be created.

Working Notes:

1. Calculation of Rectified Profits

	A Ltd.(₹)	*B Ltd. (₹)*
Value of inventory as given	2,20,000 (Overstated)	5,00,000 (Actual)
Adjustment therein due to incorrect valuation will be reduced from profits	2,20,000 x 10/110 = 20,000	5,00,000 x 5/100 = 25,000

2. Computation of Shares to be issued as purchase consideration

	A Ltd. ₹	*B Ltd.* ₹
Profit before interest & tax	6,00,000	4,40,000
Less: Reduction in profit due to incorrect inventory valuation	(20,000)	(25,000)
Less: Debenture interest		(40,000)
Profit before tax	5,80,000	3,75,000
Less: Tax @ 40%	(2,32,000)	(1,50,000)
Profit after tax (PAT)	3,48,000	2,25,000
Less: Preference dividend	-	(80,000)

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Profit available to equity shareholders [A]	3,48,000	1,45,000
Price Earnings Multiple [B]	15	10
Total Purchase Consideration to be given (A x B)	52,20,000	14,50,000
Equity Share Capital (Purchase Consideration x 100/125)	41,76,000	11,60,000
Securities Premium (25% of the above)	10,44,000	2,90,000

3. **Bank Account**

Date	Particulars		₹	Date	Particulars	₹
1.1.2014	To Share Application Money (20,00,000 x ₹ 14)		2,80,00,000	1.1.2014	By Futures Trading A/c	2,80,00,000
1.2.2014	To 12.5% TOD		15,00,000	1.2.2014	By Preliminary Expenses	12,00,000
31.3.2014	To Future Trading A/c [(2,80,00,000 x (18/100) x (100/60) + 2,80,00,000}		3,64,00,000	31.3.2014	By Working Capital expenses	2,00,000
31.3.2014	To Dividend received			31.3.2014	By Dividends Paid [(41,76,000 + 11,60,000) x 3.5/100]	1,86,760
	A Ltd (3,00,000 x 10 x 5%)	1,50,000		31.3.2014	By TOD Interest (15,00,000 x 12.5/100 x 2/12)	31,250
	B Ltd. (1,20,000 x 10 x 2 %)	24,000	1,74,000	31.3.2014	By Debenture Interest (80,000 x ₹ 10 x 5/100 x 3/12)	10,000
				31.3.2014	By Preference Dividend (1,00,000 x ₹ 10 x 8/100 x 3/12)	20,000
				31.3.2014	By 12.5% TOD	15,00,000
				31.3.2014	By Balance c/d	3,49,25,990
			6,60,74,000			6,60,74,000

12. (a) **Consolidated Balance Sheet of A Ltd. and its subsidiaries B Ltd. and C Ltd. as at 31st March 2014**

Particulars	*Note No.*	₹
I. Equity and Liabilities		
Shareholder's funds		

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		Note	₹
a.	Share capital	1	5,00,000
b.	Reserves and surplus	2	2,53,103
Minority Interest (96,000+30,122)			1,26,122
Current liabilities			
(a)	Trade payables	3	1,08,000
(b)	Short term provision – Proposed Dividend		50,000
(c)	Other current liabilities	4	40,000
	Total		10,77,225
II.	**Assets**		
Non-current assets			
(a)	Fixed assets		
	Tangible assets	5	4,61,225
(b)	Non-current investment		-
Current Assets			
(a)	Inventories	6	2,18,000
(b)	Trade receivable	7	2,58,000
(c)	Cash and Cash equivalents	8	1,40,000
	Total		10,77,225

Notes to Financial Statements

S. No.	*Particulars*	*Amount (₹)*	*Amount (₹)*
1.	**Share capital**		
	Issued, subscribed and paid up 50,000 equity shares of ₹ 10 each fully paid up		5,00,000
2.	**Reserves and Surplus**		
	Capital reserves (W.N.3)	30,000	
	Other reserves (W.N.7)	1,31,300	
	Profit & Loss account (W.N.6)	91,803	2,53,103
3.	**Trade Payables**		
	Sundry Creditors of A Ltd.	70,000	
	B Ltd.	20,000	
	C Ltd.	30,000	
		1,20,000	
	Less: Mutual Owings	(12,000)	1,08,000

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4.	**Other Current liabilities**		
	Due to B Ltd. (40,000 – 30,000)	10,000	
	Due to C Ltd. (1,20,000 – 90,000)	30,000	40,000
5.	**Tangible assets**		
	A Ltd.	2,00,000	
	B Ltd.	1,50,000	
	C Ltd.	1,20,000	
		4,70,000	
	Less: Unrealised profit on equipment	(8,775)	4,61,225
6.	**Inventories**		
	A Ltd.	1,00,000	
	B Ltd.	60,000	
	C Ltd.	60,000	
		2,20,000	
	Less: Unrealised profit	(2,000)	2,18,000
7.	**Trade Receivable**		
	A Ltd.	1,50,000	
	B Ltd.	40,000	
	C Ltd.	80,000	
		2,70,000	
	Less: Mutual Owings	(12,000)	2,58,000
8.	**Cash and Cash Equivalents**		
	A Ltd.	90,000	
	B Ltd.	20,000	
	C Ltd.	30,000	1,40,000

Working Notes:

1. **Statement of analysis of profits of C Ltd.**

	Capital Profit	*Revenue reserve*	*Revenue profit*
	₹	₹	₹
General Reserve on 1.8.13	15,000		
Profit and loss A/c on 1.8.13	25,000		
Increase in reserve		35,000	

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Increase in profit	____	____	35,000
	40,000	35,000	35,000
Less: Minority Interest (10%)	(4,000)	(3,500)	(3,500)
	36,000	31,500	31,500
Share of A Ltd. (30%)	12,000	10,500	10,500
Share of B. Ltd. (60%)	24,000	21,000	21,000

2. Statement of analysis of profits of B Ltd.

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

3. Statement of cost of control

	₹	₹	₹
Investment in B Ltd.			2,50,000
Investment in C Ltd.		(80,000 + 1,60,000)	2,40,000
			4,90,000
Less: Paid up value of investments			
In B Ltd.	2,40,000		
In C Ltd.	1,80,000	4,20,000	
Capital Profit			
In B Ltd.	64,000		
In C Ltd. (12.000 + 24,000)	36,000	1,00,000	(5,20,000)
Capital reserve			30,000

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4. Statement of Minority Interest

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

5. Statement showing unrealised profit on equipment sale

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

6. Statement showing Consolidated Profit and Loss Account

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

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7. Statement showing consolidated reserves

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

(b) Consolidated Balance Sheet of M Ltd. and its subsidiary N Ltd. and Joint Venture C Ltd. as at 31st March, 2014

		Particular	Note No.	₹
I.	**EQUITY AND LIABILITIES**			
1	**Shareholders' funds**			
	a.	Share capital	1	6,00,000
	b.	Reserves and surplus	2	3,19,375
2.	**Non-current liabilities**			
		Long-term borrowings [6% Debentures]		1,12,500
3.	**Current Liabilities**			
		Trade payables (75,000 + 75% of 67,500)		1,25,625
		Total		**11,57,500**
II	**ASSETS**			
1.	**Non Current assets**			
	a.	Fixed assets		
		i. Tangible assets (4,50,000 +75% of 1,50,000)		5,62,500
		ii. Intangible assets [Goodwill] (W.N.2)		1,23,000
	b.	Non-current investments [6% debentures of C Ltd.]		90,000
2.	**Current assets**			
	a.	Inventories (W.N.3)		1,83,875
	b.	Trade receivables (80,000 +75% of 45,000)		1,13,750
	c.	Cash and cash equivalents [Balances with bank] (75,000 +75% of 12,500)		84,375
		Total		**11,57,500**

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Notes to the financial statements

(1) Share capital

Particulars	₹
Authorised	
Issued, subscribed and fully paid up 60,000 shares of ₹ 100 each	6,00,000

(2) Reserves and Surplus

Particulars	₹
General reserve (W.N.4)	2,00,000
Surplus (W.N.4)	1,19,375
	3,19,375

Note: "Fixed assets" given in the balance sheet question are assumed to be tangible assets.

Working Notes:

1. Statement of analysis of profits of C Ltd.

		Capital Profit ₹	*Revenue Profit* ₹
Profit and Loss A/c as on 1.4.2013		(2,25,000)	
Profit and Loss A/c during the year (2,25,000 – 1,50,000)	75,000		
Add: Abnormal loss (9,000 – 3,000)	6,000		
To be divided in the ratio of 4 months : 8 months	81,000	27,000	54,000
Abnormal loss		(6,000)	
		(2,04,000)	54,000
Share of M Ltd. (75%)		1,53,000	40,500

2. Statement showing Cost of control

Particulars		₹
Cost of Investment		1,20,000
Add: Share of loss in net assets		
i. Share capital (75%)	1,50,000	

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ii. Capital loss (Pre-acquisition)	(1,53,000)	3,000
Goodwill		1,23,000

3. Unrealised profit on stock

Particulars	₹
M Ltd. and its subsidiary	1,40,000
C Ltd. (75% of 60,000)	45,000
Less: Unrealised profit (3,000 x 50% x 75%)	(1,125)
Net balance for Consolidated Balance Sheet	1,83,875

4. Consolidated Reserves and Surplus

Particulars	*General Reserve* ₹	*Profit and Loss A/c* ₹
M Ltd. and its subsidiary	2,00,000	80,000
Proportionate share from Joint venture		40,500
Less: Unrealised profit	______	(1,125)
Net balance for Consolidated Balance Sheet	2,00,000	1,19,375

13. Calculation of initial recognition amount of loan to employees

	Cash Inflows				
Year	*Principal* ₹	*Interest @ 5%* ₹	*Total* ₹	*PV factor*	*Present Value* ₹
2013-14	3,00,000	90,000	3,90,000	0.9090	3,54,510
2014-15	3,00,000	75,000	3,75,000	0.8263	3,09,863
2015-16	3,00,000	60,000	3,60,000	0.7512	2,70,432
2016-17	3,00,000	45,000	3,45,000	0.6829	2,35,601
2017-18	3,00,000	30,000	3,30,000	0.6208	2,04,864
2018-19	3,00,000	15,000	3,15,000	0.5644	1,77,786
Present value of loan					15,53,056

Calculation of amortised cost of loan

Year	*Amortised cost (Opening balance)*	*Interest to be recognized @ 10%*	*Instalments (including interest)*	*Amortised Cost (Closing balance)*
	[1]	*[2]*	*[3]*	*[4]-[1]+[2]-[3]*
2013-14	15,53,056	1,55,306	3,90,000	13,18,362

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2014-15	13,18,362	1,31,836	3,75,000	10,75,198
2015-16	10,75,198	1,07,520	3,60,000	8,22,718
2016-17	8,22,718	82,272	3,45,000	5,59,990
2017-18	5,59,990	55,999	3,30,000	2,85,989
2018-19	2,85,989	29,011 (Bal. Fig)	3,15,000	Nil

14. The incremental value is ₹ 3 per stock option (₹ 8 – ₹ 5). This amount is recognised over the remaining two years of the vesting period, along with remuneration expense based on the original option value of ₹ 15.

The amount of expenses recognised towards employees services received in years 1- 3 are as follows:

Year	*Calculation*	*Compensation expense for period (₹)*	*Cumulative compensation expense (₹)*
1	(500 – 110) employees ×100 options × ₹ 15 × 1/3	1,95,000	1,95,000
2	(500 – 105) employees × 100 options × (₹ 15 × 2/3 + ₹ 3 × 1/2) – ₹ 1,95,000	2,59,250	4,54,250
3	(500 – 103) employees × 100 options × (₹ 15 + ₹ 3) – ₹ 4,54,250	2,60,350	7,14,600

15. (a) Calculation of NAV of a Mutual Fund Scheme

Units as at the end of the year		*Units in Crores*
Number of units at the beginning of the year		1.00
Add: Units issued during the year		0.20
Units as at end of the year		1.20
Net Asset Value of the scheme		*₹ in crores*
Market value of Investments	(50% of ₹ 10 crores) x 80%	4.00
	10% x ₹ 10 crores - (10% below cost)	0.90
	Balance Investment at Market Price	13.60

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Total Market Value		18.50
Less : Mutual fund scheme liabilities		(1.00)
Net asset value of the scheme		17.50
NAV per Unit= B/A=	₹ 17.50 crore/1.2 crore	₹ 14.58

(b) (i) Since, the hire-purchaser paid the first instalment due on 31.3.2013, the notional principal outstanding on 1-4-2013 was ₹ 50.25 lakhs (refer W.N.).

For the year ended 31.03.2014, the instalment due of ₹ 16 lakhs has not been received. However, it was due on 31.3.2014 i.e. on the balance sheet date, and therefore, it will be classified as standard asset. Rental Ltd. will recognise ₹ 5.24 lakhs as interest income included in that due instalment and it should be treated as finance charge.

(ii) The net book value of the assets as on 31.3.2014

	₹ in lakhs
Overdue instalment	16.00
Instalments not due (₹ 16 lakhs x 3)	48.00
	64.00
Less: Finance charge not matured and hence not credited to Profit and loss account (4.11 + 2.88 + 1.52) (W.N.)	(8.51)
	55.49
Less: Provision as per para 9(2)(i) of NBFC prudential norms (Refer point (iii))	(7.49)
Net book value of assets for Rental Ltd.	48.00

(iii) Amount of Provision

	₹ in lakhs
Overdue instalment	16.00
Instalments not due (₹ 16 lakhs x 3)	48.00
	64.00
Less: Finance charge not matured and hence not credited to Profit and loss account (4.11 + 2.88 + 1.52) (W.N.)	(8.51)
	55.49

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Less: Depreciated value (cash price less depreciation for two years on SLM @ 20%*)	(48.00)
Provision to be created as per para 9(2)(i) of NBFC prudential norms	7.49

Since, the instalment of ₹ 16 lakhs not paid, was due on 31.3.14 only, the asset is classified as standard asset. Therefore, no additional provision has been made for it.

Working Note:

It is necessary to segregate the instalments into principal outstanding and interest components by using I.R.R. @ 10.42%.

(₹ in lakhs)

Time	*Opening outstanding amount (a)*	*Cash flow (b)*	*Interest @ 10.42% (c) = (a x 10.42%)*	*Principal repayment (d) = (b – c)*	*Closing outstanding (e) = (a – d)*
31-3-2012		(60)	-----	---	60.00
31-3-2013	60.00	16	6.25	9.75	50.25
31-3-2014	50.25	16	5.24	10.76	39.49
31-3-2015	39.49	16	4.11	11.89	27.60
31-3-2016	27.60	16	2.88	13.12	14.48
31-3-2017	14.48	16	1.52	14.48	0.00

16. Past profits of Apex Ltd., showed an increasing trend except in the year 2013-14. But the effects of changes in accounting policies should be eliminated to ascertain the true nature of trend. Since the company has adopted LIFO method of stock valuation and W.D.V. method of depreciation, profits shall be recomputed applying these policies consistently in all the past years. Recomputation of profits following uniform accounting policies are shown below:

(₹ in '000s)

Year	*Book Profits*	*LIFO Effect of Valuation of Stock*	*Effect of W.D.V. Depreciation*	*Profits after elimination of the effect of changes in Accounting policy*
2009-10	21,70	(4,60)	(4,90)	12,20

* As per NBFC prudential norms laid down by the RBI.

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2010-11	22,50	3,50	(3,95)	22,05
2011-12	23,70	1,50	(4,25)	20,95
2012-13	24,50	(20)	(2,90)	21,40
2013-14	21,10	-	-	21,10

After elimination of the effects of changes in accounting policies, increasing trend disappeared. Rather profits were oscillating during the last four years except in the year 2009-10. So a simple average may be taken of the last 4 years profits to arrive at the future maintainable profits:

Future Maintainable Profit (₹ in '000s) $\frac{22{,}05+20{,}95+21{,}40+21{,}10}{4}=21{,}37.50$

Note: It is assumed that in case of change in the method of calculation of depreciation assets were purchased in 2009-10 only and the effects for the change in the method has been given retrospectively.

Working Note:

Effect of LIFO Valuation: *(₹ in '000s)*

2009-10	Increase in stock as per FIFO valuation	6,00
	Less: Increase in stock per LIFO valuation	(1,40)
	Reduction in profit	4,60
2010-11	Increase in stock as per FIFO valuation	3,20
	Less: Increase in stock as per LIFO valuation	(6,70)
	Increase in profit	3,50
2011-12	Decrease in stock as per FIFO valuation	10,30
	Less: Decrease in Stock as per LIFO valuation	(8,80)
	Increase in profit	1,50
2012-13	Opening stock as per FIFO valuation	38,90
	Less: Opening stock as per LIFO valuation	(39,10)
	Reduction in profit	20

17. Calculation of value per share on yield basis (Earnings Capitalisation Method)

Particulars	
Earnings available to equity shareholders (W.N.1)	₹ 1,01,040
Normal Rate of Return (W.N.3)	14.25%
Value of business	₹ 7,09,053

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Number of equity shares outstanding	50,000
Value per share	**14.18**

Working Notes:

1. Computation of FMP available for distribution

a. Weighted average profits

Year	*Profit before tax*	*Weight*	*Product*
2009-10	1,80,000	1	1,80,000
2010-11	2,50,000	2	5,00,000
2012-13	3,00,000	3	9,00,000
2013-14	3,50,000	4	14,00,000
		10	**29,80,000**

Note: Profit of the year 2011-12 has not been considered, because it is a year of strike (Abnormal operation).

	₹
Weighted average profit = $\frac{29,80,000}{10}$	2,98,000
Less: Increase in managerial remuneration	(25,000)
PBT	2,73,000
Tax @ 40%	(1,09,200)
PAT	1,63,800
Less: Provision for replacement of fixed assets (₹ 1,63,800 x 20%)	(32,760)
	1,31,040
Less: Dividend for preference shares (₹ 2,50,000 x 12%)	(30,000)
Earnings available for distribution	1,01,040

2. Ascertainment of NRR criteria as applicable to Survey Ltd.

(A) Asset backing:

Particulars		₹
Total assets as per balance sheet		14,20,000
Add: Increase in the value of building	1,50,000	
Increase in the value of plant & machinery	2,00,000	
		3,50,000
Total		17,70,000

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Less:Outside liabilities and preference share capital		
i. Sundry creditors	1,50,000	
ii. 15% debentures	1,20,000	
iii. 12% Preference share capital	2,50,000	(5,20,000)
Assets backing for equity share capital (a-b)		12,50,000
Equity share capital		5,00,000
Asset backing		2.5 times

(B) Dividend Rates:

Dividend rates have been fluctuating in the industry while Survey Ltd. has constant dividend rates.

3. Computation of adjusted Normal Rate of Return as applicable to Survey Ltd.

Particulars	*Asset backing*	*Dividend rates*
Industry standard	2 times	fluctuating
Survey Ltd.	2.5 times	constant
Degree of Variance from standard	+25%	N.A.
Impact on risk & consequent adjustment to NRR	↓	↓
Quantum of Adjustment to NRR (assuming 100% variance=1% change)	-0.25%	-0.50% (say)

Adjusted NRR = 15%-0.25%-0.50%=14.25%.

18. Calculation of Possible Value of Brand

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

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19. Gross Value Added Statement of Yash Ltd. for the year ended on 31st March, 2014

(₹ in '000)

VALUE ADDED	*Amount*	*Amount*
Sales less return		21,350
Less: Cost of bought out materials and services (W.N.)		(15,385)
Value added from manufacturing and trading activities		5,965
Add:		
a. Interest received	20	
b. Other income	80	100
Less: Extraordinary items		
a. Surplus on sale transactions	20	
b. Loss of goods by fire	(35)	(15)
Gross value added		**6,050**
VALUE APPLIED		
Towards employees		
a. Salaries, wages and other benefits	3,685	
b. Director's remuneration	360	4,045
Towards Government		688
a. Provision for tax (including charge for Deferred tax)		
Towards providers of finance		
a. Interest on loans and overdraft	160	
b. Proposed Dividend	340	500
Towards Replacement and Expansion		
a. Depreciation	302	
b. Retained profit	515	817
Gross value applied		**6,050**

Reconciliation between gross value added and profit before tax (₹ in '000s)

Particulars		*Amount*
Profit before tax		1,558
Add: :i. Salaries, wages to employees	3,685	
ii. Remuneration to Director	360	
iii. Interest on loans and overdraft	160	
iv. Depreciation	302	

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v. Extraordinary item	(15)	4,492
Gross Value added		6,050

Working Note:

Calculation of Cost bought out materials and services

Particulars	*(₹ in '000s)*
Sales	21,350
Less: Trading Profit	(1,920)
Total Cost	19,430
Less: i. Salaries and wages	(3,685)
ii. Director's remuneration	(360)
Cost of bought out materials and services	15,385

20. (a) Net Operating Profit After Tax (NOPAT) = Profit After Tax (PAT) + Interest (net of tax)

= 205.90 + 4.85 x (1-0.25) = ₹ 209.54 crores

Debt Capital		₹ 37 crores
Equity capital (40 + 700)	=	₹ 740 crores
Capital employed	=	₹ 37 +₹ 740 = ₹ 777 crores
Debt to capital employed	=	₹ 37 crores/₹ 777 crores = 0.0476
Equity to capital employed	=	₹ 740 crores /₹ 777 crores =0.952
Interest cost before Tax		₹ 4.85 crores
Less: Tax (25% of ₹ 4.85 crores)		(₹ 1.21 crores)
Interest cost after tax		₹ 3.64 crores
Cost of debt	=	(₹ 3.64 crores/ ₹ 37 crores) x 100
	=	9.83%

According to Capital Asset Pricing Model (CAPM)

Beta for calculation of EVA should be the highest of the given beta for the last few years.

Accordingly,

Cost of Equity Capital = Risk Free Rate + Beta (Market Rate – Risk Free Rate)

= 12% + 1.10 × (15.50% - 12%)

= 12% + 1.10 × 3.5% = 15.85%

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Weighted Average Cost of Capital (WACC) = Equity to Capital Employed (CE) x Cost of Equity Capital + Debt to CE x Cost of Debt

= $0.952 \times 15.85 + 0.0476 \times 9.83$

= 15.09 + 0.47 = 15.56%

Cost of Capital Employed (COCE) = WACC × Capital Employed

= 15.56% × ₹ 777 crores = ₹ 120.90 crores

Economic Value Added (E.V.A.) = NOPAT – COCE

= ₹ 209.54 crores – ₹ 120.90 crores = ₹ 88.64 crores

(b) Value of skilled employees:

$$= \frac{1,00,000}{(1+0.15)^{(65-62)}} + \frac{1,00,000}{(1+0.15)^{(65-63)}} + \frac{1,00,000}{(1+0.15)^{(65-64)}}$$

₹ 65,751.62 + ₹ 75,614.37 + ₹ 86,956.52 = ₹ 2,28,322.51

Total value of skilled employees is ₹ 2,28,322.51 × 20 = ₹ 45,66,450.20

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Applicability of Pronouncements/Legislative Amendments/Circulars etc. for November, 2014 – Final Examination

Paper 1: Financial Reporting

I. Statements and Standards

1. Framework for the Preparation and Presentation of Financial Statements.
2. Accounting Standards

AS No.	*AS Title*
1	Disclosure of Accounting Policies
2	Valuation of Inventories
3	Cash Flow Statements
4	Contingencies and Events Occurring after the Balance Sheet Date
5	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
6	Depreciation Accounting
7	Construction Contracts (Revised 2002)
9	Revenue Recognition
10	Accounting for Fixed Assets
11	The Effects of Changes in Foreign Exchange Rates (Revised 2003)
12	Accounting for Government Grants
13	Accounting for Investments
14	Accounting for Amalgamations
15	Employee Benefits
16	Borrowing Costs
17	Segment Reporting
18	Related Party Disclosures
19	Leases
20	Earnings Per Share
21	Consolidated Financial Statements
22	Accounting for Taxes on Income
23	Accounting for Investment in Associates in Consolidated Financial Statements
24	Discontinuing Operations
25	Interim Financial Reporting

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26	Intangible Assets
27	Financial Reporting of Interests in Joint Ventures
28	Impairment of Assets
29	Provisions, Contingent Liabilities and Contingent Assets
30	Financial Instruments: Recognition and Measurement
31	Financial Instruments: Presentation
32	Financial Instruments: Disclosure

Note: Non-Applicability of Ind ASs for Nov. 2014 Examination

The MCA has hosted on its website 35 Indian Accounting Standards (Ind AS) without announcing their applicability date. Students may note that Ind ASs are not applicable for November, 2014 Examination.

II. Guidance Notes on Accounting Aspects

1. Guidance Note on Treatment of Reserves created on Revaluation of Fixed Assets.
2. Guidance Note on Accrual Basis of Accounting.
3. Guidance Note on Accounting Treatment for Excise Duty.
4. Guidance Note on Terms Used in Financial Statements.
5. Guidance Note on Accounting for Depreciation in Companies.
6. Guidance Note on Availability of Revaluation Reserve for Issue of Bonus Shares.
7. Guidance Note on Accounting Treatment for MODVAT/CENVAT.
8. Guidance Note on Accounting for Corporate Dividend Tax.
9. Guidance Note on Accounting for Employee Share-based Payments.
10. Guidance Note on Accounting for Credit Available in respect of Minimum Alternate Tax under the Income Tax Act, 1961.
11. Guidance Note on Measurement of Income Tax for Interim Financial Reporting in the context of AS 25.
12. Guidance Note on Applicability of Accounting Standard (AS) 20, Earnings per Share.
13. Guidance Note on Remuneration paid to key management personnel – whether a related party transaction.
14. Guidance Note on Applicability of AS 25 to Interim Financial Results.
15. Guidance Note on Turnover in case of Contractors.
16. Guidance Note on the Revised Schedule VI to the Companies Act, 1956 (Schedule III to the Companies Act, 2013).

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PAPER – 2: STRATEGIC FINANCIAL MANAGEMENT

QUESTIONS

Interest Rate Guarantee

1. Two companies ABC Ltd. and XYZ Ltd. approach the DEF Bank for FRA (Forward Rate Agreement). They want to borrow a sum of ₹ 100 crores after 2 years for a period of 1 year. Bank has calculated Yield Curve of both companies as follows:

Year	XYZ Ltd.	ABC Ltd.*
1	3.86	4.12
2	4.20	5.48
3	4.48	5.78

*The difference in yield curve is due to the lower credit rating of ABC Ltd. compared to XYZ Ltd.

(i) You are required to calculate the rate of interest DEF Bank would quote under 2V3 FRA, using the company's yield information as quoted above.

(ii) Suppose bank offers Interest Rate Guarantee for a premium of 0.1% of the amount of loan, you are required to calculate the interest payable by XYZ Ltd. if interest in 2 years turns out to be

(a) 4.50%

(b) 5.50%

Portfolio Management

2. Mr. A has a portfolio of ₹ 5 crore consisting of equity shares of X Ltd. and Y Ltd. with beta of 1.15. Other information is as follows:

Spot Value of Index Future = 21000

Multiplier = 150

You are requested to reduce beta of portfolio to 0.85 and increase beta to 1.45 by using:

(a) Change in composition through Risk Free securities

(b) Index futures

Leasing

3. AGD Co is a profitable company which is considering the purchase of a machine costing ₹ 32,00,000. If purchased, AGD Co would incur annual maintenance costs of ₹ 2,50,000. The machine would be used for three years and at the end of this period would be sold for ₹ 5,00,000. Alternatively, the machine could be obtained under an operating lease for an annual lease rental of ₹ 12,00,000 per year, payable in advance. AGD Co can claim depreciation @ 25% on WDV basis. Annual lease rental will be paid in the beginning of each year.

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The company pays tax on profits at an annual rate of 30% and all tax liabilities are paid one year in arrears.

Required:

(1) Using an after-tax borrowing rate of 7%, evaluate whether AGD Co should purchase or lease the new machine.

(2) Suppose a bank had offered to lend AGD Co ₹ 32,00,000 for a period of five years interest payable every six months, then you are required to:

(i) Calculate the Annual Percentage Rate (APR) implied by the bank's offer with interest payable every six months.

(ii) Calculate the amount of installment payable at the end of each six-month period if the offered loan is to be repaid in equal installments.

Bond Refunding

4. M/s Transindia Ltd. is contemplating calling ₹ 3 crores of 10 years, ₹ 1,000 bond issued 5 years ago with a coupon interest rate of 14 per cent. The bonds have a call price of ₹ 1,015 and had initially collected proceeds of ₹ 2.91 crores due to a discount of ₹ 30 per bond. The initial floating cost was ₹ 3,60,000. The Company intends to sell ₹ 3 crores of 12 per cent coupon rate, 5 years bonds to raise funds for retiring the old bonds. It proposes to sell the new bonds at their par value of ₹ 1,000. The estimated floatation cost is ₹ 2,00,000. The company is paying 40% tax. The new bonds shall be issued 2 months before retiring old bonds to avoid any market risk and using the proceeds from new issue to retire the old bonds. What is the feasibility of refunding bonds?

Capital Budgeting

5. XYZ Food Pvt. Ltd., a franchisee of Domino's (World famous food chain for delivering pizza at home) is considering a proposal of acquiring a fleet of motorbikes for delivery of pizzas at home of customers. Since pizzas are also delivered in late night and bikes are handled by different delivery boys (due shift working) the use of fleet will be very heavy. Hence it is expected that the motorbike shall be virtually worthless and scrapped after a period of 3 years. However they are taken out of services before 3 years there will be a positive 'abandonment' cash flow.

The initial cost of the bike will be ₹1,00,000. The expected post tax benefit (cash inflows) from the use of bike and abandonment cash inflows are as follows:

Year	Operating Cash Flows (₹)	Abandonment Cash Flows at end of year (₹)
1	42,000	62,000
2	40,000	40,000
3	35,000	0

The cost of capital of XYZ Pvt. Ltd. is 10%. You are required to evaluate the proposal of acquisition of bikes and recommend preferable life of the same.

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Security Valuation

6. Calculate the value of share from the following information:

Profit of the company	₹ 290 crores
Equity capital of company	₹ 1,300 crores
Par value of share	₹ 40 each
Debt ratio of company	27
Growth rate of the company for first 5 years	8%
Growth rate of the company for the 6 year and onward	5%
Beta 0.1; risk free interest rate	8.7%
Market returns	10.3%
Capital expenditure per share	₹ 47
Depreciation per share	₹ 39
Change in Working capital	₹ 3.45 per share

Right Issue

7. Pragya Limited has issued 75,000 equity shares of ₹ 10 each. The current market price per share is ₹ 24. The company has a plan to make a rights issue of one new equity share at a price of ₹ 16 for every four share held.

   You are required to:

   (i) Calculate the theoretical post-rights price per share;

   (ii) Calculate the theoretical value of the right alone;

   (iii) Show the effect of the rights issue on the wealth of a shareholder, who has 1,000 shares assuming he sells half of his rights; and exercise the remaining 50%.

   (iv) Show the effect, if the same shareholder does not take any action and ignores the issue.

Business Valuation

8. A valuation done of an established company by a well-known analyst has estimated a value of ₹ 525 lakhs, based on the current year's free cash flow of ₹ 20 lakhs and an expected growth rate of 5%.

   While going through the valuation procedure, you found that the analyst has made the mistake of using the book values of debt and equity in his calculation. While you do not know the book value weights he used, you have been provided with the following information:

   (i) Company has a cost of equity of 12%,

   (ii) After tax cost of debt is 6%,

(iii) The market value of equity is three times the book value of equity, while the market value of debt is equal to the book value of debt.

You are required to estimate the correct value of the company.

Foreign Exchange Risk Management

9. Your forex dealer had entered into a cross currency deal and had sold US $ 10,00,000 against EURO at US $ 1 = EURO 1.4400 for spot delivery.

   However, later during the day, the market became volatile and the dealer in compliance with his management's guidelines had to square – up the position when the quotations were:

Spot US $ 1	INR 61.4300/4500
Spot US $ 1	EURO 1.4250/4350

   What will be the gain or loss in the transaction?

10. Followings are the spot exchange rates quoted at three different forex markets:

USD/INR	59.25/ 59.35 in Mumbai
GBP/INR	102.50/ 103.00 in London
GBP/USD	1.70/ 1.72 in New York

   The arbitrageur has USD1,00,00,000. Assuming that bank wishes to retain an exchange margin of 0.125%, explain whether there is any arbitrage gain possible from the quoted spot exchange rates.

Indian Capital Market

11. A Mutual Fund is holding the following assets in ₹ Crores :

Investments in diversified equity shares	90.00
Cash and Bank Balances	10.00
	100.00

   The Beta of the portfolio is 1.1. The index future is selling at 4300 level. The Fund Manager apprehends that the index will fall at the most by 10%. How many index futures he should short for perfect hedging? One index future consists of 50 units.

   Substantiate your answer assuming the Fund Manager's apprehension will materialize. Portfolio Theory

12. A company is long on 10 MT of copper @ ₹ 474 per kg (spot) and intends to remain so for the ensuing quarter. The standard deviation of changes of its spot and future prices are 4% and 6% respectively, having correlation coefficient of 0.75.

   What is its hedge ratio? What is the amount of the copper future it should short to achieve a perfect hedge?

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13. On 31-8-2011, the value of stock index was ₹ 2,200. The risk free rate of return has been 8% per annum. The dividend yield on this Stock Index is as under:

Month	Dividend Paid (p.a.)
January	3%
February	4%
March	3%
April	3%
May	4%
June	3%
July	3%
August	4%
September	3%
October	3%
November	4%
December	3%

Assuming that interest is continuously compounded daily, find out the future price of contract deliverable on 31-12-2011. Given: $e^{0.01583} = 1.01593$

Dividend Decision

14. The following information relates to Maya Ltd:

Earnings of the company	₹ 10,00,000
Dividend payout ratio	60%
No. of Shares outstanding	2,00,000
Rate of return on investment	15%
Equity capitalization rate	12%

(i) What would be the market value per share as per Walter's model?

(ii) What is the optimum dividend payout ratio according to Walter's model and the market value of company's share at that payout ratio?

Financial Services

15. M/s Atlantic Company Limited with a turnover of ₹ 4.80 crores is expecting growth of 25% for forthcoming year. Average credit period is 90 days. The past experience shows that bad debt losses are 1.75% on sales. The Company's administering cost for collecting receivable is ₹ 6,00,000/-.

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It has decided to take factoring services of Pacific Factors on terms that factor will by receivable by charging 2% commission and 20% risk with recourse. The Factor will pay advance on receivables to the firm at 16% interest rate per annum after withholding 10% as reserve.

Calculate the effective cost of factoring to the firm. (Assume 360 days in a year).Dividend Decision

Mutual Fund

16. On 1-4-2012 ABC Mutual Fund issued 20 lakh units at ₹ 10 per unit. Relevant initial expenses involved were ₹ 12 lakhs. It invested the fund so raised in capital market instruments to build a portfolio of ₹ 185 lakhs. During the month of April, 2012 it disposed off some of the instruments costing ₹ 60 lakhs for ₹ 63 lakhs and used the proceeds in purchasing securities for ₹ 56 lakhs. Fund management expenses for the month of April, 2012 was ₹ 8 lakhs of which 10% was in arrears. In April, 2012 the fund earned dividends amounting to ₹ 2 lakhs and it distributed 80% of the realized earnings. On 30-4-2012 the market value of the portfolio was ₹ 198 lakhs.

    Mr. Akash, an investor, subscribed to 100 units on 1-4-2012 and disposed off the same at closing NAV on 30-4-2012. What was his annual rate of earning?

Money Market Instruments

17. M Ltd. has to make a payment on 30th January, 2010 of ₹ 80 lakhs. It has surplus cash today, i.e. 31st October, 2009; and has decided to invest sufficient cash in a bank's Certificate of Deposit scheme offering an yield of 8% p.a. on simple interest basis. What is the amount to be invested now?

Mergers and Acquisitions

18. Yes Ltd. wants to acquire No Ltd. and the cash flows of Yes Ltd. and the merged entity are given below:

					(₹ In lakhs)
Year	1	2	3	4	5
Yes Ltd.	175	200	320	340	350
Merged Entity	400	450	525	590	620

    Earnings would have witnessed 5% constant growth rate without merger and 6% with merger on account of economies of operations after 5 years in each case. The cost of capital is 15%.

    The number of shares outstanding in both the companies before the merger is the same and the companies agree to an exchange ratio of 0.5 shares of Yes Ltd. for each share of No Ltd.

    PV factor at 15% for years 1-5 are 0.870, 0.756; 0.658, 0.572, 0.497 respectively.

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You are required to:

(i) Compute the Value of Yes Ltd. before and after merger.

(ii) Value of Acquisition and

(iii) Gain to shareholders of Yes Ltd.

19. The following is the Balance-sheet of Grape Fruit Company Ltd as at March 31st, 2011.

Liabilities	(₹ in lakhs)	Assets	(₹ in lakhs)
Equity shares of ₹ 100 each	600	Land and Building	200
14% preference shares of ₹ 100/- each	200	Plant and Machinery Furniture and Fixtures	300 50
13% Debentures	200	Inventory	150
Debenture interest accrued and payable	26	Sundry debtors Cash at bank	70 130
Loan from bank	74	Preliminary expenses	10
Trade creditors	340	Cost of issue of debentures	5
		Profit and Loss account	525
	1440		1440

The Company did not perform well and has suffered sizable losses during the last few years. However, it is felt that the company could be nursed back to health by proper financial restructuring. Consequently the following scheme of reconstruction has been drawn up:

(i) Equity shares are to be reduced to ₹ 25/- per share, fully paid up;

(ii) Preference shares are to be reduced (with coupon rate of 10%) to equal number of shares of ₹ 50 each, fully paid up.

(iii) Debenture holders have agreed to forgo the accrued interest due to them. In the future, the rate of interest on debentures is to be reduced to 9 percent.

(iv) Trade creditors will forego 25 percent of the amount due to them.

(v) The company issues 6 lakh of equity shares at ₹ 25 each and the entire sum was to be paid on application. The entire amount was fully subscribed by promoters.

(vi) Land and Building was to be revalued at ₹ 450 lakhs, Plant and Machinery was to be written down by ₹ 120 lakhs and a provision of ₹15 lakhs had to be made for bad and doubtful debts.

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Required:

(i) Show the impact of financial restructuring on the company's activities.

(ii) Prepare the fresh balance sheet after the reconstructions is completed on the basis of the above proposals.

20. Write a short note on

(a) Impact of GDRs on Indian Capital Market

(b) Types of risks foreign exchange dealings are exposed to

(c) Constraints on paying Dividend

(d) Types/ Forms of Factoring

(e) Treasury bills

SUGGESTED ANSWERS/HINTS

1. (i) DEF Bank will fix interest rate for 2V3 FRA after 2 years as follows:

XYZ Ltd.

$(1+r)\,(1+0.0420)^2 = (1+0.0448)^3$

$(1+r)\,(1.0420)^2 = (1.0448)^3$

$r = 5.04\%$

Bank will quote 5.04% for a 2V3 FRA.

ABC Ltd.

$(1+r)\,(1+0.0548)^2 = (1+0.0578)^3$

$(1+r)\,(1.0548)^2 = (1.0578)^3$

$r = 6.38\%$

Bank will quote 6.38% for a 2V3 FRA.

(ii)

		4.50%- Allow to Lapse	5.50%- Exercise
Interest	₹ 100 crores X 4.50%	₹ 4.50 crores	-
	₹ 100 crores X 5.04%	-	₹ 5.04 crores
Premium (Cost of Option)	₹ 100 crores X 0.1%	₹ 0.10 crores	₹ 0.10 crores
		4.60 crores	5.14 crores

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2. **(i)** Reduction of beta to 0.85

(a) Reduction in beta through change in composition of securities whose beta is zero (β0)

βd = W1 x βe + W2 x β0

0.85 = W1 x 1.15 + (1 - W1) x 0

W1 = 0.85/1.15 = 0.739

So, W2 = 1 – 0.739 = 0.261

Thus, ₹ 3.695 crores (₹ 5 crores x 0.739) shall remain invested in portfolio and remaining ₹ 1.305 crores shall be invested in risk free securities (say Treasury bills)

(b) By using Index Futures

No. of Stock Index Futures to be short

$$= \text{Existing Beta } (\beta) \times \frac{\text{Value of Spot Position to be hedged}}{\text{Value of one Future Contract}}$$

$$= \quad 1.15 \times \frac{₹\,1.305 \text{ crore}}{21000 \times 150} = 1.15 \times 4.14$$

= 4.76 or say 5 contracts

Thus, instead of swapping ₹ 1.305 crore to risk free securities, the portfolio manager Mr. A can also reduce beta to 0.85 by selling 4.76 or 5 stock index futures.

(ii) Increasing beta to 1.45

(a) β shall be increased by investing additional amount in equity shares.

βd = W1 x βe + W2 x β2

1.45 = W1 x β1 + W2 x β2

1.45 = W1 x 1.15 + (1 - W1) x 0

W1 = 1.45/1.15 = 1.26

This can be achieved by:

(i) Holding on ₹5 crore worth of shares

(ii) Selling short Risk Free Securities of ₹1.30 crores (0.26 X ₹5 crores) i.e. borrowing ₹1.30 crores and using proceeds to buy ₹1.30 crores of additional shares.

(b) Increasing beta by using Index Futures i.e. buying Index futures of ₹1.495 crores (1.15 x ₹1.30 crores).

The number of contracts to be bought

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$= \frac{1.495 \text{ crores}}{21000 \times 150} = 4.746$ or say 5 contracts

3. (1) Workings-

Tax benefits on Depreciation

Year	Opening Value	Depreciation/ STCL	Closing Value	Tax Benefit	Taken in year
1	32,00,000	8,00,000	24,00,000	2,40,000	2
2	24,00,000	6,00,000	18,00,000	1,80,000	3
3	18,00,000	13,00,000		3,90,000	4

Borrowing to buy evaluation

	Year 0	Year 1	Year 2	Year 3	Year 4
Acquisition/ Disposal	(32,00,000)			5,00,000	
Tax Benefit on Depreciation			2,40,000	1,80,000	3,90,000
Maintenance Cost		(2,50,000)	(2,50,000)	(2,50,000)	
Tax benefit of Maintenance Cost			75,000	75,000	75,000
Cash Flow	(32,00,000)	(2,50,000)	65,000	5,05,000	4,65,000
PVF@7%	1.00	0.935	0.873	0.816	0.763
PV	(32,00,000)	(2,33,750)	56,745	4,12,080	3,54,795

PV of Borrowing to Buy = ₹ 26,10,130

Lease evaluation

	Year 0	Year 1	Year 2	Year 3	Year 4
Lease Rental	(12,00,000)	(12,00,000)	(12,00,000)		
Tax Benefit on Lease Rental			3,60,000	3,60,000	3,60,000
Cash Flow	(12,00,000)	(12,00,000)	(8,40,000)	3,60,000	3,60,000
PVF@7%	1.00	0.935	0.873	0.816	0.763
PV	(12,00,000)	(11,22,000)	(7,33,320)	2,93,760	2,74,680

PV of leasing Option = ₹ 24,86,880

Since outflow is less in case of leasing option the company should opt for the same.

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(2) (i) Interest payable every six months means that the bank will require 5% every six months accordingly equivalent annual percentage rate shall be calculated as follows:

$[(1{\cdot}05)^2 - 1] \times 100 = 10{\cdot}25\%$

(ii) Amount of installment shall be calculated by using annuity tables as follows:

A = ₹ 32,00,000/7·722 = ₹ 4,14,400

4. NPV for bond refunding

	₹
PV of annual cash flow savings (W.N. 2)	
(3,25,600 × PVIFA 7.20*%,5) i.e. 4.0783	13,27,894
Less: Initial investment (W.N. 1)	6,38,000
NPV	6,89,894

* 12.00(1 - 0.40)

Recommendation: Refunding of bonds is recommended as NPV is positive.

Working Notes:

(1) Initial investment:

(a) Call premium

Before tax (1,015 – 1,000) × 30,000	4,50,000	
Less: tax @ 40%	1,80,000	
After tax cost of call prem.		2,70,000

(b) Floatation cost 2,00,000

(c) Overlapping interest

Before tax (0.14 × 2/12 × 3 crores)	7,00,000	
Less: tax @ 40%	2,80,000	
After tax cost of Overlapping interest		4,20,000

(d) Tax saving on unamortised discount on old bond 5/10 × 9,00,000 × 0.4 (1,80,000)

(e) Tax savings from unamortised floatation Cost of old bond 5/10 × 3,60,000 × 0.4 (72,000)

6,38,000

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(2) Annual cash flow savings:

(a) Old bond

(i)	Interest cost (0.14 × 3 crores)	42,00,000	
	Less tax @ 40%	16,80,000	25,20,000
(ii)	Tax savings from amortisation of discount 9,00,000/10 × 0.4		(36,000)
(iii)	Tax savings from amortisation of floatation cost 3,60,000/10 × 0.4		(14,400)
	Annual after tax payment under old bond (A)		24,69,600

(b) New bond

(i)	Interest cost before tax (0.12 × 3 crores)	36,00,000	
	Less tax @ 40%	14,40,000	21,60,000
(ii)	Tax savings from amortisation of floatation cost (0.4 × 2,00,000/5)		(16,000)
	Annual after tax payment under new bond (B)		21,44,000
	Annual cash flow savings [(A) – (B)]		3,25,600

5. Statement showing NPV of the motor bike if operated 3 years

Particulars	Year	Cash Flows (₹)	PVF @ 10%	PV of Cash Flows (₹)
Initial Investment	0	(1,00,000)	1.00	(1,00,000)
Cash Flows	1	42,000	0.909	38,178
	2	40,000	0.826	33,040
	3	35,000	0.751	26,285
NPV				(2,497)

Statement showing NPV of the motor bike if operated 2 years

Particulars	Year	Cash Flows (₹)	PVF @ 10%	PV of Cash Flows (₹)
Initial Investment	0	(1,00,000)	1.00	(1,00,000)
Cash Flows	1	42,000	0.909	38,178
	2	80,000	0.826	66,080
NPV				4,258

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Statement showing NPV of the motor bike if operated 1 year

Particulars	Year	Cash Flows (₹)	PVF @ 10%	PV of Cash Flows (₹)
Initial Investment	0	(1,00,000)	1.00	(1,00,000)
Cash Flows	1	1,04,000	0.909	94,536
NPV				(5,464)

Recommendation: Thus, from above it is clear that the preferable life of bike is 2 years.

6. No. of Shares = $\frac{₹\ 1,300 \text{ crores}}{₹\ 40 \text{ crores}}$ = 32.5 Crores

$$\text{EPS} = \frac{\text{PAT}}{\text{No.of shares}}$$

$$\text{EPS} = \frac{₹\ 290 \text{ crores}}{32.5 \text{ crores}} = ₹\ 8.923$$

FCFE = Net income – [(1-b) (capex – dep) + (1-b) (ΔWC)]

FCFE = 8.923 – [(1-0.27) (47-39) + (1-0.27) (3.45)]

= 8.923 – [5.84 + 2.5185] = 0.5645

Cost of Equity = $R_f + ß (R_m – R_f)$

= 8.7 + 0.1 (10.3 – 8.7) = 8.86%

PV of FCFE for 5 years

Year	FCFE (₹)	PVF@8.86%	PV (₹)
1	0.6096	0.9186	0.5600
2	0.6584	0.8438	0.5556
3	0.7111	0.7752	0.5512
4	0.7680	0.7121	0.5469
5	0.8294	0.6541	0.5425
			2.7562

$$P_5 = \frac{FCFE(1+g)}{K_e - g} = \frac{0.8294(1.05)}{0.0886 - 0.05} = \frac{0.8709}{0.0386} = ₹\ 22.56$$

$$\text{PV of } P_5 = \frac{22.56}{(1.0886)^5} = ₹22.56 \text{ crore} \times 0.6541 = ₹14.76$$

$\therefore$ Value of Share = ₹ 2.7562 + ₹14.76 = ₹17.52

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7. **(i)** Calculation of theoretical Post-rights (ex-right) price per share:

Ex-right value = $\left[\frac{MN + SR}{N + R}\right]$

Where,

M = Market price,

N = Number of old shares for a right share

S = Subscription price

R = Right share offer

$= \left[\frac{(₹\ 24 \times 4) + (₹\ 16 \times 1)}{4 + 1}\right]$ = ₹ 22.40

(ii) Calculation of theoretical value of the rights alone:

= Ex-right price – Cost of rights share

= ₹ 22.40 – ₹ 16 = ₹ 6.40

(iii) Calculation of effect of the rights issue on the wealth of a shareholder who has 1,000 shares assuming he sells half of his rights & exercises remaining 50%:

		₹
(a)	Value of shares before right issue (1,000 shares × ₹ 24)	24,000
(b)	Value of shares after right issue (1,125 shares × ₹ 22.40)	25,200
	Add: Sale proceeds of rights renunciation (125 shares × ₹ 6.40)	800
	Less: Additional Investment (125 shares × ₹ 16)	(2,000)
		24,000

There will be no impact on the wealth of the shareholder.

(iv) Calculation of effect if the shareholder does not take any action and ignores the issue:

	₹
Value of shares before right issue (1,000 shares × ₹ 24)	24,000
Less: Value of shares after right issue (1,000 shares × ₹ 22.40)	22,400
Loss of wealth to shareholders, if rights ignored	1,600

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8. Cost of capital by applying Free Cash Flow to Firm (FCFF) Model is as follows:-

Value of Firm = V_0 = $\frac{FCFF_1}{K_c - g_n}$

Where –

FCFF1 = Expected FCFF in the year 1

Kc = Cost of capital

gn = Growth rate forever

Thus, ₹ 525 lakhs = ₹ 20 lakhs(1+0.05) /(Kc-g)

Since g = 5%, then Kc = 9%

Now, let X be the weight of debt and given cost of equity = 12% and cost of debt = 6%, then 12% (1 – X) + 6% X = 9%

Hence, X = 0.50, so book value weight for debt was 50%

∴ Correct weight should be 75% of equity and 25% of debt.

∴ Cost of capital = Kc = 12% (0.75) + 6% (0.25) = 10.50%

and correct firm's value = ₹ 21 lakhs/(0.105 – 0.05) = ₹ 381.82 lakhs.

9. The amount of EURO bought by selling US$

US$ 10,00,000 * EURO 1.4400	=	EURO	14,40,000
The amount of EURO sold for			
buying USD 10,00,000 * 1.4350	=	EURO	14,35,000
Net Gain in the Transaction	=	EURO	5,000

To sell EURO 5,000 in the market @

(a) USD 1 = EURO 1.4350 &

(b) USD1 = INR 61.4300

Cross Currency buying rate of EUR/INR is ₹ 61.4300 / 1.4350 i.e. ₹ 42.8084

Gain in the Transaction ₹ 42.8084 * 5000 = ₹ 2,14,042.00

10. The arbitrageur can proceed as stated below to realize arbitrage gains.

(i) Buy GBP at New York for USD USD 1,00,00,000

GBP/USD	1.72
Add: Exchange Margin @ 0.125%	0.002
	1.722

Accordingly, GBP acquired in exchange of USD1,00,00,000 is GBP 58,07,200

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(ii) Sell these GBP at London Market and get INR

GBP/INR	102.50
Less: Exchange Margin@ 0.125%	0.13
	102.37
INR on conversion of GBP (58,07,200 X 102.37)	INR 59,44,83,064

(iii) Acquire USD by selling INR at Mumbai

USD/INR	59.35
Add: Exchange Margin @ 0.125%	0.07
	59.42

Accordingly, USD acquired in exchange of INR $\frac{59,44,83,064}{59.42}$ is USD 1,00,04,763

Net Gain (USD 1,00,04,763 - USD 1,00,00,000) USD 4,763

11. Number of index future to be sold by the Fund Manager is:

$$\frac{1.1 \times 90,00,00,000}{4,300 \times 50} = 4,605$$

Justification of the answer:

Loss in the value of the portfolio if the index falls by 10% is

₹ $\frac{11}{100}$x90 Crore = ₹ 9.90 Crore.

Gain by short covering of index future is: $\frac{0.1 \times 4,300 \times 50 \times 4,605}{1,00,00,000}$ = 9.90 Crore

This justifies the answer cash is not part of the portfolio.

12. The optional hedge ratio to minimize the variance of Hedger's position is given by:

$$H= \rho\frac{\sigma S}{\sigma F}$$

Where

σS= Standard deviation of ΔS

σF=Standard deviation of ΔF

ρ= coefficient of correlation between ΔS and ΔF

H= Hedge Ratio

ΔS = change in Spot price.

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ΔF= change in Future price.

Accordingly

$$H = 0.75 \times \frac{0.04}{0.06} = 0.5$$

No. of contract to be short = 10 x 0.5 = 5

Amount = 5000 x ₹ 474 = ₹ 23,70,000

13. The duration of future contract is 4 months. The average yield during this period will be:

$$\frac{3\% + 3\% + 4\% + 3\%}{4} = 3.25\%$$

As per Cost to Carry model the future price will be

$$F = Se^{(r_f - D)t}$$

Where S = Spot Price

r_f = Risk Free interest

D = Dividend Yield

t = Time Period

Accordingly, future price will be

= ₹ 2,200 $e^{(0.08 - 0.0325)\times 4/12}$ = ₹ 2,200 $e^{0.01583}$

= ₹ 2,200 x 1.01593 = ₹ 2235.05

14. MAYA Ltd.

(i) Walter's model is given by –

$$p = \frac{D + (E - D)(\gamma / k_e)}{k_e}$$

Where, p = Market price per share,

E = Earning per share – ₹ 5

D = Dividend per share – ₹ 3

γ = Return earned on investment – 15%

k_e = Cost of equity capital – 12%

$$\therefore\ p = \frac{3 + (5-3) \times \frac{0.15}{0.12}}{0.12} = \frac{3 + 2 \times \frac{.15}{.12}}{.12} = ₹\ 45.83$$

(ii) According to Walter's model when the return on investment is more than the cost of equity capital, the price per share increases as the dividend pay-out ratio

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decreases. Hence, the optimum dividend pay-out ratio in this case is Nil. So, at a payout ratio of zero, the market value of the company's share will be:-

$$\frac{0+(5-0)\times\frac{.15}{.12}}{0.12} = ₹\ 52.08$$

15. Expected Turnover = ₹ 4.80 crore + 25% i.e. ₹ 1.20 crore = ₹ 6.00 crore

	₹ in Lacs	₹ in Lacs
Advance to be given:		
Debtors ₹6.00 crore x 90/360	150.00	
Less: 10% withholding	15.00	135.00
Less: Commission 2%		3.00
Net payment		132.00
Less: Interest @16% for 90 days on ₹132 lacs		5.28
		126.72
Calculation of Average Cost:		
Total Commission ₹6.00 crore x 2%		12.00
Total Interest ₹ 5.28 lacs x 360/90		21.12
		33.12
Less: Admin. Cost	6.00	
Saving in Bad Debts (₹600 lacs x 1.75% x 80%)	8.40	14.40
		18.72
Effective Cost of Factoring $\frac{₹18.72\text{ lacs}}{₹126.72\text{ lacs}}\times 100$		14.77%

16.

	Amount in ₹ lakhs	Amount in ₹ lakhs	Amount in ₹ lakhs
Opening Bank (200 - 185 -12)	3.00		
Add: Proceeds from sale of securities	63.00		
Add: Dividend received	2.00	68.00	
Deduct:			
Cost of securities purchased	56.00		
Fund management expenses paid (90% of 8)	7.20		
Capital gains distributed = 80% of (63 – 60)	2.40		

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Dividend distributed =80% of 2.00	1.60	67.20	
Closing Bank			0.80
Closing market value of portfolio			198.00
			198.80
Less: Arrears of expenses			0.80
Closing Net Assets			198.00
Number of units (Lakhs)			20
Closing NAV per unit (198.00/20)			9.90

Rate of Earning (Per Unit)

	Amount
Income received (₹ 2.40 lakhs + ₹ 1.60 lakhs)/20 lakhs	₹ 0.20
Loss: Loss on disposal (₹ 10 – ₹ 9.90)	₹ 0.10
Net earning	₹ 0.10
Initial investment	₹ 10.00
Rate of earning (monthly)	1%
Rate of earning (Annual)	12%

17. Calculation of Investment Amount

Amount required for making payment on 30th January, 2010 = ₹ 80,00,000

Investment in Certificates of Deposit (CDs) on 31st October, 2009

Rate of interest = 8% p.a.

No. of days to maturity = 91 days

Interest on ₹ 1 of 91 days

(Re. 1 × 0.08 × 91/365) = 0.0199452

Amount to be received for Re. 1

(Re.1.00 + ₹ 0.0199452) = 1.0199452

Calculation of amount to be invested now to get ₹ 80 lakhs after 91 days:

$$= \frac{₹\ 80,00,000}{₹\ 1.0199452} = ₹\ 78,43,558.65$$

Or, ₹ 78,43,600 or ₹ 78,44,000 approximately.

18. (i) Working Notes:

Present Value of Cash Flows (CF) upto 5 years

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Year End	CF of Yes Ltd. (₹ lakhs)	PVF @15%	PV of CF (₹ lakhs)	CF of Merged Entity (₹ lakhs)	PV of CF of Merged Entity (₹ lakhs)
1	175	0.870	152.25	400	348.00
2	200	0.756	151.20	450	340.20
3	320	0.658	210.56	525	345.45
4	340	0.572	194.48	590	337.48
5	350	0.497	173.95	620	308.14
			882.44		1679.27

PV of Cash Flows of Yes Ltd. after the forecast period

$TV_5 = \frac{CF_5(1+g)}{K_e - g} = \frac{350(1+0.05)}{0.15-0.05} = \frac{367.50}{0.10}$ = ₹3675 lakhs

PV of TV_5 = ₹3675 lakhs x 0.497 = ₹1826.475 lakhs

PV of Cash Flows of Merged Entity after the forecast period

$TV_5 = \frac{CF_5(1+g)}{K_e - g} = \frac{620(1+0.06)}{0.15-0.06} = \frac{657.20}{0.09}$ = ₹7302.22 lakhs

PV of TV_5 = ₹7302.22 lakhs x 0.497 = ₹3629.20 lakhs

(i) Value of Yes Ltd.

	Before merger (₹lakhs)	After merger (₹lakhs)
PV of CF (1-5 years)	882.440	1679.27
Add: PV of TV_5	1826.475	3629.20
	2708.915	5308.47

(ii) Value of Acquisition

= Value of Merged Entity – Value of Yes Ltd.

= ₹5308.47 lakhs – ₹2708.915 lakhs = ₹2599.555 lakhs

(iii) Gain to Shareholders of Yes Ltd.

Share of Yes Ltd. in merged entity = ₹5308.47 lakhs x $\frac{1}{1.5}$ = ₹3538.98 lakhs

Gain to shareholder = Share of Yes Ltd. in merged entity – Value of Yes Ltd. before merger

= ₹3538.98 lakhs - ₹2708.915 = ₹830.065 lakhs

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19. Impact of Financial Restructuring

(i) Benefits to Grape Fruit Ltd.

	₹ in lakhs
Reduction of liabilities payable	
Reduction in equity share capital (6 lakh shares x ₹75 per share)	450
Reduction in preference share capital (2 lakh shares x ₹50 per share)	100
Waiver of outstanding debenture Interest	26
Waiver from trade creditors (₹340 lakhs x 0.25)	85
	661
Revaluation of Assets	
Appreciation of Land and Building (₹450 lakhs - ₹200 lakhs)	250
Total (A)	911

(ii) Amount of ₹911 lakhs utilized to write off losses, fictious assets and over- valued assets.

Writing off profit and loss account	525
Cost of issue of debentures	5
Preliminary expenses	10
Provision for bad and doubtful debts	15
Revaluation of Plant and Machinery (₹300 lakhs – ₹180 lakhs)	120
Total (B)	675
Capital Reserve (A) – (B)	236

(iii) Balance sheet of Grape Fruit Ltd as at 31st March 2011 (after re-construction)

(₹ in lakhs)

Liabilities	Amount	Assets		Amount
12 lakhs equity shares of ₹ 25/- each	300	Land & Building Plant & Machinery		450 180
10% Preference shares of ₹ 50/- each	100	Furnitures & Fixtures Inventory		50 150
Capital Reserve	236	Sundry debtors	70	
9% debentures	200	Less: provision for		
Loan from Bank	74	Bad & doubtful debts.	15	55
Trade Creditors	255	Cash-at-Bank (Balancing figure)*		280
	1165			1165

*Opening Balance of ₹130/- lakhs + Sale proceeds from issue of new equity shares ₹150/- lakhs.

20. (a) After the globalization of the Indian economy, accessibility to vast amount of resources

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was available to the domestic corporate sector. One such accessibility was in terms of raising financial resources abroad by internationally prudent companies. Among others, GDRs were the most important source of finance from abroad at competitive cost. Global depository receipts are basically negotiable certificates denominated in US dollars, that represent a non- US company's publicly traded local currency (Indian rupee) equity shares. Companies in India, through the issue of depository receipts, have been able to tap global equity market to raise foreign currency funds by way of equity.

Since the inception of GDRs, a remarkable change in Indian capital market has been observed. Some of the changes are as follows:

(i) Indian capital market to some extent is shifting from Bombay to Luxemburg and other foreign financial centres.

(ii) There is arbitrage possibility in GDR issues. Since many Indian companies are actively trading on the London and the New York Exchanges and due to the existence of time differences, market news, sentiments etc. at times the prices of the depository receipts are traded at discounts or premiums to the underlying stock. This presents an arbitrage opportunity wherein the receipts can be bought abroad and sold in India at a higher price.

(iii) Indian capital market is no longer independent from the rest of the world. This puts additional strain on the investors as they now need to keep updated with worldwide economic events.

(iv) Indian retail investors are completely sidelined. Due to the placements of GDRs with Foreign Institutional Investor's on the basis free pricing, the retail investors can now no longer expect to make easy money on heavily discounted right/public issues.

(v) A considerable amount of foreign investment has found its way in the Indian market which has improved liquidity in the capital market.

(vi) Indian capital market has started to reverberate by world economic changes, good or bad.

(vii) Indian capital market has not only been widened but deepened as well.

(viii) It has now become necessary for Indian capital market to adopt international practices in its working including financial innovations.

(b) A firm dealing with foreign exchange may be exposed to foreign currency exposures. The exposure is the result of possession of assets and liabilities and transactions denominated in foreign currency. When exchange rate fluctuates, assets, liabilities, revenues, expenses that have been expressed in foreign currency will result in either foreign exchange gain or loss. A firm dealing with foreign exchange may be exposed to the following types of risks:

(i) **Transaction Exposure:** A firm may have some contractually fixed payments and receipts in foreign currency, such as, import payables, export receivables, interest payable on foreign currency loans etc. All such items are to be settled

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in a foreign currency. Unexpected fluctuation in exchange rate will have favourable or adverse impact on its cash flows. Such exposures are termed as transactions exposures.

(ii) **Translation Exposure:** The translation exposure is also called accounting exposure or balance sheet exposure. It is basically the exposure on the assets and liabilities shown in the balance sheet and which are not going to be liquidated in the near future. It refers to the probability of loss that the firm may have to face because of decrease in value of assets due to devaluation of a foreign currency despite the fact that there was no foreign exchange transaction during the year.

(iii) **Economic Exposure:** Economic exposure measures the probability that fluctuations in foreign exchange rate will affect the value of the firm. The intrinsic value of a firm is calculated by discounting the expected future cash flows with appropriate discounting rate. The risk involved in economic exposure requires measurement of the effect of fluctuations in exchange rate on different future cash flows.

(c) Constraints on paying Dividedends

(i) Legal: Under Section 205(1) of the Companies Act 1956, dividend is to be paid out of current profits or past profits after depreciation. The Central Government can allow a company to pay dividend for any financial year out of profits of the company without providing for depreciation if it is in the public interest. Dividend is to be paid in cash but a company is allowed to capitalise profits or reserves (retained earnings) for issuing fully paid bonus shares. Capital profit may also be distributed as dividends if articles permit.

(ii) Liquidity: Payment of dividends means outflow of cash. Ability to pay dividends depends on cash and liquidity position of the firm. A mature company does not have much investment opportunities, nor are funds tied up in permanent working capital and, therefore has a sound cash position. For a growth oriented company in spite of good profits, it will need funds for expanding activities and permanent working capital and therefore it is not in a position to declare dividends.

(iii) Access to the Capital Market: By paying large dividends, cash position is affected. If new shares have to be issued to raise funds for financing investment programmes and if the existing shareholders cannot buy additional shares, control is diluted. Payment of dividends may be withheld and earnings areutilised for financing firm's investment opportunities.

(iv) Investment Opportunities: If investment opportunities are inadequate, it is better to pay dividends and raise external funds whenever necessary for such opportunities.

(d) Depending upon the features built into the factoring arrangement to cater to the varying needs of trade/citizens, there can be different kinds of factoring:

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Recourse and Non-recourse Factoring: Under a recourse factoring arrangement, the factor has recourse to the client (firm) if the debt purchased/receivable factored turns out to be irrecoverable. In other words, the factor does not assume credit risks associated with the receivables. The factor does not have the right to recourse in the case of non-recourse factoring. The loss arising out of irrecoverable receivables is borne by him, as a compensation for which he charges a higher commission.

Advance and Maturity factoring: The factor paid a pre specified portion, ranging between three-fourths to nine tenths, of the factored receivables in advance, the balance being paid upon collection/on the guaranteed payment date. A drawing limit, as a pre- payment, is made available by the factor to the client as soon as the factored debts are approved/the invoices are accounted for. The client has to pay interest (discount) on the advance/repayment between the date of such payment and the date of actual collection from the customers/or the guaranteed payment date, determined on the basis of the prevailing short-term rate, the financial standing of the client and the volume of the turnover.

Full factoring: This is the most comprehensive form of factoring combining the features of all the factoring services specially those of non-recourse and advance factoring. It is also known as old line factoring.

Disclosed and undisclosed Factoring: In disclosed factoring, the name of the factor is disclosed in the invoice by the supplier-manufacturer of the goods asking the buyer to make payment to the factor, the name of the factor is not disclosed in the invoice in undisclosed factoring although the factor maintains the sales ledger of the supplier-manufacturer. The entire realization of the business transaction is done in the name of the supplier company but all control remains with the factor.

Domestic and export/Cross Border Factoring: If the three parties involved, namely, customer (buyer), client, (seller-supplier) and factor (financial intermediary) are domiciled in the same country then it is known as domestic factoring. There are usually four parties involved to a cross border factoring transaction. They are :

1. Exporter (client)
2. Importer (customer)
3. Export factor
4. Import Factor

It is also known as two-factor system.

(e) Treasury bills are short-term debt instruments of the Central Government, maturing in a period of less than one year. Treasury bills are issued by RBI on behalf of the Government of India for periods ranging from 14 days to 364 days through regular auctions. They are highly liquid instruments and issued to tide over short-term liquidity shortfalls.

Treasury bills are sold through an auction process according to a fixed auction calendar announced by the RBI. Banks and primary dealers are the major bidders in

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the competitive auction process. Provident Funds and other investors can make non-competitive bids. RBI makes allocation to non-competitive bidders at a weighted average yield arrived at on the basis of the yields quoted by accepted competitive bids. These days the treasury bills are becoming very popular on account of falling interest rates. Treasury bills are issued at a discount and redeemed at par. Hence, the implicit yield on a treasury bill is a function of the size of the discount and the period of maturity. Now, these bills are becoming part of debt market. In India, the largest holders of the treasury bills are commercial banks, trust, mutual funds and provident funds. Although the degree of liquidity of treasury bills are greater than trade bills, they are not self liquidating as the genuine trade bills are. T-bills are claim against the government and do not require any grading or further endorsement or acceptance.

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PAPER – 3 : ADVANCED AUDITING AND PROFESSIONAL ETHICS

QUESTIONS

Standards on Auditing, Statements and Guidance Notes

1. (a) CA Ashutosh has been appointed as an auditor of Awesome Health Ltd. for the financial year 2013-14 which was audited by CA Amrawati in 2012-13. As the Auditor of Awesome Health Ltd., state the steps that CA Ashutosh would take to ensure that the Closing Balances of the financial year 2012-13 have been brought to account in 2013-14 as Opening Balances and the Opening Balances do not contain any misstatements.

   (b) A Company outsourced the activity of accounting data maintainance to the Service Organisation to achieve cost reduction. As a Statutory Auditor of such company, what are the precautions/checks that you would consider for conducting the audit?

2. (a) While compiling the financial statements of Discrepancy Ltd., you observed that the information supplied by the company is incomplete, incorrect and few of the Accounting Standards have not been followed. Describe, in brief, the procedure you will follow in the above situation.

   (b) While doing the audit of Prakash Ltd., CA Prateek, the auditor, requires reports from experts for the purpose of audit evidence. What type of reports/ opinions he can obtain and to what extent he can rely upon the same?

Audit Strategy Planning and Programming

3. You are the manager responsible for the audit of Value Ltd. which has a year end of 31 March. This is the first year that your firm has undertaken the audit of Value Ltd., having succeeded the previous auditors at the last annual general meeting following a successful tender for the audit. Your firm has an office in Mumbai and in 25 other location throughout the India.

   You have had preliminary discussions with the management of Value Ltd. and obtained some background information about the company. The company produces fertilizer in a factory on the outskirts of Liverpool. The head office is situated in Mumbai. There are ten depots throughout the country which hold large stocks of fertilizer so that local demand for its products can be met quickly. Inventory records are not maintained and a full count is carried out at the year end.

   You have also read recent government press release that indicates that 'L', a product which forms a major part of the company's sales, contains a chemical that has been identified as being potentially dangerous to those who handle it. An official government working party has been set up to review the situation.

   Requirement

   (a) Identify the circumstances that should be taken into account when planning the audit of Value Ltd., and set out your outline audit approach in these areas.

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(b) Explain the objectives of audit planning.

Risk Assessment and Internal Control

4. You are the auditor of Vishakha Steel Pressing Limited, which manufactures small pressing from sheet-steel. The process generates scrap steel which is placed daily by the work force into a bin kept for that purpose in the yard. Every Friday a lorry arrives from a small local scrap merchant. The bin is loaded on to the lorry and replaced by an empty bin. The weight is obtained by the gatekeeper using the company weighbridge. He notes the weight in a book kept for that purpose in the gate office. Each month a cheque is received through the post from the scrap merchant accompanied by a remittance advice stating the weight of scrap collected, the price and the amount of the cheque. The cheque is banked by the cashier and the remittance advice is filed. There are no other procedures in this area:

   You are required to:

   (a) Suggest major improvements to be made in the internal control in this area.

   (b) Suggest key audit procedures under these circumstances to mitigate audit risk.

Audit under CIS Environment and Special Audit Techniques

5. (a) Zantacs, a limited company having turnover of approximately ₹ 80 crores uses a tailor made accounting software package. In the said package, all transactions are recorded, processed and the final accounts generated from the system. The management tells you that in view of the voluminous nature of day books, there is no need to print them and that audit can be conducted on the computer itself. The management further assures you that any 'query based reports' as required can be generated and printed. As a statutory auditor of the company, enumerate the procedures you would adopt to conduct the audit.

   (b) "The auditor must evaluate major clauses of control used in a Computerised Information system to enhance its reliability" – Comment.

The Company Audit

6. As an auditor, how would you deal with the following situations:

   (a) Ram and Hanuman Associates, Chartered Accountants in practice have been appointed as Statutory Auditor of Krishna Ltd. for the accounting year 2013-2014. Mr. Hanuman, a partner of the Ram and Hanuman Associates, holds 100 equity shares of Shiva Ltd., a subsidiary company of Krishna Ltd.

   (b) Nick Ltd. is a subsidiary of Ajanta Ltd., whose 20% shares have been held by Central Government, 25% by Uttar Pradesh Government and 10% by Madhya Pradesh Government. Nick Ltd. appointed Mr. Prem as statutory auditor for the year.

   (c) Contravene Ltd. appointed CA Innocent as an auditor for the company for the current financial year. Further the company offered him the services of actuarial,

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investment advisory and investment banking which was also approved by the Board of Directors.

(d) Mr. Amar, a Chartered Accountant, bought a car financed at ₹ 7,00,000 by Chaudhary Finance Ltd., which is a holding company of Charan Ltd. and Das Ltd. He has been the statutory auditor of Das Ltd. and continues to be even after taking the loan.

7. As an auditor, how would you deal with the following situations:

(a) M/s XYZ & Co., auditors of Goodwill Education Foundation, a recognised nonprofit organisation feels that the standards on auditing need not to be applied as Goodwill Education Foundation is a non-profit making concern.

(b) Rama Pvt. Ltd. is a private company having paid up share capital of rupees twenty-five crore but having public borrowing from nationalized banks and financial institutions of rupees forty crore. The company appointed CA Raman as an auditor in its AGM dated 29th September, 2014.

You are required to state the following provisions as the section 139 of the Companies Act, 2013 in case of an individual auditor or an audit firm, both-

(i) Rotation of auditor;

(ii) Cooling off period;

(iii) Common partner(s) to the other audit firm whose tenure has expired;

(iv) Transitional period for the adoption of new Companies Act;

(v) Right of the company to remove an auditor;

(vi) Rotation between partners of audit firm;

(c) MSY & Co. is an Audit Firm having partners CA Mukti, CA Shakti and CA Yukti. CA Mukti, CA Shakti and CA Yukti are holding appointment as an Auditor in 4, 6 and 10 Companies respectively.

(i) Provide the maximum number of Audits remaining in the name of MSY & Co.

(ii) Provide the maximum number of Audits remaining in the name of individual partner i.e. CA Mukti, CA Shakti, CA Yukti.

(d) State the provisions relating to filling of casual vacancies as per section 139 (8) of the Companies Act, 2013 and casual vacancy due to resignation.

Liabilities of Auditor

8. Indicate the precise nature of auditor's liability in the following situations and support your views with authority, if any:

(a) A misstatement had occurred in the prospectus issued by the company.

(b) Certain weaknesses in the internal control procedure in the payment of wages in a large construction company were noticed by the statutory auditor who in turn brought the same to the knowledge of the Managing Director of the company. In the

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subsequent year huge defalcation came to the notice of the management. The origin of the same was traced to the earlier year. The management wants to sue the auditor for negligence and also plans to file a complaint with the Institute.

Audit Report

9. (a) The auditor of Chand Ltd. did not report on the matters, specified under section 143(1) of the Companies Act, 2013, on which he inquired into, because of the reason that he was satisfied. But the management of the company wanted the auditor to report on those matters so that the members can also be aware of the true position of the company. Comment as to whether the auditor is required to report the matters, specified under the Act, he inquired into and whether the contention of the management is sustainable.

   (b) An auditor became aware of a matter regarding a company, only after he had issued his audit opinion. Had he become aware of the same prior to his issuing the audit report, he would have issued a different opinion.Comment.

   (c) The audit report of P Ltd. for the year 2012-13 contained a qualification regarding non-provision of doubtful debts. As the statutory auditor of the company for the year 2013-14, how would you report, if the company does not make provision for doubtful debts in 2012-13?

   (d) XYZ Ltd. Co. gave a donation of ₹ 50,000 each to a Charitable Society running a school and a trust set up for the service of Blind during financial year ending on 31st March, 2014. The average net profits of the company for the last three years were 15 lakhs. Comment.

10. State the matters to be specified in Auditor's Report in terms of provisions of Section 143(3) of the Companies Act, 2013.

Audit of Banking Company

11. (a) As a branch auditor of a nationalised bank, how would you verify the following?

       (1) Advances to DOT COM Companies.

       (2) Balances in account of a bank situated in a foreign country.

    (b) As the concurrent auditor of Nagpur Main Branch of XYZ Bank Ltd. state the issues which have to be considered in the audit of advances.

Audit of General Insurance Company

12. Enumerate the steps to be taken by an auditor for the verification of Re-insurance outward by a General Insurance Company.

Cost Audit

13. You have been appointed as Cost Auditor of M/s PQR Ltd. State the functions of Cost Auditor in respect of the following:

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(i) Inventory

(ii) Labour

(iii) Overhead and indirect expenditure.

(iv) Work in Progress

Audit of Co-operative Societies

14. Mention the duties of Auditor of Co-operative Societies in regard to the following:

(a) Over-due interest.

(b) Compliance with provisions of Co-operative Act and Rules thereunder.

(c) Special Report to Registrar of Co-operative Societies.

Audit under Fiscal Laws

15. (a) Concession Ltd. is engaged in the business of manufacturing of threads. The company recorded the turnover of ₹ 1.13 crore during the financial year 2013-14 before adjusting the following:

Discount allowed in the Sales Invoice	₹ 8,20,000
Cash discount (other than allowed in	
Cash memo/ sales invoice)	₹ 9,20,000
Trade discount	₹ 2,90,000
Commission on Sales	₹ 6,00,000
Sales Return (F.Y. 2012-13)	₹ 1,60,000
Sale of Investment	₹ 6,60,000

You are required to ascertain the effective turnover to be considered for the prescribed limit of tax audit under the relevant Act and guide the company whether the provisions relating to tax audit applies.

(b) Mr. Verma carries on the business of dealing and export of diamonds. For the year ended 31st March 2014, you as the tax auditor find that the entire exports are to another firm in U.S.A. which is owned by Mr. Verma's brother. Comment.

Audit of Non Banking Financial Companies

16. You are the auditor of Sample Ltd., a NBFC registered with RBI. What is the procedure you would pursue to ensure that the NBFC Public Deposit Directions have been followed by Sample Ltd.?

Internal Audit, Management and Operational Audit

17. (a) Interior Pvt. Ltd. is a manufacturing company having turnover of ₹ 210 crore but having maximum outstanding loan from public financial institution of ₹ 90 crore only during the preceding financial year. You are required to state whether the company is liable for internal audit as per the provisions of the Companies Act, 2013.

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(b) As an External auditor of Interior Pvt. Ltd., explain the important aspects to be considered in the evaluation of Internal Audit Function.

Investigation and Due Diligence

18. Sri Ramaswami is above 80 years old and wishes to sell his proprietary business of manufacture of specialty chemicals. C Ltd. wants to buy the business and appoints you to carry out a due diligence audit to decide whether it would be worthwhile to acquire the business.

    What procedures you would adopt before you could render any advice to C Ltd.?

Professional Ethics

19. Comment on the following with reference to the Chartered Accountants Act, 1949, and Schedules to the Act:

    (a) CA N, in practice, started project consultancy work as a part of his practice and to advance the same, sent mail to all the CAs in the country informing them of his services and for securing professional work.

    (b) CA T, in practice, was appointed to carry out Internal audit of a stock broker, listed with BSE. However, he failed to intimate his appointment to the statutory auditors of the company. The statutory auditor feels this is violation of professional ethics.

    (c) Mr. Ram, a Chartered Accountant in practice, received ₹ 15,00,000 on 15th December, 2013 on behalf of one of his clients, who has gone to USA. Mr. Ram deposited the said amount in his saving bank account (SB Account). As per instruction of the client, the said amount is to be returned to the client on March 31, 2014 when he will return to India. On the occasion of birthday of his wife Sita, Mr. Ram withdrew ₹ 5,00,000 and spent on Birthday party. He re-deposited ₹ 5,00,000 in the said SB account on 25th March, 2014 and then returned the entire amount of ₹ 15,00,000 to the client on March, 31, 2014.

    (d) CA. Smart, a CA in practice runs his proprietorship firm as "M/s Smart & Co.". His annual gross receipts are in excess of ₹ 40 Lakhs. He maintains a small pocket diary in which he writes the fees received from various clients. Based on his record, he prepares and files his income tax return.

Other Miscellaneous Chapters

20. Write short notes on the following:

    (a) Constitution of Audit Committee under Section 177 of the Companies Act, 2013.

    (b) Areas to be examined in Comprehensive Audit of public enterprises.

    (c) Sauda Book.

    (d) Appointment of Auditor.

    (e) Collection of evidences by Peer reviewer.

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SUGGESTED ANSWERS/HINTS

1. (a) **Obtaining sufficient appropriate audit evidence while conducting Initial Audit Engagement :** According to SA 510 on "Initial Audit Engagements- Opening Balances", the objective of the Auditor while conducting an initial audit engagement with respect to opening balances is to obtain sufficient appropriate audit evidence so that the-

(i) opening balances of the preceding period have been correctly brought forward to the current period;

(ii) opening balances do not contain any misstatement that materially affect the current period's financial statements; and

(iii) appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, or changes thereto are properly accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

Being a new assignment, audit evidence regarding opening balances can be obtained by perusing the copies of the audited financial statements.

For current assets and liabilities, some audit evidence about opening balances may be obtained as part of the current period's audit procedures. For example, the collection/ payment of opening accounts receivable/ accounts payable during the current period will provide some audit evidence of their existence, rights and obligations, completeness and valuation at the beginning of the period.

In respect of other assets and liabilities such as property plant and equipment, investments, long term debts, the auditor will examine the records relating to opening balances. The auditor may also be able to get the confirmation from third parties (e.g., balances of long term loan obtained from banks can be confirmed from the Bank Loan statement).

(b) **Precautions to be taken by auditor in case Accounting Data Processed by Service Organisation:** A client may use a service organisation such as one that executes transactions and maintains related accountability or records transactions and processes related data (e.g., a computer systems service organisation). If a client uses a service organisation, certain policies, procedures and records maintained by the service organisation might be relevant to the audit of the financial statements of the client. Consequently, the auditor would consider the nature and extent of activities undertaken by service organisations so as to determine whether those activities are relevant to the audit and, if so, to assess their effect on audit risk.

SA 402 on "Audit Considerations relating to an Entity Using a Service Organisation" deals with the user auditor's responsibility to obtain sufficient appropriate audit evidence when a user entity uses the services of one or more service organisations.

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While planning the audit, the auditor of the client should determine the significance of the activities of the service organisation to the client and their relevance to the audit. In doing so, the auditor of the client would need to consider the following, as appropriate:

(i) The nature of the services provided by the service organisation and the significance of those services to the user entity, including the effect thereof on the user entity's internal control.

(ii) The nature and materiality of the transactions processed or accounts or financial reporting processes affected by the service organisation.

(iii) The degree of interaction between the activities of the service organisation and those of the user entity.

(iv) The nature of the relationship between the user entity and the service organisation, including the relevant contractual terms for the activities undertaken by the service organisation.

2. (a) Compilation of Financial Information: According to SRS 4410 "Engagement to Compile Financial Information", an accountant would normally have to rely on the management for most of the information needed to compile the financial statements or other financial information, including accounting estimates as well as the fact that the information given to the accountant is complete and reliable. If in the course of compilation of financial statements, it is observed that the information supplied by the entity is incorrect, incomplete or otherwise unsatisfactory, the accountant should perform following procedures:

(i) Make any enquiries of management to assess the reliability and completeness of the information provided;

(ii) Assess internal controls prevailing in the entity; and

(iii) Verify any matters or explanations.

If the accountant becomes aware that the information supplied by management is incorrect, incomplete, or otherwise unsatisfactory, the accountant should consider performing the procedures listed above and request management to provide additional information. This may be asked in the form of management representation letter covering significant information or explanations given orally on which he considers representations are required. If the management refuses to provide additional information, the accountant should withdraw from the engagement, informing the entity of the reasons for such withdrawal.

If one or more accounting standards are not complied with, the same should be brought to the notice of the management and if the same is not rectified by the management, the accountant should include the same in notes to the accounts and the compilation report to the management.

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The accountant should read the compiled information and consider whether it appears to be appropriate in form and free from obvious material misstatements. The identified financial reporting framework and any known departures therefrom should be disclosed within the financial information, though their effects need not be quantified.

(b) As per SA 620, "Using the work of an Auditor's Expert", during the audit, the auditor may seek to obtain, in conjunction with the client or independently, audit evidence in the form of reports, opinions, valuations and statements of an expert.

While doing audit, CA Prateek, the auditor can obtain the following types of reports, or opinions or statements of an expert for the purpose of audit evidence:

- The valuation of complex financial instruments, land and buildings, plant and machinery, jewelry, works of art, antiques, intangible assets, assets acquired and liabilities assumed in business combinations and assets that may have been impaired.
- The actuarial calculation of liabilities associated with insurance contracts or employee benefit plans.
- The estimation of oil and gas reserves.
- The valuation of environmental liabilities, and site clean-up costs.
- The interpretation of contracts, laws and regulations.
- The analysis of complex or unusual tax compliance issues.

When the auditor intends to use the work of an expert, he shall evaluate the adequacy of the auditor's expert's work, including the relevance and reasonableness of that expert's findings or conclusions, and their consistency with other audit evidence; if that expert's work involves use of significant assumptions and methods, the relevance and reasonableness of those assumptions and methods in the circumstances; and if that expert's work involves the use of source data that is significant to his work, the relevance, completeness, and accuracy of that source data.

If the auditor determines that the work of the auditor's expert is not adequate for the auditor's purposes, he shall agree with that expert on the nature and extent of further work to be performed by that expert; or perform further audit procedures appropriate to the circumstances.

3. Audit Planning

Circumstances	Outline audit approach
This is the first year that the firm has undertaken the audit of Value Ltd.	• In order to be satisfied about the previous financial statements the auditor should : 1. Hold consultations with management. 2. Review client's records, working papers and accounting and control procedures for the previous period.

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	3. (Possibly) hold consultations with the previous auditor. 4. Be familiarizing with the nature of the business, market, accounting systems etc by discussions with management and by review of interim/management accounts.
Value Ltd.has - A head office in Mumbai - A factory in Liverpool - Ten depots throughout the country	• The staff must be planned to carry out the audit from the firm's offices throughout the country. • They must all be adequately briefed and provided with a copy of the audit plan detailing their specific tasks and deadlines.
No inventory records have been maintained but a full inventory count is to be carried out at the year end.	• It is very important that the auditors are satisfied with the inventory count. • The written count instruction must be reviewed well in advance of the year end, so that improvement can be suggested by the auditors and incorporated into the client's instructions. • The auditors should ensure that sufficient staff with the necessary experienced is available to attend the count at all material locations.
'L', a major product of the company, has been identified as being potentially dangerous.	Ascertain - For how long Value Ltd. has been selling 'L'and in what quantity? - How much 'L' the company now holds in inventory? Ensure that the firm keeps up-to-date with the findings of the government working party. Consider whether any of the employees of Value Ltd. may have been harmed and, if so, the consequential liability of the company to them.

(b) Objectives of audit planning

(i) **To ensure that appropriate attention is devoted to important areas of the audit:** This is done via a formal written audit plan, laying down the objectives and the procedures to be followed in order to meet those objectives.

(ii) **To facilitate review:** Work should be delegated to staff with the appropriate level of experience. All work should be properly supervised and reviewed by

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amore senior member of staff.

(iii) To ensure that potential problems are identified: The auditor must ensure that resources are directed towards material/high risk areas.

(iv) To assist in the proper assignment of work: This may be to members of the audit team or to experts or other auditors. It helps the audit to proceed in a timely and efficient manner.

4. (a) Improvements to be made in the internal control in this area:

(i) Ensure that all scrap is put into the bin by the work force. This can be achieved by documenting the scrap generated in every production lot/shift/day.

(ii) Check should be available that the merchant is paying the best prices for the scrap. This can be achieved by getting a quote periodically from few dealers or getting market price and validation.

(iii) Ensure that quantity collected is paid for this can be achieved by company quantity lifted with the amount paid/quantity for which payment is received.

(iv) An independent official should attend the weighing and the enter in the book.

(b) Key audit procedures under these circumstances to mitigate audit risk:

(i) Budget figures should be prepared for waste and compared to actual waste and variance being investigated.

(ii) Compare remittance advices/related quantity and reconcile with the quantity in gate keeper's book.

(iii) Ensure all entries in the weight book is paid for.

(iv) Ensure all remittance matching entries in the cash book.

(v) Review the reasonableness of total scarp sold during the period by comparing with manufacturing records of steel used in processing.

5. (a) A key feature of the accounting software package used by the company definitely involves the absence of a clear audit trail. In other words, transactions cannot be easily traced or co-related from the individual supporting documents of those transactions. Moreover, the management does not wish to print the daybooks in view of the voluminous nature since it may involve extensive costs. This has naturally led to extensive dependence by management upon the "exception reporting" principle.

From the auditor's point of view, it must also be conceded, the exception reports in the form of 'query-based reports' which isolate the above data provide him with the very material that he requires for most of his verification work. The only problem which it raises, and it is a serious one, is that he cannot simply assume that the programmes which produce the exception reports are reliable in respect of the following factors:

(i) operating accurately;

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(ii) printing out all the exceptions which exist; and

(iii) bound by programmed control parameters which meet the company's genuine internal control requirements.

In view of the above, whether management relies upon exception reports, it effectively eliminated the audit trail between input and output and the auditor is forced to test the invisible processes which purport to embody the controls, and produce the output such as it is. These tests, which invariably involve the use by the auditor of the computer itself, are known as tests through the machine. In the 'through the machine' approach, the auditor starts by proving the accuracy of the input data, and then thoroughly examines (by applying tests) the processing procedures with a view to establishing the following that:

(i) all input is actually entered into the computer.

(ii) neither the computer nor the operators can cause undetected irregularities in the final reports.

(iii) the programmes appear, on the evidence of rejection and exception routines, to be functioning correctly.

(iv) all operator intervention during processing is logged and scrutinised by the DP manager.

The auditor in such circumstances will have to first evaluate the existing controls. For the same, he has to do the following:

(i) Evaluate the internal control system especially the controls and checks existing for recording the transactions, i.e., he has to verify at what level transactions can be entered into the system and what checks are available to prevent any unauthorised data entry and for rectifying errors/omissions in the transactions entered.

(ii) Evaluate at what level there authority is given for modification of transactions already entered. Is there any authority given only to a senior employee to carry out modifications? Or is it that once transactions are entered and validated, no further modifications are possible thereto.

(iii) Whether there is a provision in the software for carrying out an on line audit of transactions, i.e. whether there a separate module in the package, where a separate password given to the auditor and once he has seen and approved a particular transaction/set of transactions, the same would be locked and no modifications would be possible by anyone (including the senior most employee) in the company.

(iv) Whether there are proper procedures for backup of data on a regular basis and whether the said procedures are being strictly followed.

(v) In case of any loss of data whether there is a clear defined recovery procedure

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to minimize the loss of data due to power failures or any human errors.

(vi) The auditor may introduce some dummy data into the system and see the results obtained.

After the auditor has evaluated the above procedures, he has to prepare an audit plan depending on the results obtained from his earlier evaluation. Since the daybooks are not being printed, the plan can contain procedures wherein data is verified directly on the computer from the vouchers/invoices, etc. The audit plan will also require a lot of analytical procedures to be performed. Depending on the importance of various expense heads and other important account heads, the auditor will also obtain various reports from the system depending on various queries that he would have to identify. Some illustrative reports can be:

(i) To check whether proper classification is done for revenue/capital - a report can be obtained of all purchases (not being raw materials or other routine purchases) exceeding ₹ one lakh.

(ii) To check whether all freight outward bills are accounted for a report containing a month-wise co-relation between goods despatched and freight amount paid. The same can be further co-related with the freight rates obtained from the bills.

Once the auditor has performed the above procedures, he would be able to form an opinion whether reliance can be placed on the accounting systems and the data recorded. If the auditor finds that reliance cannot be placed on the systems he can inform the management about the fact and also that the daybooks, etc., will need to printed to allow him to conduct the audit. The finalisation procedures to be followed even under this system would remain more or less similar to other accounting systems. The auditor can obtain reports of depreciation on fixed assets, inventory valuation and using the normal procedures find out whether reliance can be placed on them, e.g., if while valuing stocks the system is using the LIFO method, the same would not be acceptable and will need to be modified. Similarly depreciation calculations will have to verify on a random basis to find out its reliability.

(b) The reliability of a component is a function of control that acts on the component. In a computer system the following are the major types of controls and used to enhance component reliability which the auditor must evaluate:

(i) ***Authenticity Control***: They are exercised to verify the identity of the individuals or process involved in a system. (Pass word, digital signature etc.)

(ii) ***Accuracy Control***: These attempts to ensure the correctness of the data and processes in a system (Programme validation check).

(iii) ***Completeness Control***: This ensures that no data is missing and all processing is carried through to its proper conclusion.

(iv) ***Privacy Control***: This ensures the protection of data from inadvertent or unauthorised disclosure.

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(v) ***Audit Trail Controls***: This ensures the traceability of all events occurred in a system.

(vi) ***Redundancy Control***: It ensures that processing of data is done only once.

(vii) ***Existence Control****:* It attempts to ensure the on going availability of all system resources.

(viii) ***Asset safeguarding controls****:* It attempts to ensure that all resources within a system are protected from destruction or corruption.

(ix) ***Effectiveness Control***: It attempts to ensure that the system achieves its goals.

(x) ***Efficiency Control***: It attempts to ensure that a system uses minimum resources to achieve its goals.

6. (a) Auditor holding securities of a company : As per sub-section (3)(d)(i) of Section 141 of the Companies Act, 2013 along with Rule 10 of the Companies (Audit and Auditors) Rule, 2014, a person shall not be eligible for appointment as an auditor of a company, who, or his relative or partner is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company. Provided that the relative may hold security or interest in the company of face value not exceeding rupees one lakh.

Also, as per sub-section 4 of Section 141 of the Companies Act, 2013, where a person appointed as an auditor of a company incurs any of the disqualifications mentioned in sub-section (3) after his appointment, he shall vacate his office as such auditor and such vacation shall be deemed to be a casual vacancy in the office of the auditor.

In the present case, Mr. Hanuman, Chartered Accountant, a partner of M/s Ram and Hanuman Associates, holds 100 equity shares of Shiva Ltd. which is a subsidiary of Krishna Ltd. Therefore, the firm, M/s Ram and Hanuman Associates would be disqualified to be appointed as statutory auditor of Krishna Ltd. as per section 141 (3)(d)(i), which is the holding company of Shiva Ltd., because Mr. Hanuman one of the partner is holding equity shares of its subsidiary.

(b) According to Section 139 (7) of the Companies Act, 2013, the auditors of a government company shall be appointed or re-appointed by the Comptroller and Auditor General of India. As per section 2(45), a Government company is defined as any company in which not less than 51% of the paid-up share capital is held by the Central Government or by any State Government or Governments or partly by the Central Government and partly by one or more State Governments and includes a company which is a subsidiary of a Government Company as thus defined".

In the given case Ajanta Ltd is a government company as its 20% shares have been held by Central Government, 25% by U.P. State Government and 10% by M.P. State Government. Total 55% shares have been held by Central and State

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governments. Therefore, it is a Government company.

Nick Ltd. is a subsidiary company of Ajanta Ltd. Hence Nick Ltd. is covered in the definition of a government company. Therefore, the Auditor of Nick Ltd. can be appointed only by C & AG.

Consequently, appointment of Mr. Prem is invalid and he should not give acceptance to the Directors of Nick Ltd.

(c) Services not to be Rendered by the Auditor: Section 144 of the Companies Act, 2013 prescribes certain services not to be rendered by the auditor. An auditor appointed under this Act shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case may be, but which shall not include any of the following services (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company), namely:

(i) accounting and book keeping services;

(ii) internal audit;

(iii) design and implementation of any financial information system;

(iv) actuarial services;

(v) investment advisory services;

(vi) investment banking services;

(vii) rendering of outsourced financial services;

(viii) management services; and

(ix) any other kind of services as may be prescribed.

Further section 141(3)(i) of the Companies Act, 2013 also disqualify a person for appointment as an auditor of a company who is engaged as on the date of appointment in consulting and specialized services as provided in section 144.

In the given case, CA Innocent was appointed as an auditor of Contravene Ltd. He was offered additional services of actuarial, investment advisory and investment banking which was also approved by the Board of Directors. The auditor is advised not to accept the services as these services are specifically notified in the services not to be rendered by him as an auditor as per section 144 of the Act.

(d) According to section 141 (3)(d) (ii) of the Companies Act, 2013, a person is not eligible for appointment as auditor of any company, If he is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of rupees five lakh.

In the given case Mr. Amar is disqualified to act as an auditor under section141 (3)(d) (ii) as he is indebted to M/s Chaudhary Finance Ltd. for more than 5'00'000 ₹ Also according to Section141 (3)(d) (ii) he cannot act as an auditor of any subsidiary of Chaudhary Finance Ltd. i.e. he is also disqualified to work in Charan Ltd. & Das

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Ltd. Therefore he has to vacate his office in Das Ltd. Even though it is a subsidiary of Chaudhary Finance Ltd.

Hence audit work performed by Mr. Amar as an auditor is invalid, he should vacate his office immediately and Das Ltd should appoint another auditor for the company.

7. (a) Compliance with Standards on Auditing : As per sub section 9 of section 143 of the Companies Act, 2013, every auditor shall comply with the auditing standards. Further as per sub section 10 of section 143 of the Act, the Central Government may prescribe the standards of auditing or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under section 3 of the Chartered Accountants Act, 1949, in consultation with and after examination of the recommendations made by the National Financial Reporting Authority.

Provided that until any auditing standards are notified, any standard, or standards of auditing specified by the Institute of Chartered Accountants of India shall be deemed to be the auditing standards.

Further, the Preface to Standards on Auditing gives the scope of the Standards on Auditing. As per the Preface, the SAs will apply whenever an independent audit is carried out; that is, in the independent examination of financial statements/information of any entity; whether profit oriented or not and irrespective of its size, or legal form (unless specified otherwise) when such an examination is conducted with a view to expressing an opinion thereon.

Also while discharging their attest function; it is the duty of the Chartered Accountant to ensure that SAs are followed in the audit of financial information covered by their audit reports.

In the given case, even though the client is a non-profit oriented entity the SAs shall apply and the auditor shall be guilty of professional misconduct for failing to discharge his duty in case of non-compliance with SAs.

(b) (i) Rotation of Auditor: The provisions related to rotation of auditor are applicable to those companies which are prescribed in Companies (Audit and Auditors) Rules, 2014, which prescribes the following classes of companies excluding one person companies and small companies, namely:-

(a) all unlisted public companies having paid up share capital of rupees ten crore or more;

(b) all private limited companies having paid up share capital of rupees twenty crore or more;

(c) all companies having paid up share capital of below threshold limit mentioned in (a) and (b) above, but having public borrowings from financial institutions, banks or public deposits of rupees fifty crores or more.

As per Section 139(2) of the Companies Act, 2013, no listed company or a

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company belonging to such class or classes of companies as mentioned above, shall appoint or re-appoint-

(a) an individual as auditor for more than one term of five consecutive years; and

(b) an audit firm as auditor for more than two terms of five consecutive years.

In the given case, Rama Pvt. Ltd. is a private company having paid up share capital of rupees twenty-five crore but having public borrowing from nationalized banks and financial institutions of rupees forty crore. The company appointed CA Raman as an auditor in its AGM dated 29th September, 2014.

The provisions relating to rotation of auditor will be applicable as the paid up share capital exceeds rupees twenty crore. Therefore, Rama Pvt. Ltd. shall appoint CA Raman as an auditor of the company for not more than one term of five consecutive years and CA Raman will hold office of Auditor from the conclusion of this meeting upto conclusion of sixth AGM i.e. AGM to be held in the year 2019.

(ii) Cooling off period: As per the proviso to section 139(2) of the Companies Act, 2013:-

(1) an individual auditor who has completed his term under clause (a) shall not be eligible for re-appointment as auditor in the same company for five years from the completion of his term;

(2) an audit firm which has completed its term under clause (b), shall not be eligible for re-appointment as auditor in the same company for five years from the completion of such term.

Therefore, CA Raman shall not be re-appointed as Auditor in Rama Pvt. Ltd. for further term of five years i.e. he cannot be appointed as Auditor upto year 2024.

(iii) Common partner(s) to the other audit firm whose tenure has expired: As per the second proviso to section 139(2) of the Companies Act, 2013, as on the date of appointment, no audit firm having a common partner or partners to the other audit firm, whose tenure has expired in a company immediately preceding the financial year, shall be appointed as auditor of the same company for a period of five years. For Example, M/s XYZ & Co., is an audit firm having partner Mrs. X, Mr. Y and Mr. Z, whose tenure has expired in the company immediately preceding the financial year. M/s ABZ& Co., is another audit firm in which Mr. Z is a common partner, will also be disqualified for the same company along with M/S XYZ & Co.for the period of five years.

(iv) Transitional period for the adoption of new Companies Act: As per the third proviso to section 139(2) of the Companies Act, 2013, every company, existing on or before the commencement of this Companies Act, 2013 which is

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required to comply with provisions of this sub-section, shall comply with the requirements of this sub-section within three years from the date of commencement of this Act. For example-

(1) Mr Ram, a Chartered Accountant, is an individual auditor of M/s. Pinaco Ltd by last 5 years as on March, 2013 (i.e. existing on or before the date of Commencement of Companies Act, 2013), here a break in the term for a continuous period of five years will not be considered as fulfilling the requirement of rotation. Thus, Mr Ram can continue the audit of M/s. Pinaco Ltd. for another 3 years due to transitional effect, i.e. aggregate period in the same company will be 8 years.

(2) M/s Ram Associates, a Chartered Accountants Audit Firm, is doing audit of M/s. Pinaco Limited by last 11 years as on March, 2013 (i.e. existing on or before the date of Commencement of Companies Act, 2013), here a break in the term for a continuous period of two terms of five consecutive years will not be considered as fulfilling the requirement of rotation. Thus, M/s Ram Associates can continue the audit of M/s. Pinaco Ltd. for another 3 years due to transitional effect, i.e. aggregate period in the same company will be 14 years.

(v) Right of the company to remove an Auditor: As per the fourth proviso to section 139(2) of the Companies Act, 2013, it has also been provided that right of the company to remove an auditor or the right of the auditor to resign from such office of the company shall not be prejudiced.

(vi) Rotation between partners of audit firm: Under section 139(3) of the Act, subject to the provisions of this Act, members of a company may resolve to provide that-

(a) in the audit firm appointed by it, the auditing partner and his team shall be rotated at such intervals as may be resolved by members; or

(b) the audit shall be conducted by more than one auditor.

Further, it is important to note that as per the section 139(4) of the Companies Act, 2013, the Central Government may, by rules, prescribe the manner in which the companies shall rotate their auditors in pursuance of section 139(2) of the Act.

(c) Ceiling Number of Audit: As per section 141(3)(g) of the Companies Act, 2013, a person shall not be eligible for appointment as an auditor if he is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such person or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies;

As per section 141 (3)(g), this limit of 20 company audits is per person. In the case of an audit firm having 3 partners, the overall ceiling will be 3 × 20 = 60 company audits. Sometimes, a chartered accountant is a partner in a number of auditing

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firms. In such a case, all the firms in which he is partner or proprietor will be together entitled to 20 company audits on his account.

In the given case, CA Mukti is holding appointment in 4 companies, whereas CA Shakti is having appointment in 6 Companies and CA Yukti is having appointment in 10 Companies. In aggregate all three partners are having 20 audits.

(i) Therefore, MSY & Co. can hold appointment as an auditor of 40 more companies:

Total Number of Audits available to the Firm	= 20*3	=	60
Number of Audits already taken by all the partners			
In their individual capacity	= 4+6+10	=	20
Remaining number of Audits available to the Firm		=	40

(ii) With reference to above provisions an auditor can hold more appointment as auditor = ceiling limit as per section 141(3)(g)- already holding appointments as an auditor. Hence (1) CA Mukti can hold: 20 - 4 = 16 more audits. (2) CA Shakti can hold 20-6 = 14 more audits and (3) CA Yukti can hold 20-10 = 10 more audits.

(d) As per Section 139(8), any casual vacancy in the office of an auditor shall-

(i) **In the case of a company other than a company whose accounts are subject to audit by an auditor appointed by the Comptroller and Auditor-General of India**, be filled by the Board of Directors within thirty days.

If such casual vacancy is as a result of the resignation of an auditor, such appointment shall also be approved by the company at a general meeting convened within three months of the recommendation of the Board and he shall hold the office till the conclusion of the next annual general meeting;

(ii) **In the case of a company whose accounts are subject to audit by an auditor appointed by the Comptroller and Auditor-General of India**, be filled by the Comptroller and Auditor-General of India within thirty days:

It may be noted that in case the Comptroller and Auditor-General of India does not fill the vacancy within the said period the Board of Directors shall fill the vacancy within next thirty days.

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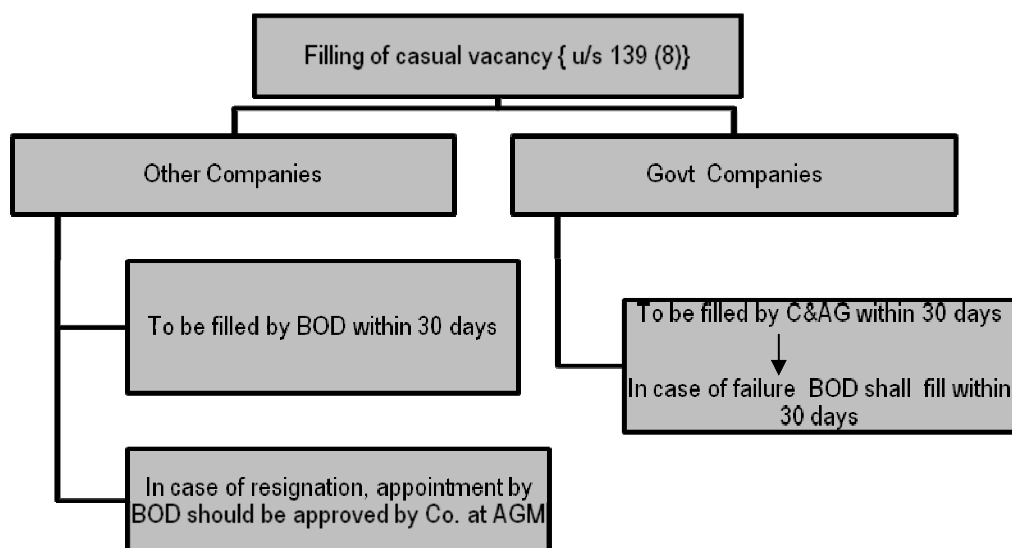

Casual Vacancy by Resignation: As per section 140 (2) the auditor who has resigned from the company shall file within a period of thirty days from the date of resignation, a statement in the prescribed form ADT–3 (as per Rule 8 of CAAR) with the company and the Registrar, and in case of the companies referred to in section 139(5) i.e. subsequent auditor of Government company, the auditor shall also file such statement with the Comptroller and Auditor-General of India, indicating the reasons and other facts as may be relevant with regard to his resignation. In case of failure the auditor shall be punishable with fine which shall not be less than fifty thousand rupees but which may extend to five lakh rupees as per section 140 (3).

8. (a) Under section 35 (1) of the Companies Act, 2013, where a person has subscribed for securities of a company acting on any statement included, or the inclusion or omission of any matter, in the prospectus which is misleading and has sustained any loss or damage as a consequence thereof, the company and every person who—

(i) is a director of the company at the time of the issue of the prospectus;

(ii) has authorized himself to be named and is named in the prospectus as a director of the company, or has agreed to become such director, either immediately or after an interval of time;

(iii) is a promoter of the company;

(iv) has authorised the issue of the prospectus; and

(v) is an expert referred to in sub-section (5) of section 26, shall, without prejudice to any punishment to which any person may be liable under section 36, be liable to pay compensation to every person who has sustained such loss or damage.

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No person shall be liable under sub-section (1) of section 35, if he proves—(i) that, having consented to become a director of the company, he withdrew his consent before the issue of the prospectus, and that it was issued without his authority or consent; or (b) that the prospectus was issued without his knowledge or consent, and that on becoming aware of its issue, he forthwith gave a reasonable public notice that it was issued without his knowledge or consent.

Notwithstanding anything contained in this section, where it is proved that a prospectus has been issued with intent to defraud the applicants for the securities of a company or any other person or for any fraudulent purpose, every person referred to in subsection (1) of section 35 shall be personally responsible, without any limitation of liability, for all or any of the losses or damages that may have been incurred by any person who subscribed to the securities on the basis of such prospectus.

(b) In the given case, certain weaknesses in the internal control procedure in the payment of wages in a large construction company were noticed by the statutory auditor and brought the same to the knowledge of the Managing Director of the company. In the subsequent year, a huge defalcation took place, the ramification of which stretched to the earlier year. The management of the company desires to sue the statutory auditor for negligence. The precise nature of auditor's liability in the case can be ascertained on the basis of the under noted considerations:

(i) Whether the defalcation emanated from the weaknesses noticed by the statutory auditor, the information regarding which was passed on to the management; and

(ii) Whether the statutory auditor properly and adequately extended the audit programme of the previous year having regard to the weaknesses noticed.

SA 265 on "Communicating Deficiencies in Internal Control to Those Charged with Governance and Management" clearly mentions that, "The auditor shall determine whether, on the basis of the audit work performed, the auditor has identified one or more deficiencies in internal control. If the auditor has identified one or more deficiencies in internal control, the auditor shall determine, on the basis of the audit work performed, whether, individually or in combination, they constitute significant deficiencies. The auditor shall communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis. The auditor shall also communicate to management at an appropriate level of responsibility on a timely basis". The fact, however, remains that, weaknesses in the design of the internal control system and non-compliance with identified control procedures increase the risk of fraud or error. If circumstances indicate the possible existence of fraud or error, the auditor should consider the potential effect of the suspected fraud or error on the financial information. If the auditor believes the suspected fraud or error could have a material effect on the financial information, he should perform such modified or additional procedures as

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he determines to be appropriate. Thus, normally speaking, as long as the auditor took due care in performing the audit work, he cannot be held liable.

9. (a) **Reporting of Matters contained under Section 143(1) of the Companies Act, 2013:** Section 143(1) of the Act deals with the duties of an auditor requiring him to make an inquiry in respect of specified matters amongst other matters. The matters in respect of which the inquiry has to be made by the auditor are relating to loans and advances on the basis of security, transactions represented merely by book entries, investments sold at less than cost price, loans and advances shown as deposits, personal expenses charged to revenue account etc. Since the law requires the auditor to make an inquiry, the Research Committee of the Institute opined that the auditor is not required to report on the matters specified in sub-section (1) unless he has any special comments to make on any of the items referred to therein. If the auditor is satisfied as a result of the inquiries, he has no further duty to report that he is so satisfied. In such a case, the content of the Auditor's Report will remain exactly the same as the auditor has to inquire and apply his mind to the information elicited by the inquiry, in deciding whether or not any reference needs to be made in his report.

Therefore, it could be said that the auditor should make a report to the members in case he finds answer to any of these matters in adverse. Consequently, the auditor of Chand Ltd. is correct in non-reporting on the matters specified in Section 143(1) of the Act and hence, the contention of the management is not sustainable.

(b) Section 146 of the Companies Act, 2013 empowers the auditors of a company to attend any general meeting of the company; to receive all the notices and other communications relating to the general meeting, unless otherwise exempted by the company, and to be heard at any general meeting in any part of the business of the meeting which concerns them as auditors.

Where the auditor has reason to believe that the directors concealed deliberately a serious fact from the shareholders which came to his note after issuance of the audit report, he should exercise this right. Normally speaking, an auditor considers subsequent events only upto the date of issuance of the audit report.

The discovery of a fact after issuance of the financial statements that existed at the date of the audit report which would have caused the revision of the audit report, requires the auditor to bring this to the notice of shareholders.

Likewise, it may be advisable for the auditor to attend the meeting with a view to bringing to the notice of the shareholders any matter which came to his knowledge subsequent to his signing the report and if it had been known to him at the time of writing his audit report, he would have drawn up the report differently; or where the accounts have been altered after the report was attached to the accounts.

(c) Auditor's responsibilities in cases where audit report for an earlier year is qualified is given in SA 710 "Comparative Information – Corresponding Figures and

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Comparative Financial Statements". As per SA 710, When the auditor's report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion and the matter which gave rise to the modified opinion is resolved and properly accounted for or disclosed in the financial statements in accordance with the applicable financial reporting framework, the auditor's opinion on the current period need not refer to the previous modification.

SA 710 further states that if the auditor's report on the prior period, as previously issued, included a qualified opinion and the matter which gave rise to the modification is unresolved, the auditor shall modify the auditor's opinion on the current period's financial statements. In the Basis for Modification paragraph in the auditor's report, the auditor shall either:

(i) Refer to both the current period's figures and the corresponding figures in the description of the matter giving rise to the modification when the effects or possible effects of the matter on the current period's figures are material; or

(ii) In other cases, explain that the audit opinion has been modified because of the effects or possible effects of the unresolved matter on the comparability of the current period's figures and the corresponding figures.

In the instant Case, if P Ltd. does not make provision for doubtful debts the auditor will have to modify his report for both current and previous year's figures as mentioned above. If however, the provision is made, the auditor need not refer to the earlier year's modification.

(d) Donation to Charitable Institutions*:* Section 181 of the Companies Act, 2013 provides that the Board of Directors of a company may contribute to bona fide charitable and other funds with prior permission of the company in general meeting for such contribution in case any amount the aggregate of which, in any financial year, exceed five per cent of its average net profits for the three immediately preceding financial years.

Facts of the case: In the instant case, the company has given donation of ₹ 50,000/- each to the two charitable organisations which amounts to 1,00,000. Assuming that the charitable organisations are not related to the business of the company, the average profits of the last 3 years is ₹ 15 lakhs and the 5% of this works out to ₹ 75,000. Hence the maximum of donation could be ₹ 75,000 only. For excess of ₹ 25,000 the company is required to take prior permission in general meeting which is not been taken.

Conclusion: By paying donations of ₹ 1,00,000 which is more than ₹ 75,000, the Board has contravened the provisions of Section 181 of the Companies Act, 2013. Hence the auditor should qualify his report accordingly.

10. Duty to Report: As per sub section 3 of section 143 of the Companies Act, 2013, the auditor's report shall also state –

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(a) whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for the purpose of his audit and if not, the details thereof and the effect of such information on the financial statements;

(b) whether, in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purposes of his audit have been received from branches not visited by him;

(c) whether the report on the accounts of any branch office of the company audited under sub-section (8) by a person other than the company's auditors has been sent to him under the proviso to that sub-section and the manner in which he has dealt with it in preparing his report;

(d) whether the company's balance sheet and profit and loss account dealt with in the report are in agreement with the books of account and returns;

(e) whether, in his opinion, the financial statements comply with the accounting standards;

(f) the observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company;

(g) whether any direct is disqualified from being appointed as a director under sub-section (2) of the section 164;

(h) any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith;

(i) whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls;

(j) such other matters as may be prescribed.

Further, Rule 11 of the Companies (Audit and Auditors) Rules, 2014 prescribes the other matters to be included in auditor's report. The auditor's report shall also include their views and comments on the following matters, namely:-

(i) whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;

(ii) whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts;

(iii) whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.

11. (a) (1) Advances to DOT COM Companies

(i) Evaluate the efficacy of internal control system in general to ascertain

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whether an advance is made only after satisfying itself as to the credit worthiness of the borrower and after obtaining sanction from the appropriate authorities of the bank. The sanction for an advance must specify, among other things, the limit of borrowing, nature of security, margin to be kept, interest, terms of repayment, etc. Also see that all the necessary documents, e.g., agreements, demand promissory notes, letters of hypothecation, etc. have been executed by the parties before advances are made.

(ii) Examine loan documents such as certificate of commencement of business, resolution of board of directors, and resolution of shareholders.

(iii) Verify the business plan of the company especially where the revenue model is in place. Verify whether the company depends only on outside funding or can self generate funds.

(iv) Examine in case the security is in the form of mortgage, apart from mortgage deed (in the case of English Mortgage) or letter of intent to create mortgage (in the case of Equitable Mortgage), the evidence of registration of the charge with the Registrar of Companies.

(v) Review the operation of advance account to see that limit is not generally exceeded; that the account is not becoming stagnant; that the customer is not drawing against deposits which are not free from lien; that the account is not window-dressed by running down overdrafts at the year end and again drawing further advances in the new year, etc.

(vi) Examine whether there is a healthy turnover in the account. It should be seen that the frequency and the amounts of credits in the account are commensurate with the sanctioned limit and the nature and volume of business of the borrower. Any unusual items in the account should be carefully examined by the auditor. If the auditor's review indicates any unhealthy trends, the account should be further examined. The auditor's examination should also cover transactions in the post-balance sheet date period. Large transactions in major accounts particularly as at the year-end may be looked into to identify any irregularities in these accounts.

(vii) Review periodic statements, cash flow statements, latest financial statements, etc. to assess the recoverability of advances.

(viii) Verify whether the advance is secured and determine whether the security is legally enforceable, i.e., whether the necessary legal formalities regarding documentation, registration, etc., have been complied with; whether the security is in the effective control of the bank; and to what extent the value of the security, assessed realistically, covers the amount outstanding in the advance.

(ix) Ensure that proper provisioning norms have been applied in view of non-

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observance of terms, coupled with irregular payment of interest and default in repayment of instalments, if any.

(2) Balances in Account of a Bank situated in a Foreign Country

(i) Verify the ledger balances in each account with reference to the bank confirmation certificates and reconciliation statements as at the year-end.

(ii) Review the reconciliation statements and pay particular attention to the following.

(a) Examine that no debit for charges or credit for interest is outstanding and all the items which ought to have been taken to revenue for the year have been so taken. This should be particularly observed when the bills collected, etc., are credited with net amount and entries for commission, etc. are not made separately in the statement of account.

(b) Examine that no cheque sent or received in clearing is outstanding. As per the practice prevalent among banks, any cheques returned unpaid are accounted for on the same day on which they were sent in clearing or on the following day.

(c) Examine that all bills or outstanding cheques sent for collection and outstanding as on the closing date have been credited subsequently.

(iii) Examine the large transactions in inter-bank accounts, particularly towards the year-end, to ensure that no transactions have been put through for window-dressing.

(iv) Check original deposit receipts in respect of balances in deposit accounts in addition to confirmation certificates obtained from banks in respect of outstanding deposits.

(v) Check whether these balances are converted into the Indian currency at the exchange rates prevailing on the balance sheet date and ensure compliance with AS 11 on "The Effects of Changes in Foreign Exchange Rates".

(b) The items to be covered in the concurrent audit of advances of a bank are as follows:

(i) Ensure that loans and advances are sanctioned properly.

(ii) Verify whether the sanctions are in accordance with the delegated authority.

(iii) Ensure that securities and documents have been received and properly charged/registered.

(iv) Ensure that post disbursement supervision and follow up is proper.

(v) Verify whether there is any misuse of loans and advances and whether there

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are instances indicative of diversion of funds.

(vi) Check whether letters of credit issued by the branch are within the delegated power and ensure that they are genuine trade transactions.

(vii) Check bank guarantees issued are properly worked and recorded.

(viii) Ensure proper follow up of overdue bills of exchange.

(ix) Verify the classifications of advances are as per RBI directions.

(x) Verify whether the submission of claims to DICGC and ECGC is in time.

(xi) Verify the instances of exceeding delegated powers have been promptly reported.

(xii) Verify the frequency and genuineness of such exercise of authority beyond to delegated powers of the concerned officials.

12. Verification of Re-insurance outward : The following steps may be taken by the auditor in the verification of re-insurance outward;

(i) The auditor should verify that re-insurance underwriting returns received from the operating units regarding premium, claims paid, outstanding claims tally with the audited figures of premium, claims paid and outstanding claims.

(ii) The auditor should check whether the pattern of re-insurance underwriting for outward cessions fits within the parameters and guidelines applicable to the relevant year.

(iii) The auditor should also check whether the cessions have been made as per the stipulation applicable to various categories of risk.

(iv) The auditor should verify whether the cessions have been made as per the agreements entered into with various companies.

(v) It should also be seen whether the outward remittances to foreign re-insurers have been done as per the foreign exchange regulations.

(vi) It should also be seen whether the commission on cession has been calculated as per the terms of the agreement with the re-insurers.

(vii) The auditor should verify the computation of profit commission for various automatic treaty arrangements in the light of the periodical accounts rendered and in relation to outstanding loss pertaining to the treaty.

(viii) The auditor should examine whether the cash loss recoveries have been claimed and accounted on a regular basis.

(ix) The auditor should also verify whether the Claims Paid item appears in Outstanding Claims list by error. This can be verified at least in respect of major claims.

(x) He should see whether provisioning for outstanding losses recoverable on cessions have been confirmed by the re-insurers and in the case of major claims, documentary support should be insisted and verified.

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(xi) Accounting aspects of the re-insurance cession premium, commission receivable, paid claims recovered, and outstanding losses recoverable on cessions have to be checked.

(xii) The auditor should check percentage pattern of gross to net premium, claims paid and outstanding claims to ensure comparative justification.

(xiii) The auditor should also check that the re-insurers balance on cessions and whether the sub ledger balances tallies with the general ledger balances.

(xiv) The auditor should review the individual accounts to find out whether any balance requires provisioning / write off or write back.

(xv) He should verify whether the balances with re-insurers are supported by necessary confirmation obtained from them.

(xvi) He should verify whether opening outstanding claims not paid during the year find place in the closing outstanding claims vis-a-vis the reinsurance inwards outstanding losses recoverable on cessions appears in both opening and closing list. If not, the reason for the same should be analysed.

(xvii) Any major event after the Balance Sheet date which might have wider impact with reference to subsequent changes regarding the claim recovery both paid and outstanding and also re-insurance balances will need to be brought out suitably.

13. **Functions of Cost Auditor**: The Institute of Cost and Works Accountants of India has detailed the principal functions of a cost auditor by way of comparison with the functions of the auditor of financial accounts. The principal functions of cost auditor, according to the aforesaid Institute are the following:

(i) Inventory

(a) Is the size of the inventory adequate or excess compared with the production programme?

(b) Is the provision most economical?

(c) Does it ensure optimum order size?

(d) Does it take into account the storage cost on the one hand, and carrying cost on the other?

(e) Does it take note of lead time of the various items or groups of items?

(f) Does the receipt and issue system cause any bottle-neck in production?

(g) Does it involve too many forms and too much paper work?

(h) Is there any room for reduction of inventory cost consistent with production needs?

(i) Is the inventory as per the priced store ledger and as certified by the management physically correct?

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(j) Is the same amount of attention and care given to monies translated into material things like raw materials, stores and supplies of all kinds as given to liquid cash?

(k) Does the issue of raw materials make the production in accordance with the standard or schedule or otherwise or covered by authorised schedule?

(i) Is the expenditure of consumable stores within the standard? If not, why not?

(ii) Labour -

(a) Proper utilisation of labour and increase in productivity are now receiving attention, several productivity teams have emphasised importance of higher productivity. It is, therefore, essential to assess the performance efficiency of labour and compare it with standard performance, so that labour utilisation could be progressively improved. The labour force in Indian industries is generally very high compared to similar types of industries in other developed countries. Our aim should be to reach that level, though not immediately but over some time. A study of this nature would give an idea where the inefficiency lies so that timely and adequate steps could be taken to ensure maximum utilisation of labour to reduce labour cost.

(b) Cost of labour is allocated to different jobs with reference to time or job cards.

(iii) Overheads and indirect expenditure - The cost auditor will see and certify:

(a) that allocation of indirect expenditure over production, sales, and distribution is logical and correct;

(b) that compared with the value of production in a production shop, overhead charges are not excessive;

(c) that actual indirect expenditure does not exceed budgets or standard expenditure significantly and that any variations are satisfactorily explained and accounted for;

(d) that the relation of indirect expenditure in keeping with the load on individual production shop is appropriate;

(e) correctness of appropriate allocation of overhead expenditure (both production and sales) will be certified by the cost auditor;

(f) that allocation of overheads between finished products and unfinished products is in accordance with correct principles.

(iv) Work-in Progress - The Cost Auditor will see the following:

(a) that work-in-progress has been physically verified and that it agrees with the balance in the incomplete cost card;

(b) that valuation of the work-in-progress is correct with reference to stage of completion of each job or process and the value job cost cards or process cost sheet;

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(c) that there is no over-valuation or under-valuation of opening work-in-progress or closing work-in-progress, thereby artificially pushing up and down net profits or net assets as the case may be;

(d) that the volume and value of work-in-progress is not disproportionate compared with the finished out-turn.

14. (a) Overdue interest: Overdue interest should be excluded from interest outstanding and accrued due while calculating profit. Overdue interest is interest accrued or accruing in accounts, the amount of which the principal is overdue. In practice an overdue interest reserve is created and the credit of overdue interest credited to interest account is reduced.

(b) Compliance with provisions of the Act and Rules: An auditor of a co-operative society is required to point out the infringement with the provisions of the relevant Co-operative Act Rules and bye-laws. The auditor of a co-operative society is also required to point out various irregularities, improprieties, and departure from the provision of the Act, rules framed thereunder and the bye-laws of the society. The financial implications of such infringements should be properly assessed and quantified by the auditor and they should be reported. Some of the State laws contain restrictions on the payment of dividends, which should be noted by the auditor and if dividend is declared in excess of the prescribed percentage, the fact should be reported by the auditor. Auditor should also ensure that various provisions in the Co-operative Societies Act, such as, restriction on borrowings, investment of funds, contribution to education funds, restriction on loans, etc are also complied with.

(c) Special Report to the Registrar: The auditors are required to report on number of matters as prescribed in various states. In addition to the main report, the auditors are also required to submit by way of schedules/audit memorandum information on the working of the company as well. During the course of audit, if the auditor notices that there are some serious irregularities in the working of the society he may report these special matters to the Registrar, drawing his specific attention to the points. The Registrar on receipt of such a special report may take necessary action against the society. In the following cases, for instance a special report may become necessary:

(i) Personal profiteering by members of managing committee in transactions of the society, which are ultimately detrimental to the interest of the society.

(ii) Detection of fraud relating to expenses, purchases, property and stores of the society.

(iii) Specific examples of mis-management. Decisions of management against co-operative principles.

(iv) In the case of urban co-operative banks, disproportionate advances to vested interest groups, such as relatives of management, and deliberate negligence

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about the recovery thereof. Cases of reckless advancing, where the management is negligent about taking adequate security and proper safeguards for judging the credit worthiness of the party.

15. (a) The provisions relating to tax audit under section 44AB of the Income Tax Act, 1961 applies to every person carrying on business, if his total sales, turnover or gross receipts in business exceed the prescribed limit of ₹ 1 crore (w.e.f. A.Y. 2013-14) and to a person carrying on a profession, if his gross receipts from profession exceed the prescribed limit of ₹ 25 lakhs (w.e.f. A.Y. 2013-14) in any previous year. However, the term "sales", "turnover" or "gross receipts" are not defined in the Act, and therefore the meaning of the aforesaid terms has to be considered for the applicability of the section.

Some of the merit consideration in this regard as discussed in the Guidance Note issued by the Institute are given below-

(i) Discount allowed in the sales invoice will reduce the sale price and, therefore, the same can be deducted from the turnover.

(ii) Cash discount otherwise than that allowed in a cash memo/sales invoice is in the nature of a financing charge and is not related to turnover. Therefore, should not be deducted from the turnover.

(iii) Turnover discount is normally allowed to a customer if the sales made to him exceed a particular quantity. As per trade practice, it is in the nature of trade discount and should be deducted from the figure.

(iv) Special rebate allowed to a customer can be deducted from the sales if it is in the nature of trade discount. If it is in the nature of commission on sales, the same cannot be deducted from the figure of turnover.

(v) Price of goods returned should be deducted from the turnover even if the returns are from the sales made in the earlier year/s.

(vi) Sale proceeds of any shares, securities, debentures, etc., held as investment will not form part of turnover. However if the shares, securities, debentures etc., are held as stock-in-trade, the sale proceeds thereof will form part of turnover.

In the given case, Concession Ltd. is engaged in manufacturing business. Therefore, the tax audit would be applicable if the turnover exceeds ₹ 1 crore during the financial year 2013-14. The calculation of effective turnover for the prescribed limit purpose, in accordance with abovementioned conditions, is given below:

Recorded turnover during the year	₹ 1,13,00,000
Less: (i) Discount allowed in the Sales Invoice	(₹ 8,20,000)
(ii) Trade discount	(₹ 2,90,000)
(iii) Sales Return	(₹ 1,60,000)
Effective turnover	₹ 1,00,30,000

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The effective turnover of Concession Ltd. is Rupees one crore and thirty thousand only which is over and above the prescribed limit for tax audit under section 44AB of the Income tax Act, 1961. Thus, the provisions related to tax audit are applicable to the company and is therefore liable for tax audit.

(b) Clause 18 of form 3CD, annexed to the tax audit report in Form 3CA/3CB, requires the tax auditor to specify particulars of payments made to person specified undersection 40(A)(2)(b) of the Income Tax Act 1961. Persons specified in the said section are relatives of an assessee and sister concerns, etc. In the instant case, however, Mr. Verma has not made any payments to his brother. On the contrary, he must have received payments from him against exports made and, thus, this clause would be required to verify whether the exports are genuine, i.e. , whether the diamonds have been delivered by verifying the necessary delivery documents, relevant invoices, etc., the reasonableness of the price and whether the export realization have been received.

16. NBFC Public Deposit Directions - The auditors must ascertain whether the company is a loan company or an investment company or a hire purchase finance company or an equipment leasing company as per the classification, if any, assigned to the NBFC by the RBI. In case, the NBFC has not been classified by the RBI, the classification of a company will have to be determined after a careful consideration of various factors such as particulars of earlier registration granted, if any, particulars furnished in the application form for registration, company's Memorandum of Association and its financial results. Thereafter, it must be ascertained whether the company has complied with the following aspects in relation to the activity of mobilisation of public deposits.

(i) The ceiling on quantum of public deposits has been linked to its credit rating as given by an approved credit rating agency. Obtain a copy of the credit rating assigned to NBFC and check whether the public deposits accepted/held by it are in accordance with the level of credit rating assigned to it.

In the event of a downgrading of credit rating, the auditor should bear in mind that the NBFC will have to reduce its public deposits in accordance with the revised credit rating assigned to it within a specified time frame.

(ii) Test checks the interest calculations in respect of public deposits mobilised by a NBFC to ascertain that the NBFC has not paid interest in excess as per specification. Likewise, test check the brokerage calculations with the bills and vouchers for reimbursement of out of pocket expenses submitted by a broker to ascertain that the NBFC has not paid brokerage in excess by way of reimbursement of expenses to brokers.

(iii) Ascertain whether the NBFC has accepted or renewed any public deposit only after a written application form the depositor in the form to be supplied by the company, and shall contain all particulars specified in the Non-Banking Financial Companies and Miscellaneous Non Banking Companies (Advertisement) Rules, 1977.Further

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ensure whether it contain the specific category of depositor, i.e., whether depositor is a shareholder or a director or a promoter or a member of public.

(iv) Verify the deposit register maintained by a NBFC and test check the particulars that have been entered therein in respect of each depositor with supporting receipts issued to the depositors. Also check whether the NBFC is regularly paying its deposits on due dates and in the case of a delay/default, the reasons for the delay/default and the actual date of payment.

(v) Check whether the investments made in approved liquid assets by a NBFC holding public deposits have been lodged in safe custody with a designated scheduled commercial bank as required by the NBFC Public Deposit Directions. Obtain a certificate from the bank to that effect.

(vi) In the case of NBFCs accepting/holding public deposits ascertain whether audited statement of accounts together with a copy of the auditor's report and director's report thereon have been submitted within prescribed time limit from the date of holding the Annual general meeting.

(vii) Check whether the NBFC has filed its annual return as specified in the First Schedule before the 30th June with reference to its position as on the 31st March of each year.

(viii) In the case of NBFCs not accepting/holding public deposits, check whether a board resolution has been passed by the NBFC to the effect that it has neither accepted any public deposits nor would it accept any public deposits during the year.

(ix) In the case of Group Holding Investment Companies, check whether the NBFC has passed a board resolution to the effect that the company has invested or would invest/hold its investments in share and securities of group companies specifying the names of the companies. In addition to the above, group holding investment companies are required to give a further undertaking that it would not trade in such shares/securities and that it has neither accepted nor would it accept any public deposits during the year.

17. (a) Applicability of Provisions of Internal Audit : As per section 138 of the Companies Act, 2013, read with rule 13 of Companies (Audit and Auditors) Rules, 2014 every private company shall be required to appoint an internal auditor or a firm of internal auditors, having-

(i) turnover of two hundred crore rupees or more during the preceding financial year; or

(ii) outstanding loans or borrowings from banks or public financial institutions exceeding one hundred crore rupees or more at any point of time during the preceding financial year;

Thus, either of the condition is required to be satisfied for the applicability of the provision. The internal auditor to be appointed shall either be a chartered accountant whether engaged in practice or not or a cost accountant, or such other

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professional as may be decided by the Board to conduct internal audit of the functions and activities of the companies auditor may or may not be an employee of the company.

Interior Pvt. Ltd. is having turnover of ₹ 210 crore and maximum outstanding loan from public financial institution of ₹ 90 crore during the previous financial year. Here in the case, the turnover is over and above two hundred crore rupees i.e. either of the condition in respect of turnover or outstanding loans is satisfied. Therefore the company is liable for internal audit as per section 138 of the Companies Act, 2013.

(b) The external auditor's general evaluation of the internal audit function will assist him in determining the extent to which he can place reliance upon the work of the internal auditor. The external auditor should document his evaluation and conclusions in this respect. The important aspects to be considered in this context are:

(i) **Organisational Status -** Whether internal audit is undertaken by an outside agency or by an internal audit department within the entity itself, the internal auditor reports to the management. In an ideal situation he reports to the highest level of management and is free of any other operating responsibility. Any constraints or restrictions placed upon his work by management should be carefully evaluated. In particular, the internal auditor should be free to communicate fully with the external auditor.

(ii) **Scope of Function -** The external auditor should ascertain the nature and depth of coverage of the assignment which the internal auditor discharges for management. He should also ascertain to what extent the management considers, and where appropriate, acts upon internal audit recommendations.

(iii) **Technical Competence -** The external auditor should ascertain that internal audit work is performed by persons having adequate technical training and proficiency. This may be accomplished by reviewing the experience and professional qualifications of the persons undertaking the internal audit work.

(iv) **Due Professional Care -** The external auditor should ascertain whether internal audit work appears to be properly planned, supervised, reviewed and documented. An example of the exercise of due professional care by the internal auditor is the existence of adequate audit manuals, audit programmes and working papers.

18. A due diligence audit on behalf of C Ltd. with a view to acquiring the business shall involve following steps:

(a) **Brief history of the target and background of its promoters -** The accountant should begin the financial due diligence review by looking into the history of the company and the background of the promoters. The details of how the company was set up and who were the original promoters have to be gone into, before verification of financial data in detail. An eye into the history of the target may reveal

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its turning points, survival strategies adopted by the target from time to time, the market share enjoyed by the target and changes therein, product life cycle and adequacy of resources. It could also help the accountant in determining whether, in the past, any regulatory requirements have had an impact on the business of the target. Broadly, the accountant should make relevant enquiries about the history of target's business products, markets, suppliers, expenses, operations

(b) **Accounting policies -** The accountant should study the accounting policies being followed by the target and ascertain whether any accounting policy is inappropriate. The accountant should also see the effects of the recent changes in the accounting policies. The target might have changed its accounting policies in the recent past keeping in view its intention of offering itself for sale. The overall scope has to be based on the accounting policies adopted by the management. The accountant has to look at the main effect of accounting policies on the overall profitability and their correctness. It is reiterated that the accountant should mainly look at all material changes in Accounting Policies in the period subjected to review very carefully.

The accountant's report should include a summary of significant accounting policies used by the target, that changes that have been made to the accounting policies in the recent past, the areas in which accounting policies followed by the target are different from those adopted by the acquiring enterprise, the effect of such differences.

(c) **Review of Financial Statements -** Before commencing the review of each of the aspect covered by the financial statements, the accountant should examine whether the financial statements of the target have been prepared in accordance with the Statute governing the target, Framework for Preparation and Presentation of the Financial Statements and the relevant Accounting Standards. If not the accountant should record the deviations from the above and consider whether it warrant an inclusion in the final report on due diligence.

After having an overall view of the financial statements, as mentioned in the above paragraphs, the accountant should review the operating results of the target in great detail. It is important to make an evaluation of the profit reported by the target. The reason being the price of the target would be largely based upon its operating results. The accountant should consider the presence of an extraordinary item of income or expense that might have affected the operating results of the target. It is advisable to compare the actual figures with the budgeted figures for the period under review and those of the previous accounting period.

(d) **Taxation -** Tax due diligence is a separate due diligence exercise but since it is an integral component of the financial status of a company, it is generally included in the financial due diligence. It is important to check if the company is regular in paying various taxes to the Government. Generally taxes are levied both by the

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Central Government as well as by the State Government. Further taxes may be direct or indirect. Most of the tax laws require the enterprise to register itself with the government and it is important to check if all necessary registrations have been made. The accountant has to also look at the tax effects of the merger or acquisition.

(e) Cash Flow - A review of historical cash flows and their pattern would reflect the cash generating abilities of the target company and should highlight the major trends. It is important to know if the company is able to meet its cash requirements through internal accruals or does it have to seek external help from time to time. It is necessary to check if a) Is the company able to honour its commitments to its creditors, to the banks, to government and other stakeholders b) How well is the company able to turn its debtors and stocks c) How well does it deploy its funds d) Are there any funds lying idle or is the company able to reap maximum benefits out of the available funds?

(f) Financial Projections - The accountant should obtain from the target company the projections for the next five years with detailed assumptions and workings. He should ask the targets to give projections on optimistic, pessimistic and most likely bases.

Ordinarily, it would be desirable that the accountant evaluates the appropriateness of assumption used in the preparation and presentation of financial projections. If, the accountant is of the opinion that as assumption used by the target is unrealistic, the accountant should consider its impact on the overall valuation of the company. He should offer his comments on all the assumption, highlighting those which, in his opinion are not inappropriate. In case he feels the projections provided by the target are not achievable or aggressive he has to mention this in his report. He should thoroughly check the arithmetic of the calculations made for financial projections.

(g) Management and Employees - In the Indian context, the status of work force, staff and employees and their demands is a complex problem. In most of the companies which are available for take over the problem of excess work force is often witnessed. It is important to work out how much of the labour force has to be retained. It is also important to judge the job profile of the administrative and managerial staff to gauge which of these match the requirements of the new incumbents. Due to complex set of labour laws applicable to them, companies often have to face protracted litigation from its workforce and it is important to gauge the likely impact of such litigation.

It is important to see if all employee benefits like Provident Fund (P.F.), Employees State Insurance (E.S.I), Gratuity, leave and Superannuation have been properly paid/ provided for/funded. In case of un-funded Gratuity, an actuarial valuation of

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the liability has to be obtained from a reputed actuary. The assumptions regarding increase in salaries, interest rate, retirement etc. have to be gone into to see if they are reasonable. It is also necessary to see if the basic salary /wage considered for the valuation is correct and includes all elements subject to payment of Gratuity. In the case of PF, ESI etc. the accountant has to see if all eligible employees have been covered.

It is very important to consider the pay packages of the key employees as this can be a crucial factor in future costs. One has to carefully look at Employees Stock Option Plans; deferred compensation plans; Economic Value Addition and other performance linked pay; sales incentives that have been promised etc. It is also important to identify the key employees who will not continue after the acquisition either because they are not willing to continue or because they are to be transferred to another company within the 'group' of the target company.

(h) **Statutory Compliance -** During a due diligence this is one aspect that has to be investigated in detail. It is important therefore, to make a list of laws that are applicable to the entity as well as to make a checklist of compliance required from the company under those laws. If the company has not been regular in its legal compliance it could lead to punitive charges under the law. These may have to be quantified and factored into the financial results of the company.

In addition to the above steps, the following further points have to be seen:

(i) Reason for sale of business and the effect on turnover and profits due to the exist of the present proprietor.

(ii) The length of the lease under which business has been operating.

(iii) The unexpired period of patents if any held by the vendors.

(iv) The age of managerial staff and prospects of their continuing in service in the new environment; the effect of trained managerial staff learning the organisation in production/sales/administrative and the financial liability to pay terminal benefits/ compensation, etc.

(v) If bulk sales are to a few limited customers, the profitability should be discounted greatly, because any substantial withdrawal of customers might cause business crashes.

(vi) A company with a sound financial structure can better withstand the stresses and strains of business. A low debt-equity ratio would indicate an ability to grow through debt financing without raising equity.

(vii) The cash generated from operations; the need for redeployment of resources and funds needed for repayment of loans become major factors in determining growth potential.

(viii) The valuation of goodwill if any should be on reasonable basis having regards to all factors mentioned above.

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19 **(a)** As per clause 6 of Part I of First Schedule to the Chartered Accountants Act, a chartered accountant in practice is deemed to be guilty of professional misconduct, if he solicit clients or professional work either directly or indirectly by circular, advertisement, personal communication or interview or by any other means.

However, nothing herein contained shall be construed as preventing or prohibiting, any chartered accountant from applying or requesting for or inviting or securing professional work from another chartered accountants in practice.

In the instant case, CA N has written email to all the CA for securing professional work from them and has not approached any other person or professional or communicated with any client,

Thus as per exception to the clause 6, CA N is well within the regulation of the act and has not committed any professional misconduct.

(b) As per clause 8 of Part I of First Schedule to the Chartered Accountants Act, a chartered accountant in practice is deemed to be guilty of professional misconduct, if he accepts a position as auditor previously held by another chartered accountant or a certified auditor who has been Issued certificate under the Restricted Certificate Rules, 1932 without first communicating with him in writing.

This clause is applicable in situation of replacing of one auditor by another auditor. Internal auditor and statutory audition are parallel positions and not replacement positions. The management generally appoints the internal auditor whereas the statutory auditor will be appointed by the shareholders in the AGM. In this situation there is no need for communication by one to other.

In view of above the contention of the statutory auditor is unacceptable and there is no question of communicating in writing by Mr. T.

(c) Clause 10 of Part I of Second Schedule states that a Chartered Accountant shall be deemed to be guilty of professional misconduct if "he fails to keep money of his clients in separate banking account or to use such money for the purpose for which they are intended."

Mr. Ram received the money on 15th December, 2013 which is to be paid to the client only on March 31, 2014. Hence, it should be deposited in a separate bank account.

Since in this case Mr. Ram have failed to keep the sum of ₹ 15 lakhs in a separate Bank Account and utilised the part money for personal purpose on birthday occasion. Therefore, it amounts to professional misconduct under clause 10 of part I of Second Schedule.

Connected case Law: *Mr. R. S. Murugai Vs. (1) S K Gadh & (2) V. K. Bajaj*

(d) Chapter V of the Council General Guidelines, 2008 specifies that a member of the Institute in practice or the firm of Chartered Accountants of which he is a partner

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shall maintain and keep in respect of his/its professional practice, proper books of accounts including the following:

(i) a Cash Book

(ii) a Ledger

Thus, a Chartered Accountant in practice is required to maintain books of accounts. In the instant case, CA Smart does not maintain books of accounts and writes the fees received from various clients in small pocket diary. A small pocket diary maintained by him cannot be books of accounts.

Hence, Mr. Smart, being a practicing Chartered Accountant will be held guilty for professional misconduct for violation of Council General Guidelines, 2008.

20. (a) Constitution of Audit Committee: As per the section 177 of the Companies Act, 2013, every listed company and the following classes of companies shall constitute an Audit Committee -

(i) all public companies with a paid up capital of ten crore rupees or more;

(ii) all public companies having turnover of one hundred crore rupees or more;

(iii) all public companies, having in aggregate, outstanding loans or borrowings or debentures or deposits exceeding fifty crore rupees or more.

Explanation.- The paid up share capital or turnover or outstanding loans, or borrowings or debentures or deposits, as the case may be, as existing on the date of last audited Financial Statements shall be taken into account for the purposes of this rule.

Where a company is required to constitute an Audit Committee under section 177, all appointments, including the filling of a casual vacancy of an auditor under this section shall be made after taking into account the recommendations of such committee.

(b) Areas Covered by Comprehensive Audit :The areas covered by comprehensive audit are those of investment decisions, project formulation and management, organisation, delegation of powers and management information systems, organisational effectiveness, capacity utilisation, management of equipment, plant and machinery, production performance, use of materials, productivity of labour, idle capacity, costs and prices, development of complementary ancillary small scale industries, materials management, sales and credit control, budgetary and internal control systems, etc. The areas covered in comprehensive audit will naturally vary from enterprise to enterprise depending on the nature of the enterprise, its objectives and operations. Some of the broad areas are listed below:

- Comparison of overall capital cost of the project with the approved planned costs.

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- Production or operational outputs vis-a-vis under-utilisation of the installed capacity.
- Systems of project formulation and implementation.
- Planned rate of return
- Cost control measures.
- Research and development programmes.
- System of repairs and maintenance.
- adequate purchase policies
- Effective and economical procedures
- Project planning
- Undue waste, unproductive time for men and machines, wasteful utilisation or even non-utilisation of resources

(c) **Sauda Book**: All members are required to maintain a 'Sauda Book', which contains details of all deals transacted by them on a day to day basis. This is a basic record, which each member is required to maintain regularly on day-to-day basis. It contains the details regarding the name of the code of the client on whose behalf the deals have been done, rate and quantity of bought or sold. These details are maintained date wise. This register contains all the transactions, which may be of any of the kind mentioned below:

(i) member's own business on the Exchange

(ii) member's business on the Exchange on behalf of clients

(iii) member's business with the clients on principal-to-principal basis

(iv) member's business with the members of other Stock Exchanges

(v) member's business on behalf of his clients with the members of other Stock Exchanges

(vi) Spot transactions, etc

(d) **Appointment of Auditor:** Section 139 of the Companies Act, 2013 contains provisions regarding Appointment of Auditors. Discussion on appointment of auditors may be grouped under two broad headings-

(i) Appointment of First Auditors.

(ii) Appointment of Subsequent Auditors.

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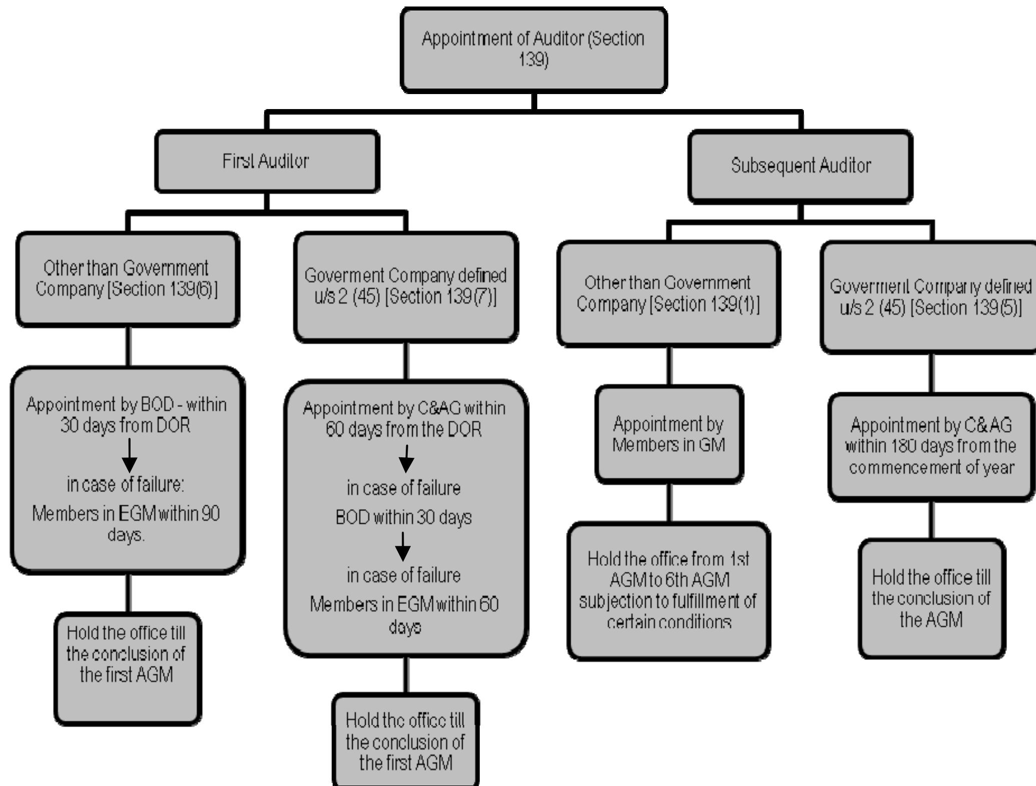

(i) Appointment of First Auditor

(1) Appointment of First Auditor in the case of a company, other than a Government Company: As per Section 139(6), the first auditor of a company, other than a Government company, shall be appointed by the Board of Directors within 30 days from the date of registration of the company.

In the case of failure of the Board to appoint the auditor, it shall inform the members of the company.

The members of the company shall within 90 days at an extraordinary general meeting appoint the auditor. Appointed auditor shall hold office till the conclusion of the first annual general meeting.

(2) Appointment of First Auditor in the case of Government Company: Section139 (7) provides that in the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government, or Governments, or partly by the Central Government and partly by one or more State Governments,

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the first auditor shall be appointed by the Comptroller and Auditor-General of India within 60 days from the date of registration of the company.

In case the Comptroller and Auditor-General of India does not appoint such auditor within the above said period, the Board of Directors of the company shall appoint such auditor within the next 30 days. Further, in the case of failure of the Board to appoint such auditor within next 30 days, it shall inform the members of the company who shall appoint such auditor within 60 days at an extraordinary general meeting. Auditors shall hold office till the conclusion of the first annual general meeting.

(ii) Appointment of Subsequent Auditor/Reappointment of Auditor

(1) Appointment of Subsequent Auditor in case of Non Government Company: Section139(1) of the Companies Act, 2013 provides that every company shall, at the first annual general meeting appoint an individual or a firm as an auditor who shall hold office from the conclusion of that meeting till the conclusion of its sixth annual general meeting and thereafter till the conclusion of every sixth meeting.

The following points need to be noted in this regard-

(i) The company shall place the matter relating to such appointment of ratification by member at every Annual General Meeting.

(ii) Before such appointment is made, the written consent of the auditor to such appointment, and a certificate from him or it that the appointment, if made, shall be in accordance with the conditions as may be prescribed, shall be obtained from the auditor.

(iii) The certificate shall also indicate whether the auditor satisfies the criteria provided in section 141.

(iv) The company shall inform the auditor concerned of his or its appointment, and also file a notice of such appointment with the Registrar within 15 days of the meeting in which the auditor is appointed.

(2) Appointment of Subsequent Auditor in case of Government Company: As per Section 139(5), in the case of a Government company or any other company owned or controlled, directly or indirectly, by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, the Comptroller and Auditor-General of India shall, in respect of a financial year, appoint an auditor duly qualified to be appointed as an auditor of companies under this Act, within a period of 180 days from the commencement of the financial year, who shall hold office till the conclusion of the annual general meeting.

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(e) **Collection of Evidence by Peer Reviewer:** A Peer Reviewer collects evidence by applying the following methods:

(a) Inspection mainly consists of examination of documentation (working papers) and other records maintained by the practice unit.

(b) Observation consists of witnessing a procedure or process being performed by others. For example, while conducting on-site review, the reviewer may review the performance of internal control.

(c) Inquiry consists of seeking appropriate information from the partner (designated by the practice unit for the purpose)/sole proprietor or other knowledgeable persons within the practice unit. The inquiries may originate from the responses to the questions given in the questionnaire. The inquiries may also arise from the inspection of documentation maintained by the practice unit.

While observation and inquiry may be considered as external independent sources of review evidence, inspection remains the most significant method for confirming the effective observance of control procedures in the practice unit. Observation and inquiry may also corroborate the evidence provided by inspection. The reviewer, in order to carry out the review effectively, should have an understanding of the documentation maintained by the practice unit.

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III. Applicability of the Companies Act, 2013

1. Accounting related sections of the Companies Act, 2013, notified in Sept, 2013, along with the clarifications issued by the Ministry of Corporate Affairs are applicable for Nov. 14 Examination.
2. Notified Sections of Chapter IX of the Companies Act, 2013 along with relevant Rules will be applicable for November, 2014 Examination.

Paper 3: Advanced Auditing and Professional Ethics

I. Statements and Standards

1. Statement on Reporting under Section 227(1A) of the Companies Act, 1956
2. Statement on the Companies (Auditor's Report) Order, 2003*
3. Framework for Assurance Engagements.

Note : *Statement on CARO, 2003 is applicable on Financial Statements prepared on or before March 31, 2014.

II. Engagements and Quality Control Standards on Auditing

S.No	*SA*	*Title of Standard on Auditing*
1	SQC 1	Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements
2	SA 200	Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Standards on Auditing
3	SA 210	Agreeing the Terms of Audit Engagements
4	SA 220	Quality Control for Audit of Financial Statements
5	SA 230	Audit Documentation
6	SA 240	The Auditor's responsibilities Relating to Fraud in an Audit of Financial Statements
7	SA 250	Consideration of Laws and Regulations in An Audit of Financial Statements
8	SA 260	Communication with Those Charged with Governance
9	SA 265	Communicating Deficiencies in Internal Control to Those Charged with Governance and Management
10	SA 299	Responsibility of Joint Auditors
11	SA 300	Planning an Audit of Financial Statements
12	SA 315	Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment

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13	SA 320	Materiality in Planning and Performing an Audit
14	SA 330	The Auditor's Responses to Assessed Risks
15	SA 402	Audit Considerations Relating to an Entity Using a Service Organization
16	SA 450	Evaluation of Misstatements Identified during the Audits
17	SA 500	Audit Evidence
18	SA 501	Audit Evidence - Specific Considerations for Selected Items
19	SA 505	External Confirmations
20	SA 510	Initial Audit Engagements-Opening Balances
21	SA 520	Analytical Procedures
22	SA 530	Audit Sampling
23	SA 540	Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures
24	SA 550	Related Parties
25	SA 560	Subsequent Events
26	SA 570	Going Concern
27	SA 580	Written Representations
28	SA 600	Using the Work of Another Auditor
29	SA 610	Using the Work of Internal Auditors
30	SA 620	Using the Work of an Auditor's Expert
31	SA 700	Forming an Opinion and Reporting on Financial Statements
32	SA 705	Modifications to the Opinion in the Independent Auditor's Report
33	SA 706	Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report
34	SA 710	Comparative Information – Corresponding Figures and Comparative Financial Statements
35	SA 720	The Auditor's Responsibility in Relation to Other Information in Documents Containing Audited Financial Statements
36	SA 800	Special Considerations-Audits of Financial Statements Prepared in Accordance with Special Purpose Framework
37	SA 805	Special Considerations-Audits of Single Purpose Financial Statements and Specific Elements, Accounts or Items of a Financial Statement
38	SA 810	Engagements to Report on Summary Financial Statements

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39	SRE 2400	Engagements to Review Financial Statements
40	SRE 2410	Review of Interim Financial Information Performed by the Independent Auditor of the Entity
41	SAE 3400	The Examination of Prospective Financial Information
42	SAE 3402	Assurance Reports on Controls At a Service Organisation
43	SRS 4400	Engagements to Perform Agreed Upon Procedures Regarding Financial Information
44	SRS 4410	Engagements to Compile Financial Information

III. Guidance Notes and other publications

1. Code of Ethics
2. Guidance Note on Independence of Auditors.
3. Guidance Note on Audit Reports and Certificates for Special Purposes.
4. Guidance Note on Audit under Section 44AB of the Income-tax Act.
5. Guidance Note on Audit of Abridged Financial Statements.
6. Guidance Note on Audit of Inventories.
7. Guidance Note on Audit of Debtors, Loans and Advances.
8. Guidance Note on Audit of Investments.
9. Guidance Note on Audit of Miscellaneous Expenditure.
10. Guidance Note on Audit of Cash and Bank Balances.
11. Guidance Note on Audit of Liabilities.
12. Guidance Note on Audit of Revenue.
13. Guidance Note on Audit of Expenses.
14. Guidance Note on Sections 227(3)(e) and (f) of the Companies Act, 1956.
15. Guidance Note on Certificate of Corporate Governance
16. Guidance Note on Computer Assisted Audit Techniques (CAATs).
17. Guidance Note on Audit of Payment of Dividend.
18. Guidance Note on Audit of Capital and Reserves.
19. Guidance Note on Auditing of Accounts of Liquidators.

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PAPER – 4: CORPORATE AND ALLIED LAWS

PART – I : RELEVANT AMENDMENTS APPLICABLE FOR NOVEMBER, 2014

Applicability of relevant Amendments/Circulars/Notifications/Regulations etc.

1. The Companies Act, 2013

(i) 45 sections of the Companies Act, 2013 along with the clarifications notified by the Ministry of Corporate Affairs (MCA).

Supplementary study material in this regard has been hosted on the student portal, ICAI at the following link http://220.227.161.86/32793ssp-p4final.pdf

(ii) Notified sections of Chapter IX: Accounts of Companies and Chapter X: Audit and Auditors of the Companies Act, 2013 along with its relevant Rules and clarifications notified by the MCA.

Supplementary study material in this regard has been hosted on the student portal, ICAI at the following link http://220.227.161.86/33649bos23281.pdf

(Hard copy of the supplementary study material is also available).

2. SEBI (Issue of Capital and Disclosure Requirement) Regulations, 2009

SEBI vide Notification dated 4th February, 2014 has issued SEBI (Issue of Capital and Disclosure Requirements) (Amendment) Regulations, 2014 which is available at the following link http://www.sebi.gov.in/cms/sebi_data/attachdocs/1391509221289.pdf

3. The Foreign Exchange Management Act, 1999

(i) The Reserve Bank of India has issued a circular dated 9th January, 2014 on Section 6 of the Foreign Exchange Management Act, 1999 which is available at the following link http://rbi.org.in/scripts/BS_CircularIndexDisplay.aspx?Id=8685

(ii) The Reserve Bank of India has issued a circular dated 4th April, 2014 on Compounding of Contraventions under FEMA, 1999 and decided to delegate further powers to the Regional Offices of Reserve Bank of India. The circular is available at the following link

http://rbidocs.rbi.org.in/rdocs/notification/PDFs/553APD04042014.pdf

Non-Applicability of the following Amendments/Circulars/Notifications

S. No.	Subject Matter
1.	* New 184 sections of the Companies Act, 2013 notified on 27th February, 2014 and 26th March, 2014 with effect from 1st April, 2014.
2.	* Rules notified under the Companies Act, 2013
3.	Provisions relating to Revival and Rehabilitation of Sick-Industrial Companies

***Out of above 184 sections of the Companies Act, 2013 along with its Rules, notified sections of Chapter IX: Accounts of Companies and Chapter X: Audit and Auditors of the Companies Act, 2013 along with its relevant Rules are also applicable for November 2014 examinations.**

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PART – II: QUESTIONS AND ANSWERS

QUESTIONS

SECTION – A: COMPANY LAW

Accounts

1. (a) SRL Ltd. is having its registered office in the city of Jaipur, has its manufacturing plant (Factory) located in the industrial area of New Delhi. The Board wants to keep all its books of accounts at New Delhi (Factory) instead of the registered office. Kindly advise as per the provisions of the Companies Act, 2013, can the Board of Directors do so?

   (b) With reference to provisions laid down under the Companies Act, 2013, advice on the following:

   (i) Which Company is required to constitute CSR (Corporate Social Responsibility) committee?

   (ii) Minimum amount of contribution towards CSR?

   (iii) Activities which are not considered as CSR activities?

Audit

2. (a) M/s Krishna & Associates is an audit firm having 2 partners namely Mr. Krishna and Mr. Shyam. Mr. Shyam is also a partner of another audit firm named M/s Kukreja & Associates. M/s Krishna & Associates was appointed as the auditors in the company Golden Smith Ltd. for two consecutive periods i.e. from year 2014 to year 2024. Advice, whether Golden Smith Ltd. can appoint M/s Kukreja & Associates as its audit firm as per the provisions of the Companies Act, 2013?

   (b) Mr. A, a Chartered accountant is an auditor of Laxman Ltd. Subsequently, from 1st June, 2014, he has started to render actuarial services to Laxman Ltd. Advice the company keeping in view the provisions of the Companies Act, 2013.

Dividend

3. The Annual General Meeting of Bhaskar Electronics Limited declared a dividend at the rate of 30 percent payable on paid up equity share capital of the Company as recommended by Board of Directors on 30th April, 2014. But the Company was unable to post the dividend warrant to Mr. Sanjay, an equity shareholder of the Company, up to 30th June, 2014. Mr. Sanjay filed a suit against the Company for the payment of dividend along with interest at the rate of 20 percent per annum for default period. Decide in the light of provisions of the Companies Act, 2013, whether Mr. Sanjay would succeed? Also state the directors' liability in this regard under the Act.

Directors

4. (a) Flora Construction Limited in its General Meeting appointed all its directors by passing one single resolution. No objection was made to the resolution. Examine

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the validity of appointment of directors explaining the relevant provisions of the Companies Act, 2013.

(b) Mr. Nishant, who does not hold any shares in his name, is appointed as Director in MKT Paper Limited on 1st April, 2014. His wife holds 10,000 Equity Shares in the company in her name singly. Certain members of the company objects to Mr. Nishant's appointment on the ground that since he does not hold any shares in his own name, his appointment is violative of the provisions of the Companies Act, 1956. Articles of the company are silent on the issue of holding any shares by a Director.

Examine the provisions of the Act and decide:

(i) Whether contention of the members is tenable?

(ii) Whether Mr. Nishant wife's shareholding in the company can be the ground for Mr. Nishant continuation as a director in the company?

(iii) What would be your answer in case Mr. Nishant is one of the subscribers of the Memorandum of Association?

5. (a) Mr. Swastik was appointed as a director at the Annual General Meeting of Bhanu Textiles Limited held on 30th September, 2013 and he carried on his duties and functions as a director. In the month of August, 2014, it was found out that there were certain irregularities in his appointment and on 31st August, 2014, his appointment was declared invalid. But Mr. Swastik continued to act as director even after 31st August, 2014. You are required to state, with reference to the provisions of the Companies Act, 2013, whether the acts done by Mr. Swastik are valid and binding upon the company?

(b) Mr. Amit is a Director of AB Limited and PQ Limited. AB Limited was regular in filing the Annual Returns but did not file annual accounts for the years ended 31st March, 2009, 2010 and 2011. AB Limited did not pay interest on loans taken from a public financial institution from 1st April, 2011 and also failed to repay matured deposits taken from public on due dates from 1st April, 2012 onwards.

Answer the following in the light of relevant provisions of the Companies Act, 1956:-

(i) Whether Mr. Amit is disqualified under Section 274 (1) (g) of the Companies Act, 1956 and if so; whether he can continue as a Director in AB Limited and also seeks reappointment when he retires by rotation at the Annual General Meeting of PQ Limited to be held in September, 2013?

(ii) Mr. Amit is proposed to be appointed as Additional Director of XY Limited in June, 2013. Is he eligible to be appointed as Additional Director in XY Limited?

6. (a) Galaxy Medicare Limited was incorporated in the year 2008. The management of the company decides to make donation to recognized political party in the year 2014. Advise the management about the restrictions and the extent up to which such donation can be made under the Companies Act, 2013. Will it make any difference if Galaxy Medicare Limited was incorporated in the year 2012?

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(b) Mr. Fin, Managing Director of Ray Fabrics Limited from last 4 years, lost his office. As per the provisions of the Companies Act, 2013, explain the following:

(i) state the compensation to be paid to Mr. Fin in relation to the loss of his office.

(ii) state the cases when no compensation is paid to the Managing Director in the situation of loss of office.

Meetings, Powers of the Boards and Related Party Transaction

7. (a) The Board of Directors of Marbles Construction Limited at a meeting held on 15th November, 2013 resolved to borrow a sum of ₹ 15 crores from a nationalized bank. Subsequently the said amount was received by the company. One of the Directors opposed the said borrowing on the ground that the said borrowing is outside the powers of the Board of Directors. The Company seeks your advice and the following data is given for your information:

(i) Share Capital ₹ 5 crores

(ii) Reserves and Surplus ₹ 5 crores

Advice the management of the company.

(b) The Board meeting of NAMO Ltd. was held on 10th June, 2014 at Lucknow at 10.30 a.m. At the time of starting the board meeting, the number of directors present were 8. The total number of directors in the company were 10. The Board transacted eight items in the board meeting on that day. At 12 noon after the completion of four items in the agenda, 5 Directors left the meeting. Examine the validity of all these transactions explaining the relevant provisions of the Companies Act, 1956.

8. (a) Explain the provisions regarding prohibition on insider trading of securities as covered under the Companies Act, 2013.

(b) Sweet Tea Limited wants to sell its tea by entering into contract with the following parties:

(1) Tea Bros. a partnership firm in which a director of Sweet Tea Limited is a partner.

(2) R & T Private Limited in which one of the director of Sweet Tea Limited is a member.

(3) Strong Tea Limited in which one of the directors of Sweet Tea Limited is a director holding 3% of the paid up capital of Strong Tea Limited.

Advise the steps that should be taken by Sweet Tea Limited taking into account the relevant provisions of the Companies Act, 1956 for entering into contracts in which the directors are interested.

Inspection and Investigation

9. A group of creditors of a company lodged a complaint with the Registrar of Companies alleging that the Directors of the company are engaged in falsification and destruction of account books and records of the company and urged the Registrar to seize the account

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books and records of the company. Discuss whether the Registrar can exercise such powers under the provisions of the Companies Act, 1956.

Compromise, Arrangements and Reconstructions

10. (a) Tigerwood Furniture Limited was merged with Woodply Furniture Limited on account of amalgamation. Some workers of Tigerwood Furniture Limited refused to join as workers of Woodply Furniture Limited and claimed compensation on the ground of premature termination of their services. Woodply Furniture Limited resists the claim of the workers on the ground that their services have been transferred to Woodply Furniture Limited in view of the order of amalgamation and merger and hence the workers must join the service of Woodply Furniture Limited and cannot claim any compensation.

    State the powers of the court about the matters that would be considered while sanctioning the scheme of amalgamation under the provisions of the Companies Act, 1956. Decide whether the contention of the workers is justified.

    (b) Hi-tech Engineering Limited engaged in the business of engineering construction and cement manufacturing, decided to concentrate on its core business of engineering construction and hive off (demerge) its cement business in favour of Premier Cement Limited. State the steps to be taken by Hi-tech Engineering Limited to give effect to the proposed demerger under the provisions of the Companies Act, 1956.

Prevention of Oppression and Mismanagement

11. A group of shareholders consisting of 25 members decide to file a petition before the Company Law Board for relief against oppression and mismanagement by the Board of Directors of Delightful Operators Limited. The company has a total of 300 members and the group of 25 members holds one –tenth of the total paid –up share capital accounting for one-fifteenth of the issued share capital. The main grievance of the group is that due to mismanagement by the board of directors, the company is incurring losses and the company has not declared any dividends even when profits were available in the past years for declaration of dividend. Advise the group of shareholders regarding the success of (i) getting the petition admitted and (ii) obtaining relief from the Company Law Board.

12. City Oriented Hospital Ltd. has two groups of Directors. A dispute arose between the two groups out of which one group controlled the majority of shares. A very serious situation arose in the administration of the company's affairs when the minority group ousted the lawful Board of Directors from the possession and control of the management of the company's factory and workshop. Books of account and statutory records were held by the minority group and consequently the annual accounts could not be prepared for two years. The majority group applied to the Company Law Board for relief under sections 397 and 398 of the Companies Act. You are required to decide with reference to the provisions of the said Act, the following issues:

    (i) Can majority of shareholders apply to the Company Law Board for relief against the oppression by the minority shareholders?

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(ii) Whether Company Law Board can grant relief in such circumstances.

Corporate Winding up and Dissolution

13. (a) The Directors of Shubra Fabrics Ltd. desire to proceed for voluntary winding up of the company and hence they are required to File 'Declaration of Solvency'. Your advice is sought about the procedure to be followed for the said purpose.

(b) Explain the term "Overriding Preferential Payments" under the provisions of the Companies Act, 1956. ABC Limited is being wound-up by the Court. The official liquidator has realized ₹ 100 lakh by selling the land and buildings mortgaged by the company in favour of its bankers. The company owes ₹ 200 lakh to the bank. The bank has claimed that the amount realised by sale of land and buildings must be paid in full to it in preference to the workmen's dues to the extent of ₹ 50 lakh. Examine the Bank's claim with reference to the provisions of the Companies Act, 1956.

Producer Company

14. Western India Cotton Producer Company Limited, having paid-up capital of ₹ 6 lakh and free reserves of ₹ 4 lakh, proposes to make the following loans and investments:

(i) Loan of ₹ 3 lakh to Mr. John, a member of the Company, for a period of one year and a loan of ₹ 2 lakh to Mr. Smith, Director of the Company for a period of six months;

(ii) Investment of ₹ 4 lakh in the equity shares of Superb Stores Limited.

State the restrictions, if any, in this regard and also the legal requirements to be complied with by the Company under the provisions of the Companies Act, 1956.

E-governance/ Offences and Penalties

15. (a) Who can file an application for allotment of DIN?

(b) What things should be taken care of with regard to supporting documents?

(c) What are the additional information/ documents required in case of a foreign national?

Companies Incorporated outside India/Miscellaneous provisions

16. (a) With reference to provisions laid down under the Companies Act, 2013, advice on the following:

(i) Display of name, etc., of foreign company

(ii) Service on foreign company

(b) Under Section 603 of the Companies Act, 1956, what are the particulars required for incorporating a prospectus to be issued by an existing foreign company?

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Corporate Secretarial Practice

17. Morbani Woods Limited decides to appoint Mr. Wahid as its Managing Director for a period of 5 years with effect from 1st May, 2013. Mr. Wahid fulfils all the conditions as specified in Part I and Part II of Schedule XIII of the Companies Act, 1956.

    The terms of appointment are as under:

    (i) Salary ₹ 1 lakh per month;

    (ii) Commission, as may be decided by the Board of Directors of the company;

    (iii) Perquisites;

    Free Housing,

    Medical reimbursement upto ₹ 10,000 per month,

    Leave Travel concession for the family,

    Club membership fee,

    Personal Accident Insurance ₹ 10 lakh,

    Gratuity, and

    Provident Fund as per Company's policy.

    You being the Secretary of the said Company, are required to draft a resolution to give effect to the above, assuming that Mr. Wahid is already the Managing Director in a public limited company.

SECTION – B: ALLIED LAWS

The Securities and Exchange Board of India (SEBI)

18. Point out the circumstances where under the following powers may be exercised by the Securities and Exchange Board of India (SEBI):

    (i) Prohibiting a company from issuing or publishing any document or advertisement soliciting money from public for issue of securities.

    (ii) Pass cease and desist order in relation to any listed company.

    What remedies are available to the companies against such orders under the SEBI Act, 1992?

19. Shyamgarh Chemicals Limited, a listed company, having a paid-up equity share capital of ₹ 80 crore and net worth of ₹ 120 crores as on 31st March, 2012 proposes to raise funds to finance its expansion programme by issue of equity shares under the "Qualified Institutions Placement Scheme."

    Answer the following with reference to the provisions of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009:

(i) What are the conditions to be satisfied by the company so that it can make Qualified Institutions Placement?

(ii) What is the maximum amount that can be raised by the company under the proposed issue of shares?

(iii) What are the restrictions, if any, with regard to pricing of issue and transferability of shares by qualified institution buyers?

Securities Contracts (Regulation) Act, 1956

20. (a) Mr. Yadav, a newly entered investor in the field of securities business seeks your advice on the investments to be made in securities of large Companies for long term purposes. With this object in view, he wants to know the meaning of the following terms commonly used in any stock exchange under the Securities Contracts (Regulation) Act, 1956.

(i) Derivative

(ii) Option in securities

(iii) Spot delivery contract.

Advise suitably.

(b) The Securities and Exchange Board of India issued an order against a stock broker to redress the grievances of the investors within the stipulated time. The stock broker failed to do so, which is an offence under the provisions of the Securities Contracts (Regulation) Act, 1956. Decide:

(i) Whether the offence committed by the stock broker is compoundable? If so, by whom?

(ii) Whether this offence can be compounded after institution of proceedings against the stock broker?

Foreign Exchange Management Act, 1999

21. (a) The Reserve Bank of India receives a complaint that an authorized person has submitted incorrect statements and information to the Reserve Bank of India in respect of receipt and utilization of Foreign Exchange. Explain the powers of the Reserve Bank of India with regard to inspection of records of the above authorized person in respect of the above complaint.

Referring to the provisions of Foreign Exchange Management Act, 1999, also state the duties of the above authorized person in this regard.

(b) During the financial year 2013-14 Mr. Bhattacharyya resided in India for a period of 180 days and thereafter went abroad. On 1st April, 2014, Mr. Bhattacharyya came back to India as an employee of a business organization. Decide the residential status of Mr. Bhattacharyya during the financial year 2013-14 under the provisions of the Foreign Exchange management Act, 1999.

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The Competition Act, 2002

22. (a) The Competition Commission of India has received a complaint that Paperwood limited has been abusing its dominant position in the food processing industry. Explain briefly the factors that will be considered by the Commissions to ascertain whether Paperwood limited enjoys a dominant position in the industry.

    (b) Mr. Alexander was a member of the Competition Commission of India. On the basis of information that he had acquired such financial interest as was likely to affect prejudicially his functions as a member of the Commission, the Central Government appointed an officer to hold an inquiry. On the basis of report of the said officer, the Central Government issued an order of removal of Mr. Alexander. Decide whether the action of the Central Government is in order under the provisions of the Competition Act, 2002?

Interpretation of Statutes, Deeds and Documents

23. In what way are the following terms considered as 'internal aid' in the interpretation of statutes?

    (A) Illustrations

    (B) Explanation

    (C) Preamble

    (D) Proviso

Banking Regulation Act, 1949, The Insurance Act, 1938, The Insurance Regulatory and Development Authority Act, 1999, The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002

24. (a) The Central Government acquired a Banking Company. The scheme of acquisition, apart from other matters, provided for the quantum of compensation payable to the shareholders of acquired bank. Some shareholders are not satisfied with the amount of compensation fixed under the scheme of acquisition.

    Is there any remedy available to the share holders under the provisions of the Banking Regulation Act, 1949?

    (b) RST Ltd. is a securitization and reconstruction company under SRFAESI Act, 2002. The certificate of registration granted to it was cancelled. State the authority which can cancel the registration and the right of RST Ltd. against such cancellation.

Prevention of Money Laundering Act, 2002

25. Explain the term "Offence of Money Laundering" within the meaning of the Prevention of Money Laundering Act, 2002. State the punishment for the offence of money laundering.

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SUGGESTED ANSWERS/HINTS

1 (a) **Maintaining the books of accounts at a place other than Registered office of the company:** According to section 128(1) of the Companies Act, 2013, every company shall prepare and keep at its registered office, books of account and other relevant books and papers and financial statement for every financial year which give a true and fair view of the state of the affairs of the company, including that of its branch office or offices, if any.

The company may also keep all or any of the books of accounts at any other place in India as the Board of directors may decide. In such a case, the company should file with the Registrar of Companies, a notice in writing giving the full address of that place within 7 days of the Boards' decision.

Thus, in the present case, SRL Ltd. can follow the above procedure and keep its books of accounts at New Delhi instead of the Registered office of the company.

(b) (i) **Which Company is required to constitute CSR committee:**

(A) Every company including its holding or subsidiary, and a foreign company defined under section 2(42) of the Companies Act, 2013 having its branch office or project office in India, having

(1) net worth of rupees 500 crore or more, or

(2) turnover of rupees 1000 crore or more or

(3) a net profit of rupees 5 crore or more

during any financial year shall constitute a Corporate Social Responsibility Committee of the Board.

(B) The CSR Committee shall institute a transparent monitoring mechanism for implementation of the CSR projects or programs or activities undertaken by the company.

(C) However, the net worth, turnover or net profit of a foreign company shall be computed in accordance with balance sheet and profit and loss account of such company as prepared in accordance with the provisions of section 381(1)(a) and section 198 of the Act.

(ii) **Amount of contribution towards CSR:**

(A) The Board of every company shall ensure that the company spends, in every financial year, at least two per cent. of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its CSR Policy.

(B) The company shall give preference to the local area and areas around it where it operates, for spending the amount earmarked for CSR activities.

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(C) If the company fails to spend such amount, the Board shall, in its report, specify the reasons for not spending the amount.

(D) Companies may build CSR capacities of their own personnel as well as those of their Implementing agencies through Institutions with established track records of at least three financial years. However, such expenditure shall not exceed five percent. of total CSR expenditure of the company in one financial year.

(iii) Activities which are not considered as CSR activities:

The *Companies (CSR Policy) Rules, 2014* provides for some activities which are not considered as CSR activities:

(A) The CSR projects or programs or activities undertaken outside India.

(B) The CSR projects or programs or activities that benefit only the employees of the company and their families.

(C) Contribution of any amount directly or indirectly to any political party under section 182 of the Act.

2. (a) According to second proviso to section 139(2) of the Companies Act, 2013, as on the date of appointment no audit firm having a common partner or partners to the other audit firm, whose tenure has expired in a company immediately preceding the financial year, shall be appointed as auditor of the same company for a period of five years.

In the instant case, if Golden Smith Ltd. wants to appoint M/s Kukreja & Associates as its audit firm, it can not do so because Mr. Shyam was the common partner between both the Audit firms. This prohibition is only for 5 years i.e. upto year 2029. After 5 years Golden Smith Ltd. may appoint M/s Kukreja & Associates as its auditors.

(b) Prohibited services: An auditor appointed under the Companies Act, 2013 shall provide to the company only such other services as are approved by the Board of Directors or the audit committee, as the case may be. But such services shall not include any of the following services (whether such services are rendered directly or indirectly to the company or its holding company or subsidiary company), namely:—

(a) accounting and book keeping services;

(b) internal audit;

(c) design and implementation of any financial information system;

(d) actuarial services;

(e) investment advisory services;

(f) investment banking services;

(g) rendering of outsourced financial services;

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(h) management services; and

(i) any other kind of services as may be prescribed.

In the instant case, Mr. A, a chartered accountant is an auditor of Laxman Ltd. and subsequently from 1st June, 2014, he has started to render actuarial services to Laxman Ltd. which falls under the prohibited services as per section 144 of the Companies Act, 2013. Therefore Mr. A is liable for the penalty under section 147 of the Companies Act, 2013.

Penalty for providing prohibited services:

(i) Penalty on company [Section 147(1)]:

If any of the provisions of section 144 is contravened, the company shall be punishable with fine which shall not be less than ₹ 25,000 but which may extend to ₹ 5 Lacs.

(ii) Penalty on officers [Section 147(1)]:

If any of the provisions of section 144 is contravened, every officer of the company who is in default shall be punishable with:

(1) Imprisonment for a term which may extend to 1 year or

(2) With fine which shall not be less than ₹ 10,000 but which may extend to ₹ 1 Lacs; or

(3) Both with imprisonment and fine.

(iii) Penalty on auditor [Section 147(2) & (3)]:

(a) If an auditor of a company contravenes any of the provisions of section 144, the auditor shall be punishable with fine which shall not be less than ₹ 25,000 but which may extend to ₹ 5 Lacs.

(b) If an auditor has contravened such provisions knowingly or willfully with the intention to deceive the company or its shareholders or creditors or tax authorities, he shall be punishable with

(1) imprisonment for a term which may extend to 1 year and

(2) fine which shall not be less than ₹ 1 Lac but which may extend to ₹ 25 Lacs.

(c) Further, where an auditor has been convicted as above, he shall be liable to—

(1) refund the remuneration received by him to the company; and

(2) pay for damages to the company, statutory bodies or authorities or to any other persons for loss arising out of incorrect or misleading statements of particulars made in his audit report..

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3. Liability for failure to pay/post dividend within prescribed time

According to Section 127 of the Companies Act, 2013, dividend has to be paid within 30 days from the date of its declaration. The posting of dividend warrant by the company within 30 days will be deemed to be payment irrespective of the fact whether the shareholder has encashed it or not. Failure to pay or post dividend warrant within 30 days constitutes an offence under the Act and the company shall be liable to pay simple interest at the rate of eighteen percent per annum during the period for which such default continues.

In the instant case, the Annual General Meeting of Bhaskar Electronics Limited declared a dividend at the rate of 30% payable on paid up equity share capital of the company as recommended by the Board of Directors on 30th April, 2014. But the company was unable to post the dividend warrant to Mr. Sanjay, an equity shareholder of the company, up to 30th June, 2014.

I In view of the above provisions, Mr. Sanjay can file a suit against the company for the payment of dividend because failure to pay or post dividend warrant within 30 days constitutes an offence under the Act. Thus, he would succeed but he is entitled for simple interest at the rate of 18% per annum (and not 20% as claimed) during the period for which such default continues.

II Every director of the company, if he is knowingly a party to the default, is punishable with simple imprisonment for a term which may extend to two years and also to a fine of one thousand rupees for every day during which such default continues.

4. (a) Section 162(1) of the Companies Act, 2013, requires that the appointment of every director shall be voted on individually. Thus, two or more directors cannot be appointed by a single resolution. However, an exception has been carried out where under if a resolution has been first passed to the effect that all the directors shall be appointed by a single resolution without any vote being against it.

As per section 162(2) of the Companies Act, 2013, any resolution in contravention of the aforesaid provisions shall be void whether or not objection was taken at the time of its being so moved.

Hence, the appointments of all directors by passing one single resolution by Flora Construction Limited in its general meeting are void.

(b) The Companies Act, 1956 does not impose any share qualification on the directors. Therefore, unless the company's articles contain a provision to that effect, a director need not be a shareholder. However, the articles usually provide for a minimum share qualification. As per Regulation 66 of Table A, a director must hold at least one share in a company. Where a share qualification is fixed by the articles of a public company or a private company which is a subsidiary of a public company, Section 270 provides that:

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(i) each director must take his qualification shares within two months after his appointment;

(ii) the nominal value of the qualification shares must not exceed ₹ 5,000.

(iii) share warrants will not count for purposes of share qualification.

If a director fails to obtain his qualification shares within two months, he vacates office automatically on the expiry of two months after the date of his appointment. However, the subscribers to the Memorandum, as per provisions of the Act and/or Articles are deemed to be the first directors of the company. They need not hold qualification shares, unless the Articles so require.

Examining the above provisions of the Act, following shall be the answers to the questions asked:

(i) Contention of members shall not be tenable, for the reasons stated above (i.e. provisions of the Act).

(ii) His wife's holding of shares shall not be the qualification for the director. If the Articles are silent, the director need not hold any shares. Articles may provide that directors need not hold any qualification shares.

(iii) If he is one of the subscribers to the memorandum, he need not hold the Qualification shares. However, as a subscriber to a Memorandum he has to take at least a share and that share entitles him to qualify as a director. Therefore, he can continue as a director in the given case.

5. (a) In accordance with the provisions of the Companies Act, 2013 as contained in section 176, acts done by a person as a director shall be valid, notwithstanding that it may afterwards be discovered that his appointment was invalid by reason of any defect or disqualification or had terminated by virtue of any provision contained in this Act or in the articles.

The Proviso to section 176 of the Companies Act, 2013, further provides that nothing in this section shall be deemed to give validity to acts done by a director after his appointment has been shown to the company to be invalid or to have terminated.

In view of the provision of section 176 of the Companies Act, 2013, the acts done by Mr. Swastik prior to 31st August, 2014 are to be treated as valid and binding on Bhanu Textiles Limited.

However in view of the Proviso to section 176 of the Companies Act, 2013, the acts done by Mr. Swastik after 31st August, 2014 shall be deemed to be invalid and not binding upon Bhanu Textiles Limited.

(b) According to section 274(1)(g) of the Companies Act, 1956, a person who is already a director of a public company becomes disqualified for being appointed as director; if the concerned company:

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(i) has not filed the annual accounts and annual returns for any continuous three financial years commencing on and after 1st April, 1999; or

(ii) has failed to repay its deposit or interest thereon on due date or redeem its debentures on due date or pay dividends and such failure continues for one year or more.

Such a person is disqualified to act as a director of any other public company for a period of five years from the date on which the public company (in which he is a director) makes default as specified in the (A) or (B) above.

(a) Here, Mr. Amit is a director of AB Ltd. and PQ Ltd. AB Ltd was regular in filing annual returns but did not file annual accounts for three years ended 31st March 2009, 2010 and 2011. The disqualification specified in 274(1)(g)(A) will not apply unless the company has committed defaults in respect of both the matters i.e. annual returns and annual accounts for three consecutive financial years. Hence, Section 274(1)(g) is not attracted in this case.

Now, AB Ltd. failed to pay interest on loans taken from a public financial institution from 1st April, 2011 onwards and also failed to repay matured deposits taken from public from 1st April, 2012 onwards. Failure to pay interest on loans taken from a public financial institution is not covered under section 274(1)(g)(B). But as AB Ltd has failed to repay its deposits on due date and the failure continues for more than one year, Mr. Amit is disqualified under section 274(1)(g)(B).

The disqualification would come into operation only at the time of appointment or reappointment of Mr. Amit as director of any other public company after the default has become effective. Till such time, Mr. Amit can continue to hold the office of director in all public companies in which he is a director. He need not vacate the office of director in AB Ltd as there is no such requirement either in section 274(1)(g) as the disqualification applies only to 'any other public company' or section 283 (Section 283 stipulates the circumstances under which the office of a director shall become vacant).

Mr. Amit cannot seek reappointment in PQ Ltd when he retires by rotation at the Annual General Meeting to be held in September, 2013.

(b) In view of his disqualification u/s 274(1)(g)(B), Mr. Amit is not eligible to be appointed as additional director in XY Ltd. in June 2013 onwards.

6. (a) Donation to Recognized Political Party: According to section 182 of the Companies Act, 2013, notwithstanding anything contained in any other provision of this Act, no Government Company and no other company which has been in existence for less than three financial years shall contribute any amount or amounts directly or indirectly to any political party. Any other company may however, contribute any amount directly or indirectly to any political party, provided that the aggregate of the amount so contributed by the company in any financial year shall

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not exceed 7.5% of its average net profits during the three immediately preceding financial years.

Thus, Galaxy Medicare Limited in the present case, can contribute to the recognized political party since it is not a Government Company and it is in existence for more than three financial years at the time of making the donation. Further, political donations can be made by Galaxy Medicare Limited only out of its profits.

Further, the political donation is required to be authorized by a resolution passed at a Board of Directors' meeting. The Company, in addition, shall disclose in its profit and loss account any amount or amounts contributed by it to any political party during the financial year to which that account relates, giving particulars of the total amount contributed and the name of the party to which such amount has been contributed.

If Galaxy Medicare Limited was registered in the year 2012, it cannot make political donations because the company has not been in existence for three financial years.

(b) (i) As per section 202 of the Companies Act, 2013, the compensation payable to Mr. Fin will be shall not exceed the remuneration which he would have earned if he had been in office for the remainder of his term (1 year) or for 3 years, whichever is shorter, calculated on the basis of the average remuneration actually earned by him during a period of 3 years immediately preceding the date on which he ceased to hold office, or where he held the office for a lesser period than three years, during such period.

In case of Mr. Fin, it will be remaining 1 year of his term as the term of the Managing Director is 5 years.

(ii) Following are the cases in which no compensation is paid to the Managing Director in the situation of the lost of office:

(a) where the director resigns from his office as a result of the reconstruction of the company, or of its amalgamation with any other body corporate or bodies corporate, and is appointed as the managing or whole-time director, manager or other officer of the reconstructed company or of the body corporate resulting from the amalgamation;

(b) where the director resigns from his office otherwise than on the reconstruction of the company or its amalgamation as aforesaid;

(c) where the office of the director is vacated under sub-section (1) of section 167;

(d) where the company is being wound up, whether by an order of the Tribunal or voluntarily, provided the winding up was due to the negligence or default of the director;

(e) where the director has been guilty of fraud or breach of trust in relation to, or of gross negligence in or gross mismanagement of, the conduct of the

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affairs of the company or any subsidiary company or holding company thereof; and

(f) where the director has instigated, or has taken part directly or indirectly in bringing about, the termination of his office.

7. (a) According to the provisions of Section 180(1)(c) of the Companies Act, 2013, there are restrictions on the borrowing powers to be exercised by the Board of directors. According to the said section, the borrowings should not exceed the aggregate of the paid up capital and free reserves. While calculating the limit, the temporary loans obtained by the company from its bankers in the ordinary course of business will be excluded. If the borrowing exceeds the mentioned limit, the board of director can excercise their power only with the consent of the company by a special resoulation. In the present case, the proposed borrowing of ₹ 15 crores from a nationalized bank is exceeding the limit mentioned i.e. aggregate of the share capital and reserves and surplus of ₹ 10 Crores. Thus, the above borrowing is beyond the powers of the Board of directors.

Thus, the management of Marbles Construction Limited, should take steps to convene the general meeting and pass a special resolution by the members in the meeting as stated in Section 180(1)(c) of the Companies Act, 2013. Then, the borrowing will be valid and binding on the company and its members.

(b) Section 287 of the Companies Act, 1956, provides for the quorum for meeting. The quorum for a meeting of the Board of Directors of a company shall be one third of its total strength (any fraction contained in the said one third being rounded off as one), or two directors, whichever is higher. Where at any time the number of interested directors exceeds or is equal to two thirds of the total strength, the number of remaining directors, that is to say, the number of directors who are not interested present at the meeting being not less than two shall be the quorum during such time. In this case, the quorum is 4 (i.e. $1/3^{rd}$ of 10 = 3 1/3 rounded off as 4).

Hence, the quorum was present at the time of commencement of meeting. As a rule, in the case of a meeting of the Board of Directors, the meeting cannot transact any business, unless a quorum is present at the time of transacting the business. It is not enough that a quorum was present at the commencement of the business. The quorum of the Board is required at every stage of the meeting and unless a quorum is present at every stage, the business transacted is void. (*Balakrishna V. Balu Subudhi AIR 1949 Pat 184*).

In the given situation four items were transacted with the quorum and thus they are valid. Other four items were transacted after 5 directors left the meeting resulting in the reduction of quorum as only 3 directors were present as against the required quorum of 4 directors. Hence, such four transactions are void.

8. (a) Prohibition on insider trading of securities (Section 195 of the Companies Act, 2013)

There was no provision under the Companies Act, 1956 for prohibition on insider trading of securities. A new section 195 of the Companies Act, 2013 which came

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into force on 12th September, 2013 provides for prohibition on insider trading of securities. According to section 195 of the Companies Act, 2013:

(i) No person including any director or key managerial personnel of a company shall enter into insider trading. But if any communication is required in the ordinary course of business or profession or employment or under any law, then the above prohibition does not apply.

(ii) "Insider trading" means—

  (a) an act of subscribing, buying, selling, dealing or agreeing to subscribe, buy, sell or deal in any securities by any director or key managerial personnel or any other officer of a company either as principal or agent if such director or key managerial personnel or any other officer of the company is reasonably expected to have access to any non-public price sensitive information in respect of securities of company; or

  (b) An act of counselling about procuring or communicating directly or indirectly any non-public price-sensitive information to any person.

(iii) "price-sensitive information" means any information which relates, directly or indirectly, to a company and which if published is likely to materially affect the price of securities of the company.

(iv) If any person contravenes the provisions of this section, he shall be punishable with imprisonment for a term which may extend to five years or with fine which shall not be less than five lakh rupees but which may extend to twenty-five crore rupees or three times the amount of profits made out of insider trading, whichever is higher, or with both.

(b) According to Section 297(1) of the Companies Act, 1956, a director of the company or his relative, a firm in which such a director or relative is a partner, any other partner in such a firm or a private company of which the director is a member or director, must not enter into contracts with company for the sale, purchase, or supply of goods, materials or services or for underwriting the subscription of any shares in, or debentures except with the consent of the Board of Directors.

According to the proviso to sub-section (1) in the case of a company having a paid-up capital of ₹ 1 crore or more, no such contract shall be entered into except with previous approval of the Central Government.

Section 297(3) provides that a director or persons connected with him may enter into a contract in the circumstances of urgent necessity without obtaining consent of the Board, even if the value of such a contract exceeds ₹ 5,000 in the aggregate, but in such a case the consent of the Board must be obtained at meeting within three months of the date of entering into the contract.

The consent of the Board is deemed to have been given only if it is accorded by a resolution of the Board and not otherwise, either before or within three months of the date of entering into the contract [sub-section (4)]

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In the present case, Sweet Tea Limited wants to sell its tea by entering into contract with the following parties:

(1) **Tea Bros, a partnership firm in which a director of Sweet Tea Limited is a partner:**

In this case, a resolution in the meeting of the Board of Directors is required to be passed before entering into a contract with Tea Bros. If due to urgency it is not possible to pass a Board resolution before entering into the contract, the requisite consent of the Board shall be obtained within three months of the date on which the contract was entered into. The director of Sweet Tea Limited who is also a partner in Tea Bros. must disclose his interest as per section 299.

(2) **R & T Private Limited in which one of the directors of Sweet Tea Limited is a member:**

In this case also, a resolution in the meeting of the Board of Directors is required to be passed before entering into a contract with R & T Private Limited. If due to urgency it is not possible to pass a Board resolution before entering into the contract, the requisite consent of the Board shall be obtained within three months of the date on which the contract was entered into. The director of Sweet Tea Limited who is also a member in R & T Private Limited must disclose his interest as per section 299.

(3) **Strong Tea Limited in which one of the directors of Sweet Tea Limited is a director holding 3% of the paid up capital of Strong Tea Limited**:

Section 297 does not cover cases of Public Limited Companies; hence the approval of Board of Directors will not be necessary. According to section 299(6), where a director or more than one directors whether alone or together holds more than 2% of the paid up capital in the other company then disclosure is required. Therefore, the interested directors must make disclosure of interest as required under section 299 as the director of Sweet Tea Limited is holding 3% of the paid up capital of Strong Tea Limited.

9. Seizure of documents by Registrar: The powers of the Registrar of Companies in respect of seizure of books and records of any company are governed by section 234-A of the Companies Act, 1956. Sub-section (1) of the said section provides that if, pursuant to the information in his possession or otherwise, the Registrar has reasonable ground to believe that books and papers of a company may be destroyed, mutilated, altered, falsified or secreted, the Registrar may make an application to the Magistrate of First Class or the Presidency Magistrate, as the case may be, having jurisdiction for an order for the seizure of such books and papers.

According to Section 234-A (2), the Magistrate, after considering the application and hearing the Registrar, may authorize the Registrar to do the following:

(i) To enter, with such assistance as may be required, the place or places where such

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books and papers are kept.

(ii) To search that place or those places in the manner as provides in the Magistrate's order.

(iii) To seize the books and papers as he considers necessary.

Section 234-A (3) authorises the Registrar to keep the seized books and papers for a period of thirty days, after which the same have to be returned to the person from whom the seizure was made. But the Registrar is empowered, before returning the said books and papers, to take copies of or extracts from them or place identification marks on them or deal with them in the manner he considers necessary.

Section 234-A (4) states that the Registrar, while conducting search and seizure, has to follow the provisions relating to search and seizure as prescribed in the Code of Criminal Procedure, 1898.

In view of the above provisions of section 234-A of the Companies Act, 1956, the Registrar of Companies is empowered to seize the books and papers of the company against whom the complaint has been made by following the procedure laid down in the section.

10. (a) While sanctioning the scheme of amalgamation, the Court under section 394 of the Companies Act, 1956 may make provision for all or any of the following matters:

(i) The transfer to the transferee company of the whole or any part of the undertaking property or liabilities of any transferor company.

(ii) The allotment by the transferee company of any shares, debenture etc, in that company which under the scheme are to be allotted by that company to any person.

(iii) The continuation of any legal proceedings by or against any transferor and transferee company.

(iv) The dissolution, without winding up of any transferor company.

(v) The provisions to be made for any persons who within such time and in such manner as the court directs, dissent from the scheme of amalgamation.

(vi) Such incidental matters as are necessary to secure that the amalgamation shall be fully and effectively carried out.

An order under section 394 of the Companies Act, 1956 transferring the property, rights and liabilities of one company to another does not automatically transfer contracts of personal service which are in their nature incapable of being transferred and no contract of service is thereby created between an employee of the transferor company on the one hand and the transferee company on the other.

In *Nokes vs. Doucaster Amalgamated collieries Ltd. (1940 (3) all 2k 549)* the House of Lords clearly stated that the workers are not furniture and their services can not be transferred without their consent. Thus, the contention of the workers of

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Tigerwood Furniture Limited against the Woodply Furniture Limited is correct and justified.

(b) Hi-Tech Engineering Ltd. can demerge its cement business with Premier Cement Ltd. by obtaining the approval of Court as provided in section 394 of the Companies Act, 1956. For this purpose, Hi-Tech Engineering Ltd. is required to take the following steps:

(1) Hi-Tech Engineering Ltd., known as "Transferor Company" for this purpose, has to prepare a scheme under which its properties and liabilities in respect of cement business will be transferred to Premier Cement Ltd., known as "Transferee Company" for this purpose. Such scheme must contain the consideration for transfer, known as "Exchange Ratio".

(2) An application under Section 391(1) of the said Act must be made to Court for an order convening meetings of creditors and/or members.

(3) Notice(s) of the meeting(s) must be sent to members/creditors as per the direction of Court. Such notice must be accompanied by a statement under Section 393(1) of the said Act setting forth the terms of the compromise or arrangement and explaining its effect in general and in particular, the effect on the interests of Managerial Personnel.

(4) To hold the said meetings and pass necessary resolution approving the scheme subject to the confirmation of Court. It may be noted that the resolution must be passed by a majority in number representing 3/4th in value of the members/creditors as required under Section 391(2) of the said Act.

(5) Thereafter, Hi-Tech Engineering Ltd. is required to move to Court jointly with Premier Cement Ltd. for approval of the scheme disclosing all material facts relating to the Company (Proviso to section 391(2). Court as required under section 394A shall give notice to the Central Government and shall take into consideration any representation received from Central Government before passing any order on the application made to it for approval of the scheme.

(6) On receipt of Court's order, Hi-Tech Engineering Ltd. is required to file a certified copy of the order with the Registrar of Companies (ROC) for registration within 30 days after making of the order by Court [(Section 394(3)]. This is very important since the non-filing of the order with ROC would make the approval order ineffective.

(7) Lastly, to proceed to give effect to the scheme as approved by Court in the manner as directed by it.

11. Section 399 of the Companies Act, 1956 provides the right to apply to the Company Law Board for relief against oppression and mis-management. This right is available only when the petitioners hold the prescribed limit of shares as indicated below:

(i) In the case of company having a share capital, not less than 100 members of the Company or not less than one tenth of the total number of its members whichever is

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less or any member or members holding not less than one tenth of the issued share capital of the company, provided that the applicant(s) have paid all calls and other dues on the shares.

(ii) In the case of company not having share capital not less than one-fifth of the total number of its members.

Since the group of shareholders do not number 100 or hold 1/10th of the issued share capital or constitute 1/10th of the total number of members, they have no right to approach the CLB for relief. However, the Central Government, if it is of the view that circumstances exist which make it just and equitable so to do, may authorize any member(s) to apply to the CLB [Section 399(4)]. So, members any approach Central Government to authorize them to approach CLB in spite of deficiency in numbers.

As regards obtaining relief from CLB, continuous losses cannot, by itself, be regarded as oppression (*Ashok Betelnut Co. P. Ltd. vs. M.K. Chandrakanth*).

Similarly, failure to declare dividends or payment of low dividends also does not amount to oppression. (*Thomas Veddon V.J. (v) Kuttanad Robber Co. Ltd*).

Thus the shareholders may not succeed in getting any relief from CLB.

12. (i) The case stated in the question relates to the provisions of sections 397 and 398 of the Companies Act, 1956 with regard to remedy available to majority shareholders.

Where the majority is prevented from protecting itself by controlling the directors at general body meetings, the majority becomes an artificial minority entitled to claim protection under section 397 and 398 *[V. Sebastean, Dr V City Hospital (Pvt.) ltd. (1985) 57 Comp. case 453 (Ker)].* Thus, the remedy under section 397 and 398 is confined not to an oppressed minority of the shareholders alone; an oppressed majority may also apply to the Company Law Board against their oppression from the side of minority shareholders. In *Sindhri Iron Foundry (Pvt.) Ltd. Re (1963) 78 E. to N. 118*, issue and allotment of a number of shares in a company whereby an admitted majority of shareholders was reduced to a minority was struck down. While granting relief to a majority group, Mitra J observed in their case;

"If the Company Law Board finds that the company's interest is being seriously prejudiced by the activities of one or the other group of shareholders, that two different registered offices at two different addresses have been set up, that two rival boards are holding meetings, that the company's business property and assets have passed into hands of unauthorized persons who have taken wrongful possession and who claim to be the shareholders and directors, there is no reason why the Company Law Board should not make appropriate orders to put an end to such matters".

(ii) Relief by the Company Law Board: The Company Law Board may give relief if it is of opinion:

1. that the company's affairs are being conducted (a) in a manner prejudicial to public interest, or (b) in a manner oppressive to any member or members;

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2. that the facts justify the compulsory winding up order on the ground that it is just and equitable that the company should be wound up;
3. that to wind up the company would unfairly prejudice the applicants.

On being satisfied about the above requirements, the Company Law Board may pass such order as it thinks fit with a view to bring an end to the matters complained of.

13. (a) Declaration of Solvency: Chapter III of part VII of the Companies Act, 1956 deals with "Voluntary winding up" of companies and in this relation section 488 of the said Act provides for filing of "declaration of solvency" on the part of the directors of the company when there is proposal for voluntary winding up of the company.

The analysis of Section 488 of the Companies Act, 1956 discloses that a declaration of solvency contains the following features -

1. It is a declaration duly supported by an affidavit, verified by a competent authority.
2. A meeting of Board of Directors is required for the purpose.
3. The declaration is made by the directors or where there are more than two directors, by the majority of the directors that they have made full inquiry into the affairs of the company and
4. That they have formed opinion that the company has no debts or that if it will be able to pay its debt in full within a period not exceeding three years from the date of commencement of winding up as may be specified in the said declaration.
5. In order that the above declaration in valid, it should be made within five weeks immediately preceding the date of passing the resolution for winding up of the company and must be delivered to the Registrar before that date.
6. Further, the said declaration should be accompanied by a copy of the auditors report on the profit and loss account of the company for the period commencing from the date of the last audited accounts upto a date practicable immediately before the date of the declaration and a balance sheet on the last mentioned date and also a statement of company's assets and liabilities as on the date of the declaration made out in accordance with the requirements laid down by clause (2) of section 488 of the Companies Act, 1956.
7. Any director of a company making a declaration under this section without having reasonable grounds for the opinion that the company will be able to pay its debts in full within the period specified in the declaration, shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to ₹ 50,000, or with both.
8. If the company is wound-up in pursuance of a resolution passed within the period of five weeks after the making of the declaration but its debts are not

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paid or provided for in full, within the period specified in the declaration, it shall be presumed, until the contrary is shown, that the director did not have reasonable grounds for his opinion.

(b) Overriding preferential payment: As per Section 529A of the Companies Act, 1956, notwithstanding anything contained in other provisions of this Act or any other law for the time being in force in the winding-up of a company – (i) workmen's dues and (ii) debts due to secured creditors to the extent such debts rank, under clause (c) of the proviso to Sub-section (1) of Section 529, pari passu with such dues, shall be paid in priority to all other debts. These debts payable under (i) and (ii) above shall be paid in full, unless the assets are insufficient to meet them, in which case they shall abate in equal proportions.

As per the above provision, the dues of the workmen and debt due to the secured creditors are to be treated pari passu and have to be treated as prior to all other dues.

In view of the stated legal position in the problem, the contention of the Bank to pay the amount in full is not valid as the debts payable to the workmen and the secured creditors shall be paid in full, unless the realized assets are insufficient to meet the due debts, in which case they shall abate in equal proportions. Here, in the given problem, the realized assets of ABC Limited is ₹ 100 lakh and debts due to the secured creditor (Bank) is ₹ 200 lakh and the workmen's dues is ₹ 50 lacs.

In the light of the provisions of Section 529 and 529A, amount to be paid towards

$$\text{Workmen's dues} = \frac{\text{Amt. realized x Workmen's dues}}{\text{Workmen's dues + secured loan}}$$

$$= ₹\ 100 \text{ lacs x } \frac{₹\ 50 \text{ lacs}}{₹\ 50 \text{ lacs} + ₹\ 200 \text{ lacs}}$$

$$= ₹\ 100 \text{ lacs x } \frac{₹\ 50}{₹\ 250}$$

$$= ₹\ 100 \text{ lacs x } \frac{1}{5} = ₹\ 20 \text{ lacs}$$

In view of the provisions of Section 529 and 529A, the contention of the bank that whole of ₹ 100 lacs realized from the sale of land, etc. shall be paid to the bank towards repayment of loan is not tenable, only a sum of ₹ 80 lacs shall be paid.

Thus, Official Liquidator will have to pay ₹ 20 Lacs to Workmen and ₹ 80 Lacs to the Bank.

14. (i) Loan etc., to member: As per section 581ZK of the Companies Act, 1956, the Board may provide financial assistance to the members of the producer company, subject to the provisions made in articles, by way of—

(a) credit facility, to any member, in connection with the business of the Producer Company, for a period not exceeding six months;

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(b) loans and advances, against security specified in articles to any member, repayable within a period exceeding three months but not exceeding seven years from the date of disbursement of such loan or advances.

However, any loan or advance to any director or his relative shall be granted only after the approval by the members in general meeting.

Thus, according to the above provision, Western India Cotton Producer Company Limited can give loan to Mr. John, a member of the company for the Period of 1 year as the Act provides that Board may provide loan to any member repayable within a period exceeding three months but not exceeding seven years from the date of disbursement of such loan.

Whereas in respect of Mr. Smith, a Director, company may give the loan only after the approval by the members in general meeting.

(ii) **Investment in other companies**: As per section 581ZL of the Companies Act, 1956, any producer company, either by itself or together with its subsidiaries, may invest, by way of subscription, purchase or otherwise, shares in any other company other than a producer company for an amount not exceeding thirty per cent of the aggregate of its paid-up capital and free reserves. Further, the provision provides that a producer company may, by special resolution passed in its general meeting and with prior approval of the Central Government, invest in excess of the limits.

Thus, according to the above provision, the Western India Cotton Producer Company Limited cannot invest an amount exceeding thirty per cent of the aggregate of its paid-up capital and free reserves i.e. ₹ 3,00,000/-(i.e., 30% of 10,00,000) in Superb Stores Limited. However, the company may invest in excess of the limits (more than 3,00,000) by special resolution passed in its general meeting and with prior approval of the Central Government.

15. **(a)** Any individual, who is an existing director of a company or intends to be appointed as a director of the company, can file an application for allotment of DIN.

(b) Please ensure following before attaching supporting documents with DIN application:

- Documents submitted are currently valid and not expired.
- Documents issued by LIC may be enclosed as Date of Birth and Address proof.
- Bank Statements, Utility Bills like telephone, electricity bill etc. furnished as residence proof are in the applicant's name only and not older than two months.
- All supporting documents attached with form DIN-1 must be duly attested by an authorized person/ authority.
- In case the director is illiterate, thumb impression should be certified from the concerned revenue authority (where the applicant resides) and then all the

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documents should be notarized or attested or if applicant is not in a position to sign the application due to medical reasons and affixed thumb impression on the application then duly attested medical certificate from Government hospital is must with the application stating the reason of his / her ailment.

(c) Details of a valid passport should be filled in form DIN-1 and a certified copy of same should be attached with DIN application. All supporting documents including photograph should be certified by the Indian Embassy or a notary in the home country of the applicant or by the Managing Director / CEO / Company Secretary of the company registered in India, in which applicant is a director. If a foreign director has a valid multiple-entry Indian visa or Person of Indian Origin card or Overseas Citizen of India card, then the attestation could also be done by Public Notary / Gazetted Officer in India or practicing CA / CS / CWA.

16. (a) (i) Display of name, etc., of foreign company

According to section 382 of the Companies Act, 2013, every foreign company shall—

(1) conspicuously exhibit on the outside of every office or place where it carries on business in India, the name of the company and the country in which it is incorporated, in letters easily legible in English characters, and also in the characters of the language or one of the languages in general use in the locality in which the office or place is situate;

(2) cause the name of the company and of the country in which the company is incorporated, to be stated in legible English characters in all business letters, bill- heads and letter paper, and in all notices, and other official publications of the company; and

(3) if the liability of the members of the company is limited, cause notice of that fact—

(A) to be stated in every such prospectus issued and in all business letters, bill-heads, letter paper, notices, advertisements and other official publications of the company, in legible English characters; and

(B) to be conspicuously exhibited on the outside of every office or place where it carries on business in India, in legible English characters and also in legible characters of the language or one of the languages in general use in the locality in which the office or place is situate.

(ii) Service on foreign company

According to section 383 of the Companies Act, 2013, any process, notice, or other document required to be served on a foreign company shall be deemed to be sufficiently served, if addressed to any person whose name and address have been delivered to the Registrar under section 380 of the Companies Act,

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2013, and left at, or sent by post to, the address which has been so delivered to the Registrar or by electronic mode.

(b) Under Section 603 of the Companies Act, 1956, the prospectus to be issued by an existing or intended Foreign Company in India must be dated and contain the following particulars:

(a) the instrument constituting or defining the constitution of the company;

(b) the enactment's or provisions under which the company was incorporated;

(c) the address of the place in India where the said instrument, enactments etc. translation thereof in English if they are in some other foreign language, can be inspected;

(d) the date on which and the country in which the company was incorporated; and

(e) whether there is a place of business in India and if so, the address of its principal office.

The provision contained in (a), (b) and (c) above, shall not be applicable if the prospectus is issued more than 2 years after the company had become entitled to commence business.

17. Draft Board Resolution

"Resolved that consent of all the directors present at the meeting be and is hereby accorded to the appointment of Mr. Wahid, who is already the Managing Director of another public limited company, and fulfils the conditions as specified in Part I and II of Schedule XIII of the Companies Act, 1956, as the Managing Director of the company for a period of 5 years effective from Ist May, 2013 subject to approval by a resolution of shareholders in a general meeting and that Mr. Wahid may be paid remuneration as follows:

(i) Salary of ₹ 1 Lakh per month

(ii) Commission

(iii) Perquisites: Free Housing, Medical reimbursement upto ₹ 10,000, Leave Travel Concession for the family, Club membership fee, Personal Accident Insurance of ₹ 10 Lakhs, Gratuity, Provident Fund etc.

Resolved further that in the event of loss or inadequacy of profits, the salary payable to him shall be subject to the limits specified in Schedule XIII.

Resolved further that the Secretary of the company be and is hereby authorised to prepare and file with the Registrar of Companies necessary Return in respect of the above appointment".

Sd/

Board of Directors

Morbani Woods Limited

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(**Note:** Since in the given case Mr. Wahid fulfils all the conditions for appointment of Managing Director as specified in Part I and II of Schedule XIII, approval of Central Government is not required)

18. Orders of SEBI and Remedies: Under section 11 of the SEBI Act, 1992, the basic duty of the SEBI is to protect the interests of investors in securities and regulate the securities market. Section 11A (1)(b) specifically empowers SEBI to prohibit any company from issuing prospectus, any offer document or advertisement soliciting money from the public for the issue of securities by general or special order.

According to section 11D, SEBI can issue, cease and desist order in respect of any listed company only if SEBI has reasonable grounds to believe that such company has indulged in insider trading or market manipulation.

Aggrieved companies may appeal against orders of SEBI made under SEBI Act, 1992, rules or regulations to the Securities Appellate Tribunal (SAT) under section 15T of the said Act. Such appeal should be filed within 45 days from the date on which a copy of the order of SEBI is received by the company.

If the company is aggrieved by the order of SAT, further appeal against the order of SAT can be made to the Supreme Court within 60 days from the date of communication of the order of SAT on any question of law arising out of such order.

19. (i) Conditions for qualified institutions placement [Chapter VIII of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009]: Shyamgarh Chemicals Limited, a listed company may make qualified institutions placement if it satisfies the following conditions:

(a) a special resolution approving the qualified institutions placement has been passed by its shareholders;

(b) the equity shares of the same class, which are proposed to be allotted through qualified institutions placement or pursuant to conversion or exchange of eligible securities offered through qualified institutions placement, have been listed on a recognised stock exchange having nationwide trading terminal for a period of at least one year prior to the date of issuance of notice to its shareholders for convening the meeting to pass the special resolution:

(c) it is in compliance with the requirement of minimum public shareholding specified in the Securities Contracts (Regulation) Rules, 1957;

(d) In the special resolution, it shall be, among other relevant matters, specified that the allotment is proposed to be made through qualified institutions placement and the relevant date referred in the regulations shall also be specified.

(ii) Restrictions on amount raised: The aggregate of the proposed qualified institutions placement and all previous qualified institutions placements made by the issuer in the same financial year shall not exceed five times the net worth of the issuer as per the audited balance sheet of the previous financial year.

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In the instant case, the net worth of Shyamgarh Chemicals Limited is ₹ 120 crore. Therefore, the maximum amount that can be raised by the company under the proposed issue of shares is ₹ 600 crore (5*120).

(iii) Restrictions on Pricing of issue and transferability of shares:

Pricing of issue: The qualified institutions placement shall be made at a price not less than the average of the weekly high and low of the closing prices of the equity shares of the same class quoted on the stock exchange during the two weeks preceding the relevant date.

Transferability of shares: The eligible securities allotted under qualified institutions placement shall not be sold by the allottee for a period of one year from the date of allotment, except on a recognised stock exchange.

20. (a) Mr. Yadav, a new investor, desirous of entering investments business in any Stock Exchange, can be advised on different terms commonly used in any Stock Exchange:

(i) **Derivative [Section 2(ac) of the Securities Contracts (Regulation) Act, 1956]**

Derivative includes –

(1) a security derived from a debt instrument, share, loan whether secured or unsecured risk instrument or contract for differences or any other form of security;

(2) a contract, which derives its value from the prices or index of prices, of underlying securities.

(ii) **Option In Securities [Section 2(d) of the Securities Contracts (Regulation) Act, 1956] :**

Option in Securities means a contract for the purchase or sale of a right to buy or sell or a right to buy and sell, securities in future, and includes a teji, a mandi, a teji mandi, a galli, a put, a call or a put and call securities.

(iii) **Spot Delivery Contract [Section 2(i) of the Securities Contracts (Regulation) Act, 1956] :**

Spot delivery contract means a contract which provides for:

(1) actual delivery of securities and the payment of a price therefore either on the same day as the date of the contract or on the next day, the actual period taken for the dispatch of the securities or the remittance of money therefore through the post being excluded from the computation of the period aforesaid if the parties to the contract do not reside in the same town or locality.

(2) transfer of the securities by the depository from the account of a beneficial owner to the account of another beneficial owner when such securities are dealt with by a depository.

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(b) According to Section 23C of the Securities Contracts (Regulation) Act, 1956, if any stock broker or sub-broker or a company whose securities are listed or proposed to be listed in a recognised stock exchange, after having been called upon by the Securities and Exchange Board of India or a recognised stock exchange in writing, to redress the grievances of the investors, fails to redress such grievances within the time stipulated by the Securities and Exchange Board of India or a recognised stock exchange, he or it shall be liable to a penalty of one lakh rupees for each day during which such failure continues or one crore rupees, whichever is less.

(i) **Composition of certain offences**: According to Section 23N of the Act, notwithstanding anything contained in the Code of Criminal Procedure, 1973, any offence punishable under Securities Contracts (Regulation) Act, 1956, not being an offence punishable with imprisonment only, or with imprisonment and also with fine, may either before or after the institution of any proceeding, be compounded by a Securities Appellate Tribunal or a court before which such proceedings are pending.

Thus, in the instant case, offence committed by the stock broker is compoundable as he is punishable with fine only as provided under section 23C.

(ii) Yes, this offence can be compounded after institution of proceedings against the stock broker as it is clearly stated under Section 23N.

21. (a) As per section 12 of the Foreign Exchange Management Act, 1999

(1) The Reserve Bank may, at any time, cause an inspection to be made by any officer of the Reserve Bank specially authorized in writing by the Reserve Bank in this behalf, of the business of any authorized person as may appear to it to be necessary or expedient for the purpose of:

(a) verifying the correctness of any statement, information or particulars furnished to the Reserve Bank;

(b) obtaining any information or particulars which such authorized person has failed to furnish on being called upon to do so;

(c) securing compliance with the provisions of this Act or of any rules, regulations, directions or orders made thereunder.

(2) It shall be the duty of every authorized person, and where such person is a company or a firm, every director, partner or other officer of such company or firm, as the case may be, to produce to any officer making an inspection under section 12 (1) such books, accounts and other documents in his custody or power and to furnish any statement or information relating to the affairs of such persons, company or firm as the said officer may require within such time and in such manner as the said officer may direct.

(b) **Residential Status under Section 2(v) of Foreign Exchange Management Act, 1999:** In accordance with the provisions of the Foreign Exchange Management Act,

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1999, as contained in section 2(v), a person in order to qualify for the purpose of being treated as a 'Person Resident in India'' in any financial year, must reside in India for a period of more than 182 days during the preceding financial year.

Mr. Bhattacharyya did not reside in India during the year 2013-2014 for more than 182 days and his residential status during the next year, i.e. 2014-2015 is non-resident even though he stayed in India from 1st April, 2014 as an employee. His residential status in 2013-2014 cannot be ascertained as his stay in India during the previous year 2012-2013 is not known.

22. (a) Abuse of Dominant position: The Competition commission while inquiring whether Paperwood limited enjoys a dominant position or not under Section 4 of the Competition Act, 2002 will take the following factors into account [Section 19(4) of the Competition Act, 2002]

(i) Market-share of the enterprise

(ii) size and resources of the enterprise

(iii) size and importance of the competitors.

(iv) economic power of the enterprise including commercial advantages over competitors.

(v) vertical integration of the enterprises or sale or service net work of such enterprises.

(vi) dependence of consumers on the enterprise.

(vii) monopoly or dominant position whether acquired as result of any statute or by virtue of being a Government company or a public sector undertaking or otherwise.

(viii) entry barriers including barriers such as regulatory barriers, financial risk, high capital cost of entry, marketing entry barriers, technical entry barriers, economies of scale, high cost of substitutable goods or services for consumers.

(ix) countervailing buying power.

(x) market structure and size of market.

(xi) social obligations and social cost.

(xii) relative advantage, by way of contribution to the economic development, by the enterprise enjoying a dominant position having or likely to have an appreciable adverse effect on competition.

(xiii) any other factor which the commission may consider relevant for the inquiry.

(b) Removal of Member of Competition Commission: Section 11(2)(d) of the Competition Act, 2002 empowers the Central Government to remove, by an order, a member of the Competition Commission of India from his office if such member has acquired such financial interest as is likely to affect prejudicially his functions as a

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member of the Competition Commission. However, provisions of Section 11(3) of the said Act put some restrictions on such power of the Central Government. According to this Section, the Central Government has to make a reference to the Supreme Court of India.

The Supreme Court shall hold an enquiry in accordance with the procedure formulated by it and then report that the member in question ought to be removed from his office on such ground.

Thus, the Central Government can remove a member of the Competition Commission of India only after following the procedure established by Section 11 of the Competition Act, 2002.

In view of the above the action of the Central Government is not in order and removal of Mr. Alexander is not valid.

23. (A) Illustrations: Illustrations form a part of the statute and considered to be of relevance and value in construing the text of the section. However, illustration can not have the effect of modifying the language of the section and can neither curtail nor expand the ambit of the section.

(B) Explanation: An Explanation may be added to include something or to exclude something from it. Explanation should normally be read as to harmonise with and clear up any ambiguity in the main section. It should be construed as to widen the ambit of the section.

(C) Preamble: The Preamble expresses the scope, object and purpose of the Act more comprehensively than the Long Title. The Preamble may recite the ground and the cause making a statute and the evil which is sought to be remedied by it.

Like the Long Tile, the Preamble of a Statute is a part of the enactment and can legitimately be used for construing it. However, the Preamble does not over-ride the plain provision of the Act but if the wording of the statute gives rise to doubts as to its proper construction, e.g., where the words or phrase has more than one meaning and a doubt arises as to which of the two meanings is intended in the Act, the Preamble can and ought to be referred to in order to arrive at the proper construction.

In short, the Preamble to an Act discloses the primary intention of the legislature but can only be brought in as an aid to construction if the language of the statute is not clear. However, it cannot override the provisions of the enactment.

(D) Proviso: The normal function of a proviso is to except something out of the enactment or to qualify something stated in the enactment which would be within its purview if the proviso were not there. The effect of the proviso is to qualify the preceding enactment which is expressed in terms which are too general. As a general rule, a proviso is added to an enactment to qualify or create an exception to what is in the enactment: ordinarily a proviso is not interpreted as stating a general rule.

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It is a cardinal rule of interpretation that a proviso to a particular provision of a statute only embraces the field which is covered by the main provision. It carves out an exception to the main provision to which it has been enacted as a proviso and to no other. (*Ram Narain Sons Ltd. vs. Assistant Commissioner of Sales Tax, AIR 1955 SC 765)*.

24. (a) Compensation to shareholders of the acquired bank: Under section 36AE of the Banking Regulation Act, 1949, the Central Government has power to acquire the undertaking of Banking Companies. When a bank is acquired by the Central Government, a scheme for the acquired bank is made in consultation with the Reserve Bank of India.

Such Scheme also provides for compensation payable to the registered shareholders of the acquired Bank (Section 36AF).

Section 36AG of the Banking Regulation Act, 1949 states that compensation is paid to the registered shareholders in accordance with the principles provided in Schedule V to the said Act.

Any shareholder aggrieved with the amount of compensation may request the Central Government to refer the matter to Tribunal to be constituted under section 36AH of the Act. If the number of representation received is not less than one-fourth of the total number of shareholders holding not less than one-fourth of the paid-up share capital of the acquired Bank, the Central Government shall constitute a Tribunal for the purpose. Thus, such matters can be resolved through the Tribunal by the Central Government and the amount of compensation determined by the Tribunal is final and binding on all concerned parties.

(b) Cancellation of Certificate of Registration under SRFAESI Act, 2002:

The Reserve Bank of India may cancel a certificate of registration granted to a securitisation and reconstruction company for the reasons stated in Section 4 of SRFAESI Act, 2002.

RST Ltd., can prefer an appeal to the Central Government (Secretary, Ministry of Finance, Government of India) within a period of 30 days from the date on which order of cancellation was communicated to it. The Central Government must also give such company a reasonable opportunity of being heard before rejecting the appeal. If RST Ltd., is holding investments of qualified institutional buyers at the time of cancellation of certificate of registration, it shall be deemed to be a securitisation and reconstruction company until it repays the entire investments held by it, together with interest if any, within such period as may be specified by the Reserve Bank.

25. Offence of Money Laundering: Section 2 (1)(y) of the Prevention of Money Laundering Act, 2002 defines the term “scheduled offence", which accordingly means –

(i) the offences specified under Part A of the Schedule; or

(ii) the offences specified under Part B of the Schedule if the total value involved in

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such offences is thirty lakh rupees or more.

(iii) The offences specified under Part C of the Schedule

These Schedule to the Act gives a list of all the above offences.

Punishment for the Offence of Money Laundering

Section 4 of the said act provides for the punishment for Money-Laundering. Whoever commits the offence of money-laundering shall be punishable with:

(i) Rigorous imprisonment for a term which shall not be less than three years, but may be extended to seven years, and

(ii) Shall also be liable to fine.

But, where the proceeds of crime involved in money-laundering relates to any offence specified under paragraph 2 of Part A of the Schedule, the maximum punishment may extend to ten years instead of seven years.

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IV Applicability of the Companies Act, 2013:

1. Auditing related sections notified in Sept, 2013 of the Companies Act, 2013 along with the clarifications notified by the Ministry of Corporate Affairs.
2. Notified sections of Chapter IX: Accounts of Companies and Chapter X: Audit and Auditors of the Companies Act, 2013 along with its relevant Rules.

   Part II of the Supplementary study material in this regard has been hosted on the student portal, ICAI at the following link http://220.227.161.86/33649bos23281.pdf

Paper 4: Corporate and Allied Laws

Applicability of relevant Amendments / Circulars / Notifications / Regulations etc. for November, 2014, Examination: Refer Page No. 129

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