Roll No. ....

NOV 2015

Total No. of Questions – 7

FINAL
GROUP-I PAPER-1
FINANCIAL REPORTING

Total No. of Printed Pages – 16

Time Allowed – 3 Hours

Maximum Marks – 100

PAC

Answer to questions are to be given only in English except in the case of candidates who have opted for Hindi Medium. If a candidate, who has not opted for Hindi Medium, answers in Hindi, his/her answers in Hindi will not be valued.

Question No. 1 is compulsory.

Candidates are required to answer any **five** questions from the remaining **six** questions.

Working notes should form part of the respective answers.

Wherever necessary, candidates are permitted to make suitable assumptions which should be disclosed by way of note.

Marks

1. (a) From the following information, you are required to compute the basic and adjusted earnings per share : **4×5 =20**

Net profit for 2013-14	₹ 11 lakhs
Net profit for 2014-15	₹ 15 lakhs
No. of shares issued before rights issue	5 lakhs
Right issue	One for every 5 held
Right issue price	₹ 15 per share
Last date of exercising right option	01-06-2014
Fair value of shares before right issue	₹ 21 per share

(b) Fine Ltd., acquired a machine on 1st April 2009 for ₹ 14 crore that had an estimated useful life of 7 years. The machine is depreciated on straight line basis and does not carry any residual value. On 1st April, 2013, the carrying value of the machine was reassessed at ₹ 10.20 crore and the surplus arising out of the revaluation being credited to revaluation reserve. For the year ended 31st March 2015, conditions indicating an impairment of the machine existed and the amount recoverable ascertained to be only ₹ 140 lakhs.

You are required to calculate the loss on impairment of the machine and show how this loss is to be treated in the books of Fine Ltd.

Fine Ltd., had followed the policy of writing down the revaluation surplus by the increased charge of depreciation resulting from the revaluation.

(c) Sagar Future is a non-banking finance company. It makes available to you the costs and market price of various investments held by it as on 31-03-2015 as under :

(Figures ₹ in Lakhs)

Scripts :		**Cost**	**Market Price**
A.	Equity Shares –		
	A	60.00	61.20
	B	31.50	24.00
	C	60.00	36.00
	D	60.00	120.00
	E	90.00	105.00
	F	75.00	90.00
	G	30.00	6.00

B.	Mutual Funds –		
	MF-1	39.00	24.00
	MF-2	30.00	21.00
	MF-3	6.00	9.00
C.	Government Securities –		
	GV-1	60.00	66.00
	GV-2	75.00	72.00

(i) Can the company adjust depreciation of a particular item of investment within a category ?

(ii) What should be the value of investments as on 31.03.2015 ?

(iii) Is it possible to off-set depreciation in investment in mutual fund against appreciation of the value of investment in equity shares and government securities ?

(d) As on 1st April, 2014, the fair value of planned assets was ₹ 1,00,000 in respect of a pension plan of Zeleous Ltd. On 30th September, 2014, the plan paid out benefits of ₹ 19,000 and received inward contribution of ₹ 49,000. On 31st March, 2015, the fair value of plan assets was ₹ 1,50,000 and present value of the defined benefit obligation was ₹ 1,47,920. Actuarial losses on the obligations for the year 2014-15 were ₹ 600.

Marks

On 1st April, 2014, the company made the following estimates, based on its market studies, understanding and prevailing prices :

	%
Interest & dividend income, after tax payable by the fund	9.25
Realised and unrealised gains on plan assets (after tax)	2.00
Fund administrative costs	–1.00
Expected rate of return	**10.25**

You are required to find the expected and actual returns on plan assets.

2. White Ltd. has 2 divisions, E and N, and their respective shares of various assets and liabilities in the company's balance sheet as on 31st March, 2015 are given below : **16**

	₹ in Lakhs		
	E Division	**N Division**	**Total**
Fixed Assets			
Cost	975	510	
Less : Depreciation	340	240	
Written-Down Value	635	270	905
Investments			175
Current Assets	525	645	
Less : Current Liabilities	275	305	
Net Current Assets	250	340	590
Total			**1670**

Financed By			
Loan Funds	–	20	530
Own Funds			
Equity Share Capital : Shares of ₹ 10 Each			420
Reserves & Surplus			720
Total			**1670**

Loan funds included, inter alia, bank loans of ₹ 20 Lakhs specifically taken for N Division and debentures of the paid-up value of ₹ 200 Lakhs redeemable at any time between 1st December, 2014 and 30th Sept., 2015

Division N has been invariably suffering losses. The company sold this division N along with its assets and liabilities to a newly formed company Bright Ltd., which was incorporated with an authorized capital of ₹ 1,200 Lakhs, divided into shares of ₹ 10 each.

Bright Ltd. allotted to White Ltd.'s shareholders its two fully paid equity shares of ₹ 10 each at par for every fully paid equity-shares of ₹ 10 each held in White Ltd. as discharge of consideration for the division taken-over.

Bright Ltd. recorded in its books the fixed assets at ₹ 400 Lakhs, current assets at ₹ 450 Lakhs and liabilities at the same value at which they appeared in the books of White Ltd.

On 1st April, 2015, White Ltd. sold all its investments for ₹ 200 Lakhs and redeemed debentures liability at 10% discount, which was included in loan funds. The cash transaction being recorded in the bank account pertaining to E Division.

Marks

You are required to,

(i) Show the journal entries in the books of White Ltd.

(ii) Prepare White Ltd.'s balance-sheet immediately after the demerger and the initial balance sheet of Bright Ltd.

(iii) Calculate the intrinsic value of the share of White Ltd. immediately before the demerger and after the demerger, and

(iv) Comment on the impact of demerger on "Shareholders' wealth".

3. X Ltd. acquired 100% (2,00,000) shares in Y Ltd. for ₹ 200 Lakhs on April 1st, 2011 when Y Ltd. was formed with share capital of ₹ 200 Lakhs. **16**

X Ltd. acquired 80% (1,60,000) shares in Z Ltd. for ₹ 400 Lakhs on April 1st, 2011 when Z Ltd. had share capital of ₹ 200 Lakhs and Reserves and Surplus of ₹ 200 Lakhs.

The company amortizes goodwill on consolidation on a SLM basis over a period of 5 years. A full year's amortization is provided if the goodwill exists for more than 6 months.

On 1st April 2014, X Ltd. sold 80,000 shares of Z Ltd. for cash consideration of ₹ 300 Lakhs.

The net assets of Z Ltd. on 31st March 2014 was ₹ 600 Lakhs. The amount of reserves and surplus was ₹ 800 Lakhs, ₹ 600 Lakhs and ₹ 400 Lakhs respectively in X Ltd., Y Ltd., and Z Ltd., on 31 March 2014.

The Balance Sheet of the companies as on 31st March 2015 were as follows :

	₹ in Lakhs		
	X Ltd.	Y Ltd.	Z Ltd.
Share Capital (₹ 100 per share)	800	200	200
Reserves and Surplus	1100	840	560
Current Liabilities	500	560	640
Total	**2400**	**1600**	**1400**
Investments at Cost			
2,00,000 Shares in Y Ltd.	200	–	–
80,000 Shares in Z Ltd.	200	–	–
Current Assets	2000	1600	1400
Total	**2400**	**1600**	**1400**

Prepare for X Ltd., Group Balance-Sheet as on 31st March, 2015 along with notes to accounts. Give workings wherever necessary.

4. (a) A company announced a Stock Appreciation Right (SAR) on 01/04/2011 for each of its 600 employees. The scheme gives the employees the right to claim cash payment equivalent to excess on market price of company's shares, on exercise date, over the exercise price ₹ 130 per share in respect of 100 shares, subject to the condition of continuous employment of 3 years. The SAR is exercisable after 31/03/14 but before 30/06/14. **8**

Particulars	2011-12	2012-13	2013-14
Fair value of SAR	25	28	32
Actual no. of employees left	25	15	10
Company estimation for left employee	3%	5%	–

On 30/06/2014 when SAR was exercised, the intrinsic value per share was ₹ 35 per share.

Show Provision for SAR account by fair value method.

(b) You are required to 8

(i) Identify Equity and Liability Components,

(ii) Compute bond liability at the end of each year, and

(iii) Pass necessary journal entries from the following information :

Number of convertible bonds	:	5000 bonds issued at the beginning of year 1
Value of Bonds	:	₹ 500 per bond
Period of Bonds	:	3 years validity
Interest Rate on the bond	:	9% p.a. payable annually
Proceeds Received	:	₹ 25 Lacs
Conversion	:	At the bond holders' discretion, conversion into 125 ordinary shares for each bond of ₹ 500.
Prevailing Market Rate	:	11% p.a., for bonds issued without conversion option
Present Value factor for 11%	:	0.900, 0.812, 0.731 (for one year, two years and three years, respectively)

Marks

5. (a) Railway Products Private Ltd. (RPPL) is engaged in the business of design and manufacture of Railways products that are supplied to Railway department. The core component of such product is outsourced by RPPL from Allied Component Ltd. (ACL), the sole manufacturer of such components. **10**

RPPL wants to gain leadership in this industry and seeks to take over ACL. RPPL estimates that its goodwill will increase on the acquisition. Minimum increased value of goodwill will be ₹ 200 Lakhs.

RPPL has made the following calculation of the economic benefits presently available and that are foreseen as a result of the acquisition :

(i) Projected cash flows for the next 5 years :

	Cash Flow forecasts (₹ in Lakhs)				
Year	**1**	**2**	**3**	**4**	**5**
RPPL	2000	2500	3000	3500	4000
ACL	600	600	800	800	1000

 Marks

(ii) The net worth of ACL is as follows :

	₹ in Lakhs	
Fixed Assets		
Tangible assets		3000
Investments (Non-Trade)		1500
Current Assets		
Inventories	1000	
Receivables	500	1500
Total		**6000**
Less : Current Liabilities		
Trade Payables	800	
Bank Loan	700	1500
Net worth (Represented by 300 Lakhs shares of ₹ 10 each and reserves and surplus ₹ 1500 Lakhs)		**4500**

(iii) Other information :

a. 20% of the fixed assets of ACL will not be required on acquisition and the same has ready buyers for ₹ 300 Lakhs.

b. Investments have a ready market for ₹ 2,000 Lakhs.

c. Currents assets include surplus inventory of ₹ 50 Lakhs that can realize ₹ 80 Lakhs.

d. The current liabilities are to be paid off immediately. A sum of ₹ 820 Lakhs are payable on account of a compensation claim awarded against ACL, which has been treated as a contingent liability in the accounts, on which 20% was provided for.

Marks

(iv) RPPL has estimated the combined cash flows post merger as follows :

Year	1	2	3	4	5
Cash Flow (₹ in Lakhs)	2800	3200	3700	4300	5000

You are required to advice RPPL the maximum value it can pay for take-over of ACL and also show current valuation of ACL as a "stand alone" equity. The discount rate of 15% is advised appropriate.

P.V. of discounting factor of 15% are as follows :

Year	1	2	3	4	5
Discounting factor (15%)	0.870	0.756	0.658	0.572	0.497

(b) Find out Leverage effect on Goodwill from the following information : **6**

(i)	Average capital employed (Equity Approach)	₹ 11,50,000
(ii)	Future Maintainable profit on equity fund (After TAX)	₹ 1,80,000
(iii)	10% long term loan	₹ 4,50,000
(iv)	Tax rate	40%
(v)	**Normal Rate of return :**	
	On equity capital employed	15%
	On long term capital employed	12%

Marks

6. (a) Vijay Ltd. furnishes the following information from which you are required to calculate the Economics Value Added (EVA) of the company and also explain the reason for the difference, if any, between the EVA as calculated by you and the MVA (Market Value Added) of Vijay Ltd. amounting to ₹ 7010 Crores. **8**

Common share of ₹ 10 Face Value	79,10,000 shares
10% debentures of ₹ 100 Face Value	2,50,000 Debentures
Tax Rate	30%
Financial Leverage	1.1 Times
Capital Reserves (₹ in Lakhs)	54
Free Reserves (₹ in Lakhs)	75
Securities Premium (₹ in Lakhs)	80

It is common practice for companies in the industry to which Vijay Ltd. belongs to pay atleast a dividend of 12% P.A. to its common shareholders.

(b) During the financial year 2014-15, Power Ltd. had the following transactions : **8**

(i) On 01.04.2014, Power Ltd. purchased a new asset of Dark Ltd. for ₹ 11,40,000. The fair value of Dark Ltd.'s identifiable net assets was ₹ 8,50,000. Power Ltd. is of the view that due to popularity of Dark Ltd.'s product, the life of goodwill is 10 years.

Marks

(ii) On 01.05.2014, Power Ltd. purchased a franchise to operate transport service from the Government for ₹ 12,00,000 and at a annual fees of 4% of transport revenues. The franchise expires after 5 years. Transport Revenue were ₹ 1,20,000 for Financial Year 2014-15. Power Ltd. projects future revenue of ₹ 2,40,000 in 2015-16 and ₹ 3,50,000 p.a. for 3 years thereafter.

(iii) On 05.07.2014, Power Ltd. was granted a patent that had been applied for by Dark Ltd. During 2014-15, Power Ltd. incurred legal cost of ₹ 1,10,000 to register the patent and an additional ₹ 3,00,000 to successfully prosecute a patent infringement suit against a competitor. Power Ltd. expects the patent's economic life to be 10 years. Power Ltd. follows an accounting Policy to amortize all intangibles on SLM basis over a maximum period permitted by Accounting Standard taking a full year amortization in the year of acquisition.

Prepare :

a. A Schedule showing the intangible section in Power Ltd. balance sheet at 31st March, 2015.

b. A Schedule showing the related expenses that would appear in the Statement of Profit and Loss of Power Ltd. for 2014-15.

Marks

7. Answer any **four** of the questions : 4×4 =16

(a) XYZ Company is engaged in the business of financial services and is undergoing tight liquidity position, since most of the assets of the company are locked in various claims/petition in a special court. XYZ has accepted inter corporate deposits (ICDs) and it is making its best efforts to settle the dues. There were claims at varied rates of interest, from lenders, from the due date of ICDs to the date of repayment. The company has provided interest, as per the terms of the contract till the due date and a note for non-provision of interest on the due date to date of repayment was accepted in the financial statements. On account of uncertainties existing regarding the determination of the amount and in the absence of any specific legal obligation at present as per the terms of the contract, the company considers that these claims are in the nature of "claims against the company not acknowledged as debt", and the same has been disclosed by way of a note in the accounts instead of making a provision in the Profit and Loss Account. State whether the treatment done by the company is correct or not. 4

(b) Company owns an office building. Company enters into a put option with an investor that permits the company to put the building to the investor for ₹ 150 million. The current value of the building is ₹ 175 million. The option expires in 5 years. The option, if exercised, may be settled through physical delivery or net cash, at company's option. How do the Company and the investor account for the option ? 4

(c). Aakash Limited is the owner of a CGU (Cash Generating Unit) block of assets whose current carrying cost is ₹ 1000 lakhs. Current carrying cost of the CGU block of assets as per Accounting and Tax records are after charging depreciation of the current year. The company, after a detailed study by its technical team, has assessed the present value recoverable amount of this CGU block of assets at ₹ 550 lakhs. The value of the block of assets as per the Income Tax records is ₹ 800 lakhs. The Approving Authority of the company have issued a signed statement confirming that the impairment in the value of CGU is only a temporary phenomenon which is reversible in subsequent periods and also assuring virtual certainty of taxable incomes in the foreseeable future. You are required to show Deferred Tax workings as per Accounting Standards in force, given the tax rate of 30% plus 10% surcharge thereon. The depreciation rate for tax purposes is 15% and that as per books is 13.91%. 4

(d) A Company enters into a fixed price forward contract to purchase one million kilograms of copper in accordance with its expected usage requirements. The contract permits the company to take physical delivery of the copper at the end of 12 months or to pay or receive a net settlement in cash, based on the change in fair value of copper. Is the contract accounted for as a derivative ? Explain. 4

Marks

(e) Due to immense loss to Nepal in the recent earthquake, one FMCG Company undertakes various commercial activities with considerable discounts and concessions at the related affected areas of Nepal for a continuous period of 3 months after earthquake. In the Financial Statements for the year 2014-15, the Management has shown the expenditure incurred on such activity as expenditure incurred to discharge Corporate Social Responsibility. State whether the intention of Management is correct. Explain with reasons. 4