

PAPER – 1 : FINANCIAL REPORTING

Question No.1 is compulsory. Candidates are required to answer any **five** questions from the remaining **six** questions.

Wherever necessary, suitable assumptions may be made and disclosed by way of a note.

Working notes should form part of the respective answers.

Question 1

- (a) (i) XYZ Limited has set-up its business in a designated backward area which entitles the company to receive from the Government of India a subsidy of 20% of the cost of investment. Having fulfilled all the conditions under the scheme, the company on its investment of ₹ 75 crore received ₹ 15 crore as subsidy from the Government in January 2021. The company wants to treat this receipt as an item of revenue and thereby reduce the losses for the year ended on 31st March, 2021.

Keeping in view the relevant Accounting Standard, examine whether this action is justified or not? **(2 Marks)**

- (ii) Caseworker Limited received a specific grant of ₹ 6 crore for acquiring the plant of ₹ 30 crore during financial year 2015-2016 having useful life of 10 years. The grant received was credited to deferred income in the Balance Sheet. During the financial year 2020-2021, due to non-compliance of conditions laid down for the grant of ₹ 6 crore, the company had to refund the grant to the Government. The balance in the deferred income on that date was ₹ 3 crore and written down value of plant was ₹ 15 crore. Keeping in view the relevant Accounting Standard:

- (1) What should be the treatment of the refund of the grant and the effect on cost of the fixed asset and the amount of depreciation to be charged during the financial year 2020-2021 in the Statement of Profit and Loss?
- (2) What should be the treatment of the refund if grant was deducted from the cost of the plant during financial year 2015-2016?

Assume depreciation is charged on fixed assets as per Straight Line Method. **(3 Marks)**

- (b) Sky Limited leased a machinery to Moon Limited on the following terms:

Particulars	(₹)
Fair value of the machinery	50,00,000
Lease term	5 years
Lease rental per annum	12,50,000
Guaranteed residual value	2,50,000
Expected residual value	5,00,000
Internal rate of return	12%

Depreciation is provided on straight line method @ 10% per annum. You are required to calculate unearned finance income as per AS 19 "Leases".

For purpose of calculation, the following discount factors @ 12% should be adopted:

Year	1	2	3	4	5
Discount factor	0.8929	0.7972	0.7118	0.6355	0.5674

(5 Marks)

- (c) ABC Limited has started construction of an asset on 1st December, 2020, which continues till 31st March, 2021 (and is expected to go beyond a year). The entity has not taken any specific borrowings to finance the construction of the asset but has incurred finance costs on its general borrowings during the construction period.

The directly attributable expenditure at the beginning of the month on this asset was ₹ 10 lakh in December 2020 and ₹ 4 lakh in each of the months of January to March 2021.

At the beginning of the year, the entity had taken Inter Corporate Deposits of ₹ 20 lakh at 9% rate of interest and had an overdraft of ₹ 4 lakh, which increased to ₹ 8 lakh on 1st March, 2021. Interest was paid on the overdraft at 10% until 1st January, 2021 and then the rate was increased to 12%.

Calculate the capitalization rate for computation of borrowing cost in accordance with AS 16 'Borrowing Costs'.

(5 Marks)

- (d) Lion Limited purchased a depreciable asset at cost of ₹ 45,000 million on 1st July, 2018. The asset has a useful life till 31st March, 2026. The estimated residual value is ₹ 650 million. The selling price of the asset on 31st March, 2021 is expected to be ₹ 25,000 million and the cost of disposal as on this date is expected to be ₹ 500 million.

The expected cash flows from the asset are as under:

Financial year	Cash Flow (₹ in million)
2021-2022	7,500
2022-2023	7,000
2023-2024	6,500
2024-2025	6,000
2025-2026	5,000

The company expects the discount rate of 9%. The company provides depreciation on straight line basis. You are required to determine the following as at 31st March, 2021:

- Carrying amount of asset
- The value in use of the asset

(iii) The impairment loss, if any

(iv) The revised carrying amount for the financial year ending 31st March, 2021.

(Discount factor @ 9% for 1, 2, 3, 4 and 5 years are 0.917, 0.842, 0.772, 0.708 and 0.650 respectively.)

(5 Marks)

Answer

- (a) (i) As per para 10 of AS 12 'Accounting for Government Grants', where the government grants are in the nature of promoters' contribution, i.e. they are given with reference to the total investment in an undertaking or by way of contribution towards its total capital outlay and no repayment is ordinarily expected in respect thereof, the grants are treated as capital reserve which can be neither distributed as dividend nor considered as deferred income.

In the given case, the subsidy received is neither in relation to specific fixed asset nor in relation to revenue. Thus, it is inappropriate to recognise government grants in the profit and loss statement, since they are not earned but represent an incentive provided by government without related costs.

The correct treatment is to credit the subsidy to Capital Reserve. Therefore, the accounting treatment followed by the company is not proper.

- (ii) As per para 21 of AS 12, the amount refundable in respect of grant related to specific fixed assets should be recorded by increasing the book value of the asset or by reducing the capital reserve or the deferred income balance, as appropriate, by the amount refundable. Where the book value of the asset is increased, depreciation on the revised book value should be provided prospectively over the residual useful life of the asset.

- (1) In the first case where grant was credited to deferred income account, the grant refunded is ₹ 6 crore and balance in deferred income is ₹ 3 crore, therefore, ₹ 3 crore will be charged to the profit and loss account for the year 2020-2021. There will be no effect on the cost of the fixed asset and depreciation charge will be same as charged in the earlier years.

- (2) In the second case where grant was deducted from the cost of the asset, initial value of the plant after deduction of grant amount of ₹ 6 crore would have been

$$= ₹ 30 \text{ crore} - ₹ 6 \text{ crore} = ₹ 24 \text{ crore.}$$

Carrying value of the plant after 5 years on 1.4.2020

$$= [(₹ 24 \text{ crore} / 10 \text{ years}) \times 5 \text{ years}] = ₹ 12 \text{ crore.}$$

Annual depreciation charge would be ₹ 2.4 crore.

On refund of grant to the Government, the book value of the plant shall be increased by ₹ 6 crore i.e. ₹ 12 crore + ₹ 6 crore = ₹ 18 crore. The increased cost of ₹ 18 crore of the plant should be amortised prospectively over remaining 5 years of useful residual life. Depreciation charge in the year 2020-2021 would be ₹ 18 crore / 5 years = ₹ 3.6 crore instead of earlier ₹ 2.4 crore.

(b) Computation of Unearned Finance Income

- (a) **Gross investment** in the lease is the aggregate of (i) minimum lease payments from the standpoint of the lessor and (ii) any unguaranteed residual value accruing to the lessor.

$$\begin{aligned}
 \text{Gross investment} &= \text{Minimum lease payments} + \text{Unguaranteed residual value} \\
 &= (\text{Total lease rent} + \text{Guaranteed residual value}) + \text{Unguaranteed residual value} \\
 &= [(\text{₹ } 12,50,000 \times 5 \text{ years}) + \text{₹ } 2,50,000] + \text{₹ } 2,50,000 \\
 &= \text{₹ } 67,50,000
 \end{aligned}$$

- (b) **Table showing present value of (i) Minimum lease payments (MLP) and (ii) Unguaranteed residual value (URV)**

Year	MLP inclusive of URV	Internal rate of return (Discount factor 12%)	Present Value	
	₹		₹	
1	12,50,000	0.8929	11,16,125	
2	12,50,000	0.7972	9,96,500	
3	12,50,000	0.7118	8,89,750	
4	12,50,000	0.6355	7,94,375	
5	12,50,000	0.5674	7,09,250	
	2,50,000 (guaranteed residual value)	0.5674	1,41,850	
			<hr/>	
			46,47,850	(i)
	2,50,000 (unguaranteed residual value)	0.5674	1,41,850	(ii)
			<hr/>	
		(i) + (ii)	<u>47,89,700</u>	(b)

$$\begin{aligned}
 \text{Unearned Finance Income} &= (a) - (b) \\
 &= \text{₹ } 67,50,000 - \text{₹ } 47,89,700 = \text{₹ } 19,60,300
 \end{aligned}$$

(c) Calculation of capitalization rate on borrowings other than specific borrowings

<i>Nature of general borrowings</i>	<i>Period of outstanding balance</i>	<i>Amount of loan (₹)</i>	<i>Rate of interest p.a.</i>	<i>Weighted average amount of interest (₹)</i>
	<i>a</i>	<i>b</i>	<i>c</i>	<i>d = [(b x c) x (a/12)]</i>
9% Debentures	12 months	20,00,000	9%	1,80,000
Bank overdraft	9 months	4,00,000	10%	30,000
	2 months	4,00,000	12%	8,000
	1 month	<u>8,00,000</u>	12%	<u>8,000</u>
		<u>36,00,000</u>		<u>2,26,000</u>

Weighted average cost of borrowings

$$= \{20,00,000 \times (12/12)\} + \{4,00,000 \times (11/12)\} + \{8,00,000 \times (1/12)\}$$

$$= 24,33,334$$

Capitalisation rate = [(Weighted average amount of interest / Weighted average of general borrowings) x 100]

$$= [(2,26,000 / 24,33,334) \times 100] = 9.29\% \text{ p.a.}$$

Alternatively, capitalisation rate for 4 months could also be calculated as below:

Calculation of capitalization rate on borrowings other than specific borrowings

Finance cost on ₹ 20 lacs 9% debentures during December 2020 to March, 2021	₹ 60,000
Interest @ 10% on overdraft of ₹ 4,00,000 in December 2020	₹ 3,333
Interest @ 12% on overdraft of ₹ 4,00,000 in January, 2021 to February, 2021	₹ 8,000
Interest @ 12% on overdraft of ₹ 8,00,000 in March, 2021	<u>₹ 8,000</u>
Total finance costs in December 2020 – March 2021	<u>₹ 79,333</u>

Weighted average borrowings during period

$$= [(20,00,000 \times 4) + (4,00,000 \times 3) + (8,00,000 \times 1)] / 4$$

$$= ₹ 25,00,000$$

Capitalisation rate for 4 months = Total finance costs during the construction period / Weighted average borrowings during the construction period

$$= 79,333 / 25,00,000 = 3.17\% \text{ for 4 months}$$

(d) (i) Calculation of carrying amount

Original cost = ₹ 45,000 million

Depreciation for 2.75 years = $[(₹ 45,000 \text{ million} - ₹ 650 \text{ million}) \times 2.75 / 7.75]$
= ₹ 15,737 million

Carrying amount on 31.3.2021 = $[₹ 45,000 \text{ million} - ₹ 15,737 \text{ million}]$
= ₹ 29,263 million (approx.)

(ii) Calculation of value in use

Year	Cash Flow (in million)	Discount @ 9%	Discounted cash flow
2021-2022	7,500	0.917	6,877.50
2022-2023	7,000	0.842	5,894.00
2023-2024	6,500	0.772	5,018.00
2024-2025	6,000	0.708	4,248.00
2025-2026	5,000	0.650	3,250.00
2025-2026	(residual) 650	0.650	<u>422.50</u>
			<u>25,710.00</u>

(iii) Calculation of impairment loss

When recoverable amount is less than carrying value

Impairment loss = Carrying amount – Recoverable amount

Value in use = ₹ 25,710 million

Selling Price = ₹ 25,000 million

Cost of disposal = ₹ 500 million

Net selling price = ₹ 24,500 million

Recoverable amount = Higher of value in use and net selling price

i.e. ₹ 25,710 million.

Impairment loss = ₹ 29,263 million - ₹ 25,710 million = ₹ 3,553 million

(iv) Revised carrying amount = Recoverable amount = ₹ 25,710 million

Question 2

Following are the summarised Balance Sheets of Takeover Limited and Giveaway Limited as on 31st March, 2021:

Particulars	Note No.	Takeover Limited (₹)	Giveaway Limited (₹)
I. Equity and Liabilities			
(1) Shareholder's funds			
(a) Share capital	1	75,00,000	15,00,000
(b) Reserve and surplus	2	1,05,00,000	52,50,000
(2) Non-current liabilities			
(a) Secured loan		30,00,000	4,50,000
(3) Current liabilities			
(a) Trade payables		45,00,000	3,00,000
Total		2,55,00,000	75,00,000
II. Assets			
(1) Non-current assets			
(a) Property, plant and equipment		90,00,000	27,00,000
(b) Non-current Investment	3	9,00,000	
(2) Current Assets			
(a) Inventories		45,00,000	37,50,000
(b) Trade Receivables		52,50,000	7,50,000
(c) Cash and Cash Equivalents	4	58,50,000	3,00,000
Total		2,55,00,000	75,00,000

Notes to Accounts:

	Particulars	Takeover Limited (₹)	Giveaway Limited (₹)
1. Share Capital			
	7,50,000 Equity shares of ₹ 10 each	<u>75,00,000</u>	
	1,50,000 Equity shares of ₹ 10 each		15,00,000
2. Reserve and surplus			
	General reserve	75,00,000	30,00,000
	Profit & loss A/c	<u>30,00,000</u>	<u>22,50,000</u>
		<u>1,05,00,000</u>	<u>52,50,000</u>

3.	Non-current investment		
	Shares in Giveaway Limited (90,000 shares)	9,00,000	-
4.	Cash and cash equivalents		
	Cash at bank	58,50,000	3,00,000

Takeover Limited holds 60% of the paid-up capital of Giveaway Limited and balance is held by a foreign company. The foreign company agreed with Takeover Limited as under:

- (1) The shares held by the Foreign Company will be sold to Takeover Limited at ₹ 55 above the nominal value per share.
- (2) The actual cost per share to the Foreign Company was ₹ 15. Gain accruing to Foreign Company is taxable @ 20%. The tax payable will be deducted from the sale proceeds and paid to Government by Takeover Limited. 50% of the consideration (after payment of tax) will be remitted (through Bank A/c) to Foreign Company by Takeover Limited.
- (3) For the balance of consideration, Takeover Limited will issue its shares at their intrinsic value. Amount payable for fractional shares allotted will be remitted along with amount due in (2) above.

It was also decided that Takeover Limited would absorb Giveaway Limited simultaneously by writing down the Fixed Assets of Giveaway Limited by 10%. The Balance Sheet figures included (i) a sum of ₹ 1,50,000 due from Giveaway Limited to Takeover Limited (ii) inventory of ₹ 2,25,000 purchased from Giveaway Limited who sold them at cost plus 20%.

Pass Journal Entries in the books of Takeover Limited to record the above arrangement on 31st March, 2021. Also prepare Balance Sheet of Takeover Limited after absorption.

(16 Marks)

Answer

Journal Entries in the books of Takeover Limited

Particulars	₹	₹
Business purchase A/c Dr. To Foreign company A/c (Being business purchased)	39,00,000	39,00,000
Foreign company A/c Dr. To Tax payable A/c To Bank A/c To Equity share capital A/c To Securities premium A/c (Being consideration paid)	39,00,000	6,00,000 16,50,017 5,39,210 11,10,773

Tangible assets A/c	Dr.	24,30,000	
Inventories A/c	Dr.	37,50,000	
Trade receivables A/c	Dr.	7,50,000	
Cash at bank A/c	Dr.	3,00,000	
To Secured loan A/c			4,50,000
To Trade payables A/c			3,00,000
To Investment in Giveaway Ltd. A/c			9,00,000
To Business purchase A/c			39,00,000
To Capital reserve A/c (Balancing Figure)			16,80,000
(Being various assets and liabilities taken over)			
Capital reserve A/c	Dr.	37,500	
To Inventories A/c			37,500
(Being elimination of unrealised profit i.e. 2,25,000/120 x 20)			
Trade payables A/c	Dr.	1,50,000	
To Trade receivables A/c			1,50,000
(Being elimination of mutual owing)			
Tax payable A/c	Dr.	6,00,000	
To Bank A/c			6,00,000
(Being tax paid to the Government)			

Takeover Ltd.**Balance Sheet as at 31st March, 2021**

Particulars	Note No.	Amount (₹)
I. Equity and Liabilities		
(1) Shareholder's funds		
Share capital	1	80,39,210
Reserves and surplus	2	1,32,53,273
(2) Non-current liabilities		
Long-term borrowings	3	34,50,000
(3) Current liabilities		
Trade payables	4	46,50,000
Total		2,93,92,483

II. Assets		
(1) Non-current assets		
Property, plant and equipment	5	1,14,30,000
(2) Current assets		
(a) Inventories	6	82,12,500
(b) Trade receivables	7	58,50,000
(c) Cash and cash equivalents		38,99,983
Total		2,93,92,483

Notes to Accounts

		₹	₹
1. Share capital			
8,03,921 shares of ₹ 10 each			80,39,210
(Out of the above, 53,921 shares of ₹ 10 each issued for consideration other than cash)			
2. Reserves and surplus			
General reserve	75,00,000		
Capital reserve	16,80,000		
Less: Unrealized profit on inventory	<u>(37,500)</u>	16,42,500	
Profit and loss account	30,00,000		
Securities premium (53,921 × 20.60)	<u>11,10,773</u>		1,32,53,273
3. Long term borrowings			
Secured loans (30,00,000 + 4,50,000)			34,50,000
4. Trade payables (45,00,000 + 3,00,000)	48,00,000		
Less: Mutual owing	<u>(1,50,000)</u>		46,50,000
5. Property, plant and equipment			
(90,00,000 + 27,00,000)	1,17,00,000		
Less: Downward revaluation	<u>(2,70,000)</u>		1,14,30,000
6. Inventories (45,00,000 + 37,50,000)	82,50,000		
Less: Unrealised profit on inventory	<u>(37,500)</u>		82,12,500
7. Trade receivables			
Trade receivables (52,50,000 + 7,50,000)	60,00,000		
Less: Mutual owings	<u>(1,50,000)</u>		58,50,000

Working Notes:**(1) Purchase consideration for 40% of share capital of Giveaway Ltd.**

$$= 1,50,000 \times 40\% \times ₹ 65 \text{ (55+ nominal value 10)} = ₹ 39,00,000$$

(2) Calculation of intrinsic value of shares of Takeover Ltd.

		₹
Total assets excluding investments in Giveaway Ltd. (2,55,00,000 – 9,00,000)		2,46,00,000
Add: Revised value of investment (1,50,000 x 60% x 65)		<u>58,50,000</u>
		3,04,50,000
Less: Outside liabilities:		
Secured loan	30,00,000	
Current liabilities	<u>45,00,000</u>	<u>(75,00,000)</u>
Net assets		<u>2,29,50,000</u>

$$\begin{aligned} \text{Intrinsic value per share} &= \text{Net assets} / \text{Number of shares} = 2,29,50,000 / 7,50,000 \\ &= ₹ 30.60 \text{ per share} \end{aligned}$$

(3) Discharge of purchase consideration by Takeover Ltd.

		Equity share capital ₹	Cash ₹	Total ₹
(i)	Payment of tax [(39,00,000 – (60,000 x 15)) x 20%]	---	6,00,000	6,00,000
(ii)	Issue of shares to foreign company [50% of (39,00,000 – 6,00,000)] = 16,50,000 No. of shares issued by Takeover Ltd. (16,50,000 / 30.60) = 53,921.57 shares Value of share capital = 53,921 x 30.60	16,49,983	-	16,49,983
(iii)	Cash payment [50% of (39,00,000 – 6,00,000)]		16,50,000	16,50,000

(iv)	Cash for fractional shares = (16,50,000 – 16,49,983)		17	17
	Total	<u>16,49,983</u>	<u>22,50,017</u>	<u>39,00,000</u>

(4) Calculation for goodwill / capital reserve to Takeover Ltd.

	₹
Total of assets as per balance sheet of Giveaway Ltd.	75,00,000
Less: 10% Reduction in the value of property, plant and equipment (₹ 27,00,000 x 10%)	<u>(2,70,000)</u>
	72,30,000
Less: Secured loan	4,50,000
Trade payables	<u>3,00,000</u>
	<u>(7,50,000)</u>
Net assets	64,80,000
Less: Purchase consideration (outside shareholders)	<u>(39,00,000)</u>
	25,80,000
Less: Investment in Giveaway Ltd. as per Balance Sheet of Takeover Ltd.	<u>(9,00,000)</u>
Capital Reserve	<u>16,80,000</u>

(5) Cash and bank balance of Takeover Ltd. after acquisition of shares

	₹
Opening balance (Takeover Ltd.)	58,50,000
Cash and bank balance of Giveaway Ltd.	<u>3,00,000</u>
	61,50,000
Less: Remittance to the foreign company	<u>(16,50,017)</u>
	44,99,983
Less: T.D.S. paid to government	<u>(6,00,000)</u>
	<u>38,99,983</u>

**(6) Unrealized profit included in inventory of Takeover Ltd. = ₹ 2,25,000 x (20/120)
= ₹ 37,500****Question 3**

Bull Ltd. acquired 100% ordinary shares of ₹ 100 each of Cow Ltd. on 1st October, 2020. On 31st March, 2021, the summarized balance sheets of the two companies were given below:

Balance Sheet as at 31st March, 2021

	Bull Ltd. (₹)	Cow Ltd. (₹)
Equity & Liabilities:		
Shareholders' fund		
Equity share capital:		
(Shares of ₹ 100 each fully paid)	50,00,000	20,00,000
Reserve & surplus:		
General reserve	24,00,000	10,00,000
Profit & loss account	5,72,000	8,20,000
Current liabilities:		
Short-term borrowings:		
Bank overdraft	7,80,000	-
Trade payable	4,48,000	2,54,000
Total	92,00,000	40,74,000
Assets:		
Non-current assets		
<u>Property, plant & equipment:</u>		
Land & buildings	17,00,000	20,00,000
Plant & machinery	24,00,000	13,50,000
<u>Long-term investments</u>		
Investment in Cow Ltd. (at Cost)	35,00,000	
Current assets		
Inventory	12,00,000	3,64,000
Trade receivables	3,00,000	3,00,000
Cash & cash equivalent	1,00,000	60,000
Total	92,00,000	40,74,000

The Profit & Loss Account of Cow Ltd. showed a credit balance of ₹ 3,00,000 on 1st April, 2020 out of which a dividend of 10% was paid on 1st November. Bull Ltd. has recognized the dividend received in the profit or loss account. Value of Plant & Machinery as on 1st October, 2020 was revalued at ₹ 20,00,000 for the purpose of acquisition. The rate of depreciation on plant & machinery is 10% on WDV method.

Following increase in value of assets and liabilities is to be considered on the acquisition date as compared to respective book value as on 1st October, 2020 for the purpose of acquisition while consolidating the balance sheets.

Liabilities	Amount in (₹)	Assets	Amount in (₹)
Trade Payables	1,00,000	Land (No increase in the value of Building)	10,00,000
		Inventories	1,50,000

- (i) It may be assumed that the inventory is still unsold on balance sheet date and the trade payables are also not yet settled.
- (ii) Also assume that the general reserve of both the companies as on 31st March, 2021 are the same as was on 1st April, 2020.
- (iii) All adjustments are required to be taken while calculating post acquisition profits.

You are required to prepare consolidated balance sheet as on 31st March, 2021. **(16 Marks)**

Answer

**Consolidated Balance Sheet of Bull Ltd. and its subsidiary Cow Ltd.
as at 31st March, 2021**

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's funds		
(a) Share capital (Shares of ₹ 100 each)		50,00,000
(b) Reserves and surplus	1	48,92,000
(2) Current liabilities		
(a) Trade payables	2	8,02,000
(b) Bank overdraft		7,80,000
Total		1,14,74,000
II. Assets		
(1) Non-current assets		
Property, plant and equipment	3	90,00,000
(2) Current assets		
(a) Inventories	4	17,14,000
(b) Trade receivables	5	6,00,000
(c) Cash and cash equivalents	6	1,60,000
Total		1,14,74,000

Notes to Accounts

			₹
1. Reserves and surplus			
Capital reserve (W.N.2)	17,85,000		
General reserve	24,00,000		
Profit and loss account (W.N.3)	<u>7,07,000</u>	48,92,000	
2. Trade payables			
Bull Ltd.	4,48,000		
Cow Ltd. (2,54,000 + 1,00,000)	<u>3,54,000</u>	8,02,000	
3. Property, plant and equipment			
Land and building			
Bull Ltd.	17,00,000		
Cow Ltd. (20,00,000 + 10,00,000)	<u>30,00,000</u>	47,00,000	
Plant and machinery			
Bull Ltd.	24,00,000		
Cow Ltd. (W.N.5)	<u>19,00,000</u>	<u>43,00,000</u>	
		<u>90,00,000</u>	
4. Inventories			
Bull Ltd.	12,00,000		
Cow Ltd. (3,64,000 + 1,50,000)	<u>5,14,000</u>	17,14,000	
5. Trade receivables			
Bull Ltd.	3,00,000		
Cow Ltd.	<u>3,00,000</u>	6,00,000	
6. Cash and cash equivalents			
Bull Ltd.	1,00,000		
Cow Ltd.	<u>60,000</u>	1,60,000	

Working Notes:

1. Analysis of Profits of Cow Ltd.

		Pre-acquisition profit	Profit and loss A/c
		₹	₹
General reserve on 1.10.2020		10,00,000	
Profit and loss A/c on 1.4.2020	3,00,000		

Less: Dividend	<u>(2,00,000)</u>	1,00,000	
	1,00,000		
Profit balance as on 31.3.2021	<u>(8,20,000)</u>		
Profit during the year	<u>7,20,000</u>		
Profit for 6 months		3,60,000	3,60,000
Upward revaluation of plant and machinery (W.N.4)	5,75,000		
Upward revaluation of land	10,00,000		
Upward revaluation of inventories	1,50,000		
Upward revaluation of trade payables	(1,00,000)	16,25,000	
Excess depreciation on plant and machinery due to upward revaluation (W.N.5)			(25,000)
Share of Bull Ltd.		30,85,000	3,35,000

2. Cost of Control

		₹
Investment	35,00,000	
Less: Dividend	<u>(2,00,000)</u>	33,00,000
Less: Paid up value of shares	20,00,000	
Pre-acquisition profit	<u>30,85,000</u>	<u>(50,85,000)</u>
Capital reserve		<u>17,85,000</u>

3. Consolidated Profit and Loss Account

	₹
Balance as per separate balance sheet	5,72,000
Less: Dividend	(2,00,000)
	3,72,000
Add: Share in Cow Ltd.	3,35,000
	7,07,000

4. Revaluation of Plant and Machinery

	₹
Value of plant and machinery as on 31.3.2021	13,50,000

Add back: Depreciation for 6 months from 1 st October, 2020 to 31 st March, 2021 $[(13,50,000 / 90\%) \times 10\% \times (6 / 12)]$	<u>75,000</u>
	14,25,000
Value as on 1 st October, 2020	<u>20,00,000</u>
Upward revaluation	<u>5,75,000</u>

5. Revised value of Plant and Machinery as on 31st March, 2021

	₹
Value of plant and machinery as on 31.3.2021	13,50,000
Add back: Depreciation for 6 months from 1 st October, 2020 to 31 st March, 2021 $[(13,50,000/90\%) \times 10\% \times (6/12)]$	75,000
Add: Upward revaluation (W.N.4)	5,75,000
Less: Revised depreciation from 1 st October, 2020 to 31 st March, 2021 $(20,00,000 \times 10\% \times 6/12)$	<u>(1,00,000)</u>
	<u>19,00,000</u>

Question 4

- (a) Max Limited has suffered huge financial losses during the financial year 2020-2021 due to the Covid pandemic and was internally discussing to implement restructuring of the company. Subsequent to the year-end but before the financial statements are approved for issue on 30th April, 2021, the Company's management announces that it will restructure the operation of the company. The management plans to make significant redundancies and to close a few divisions of company's business. However, there is no formal plan in place till the time of announcement. Should management recognize a provision in the books of accounts for financial year 2020-2021, if the company announced to restructure its operations on 20th April, 2021?

Discuss with reasons whether these events are in nature of adjusting or non-adjusting and the treatment required in light of Ind AS 10. **(4 Marks)**

- (b) What is the functional currency of an entity as per Ind AS? Whether the Company may have a different functional currency which is other than the currency of the country in which the company has been incorporated? What are the primary and secondary factors that influence determination of functional currency? **(4 Marks)**
- (c) (i) What are the classification of financial assets and financial liabilities as per Ind AS 109? Give one example of financial asset and financial liability. Also suggest the criteria on the basis of which financial assets are classified. **(3 Marks)**
- (ii) On 1st April, 2019, Sunshine Limited issued ₹ 60,00,000 7% Convertible debt instrument of face value of ₹ 100 at par. The debt instruments are redeemable at a premium of 10% on 31st March, 2023 or it may be converted into ordinary shares

at the option of the holder. The interest rate for equivalent debt instrument without conversion rights would have been 10%.

You are required to suggest if this is a compound instrument and if yes kindly separate the equity and debt portion with the necessary workings and journal entry at the inception date. **(5 Marks)**

Answer

- (a) As per paragraph 72 of Ind AS 37 'Provisions, Contingent Liabilities and Contingent Assets', a constructive obligation to restructure arises only when an entity has detailed formal plan for restructuring identifying the business or part of business concerned; the principal locations affected; the location, function, and approximate number of employees who will be compensated for terminating their services; the expenditures that will be undertaken; and when the plan will be implemented; and has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

Further, paragraph 75 of Ind AS 37 provides that a management or board decision to restructure taken before the end of the reporting period does not give rise to a constructive obligation at the end of the reporting period unless the entity has, before the end of the reporting period (a) started to implement the restructuring plan; or (b) announced the main features of the restructuring plan to those affected by it in a sufficiently specific manner to raise a valid expectation in them that the entity will carry out the restructuring.

In the given case, the management started drawing up the plan for restructuring of some of its business activities after the end of the reporting period, i.e., 2020-2021. If that be so, as per Ind AS 37, the management decisions subsequent to reporting date do not give rise to constructive obligation as of reporting date and no provision is required for restructuring costs as at 31st March 2021. As per Ind AS 10, adjusting events are those events whose evidence of conditions are available on reporting date and requires adjustment in the books of accounts. Non adjusting events are those events where evidence of conditions arose after reporting date and required disclosure in the notes to accounts, if material.

Announcing or commencing the implementation of a major restructuring after reporting period is a non-adjusting event as per Ind AS 10. Though, this is a non-adjusting event occurred after reporting period, yet it being material in nature would require its disclosure as per Ind AS 10.

- (b) **Functional currency** is the currency of the primary economic environment in which the entity operates.

Yes, a company may have a functional currency which is other than the currency of the country in which the company has been incorporated.

An entity considers the following primary factors in determining its functional currency:

- (a) the currency:
 - (i) that mainly influences sales prices for goods and services (this will often be the currency in which sales prices for its goods and services are denominated and settled); and
 - (ii) of the country whose competitive forces and regulations mainly determine the sales prices of its goods and services.
- (b) the currency that mainly influences labour, material and other costs of providing goods or services (this will often be the currency in which such costs are denominated and settled).

The following secondary factors may also provide evidence of an entity's functional currency:

- (a) the currency in which funds from financing activities (i.e. issuing debt and equity instruments) are generated.
- (b) the currency in which receipts from operating activities are usually retained.

- (c) (i) **Financial Assets are classified as financial assets subsequently measured at**
 - i. Amortised cost;
 - ii. Fair value through profit or loss; or
 - iii. Fair value through other comprehensive income

Financial Liabilities are classified as financial liability subsequently measured at

- i. Fair value through profit or loss; or
- ii. Amortised cost.

Example of financial asset is 'Investment in equity shares of another company'.

Example of financial liability is 'Trade Payable'.

An entity shall classify financial assets depending upon the *following 2 criteria and options* elected by the entity:

- (a) the entity's Business Model (BM) for managing the financial assets; and
 - (b) the Contractual Cash Flow Characteristics (CCFC) of the financial asset
- (ii) Yes, on evaluation of the terms and conditions of the financial instrument it is determined that the instrument contains both a liability and an equity component.

From the perspective of the entity, such an instrument should comprise of two components:

- A financial liability (a contractual arrangement to deliver cash or another financial asset); and
- An equity instrument (a call option granting the holder the right, for a specified period of time, to convert it into a fixed number of ordinary shares of the entity).

In the given case, the debt instrument can be redeemed at premium on maturity date i.e. 31st March, 2023 and also the instrument gives an option to the holder to convert the amount into ordinary shares on maturity date, hence, it is a compound instrument.

Accordingly, an entity recognises separately the components of a financial instrument that

- creates a financial liability of the entity and
- grants an option to the holder of the instrument to convert it into an equity instrument of the entity.

Computation of Equity and Debt Component of Convertible Debentures as on 1st April, 2019

	₹
Present value of the principal repayable after four years [60,00,000 x 1.10 x 0.683 (using 10% Discounting factor)]	45,07,800
Add: Present value of Interest [(60,00,000 x 7%) x 3.17 (4 years cumulative 10% discounting factor)]	<u>13,31,400</u>
Value of debt component	58,39,200
Value of equity component (balancing figure)	<u>1,60,800</u>
Proceeds of the issue	<u>60,00,000</u>

Journal entry at the inception date i.e. 1st April, 2019

	Dr. (₹)	Cr. (₹)
Bank A/c Dr.	60,00,000	
To 7% Debt Instrument (Liability component) A/c		58,39,200
To 7% Debt Instrument (Equity component) A/c		1,60,800
(Being the disbursement recorded at fair value)		

Question 5

The following is the Balance Sheet of Amber Limited as at 31st March, 2021:

Particulars	Note No.	(₹)
I. Equity and Liabilities:		
(1) Shareholders' Funds		
(a) Share Capital	1	92,00,000
(b) Reserve and Surplus	2	92,80,000
(2) Non-Current Liabilities		
(a) 9% Debentures		15,00,000
(b) 12% Term Loan		20,00,000
(3) Current Liabilities		
(a) 9% Debentures (Convertible at the beginning of next year)		15,00,000
(b) Trade Payables		10,00,000
(c) Dividend Payable		24,60,000
(d) Income Tax Provision		40,00,000
Total		3,09,40,000
II. Assets:		
(1) Non-Current Assets		
(a) Property, Plant and Equipment		
(i) Tangible Assets		1,40,10,000
(b) Non-current Investment	3	55,20,000
(2) Current Assets		
(a) Inventories		40,30,000
(b) Trade Receivables		40,20,000
(c) Advances		25,30,000
(d) Cash and Cash Equivalents		8,30,000
Total		3,09,40,000

Notes to Accounts:

	Particulars	(₹)
1.	Share capital	
	2,50,000 Equity shares of ₹ 10 each fully paid-up	25,00,000

	4,00,000 Equity shares of ₹ 10 each ₹ 8 paid-up	32,00,000
	5,00,000 Equity shares of ₹ 5 each fully paid-up	25,00,000
	Share suspense	10,00,000
		92,00,000
2.	Reserve and surplus	
	General reserve	51,00,000
	Profit & loss A/c	41,80,000
		92,80,000
3.	Non-current Investments	
	Investment in subsidiaries	30,20,000
	Non-trade investments	25,00,000
		55,20,000

Other information:

- (i) Profit before tax (and before deducting interest on convertible debentures) of Amber Limited for the last five years ended on 31st March were as follows 2017 - ₹ 66,00,000, 2018 - ₹ 1,22,00,000, 2019 - ₹ 1,37,00,000, 2020 - ₹ 1,57,50,000 and 2021 - ₹ 1,66,00,000.
- (ii) Non-trade investments earned @ 20% on an average.
- (iii) Expected increase in expenditure without commensurate increase in selling price ₹ 30,000.
- (iv) Annual research and development expenses in future ₹ 50,000.
- (v) Expected foreign currency loss in future (annualised) ₹ 60,000.
- (vi) Expected tax rate 25%. Tax rate in 2020-2021 - 30%.
- (vii) Normal return 15% (based on closing capital employed).

You are required to compute the following:

- (A) Intrinsic value for different categories of equity shares. For this purpose, goodwill may be taken as 3 years purchase of super profit (For calculation of future maintainable profit, weighted average is required to be taken).
- (B) Value of shares as per dividend yield. Normal dividend in the industry is 18%.
- (C) Value of shares as per EPS. Average EPS is ₹ 3 for ₹ 10 share. **(16 Marks)**

Answer**Calculation of intrinsic value of equity shares of Amber Ltd.****I. Calculation of Goodwill:**

	₹	₹
(i) Capital Employed:		
Total of asset side of the balance sheet		3,09,40,000
Less: Investment in subsidiaries	30,20,000	
Non-trade investment	<u>25,00,000</u>	<u>(55,20,000)</u>
		2,54,20,000
Less: Outside liabilities:		
Trade payables	10,00,000	
12% Term loan	20,00,000	
Tax provision	40,00,000	
9% Debentures – non-convertible	<u>15,00,000</u>	<u>(85,00,000)</u>
Capital employed		<u>1,69,20,000</u>

(ii) Future maintainable profit:

Year	Profit before tax (₹)	Weight	Product (₹)
2017	66,00,000	1	66,00,000
2018	1,22,00,000	2	2,44,00,000
2019	1,37,00,000	3	4,11,00,000
2020	1,57,50,000	4	6,30,00,000
2021	1,66,00,000	<u>5</u>	<u>8,30,00,000</u>
		<u>15</u>	<u>21,81,00,000</u>

	₹	₹
Weighted average profit before tax = 21,81,00,000 / 15		1,45,40,000
Less: Income from non-trade investments	5,00,000	
Expected increase in expenditure	30,000	
Annual R & D expenses	50,000	
Expected increase in foreign currency liability	60,000	

Interest of non-convertible debentures	<u>1,35,000</u>	<u>(7,75,000)</u>
		1,37,65,000
Less: Tax @ 25%		<u>34,41,250</u>
Expected profit after tax		<u>1,03,23,750</u>

(iii) Normal Return:

15% on capital employed

i.e. 15% on ₹ 1,69,20,000 = ₹ 25,38,000

(iv) Super profit:

Expected profit - Normal profit

₹ 1,03,23,750 – ₹ 25,38,000 = ₹ 77,85,750

(v) Goodwill:

3 years' purchase of super profit = ₹ 77,85,750 × 3 = ₹ 2,33,57,250

II. Net assets available to equity shareholders

	Amount (₹)
Goodwill as calculated in I (v) above	2,33,57,250
Tangible assets	1,40,10,000
Investment in subsidiaries	30,20,000
Non-trade investment	25,00,000
Inventories	40,30,000
Trade receivables	40,20,000
Advances	25,30,000
Cash & Cash equivalents	<u>8,30,000</u>
	5,42,97,250
Less: Outside liabilities (10,00,000+20,00,000+40,00,000+15,00,000)	<u>(85,00,000)</u>
	<u>4,57,97,250</u>

III. Valuation of equivalent number of equity shares:

	No.
2,50,000 equity shares of ₹ 10 each fully paid up	2,50,000
4,00,000 equity shares of ₹ 10 each ₹ 8 paid up (notional call to be adjusted)	4,00,000
5,00,000 equity shares of ₹ 5 each fully paid up	2,50,000

Share suspense A/c equivalent shares for ₹ 10,00,000	1,00,000
Shares for convertible debenture amounting to ₹ 15,00,000	<u>1,50,000</u>
	<u>11,50,000</u>

IV. Valuation of equity shares

Net assets as per (II) above + Notional call on 4,00,000 equity shares @ ₹ 2 each i.e. ₹ 8,00,000

$$= 4,65,97,250$$

Value per equivalent share of ₹ 10 = ₹ 4,65,97,250 / 11,50,000 = ₹ 40.52

Value per share of ₹ 10; ₹ 8 paid up = ₹ 40.52 – ₹ 2 = ₹ 38.52

Value per share of ₹ 5 fully paid up = ₹ 40.52 × 1/2 = ₹ 20.26

V. Valuation of equity shares on dividend yield basis

Dividend payable for the year ended 31.3.2021 ₹ 24,60,000

Paid up value of equity share ₹ 82,00,000

Rate of dividend (24,60,000 / 82,00,000 × 100) 30%

Value per fully paid-up share of ₹ 10

$$(30\%/18\%) \times ₹ 10 = ₹ 16.67$$

Value per share of ₹ 5

$$(30\%/18\%) \times ₹ 5 = ₹ 8.33$$

Value per share of ₹ 10, ₹ 8 paid up

$$(30\%/18\%) \times ₹ 8 = ₹ 13.33$$

Note: It has been assumed that the company will be able to maintain 30% dividend in future despite of an increase in the number of equity shares arising out of share suspense account and conversion of debentures.

VI. Valuation of equity shares as per EPS yield

	₹
Profit before tax	1,66,00,000
Less: Interest on convertible debentures	<u>(1,35,000)</u>
	1,64,65,000
Less: Tax @ 30%	<u>(49,39,500)</u>
Profit after tax	<u>1,15,25,500</u>
Equity Share Capital (25,00,000 + 32,00,000 + 25,00,000)	82,00,000

Earnings per rupee of share capital = $1,15,25,500 / 82,00,000 = ₹ 1.41$

(i) *EPS during 2020-2021:*

Share of ₹ 10 fully paid up $1.41 \times 10 = ₹ 14.10$

Share of ₹ 10, ₹ 8 paid up $1.41 \times 8 = ₹ 11.28$

Share of ₹ 5 fully paid up $1.41 \times 5 = ₹ 7.05$

(ii) *Value of shares:*

Value per share of ₹ 10 fully paid up

$$₹ \frac{14.1}{3} \times ₹ 10 = ₹ 47$$

Value per share of ₹ 10, ₹ 8 paid up

$$₹ \frac{11.28}{3} \times ₹ 10 = ₹ 37.6$$

Value per share of ₹ 5 fully paid up

$$₹ \frac{7.05}{3} \times ₹ 10 = ₹ 23.5$$

Question 6

- (a) *Shreya Limited grants 200 stock options to each of its 2,000 employees on 1st April, 2018 for ₹30, depending upon the employees at the time of vesting options. The market price of the share is ₹75.*

These options will vest at the end of year 1 if the earnings of Shreya Limited is 18% or it will vest at the end of the year 2 if the average earning of two years is 15% or lastly it will vest at the end of the third year if the average earning of 3 years will be 12%. 10,000 unvested options lapsed on 31st March, 2019, 8,000 unvested options lapsed on 31st March, 2020 and finally 7,000 unvested options lapsed on 31st March, 2021.

Following is the earnings of Shreya Limited at the end of every year:

For the year ended on 31st March, 2019 - 16%. The company expects to earn 15% in next year.

For the year ended on 31st March, 2020 - 12%. The company expects to earn 10% in next year.

For the year ended on 31st March, 2021 - 10%.

1,700 employees exercised their vested options within a year and remaining options were unexercised at the end of the contractual life. The face value of the share of the Company is ₹10. Pass necessary Journal entries to record the above transaction.

(8 Marks)

- (b) *A-One 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 31st March, 2019. Few machines were sold on hire purchase basis. The hire purchase price was set at ₹ 200 lakh as against the cash price of ₹ 160 lakh. The amount was payable as ₹ 40 lakh down payment and balance in 5 equal annual instalments. The hire vendor collected first instalment as on 31st March, 2020 but could not collect the second instalment which was due on 31st March, 2021. The company was finalising accounts for the year ending 31st March, 2021. Till 15th May, 2021, the date on which the Board of Directors signed the accounts, the second instalment was not collected. Presume IRR to be 10.42%.

Determine:

- (i) What should be the principal outstanding as on 1st April, 2020? Should the company recognise finance charges for the financial year 2020-2021 as income?
- (ii) What should be the amount of provision to be made as per prudential norms for NBFCs laid down by RBI in respect of hire purchase assets?
- (iii) What should be the net book value of assets as on 31st March, 2021 so far A-One Limited is concerned as per NBFC prudential norms requirement for provisioning in respect of hire purchase assets? **(8 Marks)**

Answer

(a)

Journal Entries

Date	Particulars	₹	₹
31.3.2019	Employees compensation expenses A/c Dr. To ESOS outstanding A/c (Being compensation expense recognized in respect of the ESOP i.e. 200 options each granted to 2,000 employees at a discount of ₹ 45 each, amortised on straight line basis over vesting years- Refer W.N.)	87,75,000	87,75,000
31.3.2019	Profit and Loss Account Dr. To Employees compensation expenses A/c (Being compensation expense charged to Profit & Loss A/c)	87,75,000	87,75,000
31.3.2020	Employees compensation expenses A/c Dr. To ESOS outstanding A/c (Being compensation expense recognized in respect of the ESOP - Refer W.N.)	26,85,000	26,85,000

31.3.2020	Profit and Loss Account To Employees compensation expenses A/c (Being compensation expense charged to Profit & Loss A/c)	Dr.	26,85,000	26,85,000
31.3.2021	Employees compensation Expenses A/c To ESOS outstanding A/c (Being compensation expense recognized in respect of the ESOP – Refer W.N.)	Dr.	54,15,000	54,15,000
	Profit and Loss A/c To Employees compensation expenses A/c (Being compensation expenses charged to Profit & Loss A/c)	Dr.	54,15,000	54,15,000
2021-2022	Bank A/c (3,40,000 x ₹30)	Dr.	1,02,00,000	
	ESOS outstanding A/c [(1,68,75,000/3,75,000) x 3,40,000]	Dr.	1,53,00,000	
	To Equity share capital (3,40,000 x ₹ 10)			34,00,000
	To Securities premium A/c (3,40,000 x ₹65)			2,21,00,000
	(Being 3,40,000 options exercised at an exercise price of ₹ 75 each)			
31.3.2022	ESOS outstanding A/c To General Reserve A/c (Being ESOS outstanding A/c on lapse of 35,000 options at the end of exercise of option period transferred to General Reserve A/c)	Dr.	15,75,000	15,75,000

Working Note:**Statement showing compensation expenses to be recognised every year**

Particulars	Year 1 (31.3.2019)	Year 2 (31.3.2020)	Year 3 (31.3.2021)
Expected vesting period (at the	2 nd year	3 rd year	3 rd year

end of the year)			
Number of options expected to vest	3,90,000 options	3,82,000 options	3,75,000 options
Total compensation expenses accrued @ 45 (i.e. 75-30)	<u>₹ 1,75,50,000</u>	<u>₹ 1,71,90,000</u>	<u>₹ 1,68,75,000</u>
Compensation expenses of the year	1,75,50,000 x $\frac{1}{2}$ = ₹ 87,75,000	1,71,90,000 x $\frac{2}{3}$ = ₹ 1,14,60,000	₹ 1,68,75,000
Compensation expenses recognized previously	<u>Nil</u>	<u>₹ 87,75,000</u>	<u>₹ 1,14,60,000</u>
Compensation expenses to be recognized for the year	<u>₹ 87,75,000</u>	<u>₹ 26,85,000</u>	<u>₹ 54,15,000</u>

- (b) (i) Since, the hire-purchaser paid the first instalment due on 31.3.2020, the notional principal outstanding on 1.4.2020 was ₹ 100.50 lakhs (refer W.N.).

In the year ended 31.03.2021, the instalment due of ₹ 32 lakh has not been received. However, it was due on 31.3.2021 i.e on the balance sheet date, and therefore, it will be classified as standard asset. A-One Ltd. will recognise ₹ 10.47 lakh as interest income included in that due instalment as this should be treated as finance charge.

(ii) **The net book value of the assets as on 31.3.2021**

	₹ in lakh
Overdue instalment	32.00
Instalments not due (₹ 32 lakh x 3)	<u>96.00</u>
	128.00
Less: Finance charge not matured and hence not credited to Profit and loss account (8.23 + 5.75 + 3.05)	<u>(17.03)</u>
	110.97
Less: Provision as per NBFC prudential norms (Refer point (iii))	<u>(14.97)</u>
Net book value of assets for A-One Ltd.	<u>96.00</u>

(iii) **Amount of Provision**

	₹ in lakh
Overdue instalment	32.00
Instalments not due (₹ 32 lakh x 3)	<u>96.00</u>
	128.00
Less: Finance charge not matured and hence not credited to Profit and loss account (8.23 + 5.75 + 3.05)	<u>(17.03)</u>

	110.97
Less: Depreciated value (cash price less depreciation for two years on SLM @ 20%*)	<u>(96.00)</u>
Provision to be created as per NBFC prudential norms	<u>14.97</u>

Since, the instalment of ₹ 32 lakhs not paid, was due on 31.3.2021 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 lakh*)

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)
31-3-2019		(120)	-----	---	120.00
31-3-2020	120.00	32	12.50	19.50	100.50
31-3-2021	100.50	32	10.47	21.53	78.97
31-3-2022	78.97	32	8.23	23.77	55.20
31-3-2023	55.20	32	5.75	26.25	28.95
31-3-2024	28.95	32	3.05	28.95	0.00

Question 7

Answer any four of the following:

- (a) Analyse and state whether Corporate Social Responsibility (CSR) provisions are applicable to the following companies with reasons thereof.

(*₹ in crore*)

Particulars	X Ltd.	Y Ltd.	Z Ltd.
Net Worth	650	300	490
Turnover	850	1,500	900
Net Profit	4.8	3.70	3

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

- (b) Whether Corporate Governance report is mandatory in the annual report of Listed Companies? What are the disclosures required to be made in the corporate governance section of the annual report?
- (c) A Mutual Fund purchased 20,000 debentures of a company on 1st June, 2020 for ₹21,50,000 and further 10,000 debentures on 1st November, 2020 for ₹10,97,500. The debentures carry fixed annual coupon of 9%, payable on every 31st March and 30th September. On 28th February, 2021, the fund sold 12,000 of these debentures for ₹13,56,000. Nominal value per debenture is ₹100.
- You are required to prepare Investment in Debenture A/c in books of the Mutual Fund.
- (d) List any five major changes in Ind AS 7 "Cash Flow Statement" vis-a-vis notified AS 3 "Cash Flow Statement".
- (e) Define Value Added (VA) concept in financial reporting and how Gross Value Added (GVA) is calculated? **(4 x 4 = 16 Marks)**

Answer

- (a) A company which meets the net worth, turnover or net profits criteria in immediately preceding financial year will need to apply CSR provisions as per sections 135(2) to (5) read with the CSR Rules.

As per the criteria -

- (1) Net worth greater than or equal to ₹ 500 Crore: This criterion is satisfied in case of X Ltd.
- (2) Sales greater than or equal to ₹ 1,000 Crore: This criterion is satisfied in case of Y Ltd.
- (3) Net profit greater than or equal to ₹ 5 crore: This criterion is not satisfied in case of any company.

Based on above, the CSR provisions are applicable to companies X Ltd. and Y Ltd.

Note: It is assumed that the given figures in the question for respective companies belong to immediately preceding financial year.

- (b) As per SEBI Listing Regulations, 2015 (LODR), regulation 27(2) states that it is mandatory for every listed company to submit corporate governance report within fifteen days from the quarter-end. Therefore, all the listed entities need to comply with the provision.

However, there are certain exceptions:

A listed entity

- having paid-up equity share capital which is not exceeding ten crores and

- not having a net worth which is exceeding twenty-five crores as on the last day of the previous financial year.
- which has listed its securities on the SME exchange.

The following disclosures shall be made in the section on the corporate governance of the annual report:

- (1) A brief statement on listed entity's philosophy on code of governance
- (2) Board of directors
- (3) Audit committee
- (4) Nomination and Remuneration Committee
- (5) Remuneration of Directors
- (6) Stakeholders' grievance committee
- (7) General body meetings
- (8) Means of communication
- (9) General shareholder information
- (10) Other Disclosures

(c) **Investment in Debentures A/c**

		₹			₹
1 st June, 2020	To Bank	21,50,000	1 st June, 2020	By Interest Recoverable (Note 1)	30,000
1 st Nov., 2020	To Bank	10,97,500	1 st Nov., 2020	By Interest Recoverable (Note 2)	7,500
28 th Feb., 2021	To Interest Recoverable (Note 3)	45,000	28 th Feb., 2021	By Bank	13,56,000
28 th Feb., 2021	To Profit on disposal (Note 4)	27,000	31 st March, 2021	By Balance c/d	19,26,000
		<u>33,19,500</u>			<u>33,19,500</u>

Working Notes:

1. $20,000 \times 100 \times 9/100 \times 2/12 = ₹ 30,000$
2. $10,000 \times 100 \times 9/100 \times 1/12 = ₹ 7,500$
3. $12,000 \times 100 \times 9/100 \times 5/12 = ₹ 45,000$

4. Cost of investments (per unit)	= $[(21,50,000 - 30,000) + (10,97,500 - 7,500)]/30,000 \text{ units}$
	= $[21,20,000 + 10,90,000]/30,000 = ₹ 107$
Cost of investments sold	= ₹ 107 x 12,000 = ₹ 12,84,000
Sale proceeds	= ₹ 13,56,000 - ₹ 45,000 (interest)
	= ₹ 13,11,000
Profit	= ₹ 13,11,000 - ₹ 12,84,000 = ₹ 27,000

(d) Major Changes in Ind AS 7 vis-à-vis Notified AS 3 (Cash Flow Statement)

- (i) **Bank Overdraft Repayable on Demand:** Ind AS 7 specifically includes bank overdrafts which are repayable on demand as a part of cash and cash equivalents, whereas AS 3 is silent on this aspect.
- (ii) **Treatment of Cash Payments in Specific Cases:** Ind AS 7 provides the treatment of cash payments to manufacture or acquire assets held for rental to others and subsequently held for sale in the ordinary course of business as cash flows from operating activities. Further, treatment of cash receipts from rent and subsequent sale of such assets as cash flow from operating activity is also provided. AS 3 does not contain such requirements.
- (iii) **New Examples of Cash Flows arising from Financing Activities:** Ind AS 7 includes the following new examples of cash flows arising from financing activities:
 - (a) cash payments to owners to acquire or redeem the entity's shares
 - (b) cash proceeds from mortgages
 - (c) cash payments by a lessee for the reduction of the outstanding liability relating to a finance lease.
- (iv) **Adjustment of the Profit or Loss for the Effects of Undistributed Profits of Associates and Non-controlling Interests:** As compared to AS 3, Ind AS 7 specifically requires adjustment of the profit or loss for the effects of 'undistributed profits of associates and non-controlling interests' while determining the net cash flow from operating activities using the indirect method.
- (v) **Cash Flows associated with Extraordinary Activities:** AS 3 requires cash flows associated with extraordinary activities to be separately classified as arising from operating, investing and financing activities, whereas Ind AS 7 does not contain this requirement.

- (vi) **Disclosure of the Amount of Cash and Cash Equivalents in Specific Situations:** As compared to AS 3, Ind AS 7 requires an entity (except an investment entity) to disclose the amount of cash and cash equivalents and other assets and liabilities in the subsidiaries or other businesses over which control is obtained or lost. Ind AS 7 also requires reporting the aggregate amount of the cash paid or received as consideration for obtaining or losing control of subsidiaries or other businesses in the statement of cash flows, net of cash and cash equivalents acquired or disposed of as a part of such transactions, events or changes in circumstances. AS 3 does not contain such requirements.
- (vii) **Cash Flows arising from Changes in Ownership Interests in a Subsidiary:** Ind AS 7 requires classifying cash flows arising from changes in ownership interests in a subsidiary that do not result in a loss of control as cash flows from financing activities. AS 3 does not contain such a requirement.
- (viii) **Investment in Subsidiaries, Associates and Joint Ventures (Investees):** Ind AS 7 mentions the use of equity or cost method while accounting for an investment in an associate, joint venture or a subsidiary. It also specifically deals with the reporting of interest in an associate or a joint venture using equity method. AS 3 does not contain such requirements.
- (ix) **Use of Different Terminology and Translation of Cash Flows of a Foreign Subsidiary:** Ind AS 7 uses the term 'functional currency' instead of 'reporting currency' (as used in AS 3). Ind AS 7 also deals with translation of cash flows of a foreign subsidiary whereas in AS 3, it is not dealt with.
- (x) **Disclosures:** Ind AS 7 requires more disclosures as compared to AS 3.

Note: Students may write any 5 points out of the above 10 points.

(e) Value Added Statement

Value Added (VA) is the wealth; a reporting entity has been able to create through the collective effort of capital, management, and employees. In economic terms, value added is the market price of the output of an enterprise less the price of the goods and services acquired by transfer from other firms. VA can provide a useful measure in gauging performance and activity of the reporting entity.

The conventional VA statement is divided into two parts – the first part shows how VA is arrived at and the second part shows the application of such VA.

Gross Value Added (GVA): GVA is arrived at by deducting from sales revenue the cost of all materials and services which were brought in from outside suppliers. Besides sales revenue, any direct income, investment income and extraordinary incomes or expenses are also included in calculation of GVA. Including these items, the equation we get

(Sales revenue + Direct incomes) – Bought in cost of materials and services + Investment incomes + Extraordinary items = Retained profit + Depreciation + Wages + Interest + Tax + Dividend.