

C.A. Final (New Course)

First Study

Subject: Financial Reporting

Instructions :

- (i) *All questions are compulsory.*
- (ii) *Date of Examination : 15.02.2010*
- (iii) *Total Number of Questions : 6*
- (iv) *Total marks : 100*
- (v) *Total duration : 3 Hours*
- (vi) *Use of two colour pens (black & blue or Black or Pink etc) is NOT allowed. Use only single colour pen.*
- (vii) *Begin answer of the next question in new page.*
- (viii) *Answer all the questions serially.*

Question 1.

A Ltd. acquired 80% of both classes of shares in B Ltd. on 1.4.2007. The draft Balance Sheets of two companies on 31st March, 2008 were as follows:

Liabilities	A Ltd.	B Ltd.	Assets	A Ltd.	B Ltd.
Share Capital:					
Equity shares of Rs.10 each, full paid up	3,000	600	Plant & machinery	2,060	600
14% Preference shares of Rs.100 each, fully paid up	-	400	Furniture & fixtures	600	540
General reserve	1,900	40	Investments in equity shares of B Ltd.	1,920	-
Profit and loss account	1,600	720	in preference shares of Ltd.	320	-
Creditors	300	320	Stock	680	404
			Debtors	560	316
			Cash at bank	<u>660</u>	<u>220</u>
Total	<u>6,800</u>	<u>2,080</u>	Total	<u>6,800</u>	<u>2,080</u>

Note: Contingent liability – A Ltd.: Claim for damages lodged by a contractor against the company pending in a law-suit – Rs.1,55,000.

Additional Information:

- (i) General reserve balance of B Ltd. was the same as on 1.4.2007.
- (ii) The balance in Profit and Loss A/c of B Ltd. on 1.4.2007 was Rs.3,20,000, out of which dividend of 16% p.a. on the Equity capital of Rs.6,00,000 was paid for the year 2006-07.
- (iii) The dividend in respect of preference shares of B Ltd. for the year 2007-08 was still payable as on 31.3.2008.
- (iv) A Ltd. credited its Profit and Loss A/c for the dividend received by it from B Ltd. for the year 2006-07.
- (v) Sundry creditors of A Ltd. included an amount of Rs.1,20,000 for purchases from B Ltd., on which the later company made a loss of Rs.10,000.
- (vi) Half of the above goods were still with the closing stock of A Ltd. as at 31.3.2008.
- (vii) At the time of acquisition by A Ltd., while determining the price to be paid for the shares in B Ltd. it was considered that the value of plant and machinery was to be increased by 25% and that of furniture and fixtures reduced to 80%. There was no transaction of purchase or sale of these assets during the year. The directors wish to give effect to these revaluations in the consolidated balance sheet.
- (viii) The directors of A Ltd. are of opinion that disclosure of its contingent liability will seriously prejudice the company's position in dispute with the contractor.

Prepare consolidated balance sheet as at 31st March, 2008, assuming the rate of depreciation charged as 25% p.a. and 10% p.a. on plant and machinery and furniture and fixtures respectively. Workings should be part of the answer.

(20 Marks)

Question 2.

On 1.7.2002, Abhilash, an IIT Graduate in Mechanical Engineering, formed a Company, Abhilash Ltd. The entire Share Capital was held by Abhilash and his wife Lakshana.

On the same day, Balaji, a Management Graduate in Marketing from SP Jain Institute of Management, floated a Company Balaji Ltd. Balaji, together with his wife Subha, held 100% of the Share Capital of the Company. He commenced trading in Chennai.

To synergise the operations and also to cut down costs, Abhilash Ltd and Balaji Ltd decided that with effect from 1.7.2004 a Holding Company, Subhaiakshana Ltd would be formed to take over the Shares in both the Companies.

It was agreed that the accounts of Abhilash Ltd for the two years ended 30.6.2004 should be adjusted., as necessary, so as to conform to the accounting policies and conventions used by Balaji Ltd. Subhalakshana would then issue securities to the shareholders in Abhilash Ltd and Balaji Ltd on the following basis –

1. Rs. 10 of 9% Loan Stock 2004 for every Rs. 10 of net asset owned by each Company.
2. Rs. 10 Equity Shares based on a two-year purchase of the Profits after Taxation profits are to be the average profits of two years, with second year weighted on the basis of 2 : 1 basis.

The accounts of the two years ended 30.6.2004 showed –

Particulars	Abhilash Ltd		Balaji Ltd	
	2003	2004	2003	2004
ASSETS				
Fixed Assets : Furniture, Fixtures etc. Gross Block	1,20,000	1,20,000	1,60,000	1,60,000
Less : Accumulated Depreciation	12,000	24,000	24,000	48,000
Net Book Value	<u>1,08,000</u>	<u>96,000</u>	<u>1,36,000</u>	<u>1,12,000</u>
Trade Investments	-	-	-	3,00,000
Current Assets :				
Stock at cost	2,60,000	3,45,000	2,90,000	3,52,000
Debtors	2,92,500	4,24,000	3,24,000	4,32,000
Quoted Investments at Cost (Market Value Rs. 1,40,000)	-	1,00,000	-	-
Cash at Bank	10,000	-	35,000	-
Total	6,70,500	9,65,000	7,85,000	8,96,000
LIABILITIES				
Share Capital : Equity Shares of Rs. 10 each	2,00,000	2,00,000	2,50,000	2,50,000
Profit & Loss account	1,28,000	2,70,000	1,39,000	3,02,000
Unrealised Appreciation in investment	-	-	-	80,000
Creditors	2,60,500	3,07,000	3,00,000	3,42,000
Bank Overdraft	-	80,000	-	1,05,000
Taxation	82,000	1,08,000	96,000	1,17,000
Total	6,70,500	9,65,000	7,85,000	11,96,000

The following information is obtained :

1. **Purchases:** Both Abhilash and Balaji purchase the Steel Rods from the same supplier, who sells on a fixed price list. Abhilash Ltd and Balaji Ltd themselves apply a 50% uplift on cost, to calculate their own selling Prices. The Suppliers Price List showed –
 - 1st July 2002 Rs. 100 each
 - 1st June 2003 Rs. 110 each
 - 1st May 2004 Rs. 120 each

The number of rods purchased and sold in the periods after the price increased were:

Particulars	Abhilash Ltd		Balaji Ltd	
	Purchase	Sales	Purchase	Sales
1 st June – 30 th June 2003	1,000	800	1,200	900
1 st May – 30 th June 2004	1,500	1,000	2,900	2,500

- Stock :** Abhilash Ltd calculates the cost price of stock on FIFO basis, while Balaji Ltd uses LIFO basis.
- Depreciation:** Depreciation in both the Companies is provided on the Straight-Line Method. There had been no material change in the Fixed Assets since 1.7.2002 when the Companies commenced trading. The Fixed Assets of the two Companies are of similar nature.
- Bad Debts:** Abhilash Ltd deducts 1% from Gross Trade Debtors, as a general provision against doubtful debts.
- Debtors:** Debtors comprise the following -

Particulars	Abhilash Ltd		BalaJi Ltd	
	2002	2003	2002	2003
Trade Debtors	2,47,500	3,96,000	3,20,000	4,25,000
Prepaid Expenses	5,000	8,000	4,000	7,000
Advertising (Note)	40,000	20,000	-	-

Note: Abhilash Ltd carried out an extensive advertising campaign when commencing to trade, and decided to write off this expense equally over three years. Balaji Ltd incurred similar expenditure, which was however written off as incurred.

- Managerial Remuneration:** It was agreed by all parties that the Directors' Remuneration paid by Balaji Ltd is strictly on commercial basis, whereas that paid by Abhilash Ltd contains a "distribution of profit" element of Rs. 30,000 in each year.
- Profits:** Net Profits including investment income, after Provision for Corporate Tax were-

Year ending 30 th June...	Abhilash Ltd	Balaji Ltd
2003	1,28,000	1,39,000
2004	1,42,000	1,63,000

Required –

- Calculate the terms of the offer to be made to Abhilash Ltd and Balaji Ltd by Subhalakshana Ltd.
- Prepare the Balance Sheet of Subhalakshana Ltd after the transactions are given effect to.

(20 Marks)

Question 3.

(a) X Ltd. plans to take over B Ltd. Independent Cash Flow forecasts of both companies are as follows:

Year	X ltd (Rs in lakhs)	B ltd (Rs in lakhs)
1	200	50
2	225	65

3	250	80
4	270	95
5	285	110
6	310	120
7	350	130
8	600	150
9	610	170
10	650	180
	3750	1150

Following further information is available from the latest Balance Sheet of Beta Ltd.

Assets:		Rs. in lakhs
Fixed Assets		5,00
Stock		1,15
Debtors		50
		6,65
Less: Liabilities		
Sundry creditors	1,65	
Long term loan	2,00	(3,65)
Net assets		3,00

X Ltd. finds that fixed assets of book value Rs.75 lakhs will not be used which will fetch Rs.50 lakhs on immediate disposal. Moreover, stock will fetch Rs.140 lakhs and debtors Rs.48 lakhs immediately. But X Ltd. has to pay off the liabilities immediately. Also it has to pay Rs.110 lakhs to workers of B Ltd. whose service cannot be used. It appears that after merger X Ltd. has to invest Rs.210 lakhs for renovation of the plant and machinery at the end of 1st year and Rs.50 lakhs for modernization at the end of 2nd year after merger.

Forecast of cash flows of X Ltd. after merger :

Year	X ltd (Rs in lakhs)
1	240
2	280
3	350
4	400
5	410
6	480
7	550
8	800
9	880
10	950
	5340

Determine the maximum value of B Ltd. which its management should ask from X Ltd. You may use 20% discount rate.

(b) While closing its books of account 31st March, a NBFC has its advances classified as follows-

Particulars	Rs. In lakhs
Standard Assets	16,800
Sub-Standard Assets	1,340
Secured Portions of Doubtful Debts:	
- upto one year	320
- one year to three years	90
- more than three years	30
Unsecured Portion of Doubtful Debts	97
Loss Assets	48

Calculate the amount of provision which must be made against the advances.

(10+4=14 Marks)

Question 4.

(a) AIPL imported a machine on 01.01.2009 for GBP 24000 on deferred payment basis being payable in six annual installments at the end of the financial year, commencing from 31.03.2009. Determine the exchange difference and the carrying amounts of the liability at the end of each financial year as per Revised AS 11 on the basis of the following exchange rates :

Date	01.01.2009	31.03.2009	31.03.2010	31.03.2011	31.03.2012	31.03.2013	31.03.2014
Rate	81.00	80.50	80.25	80.75	82.00	84.50	86.25

(b) Arihant Industries has taken a loan of Euro 200,000 on 1st April, 2009, for a specific project at an interest rate of 5% per annum, payable annually. On 1st April, 2009, the exchange rate between the currencies was Rs. 54 per Euro. The exchange rate, as at 31st March, 2010, is Rs. 57 per Euro. The corresponding amount could have been borrowed by Arihant Industries in local currency at an interest rate of 11% per annum as on 1st April, 2009. Compute the amount of borrowing costs as per para 4(e) of AS-16:

(10+4=14 Marks)

Question 5.

(a) Zero Limited commenced its business on 1st April, 1996. 2,00,000 equity shares of Rs. 10 each at par and 12.5% debentures of aggregate value of Rs. 2,00,000 were issued and fully taken up. The proceeds utilised as under,:

	Rs.
Fixtures and Equipments (Estimated Life 10 years, no Scrap Value)	16,00,000
Goods Purchased for Resale at Rs. 200 per unit	6,00,000

The goods were entirely sold by 31st January, 1997 at a profit of 40% on selling price.

Collections from debtors outstanding on 31st March amounted to Rs. 60,000, goods sold were replaced at a cost of Rs. 7,20,000, the number of units purchased being the same as before. A payment of Rs. 40,000 to a supplier was outstanding as on 31st March, 1997.

The replaced goods remained entirely in stock on 31st March, 1997.

Replacement cost as at 31st March 1997 was considered to be Rs 280 per unit.

Replacement cost of fixtures and equipments (depreciation on straight line basis) was Rs. 20,00,000 as at 31st March, 1997.

Draft the Profit and Loss Account and the Balance Sheet on replacement cost (entry value) basis and

on historical cost basis.

(b) AIPL taken on lease an equipment costing Rs.3,00,000 with expected useful life of 4 years for three years. The asset would revert to AIPL under the lease agreement. The other information available in respect of lease agreement is:

- (i) The unguaranteed residual value of the equipment after the expiry of the lease term is estimated at Rs.40,000.
- (ii) The implicit rate of interest is 10%.
- (iii) The annual payments have been determined in such a way that the present value of the lease payment plus the residual value is equal to the cost of asset.

Ascertain in the hands of AIPL:

- a) The annual lease payment.
- b) The unearned finance income.
- c) The segregation of finance income, and also,
- d) Show how necessary items will appear in its profit and loss account and balance sheet in the FIRST year.

(8+8=16 Marks)

Question 6

(i) R Ltd acquired 4000 equity shares of P Ltd. at Rs 150 cum right per share. Later on P Ltd. made right issue of 1:1 at Rs. 120 per share. Calculate the cost of the investment if:

- (a) R Ltd exercised 100% of right issue.
- (b) R Ltd exercised 90% of right issue.

(ii) “Company invested 100 lakhs in April, 2009 for the acquisition of ABC Ltd doing similar business, the negotiations for which had started during the year.

State with reasons, how you would deal with this in the financial statements.

(iii) ABC Limited Company has been including interest in the valuation of closing stock. In 2009-10 the management of the company decided to follow AS 2 and accordingly interest has been excluded from the valuation of closing stock. This has resulted in a decrease in profits by Rs. 4,50,000. Is a disclosure necessary? If so, draft the same.

(6+5+5=16 Marks)