VALUE ADDED STATEMENT

A Value Added Statement (VAS) exhibits value addition or wealth creation by combined efforts of a firm's capital, management and labour. It also shows its distribution among employees (including labour and management), capital , government and the firm itself (for reinvestment)[1]. In calculation terms, it is the difference between the sales value of the product or service and the cost of brought-in-material and services.

It represents the wealth created by the organization itself and shows typically how this wealth goes to meet the cost of the following:

	Appears in P&L a/c as
Employees , managers (including directors)	Wages salaries etc (including retirements and welfare expenses)
Capital	Interest , dividend
To government for common spending	Tax

[1] The value added statement measures performance in terms of value added by the enterprise through the collective efforts of management, employees and the providers of capital. The statement shows how value added has been (i) distributed to those contributing to its creation and the government and (ii) reinvested in the business.

Value-added is the accounting synonym for Wealth creation. Thus it reflects wealth creation and wealth distribution. This translates into two very powerful and mutually supporting strategic "legs": maximum wealth creation and sensible distribution. In turn five strategic principles are involved here. Three of them relate to wealth creation and two to distribution. Optimum wealth creation is the result of (1) selling the most you can; (2) getting the best price; and (3) keeping your outside costs as low as possible. Sensible distribution is based on (4) meeting the legitimate expectations of each stakeholder and (5) encouraging continued contribution.

Value-added is the company's contribution to GDP, and therefore a contribution to national prosperity. It is the company's contribution to the market and society as a whole. It is the golden thread that binds capital, labour, management and government all together.

Reinvestment	Depreciation, retained profit

VAS is prepared on the lines of Income statement (i.e. Profit and Loss Account). While preparing this statement (on the lines of the Income statement), the above four categories the items are not considered in the statement (VAS) .

Some important points about VAS

(i) There are two types of value added statements (a) Net Value Added Statement and (b) Gross value Added Statement. The Statement, that we have referred above, is Gross VAS. In Net VAS, depreciation is considered as a part of VAS itself and not shown in distribution statement. If the question is silent regarding net or gross, we may prepare Gross VAS as it is on the lines suggested by CIMA, London.

(ii) Interest on borrowings for working capital should be considered in VAS and not in the distribution statement.

(iii) There are two opinions regarding treatment of Excise and sales tax while preparing the value added statements. As per first opinion , these should be considered while preparing the Value Added Statement. The second opinion is to show their amount should be shown in the distribution statement under the head Government . The first approach is more popular with the professional, the second is favoured by the academicians.(We may follow the first approach)

Question No. 1

The following figures for a period were called out from the books of Value Corporation:

	Rs.
Sales	24,80,000
Purchase of raw materials	10,00,000
Agent's commission	20,000
Consumable stores	25,000
Packing material	10,000
Stationery	10,000
Audit Fees	4,000
Staff welfare expenses	1,58,000
Insurance	26,000
Rent rate & taxes	16,000
Managing director's remuneration	84,000
Traveling expenses	21,000
Fuel and oil	9,000
Electricity	5,000
Materials used in repairs:	
(i) Materials to plant and machinery	24,000
(ii) Materials to buildings	10,000
Advertisement	25,000
Salaries and wages	6,30,000

Postage and telegrams	14,000
Contribution to provident fund, etc.	60,000
Directors' fees & traveling expenses	40,000
Subscription paid	2,000
Carriage	22,000
Interest on loans taken	18,000
Dividend to shareholders	30,000
Depreciation provided	55,000
Income-tax provided	1,00,000
Retained earnings	1,25,000
Opening stock :Raw materials	85,000
Finished goods	2,00,000
Closing stock :Raw materials	1,08,000
Finished goods	2,40,000

From the above you are required to prepare a statement detailing the source and disposal to added value. Does your statement corroborate the assertion of the chairman of the company in the annual general meeting that 75 per cent of added value is accounted by employee costs?

Ans. Value added statement for the period ended …………

Sales		24,80,000
Increase in F. Stock		40,000
		25,20,000
Raw material consumed	9,77,000	
Agents' commission	20,000	
Con. Stores	25,000	
Packing material	10,000	
Stationary	10,000	
Audit fees	4,000	
Insurance	26,000	
Rent	16,000	

T. Exp.	21,000	
Fuel & Oil	9,000	
Elec.	5,000	
Mat. Used in repairs	34,000	
Advertisements	25,000	
Postage	14,000	
Subscription paid	2,000	
Carriage	22,000	
		12,20,000
Value added		13,00,000

Distribution of value added

Employees & Management		Amount	%
Staff welfare	1,58,000		
MD remuneration	84,000		
Salaries and wages	6,30,000		
Cont. PF	60,000		
D. Fees	40,000	9,72,000	74.77
Government			
Taxes		1,00,000	7.69
Capital			
Dividend	30,000		
Int.	18,000	48,000	3.69
Reinvestment			
Dep.	55,000		
Retained earnings	1,25,000	1,80,000	13.85
Total		13,00,000	100

Question No. 2: Worthwhile Corporation had been preparing value added statements for the past five years. The personnel manager of the company has suggested that a value added incentive scheme when introduced will motivate employees to better performance. To introduce the scheme, it is proposed that the best index performance, i.e., employee costs to added value for the last 5 years will be used as the target index for future calculations of the bonus to be earned.

After the target index is determined, any actual improvement in the index will be rewarded, the employer and employees sharing any such bonus in the ratio 1 : 2. The bonus is given at the year-end, after profit for the year is determined.

From the following details, find out the bonus to be paid to the employees, if any, for 1987 :

Value Added Statement for 5 years (Rs.'000)

Year	*1982*	*1983*	*1984*	*1985*	*1986*
Sales	2,800	3,800	4,600	5,200	6,000
Less: Bought in					
good service	1,280	2,000	2,500	2,800	3,200
Added value	1,520	1,800	2,100	2,400	2,800
Employees costs	650	760	840	984	1,120
Dividend	100	150	200	240	300
Taxes	320	380	420	500	560
Depreciation	260	310	360	440	560
Debenture interest	40	40	40	40	40
Retained earnings	150	160	250	196	200
Added value	1,520	1,800	2,100	2,400	2,800

Summarized P&L for 1987 (Rs.000)

Sales		7,300
Cost of material	2,500	
Wages	700	
Prod. salaries	200	
Prod. expenses	700	
Dep. of Machines	500	
Adm. Salaries	300	
Adm. Expenses	300	
Adm. Depreciation	200	
Deb. Interest	40	
Salaries (sales deptt.)	60	
Sales Expenses	200	
Dep. (sales deptt. assets)	60	5,760
Profit		1,540

Ans.

	1982	1983	1984	1985	1986
Index performance	$\frac{650}{1520}$ = .43	$\frac{760}{1800}$ = .42	$\frac{840}{2100}$ = .40	$\frac{984}{2400}$ = .41	$\frac{1120}{2800}$ = .40

Best Index performance = .40

Value added statement for the year ended 31.12.1987

Sales		7300
Mat.	2500	
P. Exp.	700	
A. Exp.	300	
S. Exp.	200	3700

Value added	3600

On the basis of best index , employees should have got	: 1440
Employees got	: 1260
Total Bonus	: 180
Bonus to employees	: 120
Bonus to employers	: 60

Distribution of VA			%
Employees			
Wages	700		
Production salaries	200		
Adm. Salaries	300		
Sales salaries	60		
Bonus	120	1380	38.33
Capital			
Bonus to employer			
(assumed by way of dividend)	60		
Interest	40	100	2.78
Reinvestment			
Retained profit	1360		
Dep.	760	2120	58.89
Total		3600	100.00

Q. No. 3 : S.V. Ltd. have announced X′mas bonus for staff — 50 per cent of any value added earned in excess of $1.35 per $1 of labour. S.V. Ltd.′s results for year ended 30th September, 1990 are as follows : ($′000)

Sales			5,000	
Cost of Sales				
Cost of production:				
Materials	1,000			
Direct labour	1,200			
Factory overhead*	1,500	3,700		
Work-in-progress :				
Opening	140			
Closing	160	(20)		
Finished goods stock :				
Opening	400			
Closing	440	(40)	3,640	
Gross profit				1.360
S.& A. Overhead*				870
Trading profit				490
Royalties received				10
Net profit				500
Taxation				200
Net profit after tax				300
Dividends				100
		Profit		200

	Factory	*Selling & Admn.*
*Overhead analysis($'000)		
Wages and salaries	400	470
Equipment leasing	50	10
Depreciation	200	50
Others (rent, rates, etc)	850	340

Find the amount of bonus due to an employee whose wages is $ 5000 p.a.

Ans. VAS for year ended 30.9.90

Sales	5000	
Increase in F. Stock	40	
Increase in WIP	20	5060
Material	1000	
FO 50 + 850	900	
SAO 10+340	350	2250
VA by manufacturing activities		2810
VA by other activities		10
TOTAL VA		2820

Wage bill = 1200 +400 +470 = 2070

Bonus to staff = 0.50 [2820 – 1.35(2070)] = 12.75

Bonus as % of wages = (12.75/2070) x 100 = 0.62

Bonus to the employee = .62% of 5000 = $31

Distribution of VA

		%
Employees	2082.75	73.86
Capital (Div.)	100.00	3.55
Govt. (Tax)	200.00	7.09
Reinvestment (Dep 250 + retained profit 187.25)	437.25	15.50
Total	2820.00	100.00

Q.NO.4 The following is the Profit & Loss account of Galaxy Ltd. for the year ended 31.3.04. Prepare Gross value added statement and show the reconciliation between GVA and Profit Before Tax :

Profit and Loss account for year ended 31.3.2004 (Rs. Lakhs)

Income:			
Sales		890	
Other income		55	
		945	
Expenditure:			
Production and operational expenses (note a)	641		
Factory Expenses (administration) (note b)	33		
Interest (note c)	29		
Dep.	17	720	
PBT			225
Tax (note d)		30	
PAT			195
Balance as per last B/S		10	
		205	
Transfer to General reserve	45		
Dividend	95		140

Surplus carried to B/S 65

Notes : **(Rs. Lakhs)**

(a) Production and Operational Expenses :

Raw material	293
Stores	59
Salaries wages Gratuities etc (Admin.)	82
Cess and Local taxes	98
Other Manufacturing Expenses	109
	641

(b) Administration expenses include salaries, commission to Directors Rs. 9.00, Provision for doubtful debts Rs. 6.30.

(c) Int. on Loan from Bank for working capital 9

Interest on bank loan for fixed loan	10
Interest on loan from IFCI for fixed loan	8
Interest on debentures	2
	29

(d) The charges for taxation include a transfer of Rs.3.00 to the credit of deferred Tax Account

(e) Cess and Local taxes include excise duty, which is equal to 10 % of cost of raw material bought in .

Ans. Gross VAS for year ended 31.3.2004

Sales			890.00
Less excise			-29.30
Net sales			860.70
Production and operation exp.:			
Raw Material	293.00		
Stores	59.00		
Other manufacturing exp.	109.00	461.00	

Factory exp (Admi.)	24.00	
Interest of w. c. borrowings	9.00	494.00
Value added by trading and manufacturing activities		366.70
Other incomes		55.00
Total VA		421.70

Distribution statement

		%
Employees (82 + 9)	91.00	21.58
Govt. (income tax 27 + cess and local tax exclusive of excise 68.70)	95.70	22.69
Capital (int. + Div.)	115.00	27.27
Reinvestment (Dep + GR + Retained profit + D. Tax)	120.00	28.46
Total	421.70	100.00

Reconciliation of PBT with VA :

PBT	225.00
Employees	91.00
Cess and local taxes	68.70
Interest	20.00
Dep.	17.00
Vale Added	421.70

Q.NO. 5 On the basis of the following income statement pertaining to Brite Ltd., you are required to prepare (a) Gross VAS (b) reconciliation of Gross VA with PBT

PROFIT AND LOSS A/C OF BRITE LTD. FOR YEAR ENDED 31.3.2003 (Rs.'000)

Income			
Sales			15,27,956
Dividend and interest			130
Misc. Income			474
Total			15,28,560
Expenditure			
Production and operational expenses			
Decrease in inventory of finished goods	26,054		
Consumption of raw material	7,40,821		
Power	1,20,030		
Wages	3,81,760		
Staff welfare expenses	26,240		
Excise duty	14,540		
Other manufacturing exp.	32,565	13,42,010	
Directors' remuneration	7,810		
Other Administrative	32,640		40,450
Interest on debentures			14,400
Interest on long term loan			10,000
Interest on bank overdraft			100 Dep.
	50,600		
1457560			
PBT			71000

Tax		25,470
PAT	45530	
Profit b/d from last year	6300	
		51,830
Transferred to GR 18,212		
Dividend 22,000		
Tax on dividend 2,818		43,030
Balance c/d to B/S		8800

Ans. Gross VAS for year ended 31.3.2003

Sales (less excise)		15,13,416
Decrease in F. Stock		- 26,054
		14,87,362
Mat.	7,40.821	
Power	1,20,030	
Other Manu. exp.	32,565	
Ad. Exp.	32,640	
Int. on BO	100	9,26,156
VA by Manu. activities		5,61,206
VA by Other activities (Div& int. and misc. income)		604
Total VAT		5,61,810

Distribution statement

			%
Employees & Management :			
Wages	381760		
Staff welfare exp.	26240		
Director remuneration	7810	4,15,819	74.01

Govt.			
Income tax	25470		
Dist, tax	2818	28,288	5.04
Capital			
Int. Deb.	14400		
Int. loan	10000		
DIV.	22000	46400	8.26
Reinvestment			
Retained profit	2500		
GR	18212		
Dep	50600	71312	12.69
Total		561810	100.00

Reconciliation :

PBT	71000
Wages	381760
Staff	26240
D. Remuneration	7810
Int. Deb.	14400
Int. Loan	10000
Dep	50600
Value added	561810

Q. No. 6 From the following Profit and Loss Account of Kalyani Ltd., prepare Gross value added statement. Show also the reconciliation of Gross Value Added and Profit before Taxation :

Profit and Loss Account for the year ended 31st March, 1995 : (Amounts in Rs. Lakhs) :

		Income
Sales	206.42	
Other income	10.20	
	216.62	

Expenditure

Production and operational exp.(note 1)	166.57			
Administration expenses (note 2)	6.12			
Interest and other charges (note 3)	8.00			
Dep.	5.69	186.38		PBT
30.24 Taxes				3.00
PAT		27.24		
Investment allowance written back		0.46		
Balance as per last Balance sheet			1.35	
		29.05		
Transferred to General Reserve		- 24.30		
Proposed Dividend		- 3.00		
Surplus carried to B/S		1.75		

Notes (1) Production and operational exp. Rs. Lakhs

Decrease in stock	30.50
Consumption of material	80.57
Consumption of stores	5.30
Salaries, wages etc	12.80
Cess and Local taxes	3.20
Other Manufacturing exp.	34.20
Total	166.57

(2) Administrative expenses include inter-alia Audit fees of Rs. 1 Lakh, Salaries to Directors Rs.2.20 Lakhs and Provision for doubtful debts Rs. 2.50 Lakhs.

(3) Interest and other charges Rs. Lakhs

Int. on fixed loans from financial institution	3.90
Interest on debentures	1.80
Interest on working capital loans	2.30
Total	8.00

Ans. **Gross VAS for the year ended 31.3.1995**

Sales		206.42
Decrease in stock		-30.50
		175.92
Ram material consumed	80.57	
Stores	5.30	
Other Manu. exp.	34.20	
Audit fees	1.00	
Provision for doubtful debts	2.50	
Other administrative exp.	0,42	
Int. on working capital borrowings	2.30	126.29
VA by Manu. and trading activities		49.63
VA by other incomes		10.20
Total VA		59.83

Distribution statement

	Rs.	Rs.	%
Management & Employees:			
Salaries and wages	12.80		
Salaries and com to directors	2.20	15.00	25.07
Capital			
Interest on fixed loans	3.90		
Interest on debentures	1.80		
Dividend	3.00	8.70	14.54
Government			
Cess and local taxes	3.20		
Income tax	3.00	6.20	10.36
Reinvestment			
Dep.	5.69		
Increase in P & L	0.40		
GR	24.30		

Invest, allowance written back	-0.46	29.93	50.03
Total		59.83	100

Reconciliation of PBT with Gross VA

PBT	30.24
Salaries	12.80
Salaries and com.	2.20
Int. on deb.	1.80
Int. on fixed loans	3,90
Cess and local tax	3.20
Dep.	5.69
Gross VA	59.83

Q. No. 7 : From the following Profit & Loss A/c , prepare a Gross value added statement for the year ended 31.12.98. Show also the reconciliation between GVA and PBT.

Profit and Loss A/c for the year ended 31.12.98 (Rs.'000)

Income

Sales 6240

Other income 55

6,295

Expenditure

Production and operational exp.(note 1) 4320

Administration expenses(factory) (note 2) 180

Interest and other charges (note 3) 624

Dep. 16 5,140 PBT

1,155 Taxes 55

PAT 1,100

Balance as per last Balance sheet +60

1,160

Transferred to fixed assets replacement Reserve - 400

Proposed Dividend - 160

Surplus carried to B/S 600

Notes (1) Production and operational expenses (Rs. thousands)

Consumption of raw materials	3210
Consumption of stores	40
Local taxes	8
Salaries	620
Other manufacturing expenses	442
Total	4320

(2) Administrative expenses include salaries to directors Rs. 5 thousands

(3) Interest and other charges include :

Interest on bank overdraft (temporary nature)	109
Interest on Fixed loan from ICICI	51
Interest on working capital loan	20
Excise duties amount to one tenth of total value added by manufacturing and trading activities	

Ans. **Distribution statement**

	Rs.	Rs.	%
Management & Employees:			
Salaries	620		
Salaries to directors	5	625	33.69
Capital			
Interest on fixed loans	51		
Dividend	160	211	11.37
Government			
Local taxes	8		
Income tax	55	63	3.40
Reinvestment			

Dep.	16		
Increase in P & L	540		
Replacement reserve	400	956	51.54
Total VA		1855	100
VA by other activities		55	
VA by Manufacturing and trading activities		1800	

Excise duty = 10% of 1800 = 180

Gross VAS for the year ended 31.12.1998

Sales		6240	
Less excise duty		-180	6060
Ram material consumed		3210	
Stores		40	
Other Manu. exp.		442	
Adm. Exp.(exclusive of directors' salaries)		175	
Interest and other charges:			
Total	624		
Less excise	-180		
Interest on fixed loan	-51	393	4260
VA by Manu. and trading activities			1800
VA by other incomes			55
Total VA			1855

Reconciliation of PBT with Gross VA

PBT	1155
Salaries	620
Salaries and com.	5
Int. on fixed loans	51
Local tax	8
Dep.	16
Gross VA	1855

Q. No. 8 From the following Profit & Loss A/c , prepare a Gross value added statement . Show also the reconciliation between GVA and PBT.

Profit and Loss A/c for the year ended 31.3.2002 (Rs.'lakhs)

Income

Sales 800

Other income 50

850

Expenditure

Production and operational exp. 600

Administration expenses 30

Interest and other charges 30

Dep. 20 680 PBT

170 Taxes 30

PAT 140

Balance as per last Balance sheet 10

150

Transferred to General Reserve - 80

Proposed Dividend - 20

Surplus carried to B/S 50

Production and operation expenses :

Consumption of raw materials	320
Salaries and wages	60
Cess	20
Other manufacturing expenses	200
Total	600

Administrative Expenses:

Audit fees	6
Salaries to directors	8
Provision for doubtful debts	6
Other exp.	10
Total	30

Interest and other charges :

On working capital loans	10
On fixed loans from ICICI	15
On debentures	5
Total	30

ECONOMIC VALUE ADDED [EVA]

EVA is an accounting based technique of measuring the performance of an entity. The entity whose performance is being measured could be a division, department, project or the firm itself. The concept of EVA has been developed and popularized by Stern Steward & co.- a US consulting firm.

EVA measures how much an entity has earned over and above its cost of capital[2], which includes both debt and equity. Put simply, EVA is net operating profit[3] minus an appropriate charge for opportunity cost of all capital invested in an enterprise. As such, EVA is an estimate of true "economic" profit, or the amount by which earnings exceed or fall short of the required minimum rate of return that that shareholders and lenders could get by investing in other securities of comparable risk.

EVA = EBIT –TAX on EBIT - [C.E.xWACC]

Example: C.E. Rs.1000 crores. Debt Equity Ratio 0.20:0.80. Debt carries 15% interest, Tax 35%, cost of equity 18%, EBIT Rs.300 crores. EVA?

Answer:

Cost of debt = 15x.65 =9.75% Tax = (300x.35) =105 crores

WACC = [9.75X.20]+[18X.80] =16.35%

EVA = 300-105 - [1000X16.35%] = 31.50 crores

[2] Weighted average cost of equity and borrowed funds. It is calculated on the basis of current cost and not on the bass of historical cost.

[3] Net operating profit = EBIT – Tax on EBIT

Example (ii) calculate EVA : Financial leverage 1.40 times, cost of equity 17.50% Income tax rate 30% Capital Structure : (i) equity capital Rs.170 lakhs (ii) Retained earnings Rs.130 lakhs &(iii) 10% debentures Rs.400 Lakhs.

Answer : working note(i)

$$\text{Financial leverage} = \frac{\text{EBIT}}{\text{EBIT} - \text{Interest}}$$

$$1.40 = \frac{\text{EBIT}}{\text{EBIT} - 40}$$

Working note (ii)

Calculation of WACC

Source	Cost (X)	Weight(W)	XW
Equity	17.50	300	5250
Debe.	7.00	400	2800
		700	8050

WACC = 8050/700 = 11.50 %

Calculation of EVA :

EBIT	140
!	
Tax on EBIT	-42
	98
Cpital charge (11.50% of 700)	-80.50
EVA	17.50

The capital charge is the most distinctive and important aspect of EVA. The capital charge in EVA is what economists call an opportunity cost. It is the return that investors could expect to get by putting their money in a portfolio of other shares and debentures of comparable risk. The concept dates all the way to Adam Smith who opined that for its survival ,a business has to provide a minimum competitive return on all the capital invested in it. The cost of capital, or required rate of return, or capital charge (by whatever name we may refer it), applies to equity as well as debt.

THREE COMPONENTS OF EVA: (A) CE (B) WACC (C) OPERATING PROFIT

CE : CE means long-term funds of a company. It includes debt, preference shares and equity shares. These should be taken at their market values. Alternatively, CE may be calculated using economic values of assets and outside liabilities (except debt). CE may be taken on average basis, i.e. as compared to closing capital employed, average capital employed is preferred for EVA.

WACC : WACC is the weighted average cost of debt, cost of preference shares and cost of equity shares, weights being market values of debt, preference shares and equity shares.

In determining WACC, cost of debt is taken as after-tax, cost of preference shares is calculated before tax saving (as preference dividend is not tax deductible) and cost of equity shares is estimated on the basis of Capital Assets Pricing Model (CAPM)

OPERATING PROFIT : Operating profit refers to Earnings Before Interest and Tax. To calculate EVA, several adjustments are required to accounting operating profit so that we get operating profit which reflects true operating performance of the entity. (Accounting operating profit fails to reveal true operating profit as it is based on extreme conservatism, i.e. accounting principles have the tendency of

reporting the profit towards the lower side). A few important adjustments to accounting operating profit are as follows:

(i) For EVA purposes, all R&D outlays should be capitalized and amortized over the useful life of R&D.

(ii) Market development expenses should be capitalized and amortized.

(iii) If a company undertakes a project which will provide return after long period, the cost of project should be increased by capital charge on the investment in the project. (This capital charge should be calculated on the basis of WACC). The capital charge so capitalized should be amortized over the useful life of the project.

IMPROVEMENT IN EVA

Improvement in EVA can be achieved in four ways:

(i) Increase operating efficiency.

(ii) Taking on new investments that promise to earn more than WACC.

(iii) Get rid of those parts of business that earn less than WACC.

(iv) WACC is lowered by altering financial strategies.

FIVE FEATURES OF EVA

(i) EVA & Financial Management

(ii) EVA & Incentive compensation

(i) EVA & Divisional performance

(ii) EVA & Goal setting

(iii) EVA & Market valuation

<u>EVA & Financial management</u>

As per EVA concept, the managers should incorporate two basic principles of finance in their decision making . The first is that the primary financial objective of any company is to maximize the wealth of the shareholders. The second is that it is the continuous improvement in EVA that brings continuous increase in shareholders′ wealth.

EVA & Incentive Compensation

The objective of incentive compensation is to make managers behave like owners. They should identify themselves with the fortunes of the company. EVA is a useful tool for incentive compensation. When the bonus of managers is linked to increase in EVA, they think and act like owners. They do, all that they can, to improve EVA.

EVA & Divisional Performance

EVA is a useful tool for divisional performance appraisal. (The term division here refers to a constituent unit of company, it may be department, product, project or something like this.) By separately measuring the performance of different constituent units, their managers can be held responsible for operations under their direct control and for creation or destruction of wealth. Divisional managers should be given incentive bonus on the basis of increase in EVA of their respective divisions.

EVA & Goal Setting

Most companies set different goals for different managers. Strategic managers are expected to increase market-share, marketing managers are expected to increase the growth in revenue, Production managers are expected to produce at minimum cost and so on. The result is different and, sometimes, conflicting goals
for different managers. Under EVA, there is only one goal for each manager and that is, improve EVA. EVA based goal (i.e. goal of every manager is to improve the EVA of activities under his control) is simple and can be communicated to, and easily understood by , the managers of different levels.

EVA & Market Valuation

Market value of a company depends upon its EVA. There is high degree of correlation between EVA growth and market value addition. Increase in EVA results in increase of market value and vice- versa.

Conclusion

The most valuable resource in any company is the creativity and will to succeed that its people possess. EVA equips them with better information and better motivation to succeed.

Question : The managers of Mind Tree Ltd. were surprised at a recent article which suggested that the company's performance in the last two years had been poor. The CEO commented that turnover had increased by nearly 17% and pre-tax profit by 25% between the last two financial years, and that the company compared well with others in the same industry.

Profit and Loss account extracts for the year ($ MILLION)

	2000	2001
Turnover	326	380
Pre-tax accounting profit	67	84
Tax	23	29
PROFIT AFTER TAX	44	55
DIVIDENDS	15	18
RETAINED PROFIT	29	37

BALANCE SHEET EXTRACTS FOR YEAR ENDING ($ Million)

	2000	2001
FA	120	156
Net CA	130	160
	250	316

Equity shareholders fund	195	236
Debt	55	80
	250	316

Other Information : (i) The company's pre-tax cost of debt was estimated to be 9% in 2000 and 10% in 2001. (ii) The company's cost of equity was estimated to be 15% in 2000 and 17% in 2001. (iii) the tax rate was 35% in both 2000 and 2001. (iv) Interest expense amounted to 4 Million in 2000 and 6 Million in 2001. Estimate the EVA for each of the two years. Comment upon the performance of the company. (Adapted ACCA)

ACCOUNTING FOR NOT –FOR – PROFIT – ORGANIZATION

The accounting for not-for-profit organizations is primarily 'fund accounting'. Fund accounting essentially involves fund wise preparation of financial statements and consolidation of these funds to present the financial result / position of organization as a whole. Funds may be classified into two parts (i) Revenue funds and (ii) Specific funds (specific funds are of capital nature). Revenue funds record normal revenue transactions i.e. revenue funds are to meet the operating expenses . Revenue funds are of two types (i) Restricted revenue funds and (ii) unrestricted revenue funds.[4]

Restricted revenue funds account for resources whose use is restricted by donors. For example, AIIMS receives a grant of Rs.5,00,00,000 /- which is to be used only for cancer research over a period of three years. This amount would

[4] Refer to page 18, Suggested Answers of May 2004 exam CA Final I group (published by Board of Studies, ICAI)

be credited to "Cancer Research Restricted Revenue Fund Account." **In case of such funds, revenue is recognized to the extent of revenue expanded.** For example, suppose in the first year a sum of Rs. 1,00,00,000 is being spent towards cancer research; then this amount will be debited to the "Cancer Research Restricted Revenue Fund Account" (thus the balance left in "Cancer Research Restricted Revenue Fund Account." will be Rs.4,00,00,000) and credited to Income and Expenditure Account. Unrestricted revenue funds are used for meeting operating expenses for achieving objects of the organization.

Specific funds (these funds are of capital nature) are earmarked for well-defined purposes. Important specific funds are (i) Endowment fund (ii) Loan funds (iii) Annuity and Life Income Funds and (iv) Development funds .

Endowment funds are not to be spent currently, income out of these funds is available for restricted or general purposes. [For example, Union Budget for the year 1992-93, created an endowment fund of Rs.5,00,00,000 for Ratan Tata Library of Delhi School of Economics. This amount is not to be spent by Ratan Tata Library, income from this amount is to be spent by the Library, year after year, for purchasing the books and subscribing the journals. In this case, the income of the endowment fund is to be spent for specific purposes. Suppose the income of the endowment was available to Delhi School of Economics for any purpose, then we could have stated that the income of the endowment fund is available for general use]. Endowment fund may be perpetual or term endowment. Endowment fund referred above is perpetual endowment , its corpus amount of Rs.50000000 is never to be used; only its income is to be used. Had the case been that the Ratan Tata Library was permitted to use the income earned from the corpus for purchasing the books and subscribing the journals for ten years , and after that the corpus could be used for constructing the library building, we would have described the endowment fund as term

endowment fund.] In case of Annuity and Life Income funds[5], periodic payments are to be made from the designated funds till they are alive. In case of annuity fund, a fixed amount is to be paid periodically while in case of life income funds, payments vary with the income earned.[For example, a senior citizen transferred all his wealth to a University on the condition that the University shall be paying him Rs. 25000 p.m. so long he is alive. It is an example of Annuity Fund . Had the condition being that the university would pay him, through out his life, whatever income is earned from the wealth, it would have been a case of Life Income Fund]. Loan funds account for the resources that may be loaned to the staff. Development funds are for acquiring fixed assets and for their major repairs (i.e. capital nature repairs). [Ordinary nature repairs are to maintain the operating capacity and life of the fixed asset while capital nature repairs increase the operating capacity and life of the fixed asset.[6]] **Development funds are debited when fixed assets are completely acquired**. [In this case, the cost of fixed asset is debited to Development fund account and credited to General Fund Account.

Some other important points

Generally there are two components of such grants (i) Main grant and (ii) Grant towards overheads. Main grant is to be used very for specific purpose only and the donee has to summit accounts/ vouchers to the donor to satisfy the donor that the amount has been spent for very specific purpose only. The grant towards overheads is actually the grant to the institutions because its facilities will be burdened on account of the specific activity. In this case the AIIMS has to bear the burden of this research work For example, AIIMS's telephones may be used, its laboratories may be used, its Director has to devote some time, its building will be used, its equipments may be used, electricity may be consumed etc. The grant towards overheads is to meet the cost of all these items. The donee is not

[5] Refer to page 18, Suggested Answers of NOV 2003 exam CA Final I group (published by Board of Studies, ICAI)

[6] If nothing mentioned in the question, assume the repair to be of revenue nature.

expected to account and submit vouchers for this portion of the grant. This portion of the grant (Grant towards overheads) is transferred to the unrestricted Revenue account. Suppose in the above example, the amount of Rs.20,00,000 is towards overheads, then the amount of Rs.4,80,00,000 will be credited to "Cancer Research Restricted Revenue Fund Account" and Rs.20,00,000 will be credited to Unrestricted Revenue Fund Account (this account is also known as General Fund Account).

An important point regarding Fund Accounting is that for each fund there is a separate Bank account.

Example : A university receives two grants – one from the Ministry of Human Resources to be used for Malaria Research. This grant is of Rs.45,00,000 which includes Rs.300000 to cover indirect expenses incurred in administering the grant. The second grant is of Rs. 3500000 received from a reputed trust is to be used to set up a centre to conduct seminars on malaria related matters from time to time. During the year, it also received Rs. 500000 worth of equipment donated by a well wisher for malaria Research. During the year 2001-2002, the University spent Rs.32,25,000 of the government grant and incurred Rs.300000 overhead expenses. Rs.28,00,000 were spent from the grant received from the trust. Show Journal entries.

Sometimes the government provides grant to the not-for-profit-organization for a particular purpose on the condition that some amount will be earmarked for this purpose by the organization as well. This is known as **matching** grant. For example, take the case of a college which is being run by a trust and which gets grant from the UGC. The college wants to constitute a loan fund and for this purpose request the UGC to sanction a grant of RS. 10,00,000. Suppose the UGC sanctions the grant on the condition that the trust (which runs the college) will contribute Rs.20000. If this scheme is implemented, the college will have a

loan fund of Rs.1020000 (Rs.1000000 granted by the UGC and Rs. 20000 matching grant from the Trust).

Sometimes the applicable law/Articles of the association/trust-deed of the not-for-profit-organization provides for transfer of certain amount from unrestricted revenue fund (also known as general fund) to some specific fund. Such transfers are known as mandatory transfers. Suppose the trust deed of a trust running a college provides that the trust shall be transferring 1% of surplus to loan fund every year, the transfer so made shall be referred as mandatory transfer because there is mandate of the Trust deed behind this transfer. The transfers to specific funds (from unrestricted funds) , which are not provided by the Articles/trust/law but which are decided from time to time by the governing body/trust /BOD of the organizations, are known as non-mandatory transfers. For example while approving the accounts a trust, the trustees notice that trust has a very large amount of surplus (excess of income over expenditure) and hence decides to transfer a portion of it to the Development Fund. The transfer so made will be referred as non-mandatory transfer as the transfer is not mandated by any law/trust-deed/Articles of Association.

Question No. 1 Illustration 4 Study Material page 7.13 Noida University

Question No. 2 Illustration 1 Study Material page 7.4 Associated University

Question No.3 Illustration 2 Study Material page 7.8 From the following details in respect of loan fund of a School of management……………

Question No. 4 Illustration 3 Study Material page 7.11 Institute of World Management

Question No.5 Divine Public Health Hospital runs only an intensive care unit. For this purpose, it has hired a building at a rent of Rs.10,000 per month. The unit has undertaken to bear the cost of repair and maintenance.

The unit consisted of 50 beds and 5 more beds can be safely accommodated, when the situation demands at a charge of Rs.5 per bed per day.

During the year 1998-99, it revealed that only for 120 days in the year, the unit had full capacity of 50 patients per day and for another 80 days, it had on an average 40 beds only occupied per day. The total hire charges for this extra beds incurred for the whole year amount to Rs.4000.

Expert doctors from out station were engaged and the fees were paid on the basis of number of patients attended and time spent by them and on an average , it worked out to Rs.20,000 per month in 1998-99. The other expenses for the year were as under :

Permanent staff:

4 Supervisors, each at a salary of Rs.500 per month

8 nurses, each at a salary of Rs.300 per month

4 ward boys each at a salary of Rs.150 per month

Repairs and Maintenance Rs.7200

Cost of food supplied to patients RS.88000

Laundry charges Rs.56000

Medicine Supplied Rs. 70000

Cost of Oxygen X-ray other than directly borne for treatment of patients Rs.108000

Janitor and other services for them Rs.25000

Administration charges allocated to the unit Rs.99100

The unit has recovered an overall amount of Rs.100 per day on an average from each patient. The cost of janitor and other services is variable as it is related to number of patient days.

Prepare a Revenue Statement for the year 1998-99 and indicate the profit per patient day made by the unit. Also workout the number of patients days required by the unit to break even.

Pass Journal Entries for the next year, if the unit receives(a) donated medicines and medicinal supplies of Rs.25000 and (b) medicine expenses of Rs.85000 for the year includes Rs.5000 donated supplies.

CONCEPT OF CAPITAL MAINTENANCE

(Refer to page 1.6 of the study material)

There of two concepts of capital maintenance :

(i) Finance capital maintenance

(ii) Physical capital maintenance

Under finance capital maintenance, capital is defined in terms of nominal monetary units, "profit represents the increase in nominal money capital over the period"[7] For example, a business is started with a capital of Rs. 10,00,0000. At the end of I year of the business, its capital (without any adjustment of price level changes) is Rs,12,50,000. As per finance capital maintenance concept, its profit is Rs.2,50,000.

"The Physical capital Maintenance concept, requires the adoption of the current cost basis of measurement." [8] Under this concept, the nominal capital is adjusted for price level changes, and profit is calculated as excess of "equity shareholders fund" over inflation adjusted amount invested by the equity shareholders. Suppose a company issued equity shares of Rs.100000 on 1.4.2005. During the year, the general price level increased by 10%; at year end company's equity shareholders funds stood at Rs.1,15,000. As per Physical capital Maintenance concept, profit is Rs.5000.

Q.No.1 History Ltd. set up a factory on 1st January, 1980 at a cost of Rs.100 crores financed 50% by debentures, 30% by preference capital and 20% by equity capital. By 31st December, 1989 the debentures were repaid and preference shares were redeemed. The net asset value of per rupee of equity investment made on 1st January 1980 as on 31.12.1989 was Rs. 8 of which 10% was in fixed assets and the balance 90% was in the net working capital.
On 1st January, 1990 the company made a right issue of equity shares at a premium of 50% in the ratio of 1:1; it also made a public issue of equity shares at

---

[7] Framework of Preparation and Presentation of Financial Statement (ICIA) Page27
[8] Framework of Preparation and Presentation of Financial Statement (ICIA) Page27

a premium of 200% to the tune of 80% of equity capital after the right issue. The entire proceeds of rights and public issue were earmarked for capital expenditure .

On 31st December, 1998 the net asset value of one rupee of equity capital based on the position as on 1.1.1990 was Rs.41 of which only 1% was in fixed assets and the balance was in net working capital.

You are informed that :

(i) capital expenditure was made only in 1980 and 1990

(ii) Re.1 of 1980 was equal to Rs.3 of 1990 and Rs.15 of 1999.

History Ltd asks you to :

(a)Prepare Balance - sheets as on 1st January, 1980, 31st December 1989, 1st January 1990, 31st December 1998.

(b)Work out the retained profit over the period 1st January 1980 to 31st December 1998 under the concept of physical capital maintenance. (Nov.99 16 marks)

Q.No.2 On 31st March, 1988, when the general price index was say, 100, Forward Ltd purchased fixed assets of Rs. one crore. It had also permanent working capital of Rs. 40 Lakhs. The entire amount required for purchase and permanent working capital was financed by 10 % redeemable preference share capital.

On 31st March, 1998, the company had reserves of 1.75 crores. The general price index on that day was 200. The written down value of fixed assets was Rs.10 lakhs and they were sold for Rs.1.50 crores. The proceeds were utilized for redemption of preference shares.

On the same day (31st March, 1998), the company purchased a new factory for Rs.10 crores. The ratio of permanent working to cost of assets is to be maintained at 0.4 :1. The company raised the additional funds required by issue of equity shares. Based on the above information (a) Quantify the amount of

equity capital raised and (b) Show the Balance Sheet as on 1.4.98. (15 marks, May 98)

ACCOUNTANT'S REPORT FOR PROSPECTUS

M Ltd. intends to make a public issue to finance the purchase of 60 per cent shares in *N Ltd.* A firm of Chartered Accountants, *Topi wala & Co.* have been instructed to carry out the necessary investigation and to submit the accountants report for inclusion in the prospects.

The audited accounts of N Ltd. disclosed :

Year ended 31st Dec.	Turnover	Profit before dep. and tax	Depreciation	Issued share capital	Dividend %
1996	16,00,500	2,60,000	26,500	9,00,000	7
1997	22,01,200	2,61,000	36,700	9,00,000	11
1998	39,00,000	3,98,000	52,000	9,00,000	13
1999	43,00,000	3,81,700	44,700	9,00,000	15

2000	39,00,000	4,40,900	55,300	9,00,000	18

The summarized balance sheet as on 31st December, 2,000 showed :

Fixed Assets	*Rs.*	*Rs.*
Freehold land and buildings, at cost		2,10,000
Plant and Machinery, at cost	2,90,000	
Less: Depreciation provision	1,30,000	1,60,000
		3,70,000
Current Assets		
Stock (at the lower rate of cost (or net realizable value)	3,80,000	
Debtors	5,00,000	
Quoted investment, at cost (Market value, Rs. 1,25,000)	80,000	
Balance at Bank	80,000	
	10,40,000	
Less: Current Liabilities	1,10,000	9,30,000
		13,00,000

Share Capital : 90,000 ordinary shares	9,00,000	
Reserves		3,00,000
	12,00,000	
6% Debenture (redeemable 1.2.2001)	1,00,000	
		13,00,000

2. The stock sheets for 1996 and 1997 had been destroyed, but an assurance was received from the auditors that stocks had always been properly taken

and consistently valued. However, owing to errors, occurring in the cost records, the stock at 31st December, 2000 was valued at 5 per cent less than its true value; and furthermore the stock at 31st December, 1999 (Rs. 4,41,000) at 5 per cent more than its true value.

3. On 31.12.2000, freehold land and buildings were professionally valued at Rs. 4,00,000.
4. The depreciation charge in 1997 included an exceptional write off of Rs. 10,000 in respect of the anticipated obsolescence of some process plant which obsolescence in the event did not occur. This exceptional write off was not subsequently written back. Otherwise, depreciation on plant and machinery was provided throughout at 10 per cent per annum, on cost, which is considered reasonable in the light of the information available about the estimated useful life of the plant.
5. In 1998 the company closed down its wholesaling department which had previously 'broken even' suffering a loss on closure of Rs. 16500. The turnover of this department amounted to Rs. 80,000 in 1996, Rs. 90,000 in 1997 and Rs. 40,000 in 1998. No fixed assets were employed in this department.
6. On 1.2.2001 the debentures, which had been issued on the inception of the company, were redeemed, from the sale of one of the investments. Based on its sale price, this investment had given a dividend yield of 5 per cent in 2000 and 4 per cent in every earlier year.
7. As from 1st January, 2001 it had been agreed that in addition a director's fee of Rs. 2,000 would be paid to each of the three directors, but that these fees should not be deducted in arriving at the basic emoluments.

You are required to prepare the accountants' report to be included in prospects. Ignore taxation.

Tutorial Note

Accountant's report is to be given in the prospectus in two situations (a) when the fund raised through the prospectus are to be utilized for buying shares in some company, so that it would become subsidiary of the company issuing prospectus. For example, the prospectus is to be issued by *X Ltd.* The funds raised through the prospectus would be used for buying 60 per cent shares of *Y Ltd.* The accountant's report in the prospectus to be issued by *X Ltd.* would be about *Y Ltd.* (b) When the funds raised through the prospectus are to be utilized for acquiring more than 50 per cent interest in some running business. In this situation, the report should be about the business in which interest is to be acquired.

The accountant giving such report must be named in the prospectus and is 'expert' within the meaning of section 58 of the Companies Act 1956. He may not be actual auditor of the Company issuing prospectus but should possess the requisite qualifications under law for appointment as auditor of the company. In (a) situation, the report must be on following matters: (i) The profits or losses of the company (in which shares to be acquired) for last 5 years, (ii) the assets and liabilities of the business as on last balance sheet date. In situation (b), the report must be on the following matters: (i) the profit/loss of the business (in which interest is to be acquired) for last 5 years, and (ii) net assets of the business as on last balance sheet date but if the time interval between last balance sheet date and the date of issue of the prospectus is more than 120 days, the net assets should be given on any day which is within last 120 days of the date of issue of prospectus. For example, A Ltd. intends to acquire 60% interest in a running partnership business. the partnership's accounting year ends on 31st Dec. each year. Date of issue of prospectus (for raising funds for this acquisition purpose) is 10th A0th April, 2005. The "accountant's report" regarding the partnership should report the net assets as on 31st Dec.2004 (as the time gap between the date of prospectus and date of last B/S does not exceed 120 days). If the date of prospectus is 10th May 2005, the net assets may be reported as on

any date between 10th Jan.2005 – 9th May 2005, both days inclusive, (i.e. on any date within last 120 days of the date of the prospectus.

If the company (in which shares would be acquired) or business (in which interest is to be acquired) is less than 5-year-old, the profit/loss should be given for all years since establishment.

The reporting accountant may make necessary adjustments in his report about profit/losses and assets and liabilities.

Guidelines for preparation of accountant's Report for prospectus :

Part I

(I) The net profit may be reported after rectifying any errors located in the books of accounts or relevant documents. A note may be given for each such rectification.

(II) The profits may be reported after eliminating the effect of such items which took place in the past but which will not take place in future. A note may be given for each such elimination.

(III) A note may be given for each possible change in future profits

Part II

(I) The net assets may be reported after rectifying any errors located in the books of accounts or relevant documents. A note may be given for each such rectification.

(II) The net assets may be reported at book values. If the intention is to report the net assets at their current values, such current values may be determined by the professional valuers and may be recognized in the books of accounts.

(III) If any material change in the net assets takes place after the last B/S date, but before the date of prospectus, the net assets may be reported considering such change. A note may be given for each such change.

Notes to part I of the Accountant's report :

(a) the profits have been reported after rectifying the errors regarding stock valuation. The stock of 1999 was found over valued by Rs.21000 and that of 2000 was found undervalued by Rs.20000.
(b) The profits have been reported after writing back an unnecessary write off of Rs. 10000 of plant. The plant was written off in 1997. The profits have been reported after providing depreciation @ 10 % on Rs.10000 for all the years beginning 1997. (c) the wholesale department o the company was closed down in 1998. Loss on closure was Rs.16500. The profits have been reported after eliminating the effect of this loss as it won't occur in future. In earlier years, the department has been breaking even.
(d) On 1.2.2001, 6% debentures of Rs. 100000 were redeemed out of sale proceeds of investments of the same amount. Income from the investments, which were sold, had been Rs. 5000 in 2000 and Rs.4000 in each of earlier years. Profits have been reported after eliminating debenture interest and income from the investments which were sold. (e) Future profits of the company would be reduced by Rs. 6000 each year on account of increase in the Directors remuneration.

Notes to part II

(a) the net assets have been reported after rectifying the errors regarding the stock valuation.
(b) The net assets have been reported after writing back the unnecessary write off of plant in 1997 (Rs.10000) and after providing depreciation on the written back plant for all the years since 1997.
(c) On 1.2.2001, 6% Debentures of Rs.100000 were redeemed out of sale proceeds of investments of the same amount. The net assets have been reported after considering these transactions.

Note from examination point of view (this type of note is not given in practical life)

It is assumed that the current value of the freehold property has been recorded in the books of accounts before the date of the prospectus.

HUMAN RESOURCE ACCOUNTING

Human resource is the most important resource of any organization. It is of vital significance and constitutes a primary segment of the total resources held. A team of creative, competent, devoted and motivated people, having a will to succeed, can take an enterprise to previously unknown heights. On the contrary, manipulative, incompetent and sick-minded people lead a flourishing concern to bankruptcy.

Though human resource has been of importance for any organization since the dawn of civilization, it acquired the status of being 'vitally important' only in 20th century. In today's knowledge-based economy, it is the single most important resource, the combined value of all other resources is only a small fraction of it. Companies are making fortunes on the basis of knowledge their talented people have. Market value of these companies is many times more than their intrinsic values. Why?

These companies have an asset which does not appear in their Balance-sheets. This asset is creativity of their people who create wealth for the companies through their 'intellect'. In today's world, value of any company (whether knowledge-based or not) depends upon knowledge and dedication its people posses.

In spite of such an importance, human resource does not appear in the financial statements. Its information is provided only as a part of internal accounting and reporting for management purposes. This reduces the importance of accounting information which is supposed to help present and potential investors and other users of financial statements for framing a picture about future prospectus of the company.

To overcome the above mentioned limitations efforts have been made , though breakthrough is yet to be achieved, in last four decades to develop HRA i.e. the process of identifying and measuring data about human resources and communicating this information to the interested parties. The development of last four decades has been in the form of various models of HRA.

MODELS OF HRA

(A) Cost based models

(1) Historical costs model

(2) Replacement cost model

(B) Economic value models

(1)Opportunity cost model

(2)Discounted wages and salaries model

(1) Stochastic model

(2) Group basis valuation model

Historical costs model (Developed by R.Likert and his associates)

In this approach, the actual costs of recruiting, training, placing and developing the employees of an organization are capitalised and amortized over the expected period the employee is likely to stay with the organization. If the employee leaves before this period, unamortized amount should be written of as loss. The method is quite simple. It is simply extension of concept of proper matching of cost with revenue. As the costs of recruitment, training, placement and development provide benefits over a number of years, such costs are not matched against revenue of the year in which these are incurred, rather such costs are amortized over their useful life.

Limitations of the model

(1) It is difficult to estimate the number of years an employee is likely to stay with the organization.

(2) The basic objective of providing accounting information is to assist in decision making. Historical costs are not relevant for decision making.

(3) The model is against the provisions of AS 26

Replacement cost model (Developed by Flamholtz)

As per this model, a firm should estimate the costs of replacing a firm's existing human resources. We try to estimate the cost that the firm has to bear if it creates a new similar human organization starting from scratch. Cost includes cost of recruiting, training, placing and developing. This model is considered as improvement over the historical model as replacement costs have the advantage of being present oriented. The limitations are : (I) It is difficult to estimate the replacement cost, and (2) the model does not provide the approach of accounting the replacement cost in the financial statements.

Opportunity cost model (developed by Hekimian & Jones)

This model values human resources on the basis of opportunity cost. Opportunity cost is value or economic benefit derived from best alternative use of the resource. The model divides all the employees into two categories,(i) Scarce and (2) not scarce. The model values only scarce employees (on the basis of their opportunity cost) and does not put any value on others.

Under this model the investment center managers will bid for the scarce employees they need to recruit. These scarce employees come from within the firm.

Suppose Department X is an investment center (i.e. its manager controls not only its costs and revenue but also takes decisions about investments to be made in his department). Manager of this department requires an engineer having specific skills and qualities. This type of engineers are not readily available for being hired. Mr.A, working in Department Y of this company, has similar skills and qualities. The manager of Department X will bid for Mr.A. Suppose Mr.A is likely to serve the firm for ten years and during these years his

services will result in annual benefit of Rs.50,000 for department X, then the highest bid by the manager of Department X will be present value of Rs.50,000 annually for 10 years. Suppose cost of capital is 10%, then this value is Rs.307230. Accordingly, value of this human resource is Rs.307230.

H&J have suggested that this amount should be included in the capital base of Department X. Suppose Department X has a capital base of Rs. 20,00,000. and is expected to earn 12% on this base, i.e. Rs. 2,40,000. If this human resource is given to Department X, its capital base would be considered (for measuring the performance of this department) to be Rs.2307230 and the department shall be expected to earn 12% on Rs.2307230, i.e.Rs.276868.

The main limitation of the model is discrimination between various employees and this may lower the morale of the employees.

Discounted value of salaries wages model(Developed by Lev & Schwartz)

L&S suggested the use of an individual employee's future salaries and wages for determining his value. The value of human capital embodied in a person is the present value of his future earnings from employment.

For the purpose of this model, the firm's labour force will be divided into homogeneous groups of employees, such as skilled, semi-skilled and unskilled. Average earnings for each group are estimated and the present value of such earnings represents the value of human resource.

Suppose a company has 1000 unskilled workers. Their average annual earnings during next 10 years will be Rs. 100,000, after that for next 10 years it will be Rs. 150,000 and finally for next 10 years it will be Rs.200,000. According to this model, the value of this human resource is:

1000[(100000x6.145)+(150000x2.369)+(200000x0.913)] i.e.Rs.1152450.

The original model, as discussed above, ignores the possibility of death before retirement. The original model was later on revised and it incorporated the possibility of death before retirement.

Major Limitations:

(i) Possibility that a person may quit before retirement or death not considered.

(ii) Possibility of promotion/demotion ignored.

(iii) Estimation of future earnings is very difficult.

(iv) The basic concept of the model is difficult to digest; how can the salaries and wages payable is asset?

Illustration 3 page 6.32 Study Material

Stochastic model (Developed by Flamholtz)

This model is different from Discounted value of salaries and wages model in following respects:

(i) Discounted value of salaries and wages model considered the earnings of employees. Stochastic model considers economic benefits the firm expects from the employees.

(ii) Stochastic model considers career movement i.e. promotion and demotion.

(iii) Stochastic model considers the probability of an employee's leaving the organization before death or retirement.

Under this model, the value of human resource is present value of expected economic benefits the firm expects from it.

Example

A new employee joins a firm. He is placed to III position in the firm. In coming years he may be promoted to position II or position I. He is not likely to stay with the firm for more than five years from the date of joining. The firm gets economic benefits of Rs.200000 annually when he occupies position III, Rs.300000 annually when he occupies position II, Rs.500000 annually when he occupies position I. Cost of capital is 10%. Various probabilities required for the model are as follows.

Year →	1	2	3	4	5

Position ↓					
III	0.90	0.50	0.10	--	--
II	--	0.40	0.80	0.90	0.10
I	--	--	--	---	0.70
EXIT	0.10	0.10	0.10	0.10	0.20

Find the value of human resource.

ANSWER:

Value of human resource: .909[(200000x.90)] +.826[(200000x.50) +(300000x.40)] + .751[(200000x.10) +(300000x.80)] + .683[(300000x.90)] + .621[(300000x.10) +(500000x.70)] = Rs.........................

The limitation of the model is that it is very difficult of estimate its various parameters like probabilities and expected economic benefits.

Group basis valuation model (Developed by Jaggi & Lau)

J&L have suggested that valuation of human resources should be done on the group basis and not on an individual basis. 'Group' means a homogeneous group of employees who may not be working in the same department. They opined that it is difficult to measure service tenure, career movements (promotion/demotion) and economic benefits from human resource on individual basis. These parameters can be estimated on group basis, with improved accuracy and reduced difficulties. Hence they suggested 'group' instead of 'individual' as basis of valuation. In all other respects, this method is similar to Stochastic model.

CONCLUSION

Today's accountant very well understands the importance of "Putting the people on Balance-sheet," yet as this resource deals with such variables which are most difficult to measure, no reliable model has been developed so far. It is

suggested[9] that till the breakthrough is achieved, detailed information including their talents and achievements(i.e. qualitative aspects of people) may be given as notes to the financial statements.

MUTUAL FUND

A mutual fund is an organization (in India this organization must be in the form of a trust) that pools the savings of a number of investors - called as unit holders - who share a common goal. The money thus collected is invested by the professional fund managers in different types of securities depending upon the objectives of the scheme. The return/ loss on investment is shared by the unit holders in proportion to the number of units owned by them.

MUTUAL FUND STRUCTURE

The SEBI (Mutual funds) regulations 1996 define a mutual fund (MF) as a trust established by a sponsor to raise money through sale of units to investors under one or more schemes for investing in securities in accordance with these regulations. A MF comprises five entities :

(1) Sponsor

(2) Mutual Fund Trust

[9] This suggestion has been made by various accounting experts. It is a controversial suggestion. Most of HR managers have opposed this suggestion. They apprehends that if implemented, this suggestion will attract head-hunters and the organization will suffer a lot.

(3) Assets management company

(4) Custodian

(5) Registrar

Sponsor may be any person or corporate body that establishes the fund and registers it with SEBI. The fund must be in the form of a trust. It should be formed under Indian Trust Act 1882 and registered under Indian Registration Act,1908. The sponsor appoints Board of trustees of the trust. Alternatively, the sponsor may appoint a company as trustee and in that case the directors of the trustee company will constitute the Board of Trustees. Two-third of members of the Board of Trustees should be independent persons, not elated to the sponsor.

Sponsor/Board of Trustees appoint an asset management company to invest the funds according to the objectives of the scheme subject to the SEBI regulations. SEBI regulations provide that at least 40% of the net worth should be contributed by the sponsor. The minimum net worth of the AMC should be Rs.10 crores. The AMC operates under the direction and supervision of the Board of trustees. The AMC must be registered with SEBI. The AMC floats and manages different investment schemes in the name of trust and in accordance with SEBI regulations.

Sponsor/Board of trustees appoints a custodian for proper custody of assets of the trust. The custodian should hold a certificate of registration issued by SEBI. Sponsor / Board of trustees appoints a registrar to handle the registary work of the unit-holders.

MUTUAL FUND SCHEMES

There are wide variety of mutual fund schemes that cater to needs of investors of different age-groups , having different financial positions risk tolerance and return expectations. Each scheme has a pre-determined objective. Investments are made by MFs in equity shares, debts and money

market instruments. All mutual fund schemes are variations of these three asset classes. For example, equity fund schemes invest only in equity shares, debt fund schemes only in debt funds and money market schemes in only in money market instruments. The other schemes may invest in 2 or 3 of above mentioned types of instruments subject to pre-determined limits. For example, a balanced fund may invest 80% in debt and 20% in equity.

On the basis of their structure, all mutual fund schemes can be divided into 2 categories: (1) Open ended (2) Close ended .

- An open ended scheme is one that is available to subscription all through the year. These schemes do not have a fixed maturity . Investors can conveniently buy and sell units at net asset value based price at any time. The key feature of this type of scheme is liquidity.
- A close ended scheme has a stipulated maturity period. The fund is open for subscription for a limited period only. Generally , units of such schemes are quoted on the stock exchanges. This is the exit route for those who want to go out and entry route for those who want to invest after the subscription period is over.

The other types of schemes are (1)Tax saving schemes (2)sector specific schemes and (3)Index based schemes. Tax saving schemes are meant for those who want to save income tax under section 80 C of Income tax Act, 1961. Sector specific schemes invest only in the equity shares of a particular sector i.e. IT fund, Pharma fund, Fast moving consumer goods Fund etc. Index fund invests their funds in the equity shares included in an index.

NAV : The net assets value of any MF scheme is the current value of its all assets net of its liabilities. Division of this amount by number of outstanding units of the scheme, we get NAV per unit. NAV per unit represents the amount which the holder of one unit will get if the scheme is dissolved or liquidated (for this

calculation, forced or distress sale is not assumed, moreover the liquidation or dissolution costs are not considered). NAV per unit is generally called as NAV (ignoring the phrase "per unit ").

NAV of a fund scheme is equal to :

(1) Market value of traded listed securities
+ (2) Estimated value of (i) non-traded listed securities (ii) unlisted securities
+(3) Liquid assets/ cash
+(4) Accrued dividend/interest
-(5) Accrued expenses
-(6) Other liabilities

The most important part of calculation of NAV is valuation of non-traded listed securities and unlisted securities. (non-traded listed security is a security , which though listed, has not been traded in any stock exchange for a period of 60 days prior to the valuation date.) Non-traded listed securities and unlisted securities should be valued by Asset management company in good faith on the basis of appropriate methods. The auditors are supposed to give their opinion on such valuations, For valuation of such securities, following principles should be followed :

(1) Equity shares should be valued either on the basis of PE ratio or in combination with net assets value. The basis of PE ratio method is PE ratio of comparable PE ratio of comparable traded security. For example, equity shares of X Ltd. is non-traded security. Its EPS is Rs.20. PE ratio of Y Ltd's equity shares (which is a comparable traded security) is 10. For the purpose of valuation of equity shares, PE ratio should be taken as less than 10 (because of lower liquidity of equity shares of X Ltd.),

say 8. The value of equity shares of X Ltd. may be taken as 20x8 i.e. Rs.160.

(2) Debt instruments should be valued on the basis of Yield to maturity of the asset to be valued and adjusted YTM of the comparable traded security. Suppose face value of a debenture of X Ltd. is Rs.100. Its yield to maturity is 8%. YTM of a comparable traded security is 10% i.e. normal rate of a comparable security is 10%. Normal rate of debentures of X Ltd. may be taken slightly on higher side, say 10.50%, as Debentures of X ltd. are unlisted (lower liquidity). In this case, the value of debenture of X Ltd. would be (8/10.50)x100 = Rs 76.19.

Limits on expenses of the Mutual fund :

(1) The initial issue expenses in respect of any close-ended scheme may not exceed 6% of funds raised under that scheme. Such expenses should be amortized on weekly basis over the life of the scheme.

(2) The recurring expenses are subject to following limits:

(i) First Rs.100 crores : 2.50% of weekly of average net assets

(ii) Next Rs.300 crores : 2.25% of weekly average net assets.

(iii) Next Rs. 300 crores : 2% of weekly average net assets

(iv) on the balance : 1.75 % of weekly average net assets.

ACCOUNTS OF MUTUAL FUNDS :

Proper accounts should be maintained and get audited. Financial year should be followed as accounting year. Scheme wise annual report should be sent to the investors. A copy should be sent to SEBI within 6 months of end of financial year.

Accounting policy :

(I) Both realised gains and unrealized gains should be recognized in the financial statements. In other words, all the investments should be valued at market value as on the date of financial statements.

(II) Non-traded investments should be valued in good faith,

(III) For quoted shares dividend income should be recognized on the date on which the shares were quoted in the market as ex-dividend. For other shares, the same should be recognized on the date o f declaration.

(IV) Interest income should be recognized on accrual basis.

(V) Investments should be valued on weighted average cost basis.

(VI) Transactions regarding purchase or sale should be recognized on the date of transaction and not on the date of settlement.

(VII) Bonus shares should be recognized on the date on which the shares are quoted in the stock exchange on ex-bonus basis and right shares should be recognized on the date the shares are quoted on ex-right basis.

(VIII) Interest income which has been recognized but not received for a period of 12 months should be debited to revenue account and in future no further accrual of such income should be recognized.

Annual Report (Scheme wise) The annual report shall contain -

(i) Report of the Board of Trustees on the operations of the various schemes of the fund and the fund as a whole during the year and the future outlook of the fund; (ii) Balance Sheet and Revenue Account (iii) Auditor's Report
(iv) Brief statement of the Board of Trustees on the following aspects, namely:-
(a) Liabilities and responsibilities of the Trustees
(b) Investment objective of each scheme;
(c) Basis and policy of investment underlying the scheme;
(e) Comments of the Trustees on the performance of the scheme, with full justification.

Contents of Balance Sheet and Revenue Account :

The B/s shall give scheme-wise particulars of assets and liabilities.

(a) Market value of each type of investment , for example equity shares, preference shares, should be stated separately.
(b) The Balance-sheet shall disclose NAV at the end of accounting year.
(c) Disclose all contingent liabilities.
(d) Provision for doubtful debts, provision for accrued income(which is not likely leased) etc should be deducted out of respective assets and to be shown in the liability side.
(e) Movement in unit capital should be stated, for example :

	No. of units	Rs. Crores
Balance on 1.4.2004	1,00,00,000	10,00,00,000
Units sold during the year	50,00,000	5,00,00,000
Units repurchased during the year	(20,00,000)	(2,00,00,000)

Contents of Revenue Account : (a) Scheme wise particulars of income, expenditure and surplus should be shown.(b)Profit or loss on intra-scheme transfer should be disclosed separately (c)Appropriation of surplus between dividend and retained profit.(d)The following disclosures should be made : (i)provision for doubtful deposits, debts and accrued interest (ii)custodian and registrar fees (iii)total income and expenses expressed as a % of weekly average net assets.

MERCHANT BANKERS

Merchant Banker is person who is engaged in the business of issue management (management of issue of securities) either by making arrangement regarding selling, buying or subscribing to securities or acting as

manager, consultant, adviser or rendering corporate advisory service in relation to such issue management.

To act as a merchant banker in India, one has to get registered with SEBI. Only a body corporate other than non-banking financial company is eligible to get registration as merchant banker. The SEBI grants registrations for four categories of merchant bankers:

(i) Category I : to carry on the activity of issue management[10] and to act as advisor, consultant , manager, underwriter, portfolio manger

(ii) Category II : to act as advisor, consultant, co-manager, underwriter, portfolio manager

(iii) Category III : to act as underwriter, advisor or consultant to an issue

(iv) Category IV : to act only as advisor or consultant to an issue.

(For acting as underwriter or as portfolio manager separate registration with SEBI is required)

The minimum net worth for acting as merchant banker is given below :

Category I : Rs.5.00 crores Category II : Rs. 50.00 Lakhs

Category III: Rs. 20 Lakhs Category IV: Nil

Maintenance of books of accounts, records etc.

(1) Every merchant banker shall keep and maintain such books of accounts, records and documents so that it may be able to submit the following documents to the SEBI :-

(a) a copy of balance sheet as at the end of each accounting period;

(b) a copy of profit and loss account for that period;

(c) a copy of the auditor's report on the accounts for that period; and

---

[10] Preparation of prospectus and other information relating to the issue, determining financial structure, tie-up of financiers and final allotment and refund of the subscription.

(d) a statement of financial position.

(2) Every merchant banker shall intimate to the Board the place where the books of accounts, records and documents are maintained.

(3) every merchant banker shall, after the end of each accounting period furnish to the Board copies of the balance sheet, profit and loss account and such other documents for any other preceding five accounting years when required by the Board.

Submission of Half-yearly results

Every merchant banker shall furnish to the Board half-yearly un-audited financial results when required by the Board with a view to monitor the capital adequacy of the merchant banker.

Maintenance of books of account, records and other documents

The merchant banker shall preserve the books of accounts and other records and documents for a minimum period of five years.

Report on steps taken on Auditor's report

Every merchant banker shall within two months from the date of the auditors' report take steps to rectify the deficiencies, made out in the auditor's report.

FORMAT FOR HALF YEARLY REPORT TO BE SUBMITTED BY MERCHANT BANKERS **Refer to study material page 5.28**

SEBI' s right to inspect

The SEBI may appoint one or more persons as inspecting authority to undertake inspection of the books of accounts, records and documents of the merchant banker for any of the following purposes:

(a) to ensure that the books of account are being maintained in the manner required;

(b) that the provisions of the Act, rules, regulations are being complied with;

(c) to investigate into the complaints received from investors, other merchant bankers or any other person on any matter having a bearing on the activities of the merchant banker; and

(d) to investigate suo - moto in the interest of securities business or investors interest into the affairs of the merchant banker.

Accounting by Stockbrokers

(1) Every stock-broker shall keep and maintain the following books of accounts, records and documents namely; -

(a) Register of transactions (Sauda Book); (b) Clients ledger;
(c) General ledger; (d) Journals;
(e) Cash book; (f) Bank pass book;

(g) Documents register containing particulars of securities received and delivered in physical form and the statement of accounts and other records relating to receipt and delivery of securities provided by the Depository Participants in respect of dematerialized securities.

(h) Members' contract books showing details of all contracts entered into by him with other members of the same exchange or counterfoils or duplicates of memos of confirmation issued to such other member;

(i) Counterfoils or duplicates of contract notes issued to clients;

(j) Written consent of clients in respect of contracts entered into as principals; (k) Margin deposit book;

(l) Registers of accounts of sub- brokers;

(2) Every stock-broker shall intimate to the Board the place where the books of accounts, records and documents are maintained.

(3) Every stock- broker shall, after the close of each accounting period furnish to the Board if so required as soon as possible but not later than six months from the close of the said period a copy of the audited balance sheet and profit and loss account, as at the end of the said accounting period: Provided that, if it is not possible to furnish the above documents within the time specified, the stock-broker shall keep the Board informed of the same together with the reasons for the delay and the period of time by which such documents would be furnished.

(4) Every stock broker shall preserve the books of account and other records for a minimum period of five years.

SEBI's right to inspect

(1) Where it appears to the Board so to do, it may appoint one or more persons as inspecting authority to undertake inspection of the books of accounts, other records and documents of the stock- brokers for any of the following purposes :

(a) to ensure that the books of accounts and other books are being maintained in the manner required;

(b) that the provisions of SEBI Act, rules, regulations and the provisions of the Securities Contracts (Regulation) Act and the rules made there under are being complied with;

(c) to investigate into the complaints received from investors, other stock brokers, sub-brokers or any other person on any matter having a bearing on the activities of the stock- brokers; and

(d) to investigate suo-moto, in the interest of securities business or investors' interest, into the affairs of the stock- broker.

Procedure for inspection

(1) Before undertaking any inspection , the Board shall give a reasonable notice to the stock- broker for that purpose.

(2) where the Board is satisfied that in the interest of the investors or in public interest no such notice should be given, it may by an order in writing direct that the inspection of the affairs of the stock broker be taken up without such notice.

(3) On being empowered by the Board, the inspecting authority shall undertake the inspection.

Submission of Report to the Board

The inspecting authority shall, as soon as may be possible submit an inspection report to the Board.

Appointment of Auditor : SEBI may appoint a qualified auditor to investigate into the books of account or the affairs of the stock-broker:

NBFCs

QUES -1 What is a Non-Banking Financial Company (NBFC)?

ANS -1 A Non-Banking Financial Company (NBFC) is a company registered under the Companies Act, 1956 and is engaged in the business of loans and advances, acquisition of shares/stock /bonds/debentures / securities issued by

Government or local authority or other securities of like marketable nature, leasing, hire-purchase, insurance business, chit business but does not include any institution whose principal business is that of agriculture activity, industrial activity, sale/purchase/construction of immovable property.

A Residuary non-banking company is also a NBFC. Residuary Non-Banking Company is a class of NBFC which is a company and has as its principal business the receiving of deposits. These companies are required to maintain investments as per directions of RBI, in addition to liquid assets. The functioning of these companies is different from those of NBFC in terms of deployment of depositors' funds.

QUES 2. NBFCs are doing functions similar to banks. What is difference between banks & NBFCs ?

ANS 2. NBFCs are doing functions akin to that of banks, however there are a few differences:
i.) a NBFC cannot accept demand deposits;
ii.) it is not a part of the payment and settlement system and as such cannot issue cheques to its customers; and
iii.) deposit insurance facility is not available for NBFC depositors unlike in case of banks. iv) The requirements of Cash Reserve Ratio and Statutory liquidity ratio[11] are not

---

[11] Banks have to maintain cash reserve ratio (it is ratio of 'cash balance with RBI' to ' demand and time liabilities', it is decided by RBI from time to time subject to minimum of 3% and maximum of 20%, currently it is 5%,) and Statutory Liquidity ratio (banks are required to maintain cash or gold or approved securities the amount of which shall not be less than 25% and not more than 40 % of demand and time liabilities , currently it is 25 %) on the basis of issue price.

applicable to the NBFCs. v) Banks are barred from acquisition financing, there is no such restriction on NBFCs. vi) NBFCs do not have any ceiling on lending in the stock market, Banks have a ceiling of 5% o their total exposure .

QUES-3. Is it necessary that every NBFC should be registered with RBI?

ANS 3. In terms of provisions of the RBI Act, 1934, it is mandatory that every NBFC should be registered with RBI to commence or carry on any business of non-banking finance company.

However, to obviate dual regulation, certain category of NBFCs which are regulated by other regulators are exempted from the requirement of registration with RBI viz. Venture Capital Fund/Merchant Banking companies/Stock broking companies registered with SEBI, Insurance Company , Nidhi companies as notified under the Companies Act, 1956, Chit companies or Housing Finance Companies regulated by National Housing Bank.

QUES 4. What are the different types of NBFCs registered with RBI?

ANS 4. The NBFCs that are registered with RBI are:
i. equipment leasing company;
ii. hire-purchase company;
iii. loan company;
iv. investment company;

The above type of companies may be further classified into those accepting deposits or those not accepting deposits.

v. Residuary Non-Banking Company.

QUES 5. What are the requirements for registration with RBI?

ANS 5. A company incorporated under the Companies Act, 1956 and desirous of commencing business of non-banking financial institution as defined under Section 45 I(a) of the RBI Act, 1934 should have a minimum net owned fund of Rs 25 lakh (raised to Rs 200 lakh w.e.f April 21, 1999). The company is required to submit its application for registration in the prescribed format alongwith necessary documents for Bank's consideration. The Bank issues Certificate of Registration after satisfying itself that the conditions regarding registration.

QUES 6. Can all NBFCs accept deposits and what are the requirements for accepting Public Deposits?

ANS 6. All NBFCs are not entitled to accept public deposits. Only those NBFCs holding a valid Certificate of Registration with authorisation to accept Public Deposits can accept/hold public deposits.

QUES 7. What is the rate of interest and period of deposit which NBFCs can accept?

Presently, the maximum rate of interest a NBFC can offer is 11%. The interest may be paid or compounded at rests not shorter than monthly rests.

The NBFCs are allowed to accept/renew public deposits for a minimum period of 12 months and maximum period of 60 months. They cannot accept deposits repayable on demand.

QUES 8. What is 'deposit' and 'public deposit'?

ANS 8. 'Deposit' includes any receipt of money by way of deposit or loan or in any other form . ' Public deposit' as a 'deposit' excluding the following:

- amount received from the Central/State Government or any other source where repayment is guaranteed by Central/State Government or any

amount received from local authority or foreign government or any foreign citizen/authority/person;

- any amount received from financial institutions;
- any amount received from other company as inter-corporate deposit;
- amount received by way of subscriptions to shares, stock, bonds or debentures pending allotment or by way of calls in advance if such amount is not repayable to the members under the articles of association of the company;
- amount received from shareholders by private company;
- amount received from directors or relative of the director of a NBFC;
- amount raised by issue of bonds or debentures secured by mortgage of any immovable property or other asset of the company subject to conditions;
- the amount brought in by the promoters by way of unsecured loan;
- amount received from a mutual fund;
- any amount received by issuance of Commercial Paper.

QUES 9. Please explain the terms 'owned fund' and 'net owned fund' in relation to NBFCs?

ANS 9. 'Owned Fund' means aggregate of the paid-up equity capital and free reserves as disclosed in the latest balance sheet of the company after deducting there from accumulated balance of loss, deferred revenue expenditure and other intangible assets.

The amount of investments of such company in shares of its subsidiaries, companies in the same group and all other NBFCs and the book value of debentures, bonds, outstanding loans and advances made to and deposits with subsidiaries and companies in the same group is arrived at. The amount thus calculated, to the extent it exceeds 10% of the owned fund, is reduced from the amount of owned fund to arrive at 'Net Owned Fund'.

NBFCs Prudential Norms : RBI has issued certain norms which are to be followwed by the NBFCs. Important norms have been summarized in the following paragraphs :

Non performing Assets (NPAs) means :

(1) an asset, in respect of which, interest has remained past due for six months;

(2) a term loan inclusive of unpaid interest, when the installment is overdue for more than six months or on which interest amount remained past due for six months;

(3) a demand or call loan, which remained overdue for six months from the date of demand or call or on which interest amount remained past due for a period of six months;]

(4) a bill which remains overdue for six months;

(5) any dues on account of sale of assets or services rendered or reimbursement of expenses incurred, which remained overdue for a period of six months;

(6) the lease rental and hire purchase installment, which has become overdue for a period of more than twelve months;

Asset Classification

Every NBFC shall classify its lease/hire purchase assets, loans and advances and any other forms of credit into the following classes namely,

(i) Standard assets;

(ii) Sub-standard assets;

(iii) Doubtful assets; and

(iv) Loss assets.

"Standard asset" means the asset in respect of which, no default in repayment of principal or payment of interest is perceived and which does not disclose any problem nor carry more than normal risk attached to the business.

Sub-standard asset" means –

a. an asset which has been classified as non-performing asset for a period not exceeding 18 months[12]
b. an asset where the terms of the agreement regarding interest and / or principal have been renegotiated until the expiry of one year of satisfactory performance under the renegotiated or rescheduled or restructured terms:

"Doubtful asset" means –

i. a term loan, or
ii. a lease asset, or
iii. a hire purchase asset, or
iv. any other asset, which remains a sub-standard asset for a period exceeding 18 months;
v. equity shares of loss making company

---

[12] RBI Notification No. **RBI/2004-05/94 dated August 3, 2004**

Loss asset" means -

(a) an asset which has been identified as loss asset by the NBFC or its internal or external auditor or by the Reserve Bank of India during the inspection of the NBFC, to the extent it is not written off by the NBFC; and

(b) an asset which is adversely affected by a potential threat of non-recoverability due to either erosion in the value of security or non availability of security or due to any fraudulent act or omission on the part of the borrower;

Provisioning requirements

Every NBFC shall, after taking into account the time lag between an account becoming non-performing make provision against sub-standard assets, doubtful assets and loss assets as provided hereunder :-

Loans, advances and other credit facilities including bills purchased and discounted

(1) The provisioning requirement in respect of loans, advances and other credit facilities including bills purchased and discounted shall be as under :

(i) Loss Assets The entire asset shall be written off. If the assets are permitted to remain in the books for any reason, 100% of the outstanding should be provided for;

(ii) Doubtful Assets (a) 100% provision to the extent to which the advance is not covered by the realizable value of the security

(b) In addition to item (a) above, depending upon the period for which the asset has remained doubtful, provision to the extent of 20% to 50% of the secured

portion (i.e. estimated realizable value of the outstanding) shall be made on the following basis : -

Period for which the asset has been considered as doubtful	**% of provision**
Up to one year	20
One to three years	30
More than three years	50

iii) Sub-standard assets A general provision of 10% of total outstanding shall be made.

Question : While closing its books of accounts on 31st March, 2005 a NBFC has its advances classified as follows:

	Rs. In Lakhs
Standard assets	16,800
Sub-standard assets	1,340
secured position 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 nmade against the advances.

Income recognition

(1) The income recognition shall be based on recognized accounting principles.

(2) Income including interest/discount or any other charges on NPA shall be recognized only when it is actually realised.

(3) In respect of hire purchase assets, where installments are overdue for more than 12 months, income shall be recognized only when hire charges are actually received.

(4) In respect of lease assets, where lease rentals are overdue for more than 12 months, the income shall be recognized only when lease rentals are actually received.

Income from investments

(1) Income from dividend on shares of corporate bodies and units of mutual funds shall be taken into account on cash basis:

(2) Income from bonds and debentures of corporate bodies and from Government securities/bonds may be taken into account on accrual basis:

(3) Income on securities of corporate bodies or public sector undertakings, the payment of interest and repayment of principal of which have been guaranteed by Central Government or a State Government may be taken into account on accrual basis.

Accounting standards

Accounting Standards and Guidance Notes issued by the Institute of Chartered Accountants of India (referred to in these directions as "ICAI") shall be followed insofar as they are not inconsistent with any of these directions.

Disclosure in the balance sheet

(1) Every NBFC shall separately disclose in its balance sheet the provisions made (in respect of sub-standard assets, doubtful assets and loss assets) without netting them from the income or against the value of assets.

(2) The provisions shall be distinctly indicated under separate heads of accounts as under :-

(i) provisions for bad and doubtful debts; and

(ii) provisions for depreciation in investments.

(3) Such provisions for each year shall be debited to the profit and loss account.

RBI ANF NBFCs

RBI regulates the NBFC through the following measures :

(i) Mandatory Registration
(ii) Minimum owned funds
(iii) Only RBI authorised NBFCs can accept public deposits
(iv) RBI prescribes the ceiling of interest rate
(v) RBI prescribes the period of deposit
(vi) RBI prescribes the prudential norms regarding utilization of funds
(vii) RBI directs their invest policies particularly in case of Residuary non-banking company
(viii) RBI inspectors conduct inspections of such companies

(ix) RBI prescribes the points which should be examined and reported by the auditors of such companies.

(x) RBI prescribes the norms for preparation of Accounts particularly provisioning of possible losses

(xi) NBFCs are supposed to submit financial returns from time to time to RBI, in case of NBFC have assets more than 100 Crores of rupees, the return has to be submitted every month. Through examination and analysis of these returns, RBI keeps an eye on their functioning.

Capital Adequacy Norms (as applicable to NBFCs)
(Based on RBI circular dated 1.7.2006)

(1) Every NBFC shall maintain a minimum capital ratio consisting of Tier I and Tier II capital which shall not be less than twelve per cent of its aggregate risk weighted assets and of risk adjusted value of off-balance sheet items.

(2) The total of Tier II capital, at any point of time, shall not exceed one hundred per cent of Tier I capital.

"Tier-I Capital" means owned fund as reduced by investment in shares of other NBFC and in shares, debentures, bonds, outstanding loans and advances including hire purchase and

lease finance made to and deposits with subsidiaries and companies in the same group exceeding, in aggregate, ten per cent of the owned fund;

"Owned fund" means paid up equity capital, preference shares which are compulsorily convertible into equity, free reserves, balance in share premium account and capital reserves representing surplus arising out of sale proceeds of asset, excluding reserves created by revaluation of asset, as reduced by accumulated loss balance, book value of intangible assets and deferred revenue expenditure.

"Tier-II capital" includes the following :-

(a) preference shares other than those which are compulsorily convertible into equity;
(b) revaluation reserves at discounted rate of fifty five percent;
(c) general provisions and loss reserves to the extent these are not attributable to actual diminution in value or identifiable potential loss in any specific asset and are available to meet unexpected losses, to the extent of one and one fourth percent of risk weighted assets;
(d) hybrid debt capital instruments; and
(e) subordinated debt[13].

On Balance-sheet assets

The value of each asset/item requires to be multiplied by the relevant risk weights to arrive at risk adjusted value of assets. The aggregate shall be taken into account for reckoning the minimum capital ratio. The risk weighted asset shall be calculated as the weighted aggregate of funded items as detailed hereunder :

Weighted risk assets - On-Balance Sheet items	**Percentage weight**
(i) Cash and bank balances including fixed deposits and certificate of deposits	0
(ii) Investments	
(a) Approved securities [Except at (c) below]	0
(b) Bonds of public sector banks	20
(c) fixed deposits/certificates of deposits/ bonds of public financial institutions	100
(d) Shares of all companies and debentures/bonds/commercial papers of all	

[13] "subordinated debt" means a fully paid up capital instrument, which is unsecured and is subordinated to the claims of other creditors and is free from restrictive clauses and is not redeemable at the instance of the holder or without the consent of the supervisory authority of the NBFC. The book value of such instrument shall be subjected to discounting as provided hereunder:

Remaining Maturity of the instruments	Rate of discount
(a) Up to one year	100%
(b) More than one year but up to two years	80%
(c) More than two years but up to three years	60%
(d) More than three years but up to four years	40%
(e) More than four years but up to five years	20%

to the extent such discounted value does not exceed fifty per cent of Tier I capital;

companies and units of all mutual funds 100

(iii) Current assets
(a) Stock on hire (net book value) 100
(b) Inter-corporate loans/deposits 100
(c) Loans and advances fully secured against deposits held by the company itself 0
(d) Loans to staff 0
(e) Other secured loans and advances considered good 100
(f) Bills purchased/discounted 100
(g) Others (To be specified) 100

(iv) Fixed Assets (net of depreciation)
(a) Assets leased out (net book value) 100
(b) Premises 100
(c) Furniture & Fixtures 100

(v) Other assets
(a) Income tax deducted at source (net of provision) 0
(b) Advance tax paid (net of provision) 0
(c) Interest due on Government securities 0
(d) Others (to be specified) 100

Note: Assets which have been deducted from owned fund to arrive at net owned fund shall have a weightage of `zero'.

Off-Balance - sheet items

In the RBI's directions, degrees of credit risk exposure attached to off-balance sheet items have been expressed as percentage of credit conversion factor. Hence, the face value of each item requires to be first multiplied by the relevant conversion factor to arrive at risk adjusted value of off-balance sheet item. The aggregate shall be taken into account for reckoning the minimum capital ratio. This shall have to be again multiplied by the risk weight of 100. The risk adjusted value of the off-balance sheet items shall be calculated as per the credit conversion factors of non-funded items as detailed hereunder:

Nature of item	**Credit conversion factor – %**
i) Financial & other guarantees	100
ii) Share/debenture underwriting obligations	50
iii) Partly-paid shares/debentures	100
iv) Bills discounted/rediscounted	100
v) Lease contracts entered into but yet to be executed	100
vi) Other contingent liabilities (To be specified)	50

Note: Cash margins/deposits shall be deducted before applying the conversion factor.

Q. No. 1 : You are given the B/S of Madhav Finance co. Ltd, a NBFC, as on 31st March, 2006. Calculate 'owned fund'. (Rs. Crores)

Liabilities	Amount	Assets	Amount
Equity share capital;		**Fixed assets :**	
50,00,000 equity shares of Rs. 100, Rs. 90 paid up	45.00	(a)goodwill	35.00
		(b) Assets on Lease	280.00
Reserve and surplus (including Revaluation reserve of Rs.15 crores)	105.00	(c) Other FA (premises, and furniture)	61.00
Unsecured Loans (Maturity 4 ½ years)	45.00	**Investment**s in shares of subsidiary	15.00
		Other Investments (MF	

Public Deposits	110.00	units)	11.00
Bank Borrowings	95.00	**CAs** (including Cash & Bank	
Commercial papers	40.00	Rs.25)	100.00
Inter-corporate deposit	62.00		502

Contingent Liabilities : Financial GuaranteesRs.0.55 Cr. Bills discounted Rs.1.95 Crs, Underwriting obligations Rs. 5.25 Crs.

Answer : Owned Fund = Paid up ESC + R & S (excluding Revaluation Reserve) –Intangible asset(goodwill)=45+ 90-35= 100

Q. No.2: Calculate(I)Tier I capital(II)TierII capital (III) Risk weighted assets (IV) Risk Adjusted value of off-Balance-sheet items(V)Capital adequacy ratio using the data of Q.1.

Answer : (Rs. Crores)

Tier I capital :	Owned Funds	100		
	Investment in W.O.S In excess of 10% of O.F.	-5	95	
Tier II Capital	Revaluation Reserve	6.75		
	Unsecured Loan (assuming that it is subordinated debt)	36.00	42.75	137.75

Calculation of Risk weighted assets : (Rs. crores)

	Book value (Rs.)	Risk Weight %	Adjusted value (Rs.)
Cash and bank	25.00	0	0
Other CAs	75.00	100	75
Investment in shares of subsidiary	10.00	100	10
Investment in shares of subsidiary	5.00	0	0
Investment in MFs	11.00	100	11
FA (Premises and furniture)	61.00	100	61
Goodwill	35.00	0	0
Assets on lease	280.00	100	280
Total			**437**

Risk Adjusted value of off-Balance-sheet items (Rs. Crores)

	Amt.	Conversion factor	Risk weight	Risk weighted value
Financial guarantees	Rs.0.55	100	100%	0.550
Bill discounted	Rs.1.95	100	100%	1.950
Underwriting	Rs.5.25	50	100%	2.625
Total				**5.125**

Total risk adjusted (weighted) Items : 437 + 5.125 = 442.125

Capital adequacy ratio : (137.75 / 442.125)x100 = 31.16

FUTURES AND OPTIONS IN INDIAN SHARE MARKETS

SEBI allowed futures and options in equity shares (also in equity shares based indices) in June 2000. In that month itself, NSE & BSE started trading in futures on Nifty and Sensex respectively. In June 2001, NSE & BSE commenced trading in options on NIFTY & SENSEX respectively. Options in 31 prominent shares started in July 2001 in both the exchanges. In November 2001, futures in

the same 31 shares started in both the exchanges. One can trade futures and options in market lots only. Market lot of Sensex is 50 units, Sensex option is 100 units, Nifty (future/option) is 200 units, ACC shares (future /option) 1500 shares, Reliance industries (future/option) is 600 shares and so on. All futures and options mature on the last Thursday of the month and are cash settled. At a time 3 series of futures and options are traded in the market. For example, if one wants to enter into futures/options in the first week of June2005, he may enter into contract maturing on last Thursday of June,2005 (this is referred as same/near month contract) or last Thursday of July,2005 (this is referred as next month contract) or last Thursday of August, 2005 (this is referred as distant month contact). Distant month contracts are not popular.

Currently, in India we have (i) futures as well as options on 46 shares[14] and (ii) index futures as well as options contracts based on the BSE's the flagship Index - SENSEX available for trading at the Stock Exchange Mumbai. We also have (i) futures as well as options on 52 shares[15] and (ii) index futures as well as options based on Nifty and CNX-IT indices of the NSE. Each contract expires on the last Thursday of the expiry month and simultaneously a new contract is introduced for trading after expiry of a contract. (In Indian stock markets Index options are of European type and share options of American type)

OPTIONS : An option is a contract that gives its owner the right (but not the obligation) to buy or to sell an underlying asset (for example, share of a company, foreign currency etc.) on or before a given date at a fixed price (this fixed price is called as Exercise price, it is also called as Strike price).

---

[14] ACC, Bajaj Auto, Bank of Baroda, Bank of India, BHEL, BPCL, Canara Bank, CIPLA, Dr.Reddy, GAIL, GRASIM, GACL, HCL, Hero Honda, Hindalco, HLL, HPCL, HDFC, ICICI Bank, IFLEX, IOCL, INFOSIS, ITC, Jet Airways, MTNL, M & M, Maruti, NALCO, NTPC, OBC. ONGC, Polaris, PNB, Ranbaxy, Reliance Energy, Reliance Industries, Satyam computers, SCI, SBI, TCS, TISCO, Tata Motors, Tata Power, Tata Tea, UBI and Wipro.

[15] Besides 46 above shares, Andhra Bank, Arvind Mills, BEL, HDFC Bank, IPCL and Syndicate Bank

Call option gives the buyer of the option the right (but not the obligation) to buy a currency or share.
Put option gives the buyer of the option the right (but not the obligation) to sell a currency or share. European option
An option that can be exercised on the specific date. American Option: An option that can be exercised on any date up to the expiry date.
Example: A & B enter into a contract under which B pays A Rs. 700 (option premium or option price) and in return A gives him the right of buying 100 shares of Reliance on a particular date at Rs. 1000 per share. B may buy 100 shares of Reliance from A at Rs. 1000 on that particular date (or he may not buy). Suppose Spot price on that date is below 1000, B won't buy the shares. If it is 1000, he may or may not buy. If the spot price is above Rs. 1000, it is natural that B will exercise his option i.e. he will buy the shares. In this example, B has limited his loss to Rs. 700 but there is no limit to his gain. The option referred in this example is "European Call option"

There are two parties in an option contract:

1) Option writer or option seller – he gives the option to the other party. In the above example, A is option writer. He receives the option premium or option price from the other party. In the above example Rs. 700 is option premium or option price.
2) Option owner or option holder – he gets "the option" or "the right (but not the obligation)" from the option writer against payment of "option premium" or "option price". In the above example, B is option owner.

In-the-money option: An option is said to be "In-the-money" when it is advantageous to exercise it.

Out-of-the money option: An option is said to the "Out-of-the-money" when it is disadvantageous to exercise it. (Naturally, is this situation, the option owner won't exercise it.)

At-the-money option: If the option holder does not lose or gain whether he exercises his option or not, the option is said to be at- the- money. (White solving questions in the examination, it is assumed that if the option is at the money, it is not exercised by its owner).

Accounting for options :

Q.No. 1 Kanhai buys two options from Arjun. Both follow calendar year as their accounting year. Give journal entries in the books of both.

Date of purchase	Type of option	Maturity date	Premium per unit	No, of units	Margin per unit	Strike price
28.3.2005	Nifty call	26.5.2005	Rs.20	200	Rs.160	2300
28.3.2005	Nifty put	26.5.2005	Rs.25	200	Rs.170	2310

Mr. Arjun was asked to pay additional margin on @ Rs. 10 per unit on call on 10th May,2005 and Rs. 12 per unit on put on 12th May,2005. Assume the spot prices on maturity to be (i) Rs. 2200 and (ii) Rs. 2400.

Q.No. 2 Kanhai buys two options from Arjun. Both follow financial year (April – March) as their accounting year. Give journal entries in the books of both.

Date of purchase	Type of option	Maturity date	Premium per unit	No, of units	Margin per unit	Strike price
28.3.2005	Nifty call	26.5.2005	Rs.20	200	Rs.160	2300
28.3.2005	Nifty put	26.5.2005	Rs.25	200	Rs.170	2310

Mr. Arjun was asked to pay additional margin on @ Rs. 10 per unit on call on 10th May,2005 and Rs. 12 per unit on put on 12th May,2005.

On 31st March 2005, premium per unit (on nifty call, 26th May 2005 maturity, maturity price Rs.2300) was Rs.10. The premium per unit (on nifty put, 26th May 2005 maturity, maturity price Rs.2310)
was Rs.12.

Assume spot prices on maturity date to be (i) Rs. 2200 (ii) Rs.2400

Q. Mr. Investor buys a stock option of ABC Co. Ltd in July, 2003 with a strike price on 30.7.2003 of Rs. 250 to be expired on 30.8.2004. the premium is Rs. 20 per unit and the market lot is 100. the margin to be paid is Rs. 120 per unit. Show the accounting treatment in the books of the buyer when : (i) option is settled by delivery (ii) option is settled in cash. Spot price on maturity Rs. 260.

Hint : assume the option is call option.

CORPORATE SOCIAL REPORTING

"Society is not just another stakeholder in corporates. It is the very purpose of the corporates"

The existance of the corporates depends upon the society;

- society buys goods and services produced by the corporates,
- society provides its savings to the corporates
- society suppliers human resources to the corporates
- society provides infrastucture and other facilities to the corporates

Sometimes, the society bears the adverse impact of corporate actions, like

- society's land is acquired to run the commercial activities of the corporates
- corporate operations injure the ecology and environment
- small farmers and enterprenuers loose their livelyhoods on account of coporate businesses.

The corporates owe their very existance to the society. The society therefore expects the corporates to operate in a manner that strengthens the society and takes it forward. The conclusion is that the corporates have their social responsibilities

"Corporate Social Resposibility is a commitment to improve the wellbeing of community through discretionary business practices and contribution of corporate resources."[16] It is defined as operating a business in a manner that meets or excceds the expectations the society has from the corporate. It is a way of converting 'a good company' to 'a great company'[17].

Social responsibilities of the Corporates :

(i) Earning profits and acquiring financial strength : Corporates are expected to earn profits and acquire financial strengths by providing the quality goods and honest services to the society at affordable prices and by operating withing the legal and moral frame-works, otherwise they will not be in a position to do any social good.

(ii) Efficient use of resources : The corporates should make effcient use of the resouces and avoid their wastage, be it financil resources, human resources, energy resources, natural resources or other resources.

(iii) Products : The corporates should produce the goods and services the society needs, due care should be taken of the quality. They should not produce the goods and services which are harmful to the society.

(iv) Environment : Damage to the environment can injure the health and well being of the members of the society. Hence, the corporates should ensure that their actions do not cause any damage to the environment. Where, some nominal damge is unavoidable, corrective steps must be undertaken.

(v) Human resource : Society provide this invaluable resource to the corporates. It is expected of the corporates that they take due care for economic, social and psychological wellbeing of not only their employees but also other persons

---

[16] Philips Kotler and Nancy _ Corporate Social Responsibility

[17] A good company provides superior quality goods and services to its customers at reasonable prices. A great company makes this world a better place to live.

providing the services to the company like small contractors. Providing healthy working environment and taking care of their health is the speical responsibility of the corporates.

(vi) Community : Providing community services enahnces the image of the corporates. Providing medical check-ups and health services in the neighbourhoods, building community centres, running creches, organising tournments and entertainment events etc. create goodwill among the members of the community.

Corporates draw a lot from the society. They are expected to deliver a lot to the society. They are interdependent. The wellbeing of one depends on the wellbeing of the other.

BENEFITS OF CORPORATE SOCIAL RESPONSIBILITY :

CSR is a business strategy that works. In a world where brand value and reputation are increasingly seen as a company's most valuable assets, CSR can build the loyalty and trust that ensure a bright sustainable future. In today's world, the corporations are becoming increasingly visible. They are not judged on their results but on their behavior too. By integrating CSR into their businesses as core value, the Corporates are making a significant contribution to a better society. CSR can and should govern every aspect of business life. The rewards, both for the corporation and society at large, are enormous.

The benefits of Corporate Social Responsibility

- Improved financial performance
- Better risk and crisis management
- Reduced operating costs
- Increased worker commitment
- Enhanced brand value and
- Good relations with government

reputation	and communities
• Long-term sustainability for your company and society	• A license to operate
• Long-term return on investments	• Increased productivity

Corporate Social Reporting

Corporates reports their performaces (mainly financial performances) through various reports, mainly through annual reports. It is increasingly emphasized today that these reports shold contain the information about the corporates fulfilling their social responsibilites. In other words, the corporates are expected to report their actions regarding their social resposibilities. Corporate Social reporting refers to the reporing by the corporates on the actions taken by them on performing their social responsibilities. It is a way of demonstrating the extent to which an orgainisation is meeting its social goals.

In India, the legal requirements regarding the CSR are quite limited. The corporates are expected to report only on three matters in their annual reports. These three matters are (i) Foreign exchange earnings and spendings (ii) Energy conservations and (iii) technology absorption. In the absence of any detailed legal requirement, guidance note or accounting standard, different companies follow different ways of the CSR. A very large number of PSUs are reporing by the way of Social Income Statement , the format is given on next page :

Social Income statement

I Social Benefits and Costs to Staff :

A. *Social Benefit to Staff :*

1.Medical and Hospital facilities

2. Educational facilities

3. Canteen facilities

4. Recreation, entertainment and cultural activities

5. Hosing and township facilities 6.

Watersupply, concessional electricity and Trasnport 7.

Training and career development 8.

Provident Fund, Gratuity, Bonus, Insurance benefits 9.

Holiday, leave encashment and leave-travel benefits

10.Other Benefits

Total Benefits to Staff

B. *Social costs to staff :* 1.

Lay off and involuntary termination 2.

Extra hours put in by Officers voluntarily

Total costs to staff :

Net Benefits to Staff (A-B)

II <u>Social Benefits and Costs to Community</u>

A. *Social Benefits to community :* 1.

Taxes to Panchayat/Municipality 2.

Environment Improvements 3.

Generation of job potential 4.

Generation of Business

Total Social Benefits to Community

B. *Social Costs to Community :*

Increase in cost of living in the vicinity

Net Benefits to community (A-B)

III. Social Benefits and Costs to General Public :

A. *Social Benefits to General Public :*

1. Taxes, duties, etc. paid to State governments 2.
Taxes, duties, etc. paid to Central government

Total Benefits to General Public

B. *Social Costs to General Public :* 1.
State services consumed – Electircity 2.
Central services consumed – Telephone, Telegrams, postal services and Banking

Total social costs to general public

Net Social Benefits to General Public (A-B)

Net social income to Staff, Community and General Public(I+II+III) ....

Q. From the following information taken from the books of F Ltd. relating to staff and community benefits, prepare a statement classifying the various items under the appropriate heads, required under Corporate Social Reporting : (Rs.)

Environmnetal Improvements	20,10,000
Medical facilities	45,00,000
Training facilities	10,25,000
Generation of Jub opportunities	60,75,000
Municipal taxes	10,70,000
Increase in cost of living in the vicnity due to a thermal power station	16,55,000
Concessional transport and water supply	11,25,000
Extra work put in by staff and officers for the drought relief	18,50,000

Leave encashment	52,00,000
Educational facilities for childern of staff members	21,60,000
Subsidisd canteen facilities	14,40,000
Generation of Business	25,50,000

Employee Stock Options Plans

ESOPs are used as a way by the companies to reward management and employees and link their interests with those of the company and other shareholders. Many companies use employee stock options plans to compensate, retain, and attract employees. These plans are contracts between a company and its employees that give employees the right to buy a specific number of the company's shares at a fixed price within a certain period of time. Employees who are granted stock options hope to profit by exercising their options. Here's an example of an employee stock option plan: an employee is granted the option to purchase 1,000 shares of the company's stock at the price of Rs.20 per share. The Plan allow the employee to exercise his options after 3 years[18] provided the employee continues in service of the company. Exercise period is 2 years[19]. Suppose after three years the price of the stock increases to Rs. 100 per share, for example, the employee may exercise his option and buy 1000

[18] Here the vesting period is three years. Vesting means getting the right to exercise the option. In this example, the employee gets the right of exercising the option after three years from the date of the grant of the option provided he continues in the employment of the company.

[19] Suppose the option is granted on 1.1.2003. The employee gets the right of exercising the option on 1.1.2006. He may exercise the option up to 1.1.2008 i.e. on or after 1.1.2006 and up to 1.1.2008, he may apply to the company to issue him 1000 shares against the payment of Rs. 20 per share. If the exercise period lapses the vested option lapses and no right shall accrue to the employee thereafter. The employee may exercise all the options vested in him in one stroke or choose to exercise a number of options within the exercise period.

Upon vesting, the employee gets an unfettered right to apply for the issue of shares . In the event of an employee resigning from the services of the company or his employment being terminated for whatever reasons, all unvested options shall expire as on that date, but the employee would retain all the vested options (except only when the employment is being terminated for some misconduct)

shares @ Rs. 20 per share.

SEBI Guidelines :

(I)The ESOP shall be approved by the shareholders by a special resolution. The resolution shall contain terms and conditions of the Plan.

(II) Lock-in period, vesting and exercise of options

(i) There should be a minimum period of one year between the grant of options and vesting.

(ii) There should be a maximum period of eight years between the grant of options and vesting.

(iii) Employee options must be exercised within a maximum period of five years from the date of vesting.

(iv) Shares issued in exercise of options shall not be subject to any lock-in period.

(III) Options are not be transferable.

(IV) Board of Directors shall disclose either in the Directors Report or in the annexure to the Director's Report, the details of the operation of the ESOP.

(V) the Board of Directors shall at each AGM place before the members a certificate from the auditors of the company that the scheme has been implemented in accordance with SEBI guidelines and in accordance with the resolution of the company in general meeting.

Q. A company has its share capital divided into shares of Rs. 10 each. On 1st April, 2004, it granted 10000 employees stock options at Rs. 40, when the market price was Rs. 130. The options were to be exercised between 16th Dec. 2004 and 15th March 2005. The employees exercised their options for 9500

shares only; the remaining options lapsed. The company closes its books on 31st March every year. Journalize.

Employee Stock Purchase Plans

Employee Stock Purchase Plan (ESPP) means a plan under which the company offers shares to employees as part of a public issue. Such plans are designed to promote employee stock ownership broadly within the firm. Many companies such plans to compensate, retain, and attract employees.

SEBI Guidelines

- The ESPP should be approved by the shareholders by a special resolution which should specify the price of the shares and also the number of shares to be offered to each employee. The number of shares offered may be different for different categories of employees.

- Companies have full freedom to price the shares under an ESPP at any level.

- Shares issued under an ESPP shall be locked in for a period of one year. However if the ESPP is part of a public issue and the shares are issued to employees at the same price as in the public issue, the shares shall not be subject to any lock-in.

- The details of the shares issued under the ESPP and the terms and conditions thereof shall be disclosed in the Directors' report or in an annexure thereto.

Corporate Governance

Corporate governance is commonly referred to as a system by which the corporates are directed and controlled. It is the process by which the corporate's objectives are established, achieved and monitored. Corporate governance is concerned with the relationships and responsibilities between the board, management, shareholders and other relevant stakeholders[20] within a legal and regulatory framework. Corporate Governance

[20] The principal players of a corporate are the shareholders, management and the board of directors. Other stakeholders include employees, suppliers, customers, banks and other lenders, regulators, the environment and the community at large.

is to conduct the business of a corporate in such ways that the interest of all its stakeholders (within regulatory frame-work) are served.

Corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the Board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it provides the structure through which the corporate objectives are set, and also provides the means of attaining those objectives and monitoring performance. Corporate Governance is about promoting corporate fairness[21], transparency[22] and accountability[23].

Good governance contributes to good performance. The objective of good governance is to promote strong, viable and competitive corporations. Boards of directors are stewards of the corporation's assets and their behaviour should be focused on adding value to those assets by working with management to build a successful corporation and enhance shareholder value and to take care of interest of all other stakeholders[24]. Corporate governance is the key mechanism through which this trust is maintained across all stakeholders.

A country's economy depends on the drive and efficiency of its Corporates. Thus the effectiveness with which the corporates are governed determines their competitive position in the international economic scenario.Corporate governance is a key element in enhancing investor confidence, promoting competitiveness, and ultimately improving economic growth. The governance of corporates is more important for world economic growth than the governance of countries. It is at the top of the international development agenda.

Principles

Commonly accepted principles of corporate governance include:

Rights and equitable treatment of shareholders: Organisations should respect the rights of shareholders and help them to exercise their rights.

Interests of other stakeholders: Organisations should recognise that they have legal and other obligations to all legitimate stakeholders.

---

[21] Fairness means that all the stakeholders are treated equvitably and have the opportunity for redress for violation of their rights.

[22] Transparency of clear information with which meaningful analysis of a company and its actions can be made. The disclosure of financial and operational information and internal processes of management enable outsiders to understand the organisation.

[23] Accountability of the board to shareholders means that the shareholders have the right to receive information on the financial stewardship of their investment and exercise power to reward or remove the directors entrusted to run the company.

[24] "Corporate Governance means doing everything better, to improve relations between companies and their stakeholders."

Role and responsibilities of the board: The board needs a range of skills and understanding to be able to deal with various business issues and have the ability to review and challenge management performance.

Integrity and ethical behaviour: Organisations should develop a code of conduct for their directors and executives that promotes ethical and responsible decision making.

Disclosure and transparency: Organisations should clarify and make publicly known the roles and responsibilities of board and management to provide shareholders with a level of accountability. Disclosure of material matters concerning the organisation should be timely and balanced to ensure that all stakeholders have access to factual information.

Corporate governance In India :
Corporate governance initiatives in India began in 1998 with the Desirable Code of Corporate Governance – a voluntary code published by the CII. The first formal regulatory framework for listed companies specifically for corporate governance was established by the SEBI, February 2000, on the basis of recommendations of the Kumarmangalam Birla Committee Report. The regulatory framework was later on revised on the basis of Narain Murthy Committee report. Currently, the listed companies are required to comply with the following conditions (popularly known as clause 49 of the listing agreement) as stipulated by the SEBI.

I Composition of Board

(i) The Board of directors of the company shall have an optimum combination of executive and non-executive directors with not less than fifty percent of the board of directors comprising of non-executive directors.

(ii) Where the Chairman of the Board is a non-executive director, at least one-third of the Board should comprise of independent directors and in case he is an executive director, at least half of the Board should comprise of independent directors.

II Audit Committee

(A) Qualified and Independent Audit Committee
(i) A qualified and independent audit committee shall be set up with at least 3 directors as members. Two-thirds of the members of audit committee shall be independent directors.
(ii) All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise.
(iii) The Chairman of the Audit Committee shall be an independent director;
(iv)The Chairman of the Audit Committee shall be present at Annual General Meeting to answer shareholder queries;
(v) The Company Secretary shall act as the secretary to the committee.

(B) Meeting of Audit Committee
The audit committee should meet at least four times in a year and not more than four months shall elapse between two meetings.

(C) Role of Audit Committee
1. Oversight of the company's financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct, sufficient and credible.
2. Recommending to the Board, the appointment, re-appointment and, if required, the replacement or removal of the statutory auditor and the fixation of audit fees.
3. Disclosure of any related party transactions
4. Qualifications in the draft audit report.
5. Reviewing, with the management, the quarterly financial statements before submission to the board for approval
6. Reviewing, with the management, performance of statutory and internal auditors, adequacy of the internal control systems.

III Disclosures

(A) Basis of related party transactions
(i) A statement in summary form of transactions with related parties in the ordinary course of business shall be placed periodically before the audit committee.
(ii) Details of material individual transactions with related parties which are not in the normal course of business shall be placed before the audit committee.
(iii) Details of material individual transactions with related parties or others, which are not on an arm's length basis should be placed before the audit committee, together with Management's justification for the same.

(B) Disclosure of Accounting Treatment
Where in the preparation of financial statements, a treatment different from that prescribed in an Accounting Standard has been followed, the fact shall be disclosed in the financial statements, together with the management's explanation as to why it believes such alternative treatment is more representative of the true and fair view of the underlying business transaction in the Corporate Governance Report.
(C) Board Disclosures – Risk management
The company shall lay down procedures to inform Board members about the risk assessment and minimization procedures.

(D) Proceeds from public issues, rights issues, preferential issues etc.
When money is raised through issuing the shares, the company shall prepare a statement regarding uses of the funds so raised.. This statement shall be certified by the statutory auditors of the company.

(E) Remuneration of Directors
(i) All pecuniary relationship or transactions of the non-executive directors vis-à-vis the company shall be disclosed in the Annual Report.
(ii) Further the following disclosures on the remuneration of directors shall be made in the section on the corporate governance of the Annual Report:
(a) All elements of remuneration package of individual directors summarized under major groups, such as salary, benefits, bonuses, stock options, pension etc.

(b) Details of fixed component and performance linked incentives, along with the performance criteria.
(c) Service contracts, notice period, severance fees.
(d) Stock option details, if any – and whether issued at a discount as well as the period over which accrued and over which exercisable.
(iii) The company shall publish its criteria of making payments to non-executive directors in its annual report.

IV. CEO/CFO certification
The CEO and the CFO shall certify to the Board that:
(a) They have reviewed financial statements and the cash flow statement for the year and that to the best of their knowledge and belief :
(i) these statements do not contain any materially untrue statement or omit any material fact or contain statements that might be misleading;
(ii) these statements together present a true and fair view of the company's affairs and are in compliance with existing accounting standards, applicable laws and regulations.
(b) There are, to the best of their knowledge and belief, no transactions entered into by the company during the year which are fraudulent, illegal or violative of the company's code of conduct.
(c) They accept responsibility for establishing and maintaining internal controls.

V. Report on Corporate Governance
(i) There shall be a separate section on Corporate Governance in the Annual Reports of company, with a detailed compliance report on Corporate Governance.
(ii) The companies shall submit a quarterly compliance report to the stock exchanges within 15 days from the close of quarter.

VI. Compliance
The company shall obtain a certificate from either the auditors or practicing company secretaries regarding compliance of conditions of corporate governance as stipulated in clause 49 and annex the certificate with the directors' report, which is sent annually to all the shareholders of the company. The same certificate shall also be sent to the Stock Exchanges along with the annual report filed by the company.

Holding Company accounts

There are three situations when holding –subsidiary relationship comes into existence :

(i) A company holds more than 50% voting right shares of the other company

(ii) A company has the right of appointing majority of directors of the other company

(iii) When it is the case of chain holding i.e. A is holding of B and B is holding of C . In that case C is holding of A.

In Holding Company accounts, the date of acquisition (i.e., the date on which holding company acquired the shares of subsidiary company) is quite important. We should know the date on which holding company acquired shares of subsidiary company. Any profit earned by subsidiary company before this date is pre-acquisition profit. Any profit earned by subsidiary company after this date is post-acquisition profit. Suppose holding company acquired 80 per cent shares of subsidiary company on 1.1.1997, then profits earned by subsidiary company before 1.1.1997 are referred as pre-acquisition profits.

If Holding Company receives any dividend out of pre-acquisition profits of subsidiary company, such dividend should be credited to "Investments in Shares of Subsidiary Company Account" and not to "Profit and Loss Account". For example, on 1.1.1997. *X Ltd.* purchased 80 per cent shares of *Y Ltd.*, from Mr. WYE, who has been holding these shares throughout the year 1996, for Rs. 5,00,000 (*X Ltd.* should pass the entry with Rs. 5,00,000, Investment in shares of *Y Ltd.* A/c *Dr.*, To Bank A/c). On 20.3.1997, *Y Ltd.* declared dividend of Rs. 1,00,000 for 1996. *X Ltd.* will get dividend of Rs. 80,000. (Though *X Ltd.* had not been holding these shares in 1996, Mr. WYE had been holding these shares in 1996, dividend on these 80 per cent shares would be received by *X Ltd.*, because companies pay dividend to the shareholders who hold shares on the date of declaration of dividend). *X Ltd.* should credit this dividend to "Investment in Shares of *Y Ltd.* A/c" and not to "Profit and Loss A/c". The entries should be

(i) Bank A/c *Dr.* 80,000, To Dividend A/c 80,000, (ii) Dividend A/c *Dr.* 80,000, To Investment in Shares of *Y Ltd.* A/c 80,000.

Question No. 1

A Ltd. purchased 6000 shares of *B Ltd.*, from shareholders of *B Ltd.* on 1.10.1991 for Rs. 7,00,000. Total issued capital of *B Ltd.* on that date was 7500 shares of Rs. 100 each. On 1.1.1991 *B*'s P&L A/c had a credit

balance of Rs. 4,00,000. In November 1991, *B Ltd.* issued bonus shares in the ratio of 1 : 3. *B Ltd.*'s profit for 1991 Rs. 1,10,000; 1992 Rs. 70,000; 1993 Rs. 20,000. *B Ltd.* declared and paid dividend at 9 per cent for 1991; 8 per cent for 1992 and 6 per cent for 1993. In each case, dividend was paid on 20th February of the following year. On 20th March 1994 *A Ltd.* sold 1,200 shares of *B Ltd.* at Rs. 200 per shares. Give Journal of *A*.

Tutorial Note

Before attempting this question, we should understand a few points:

(a) We do not pass any entry on receipt of bonus shares because there is no account which can be credited on receipt of these shares. There are three rules for credit. None of these rules can be applied on receipt of bonus shares. As per first rule, we credit the 'giver', here we cannot credit the account of the company giving the bonus shares because that company is not becoming our creditor. As per second rule, credit what goes out. "Nothing goes out" on receipt of bonus shares. Hence, this rule cannot be applied. As per third rule, credit the incomes and gains. Even this rule cannot be applied because receipt of bonus shares does not constitute income or gain because income or gain is said to have been earned when there is increase in wealth. Receipt of bonus shares does not increase the wealth because theoretically value of share reduces proportionately on issue of bonus shares. Suppose, a person is holding 100 shares of a company, market price Rs. 100 per share. Total wealth Rs. 10,000. Now the company issues bonus shares in the ratio of 1 : 1. Theoretically market price per share will come down to Rs. 50. He will be holding 200 shares. Total wealth = 200 × 50 = Rs. 10,000.

(b) For that accounting year in which bonus shares are issued, companies have three options :

(i) Paying full year's dividend on bonus shares (for that year).

(ii) Paying pro-rata dividend on bonus shares (for that year).

(iii) Paying no dividend on bonus shares (for that year).

(The resolution of bonus shares should specify the option, the company would follow).

These options are only for that accounting year in which bonus shares have been issued. From next accounting year, no such discrimination can be done. All the shares will rank *pari passu* from next accounting year.

Example : Accounting year 1.4.1996-31.3.1997. Company issued bonus shares on 1.10.1996. In June, 1997, the company paid a dividend of Rs. 2 per old share. On bonus shares, dividend may be (i) Rs. 2 per share, or (ii) Re 1.00 per share, or (iii) No dividend. (The resolution of bonus shares should specify the option the company would like to follow). From next year, dividend per share would be same on old as well as bonus shares.

(c) For Bonus shares, we generally assumed FIFO, i.e., we assume that bonus shares are issued out of oldest profit.

(d) For dividend, we generally assume LIFO, i.e., we assume that dividend for any year is first paid out of profit of that year; if profit for that year is not sufficient we draw out of profit of previous year; if profit for previous year is not sufficient, we draw out of profit of the year before previous year. For example, profit for 1995 is Rs. 2,00,000. Dividend for 1995 is Rs. 2,50,000. Retained Profit for 1994 is Rs. 30,000 and that of 1993 is Rs. 40,000. For 1995 dividend, we shall use Rs. 2,00,000 of 1995, Rs. 30,000 of 1994 and Rs. 20,000 of 1993 profit. This LIFO assumption is applied on annual basis, i.e., we shall assume that Rs. 20,000 shall be taken out of 1993 profit; we shall not assume that Rs. 20,000 shall be taken out of second half of 1993 profit.

CONSOLIDATED BALANCE SHEET

Before preparing Consolidated Balance Sheet, we should make four working notes about subsidiary company.

(i) Capital Profit : By Capital profit, here, we mean pre-acquisition profit that is still available, i.e., such profits which were earned by subsidiary company in pre-acquisition period and which are still available, i.e., available on the date of Consolidated Balance Sheet. Here we are not guided by nature of profit, i.e., whether it is profit of revenue nature or of capital nature, we are guided by the fact that profit was earned in pre-acquisition period. For example, pre-acquisition revenue profit is capital profit for this purpose.

Example *:* X acquired 80 per cent shares of *Y Ltd.* on 1.1.1997. On that date, *Y Ltd.*'s P & L A/c had *Cr.* balance of Rs. 5,00,000. If we have to prepare Consolidated Balance Sheet as on 1.1.1997, Capital profit is Rs. 5,00,000. On 20.3.1997 *Y Ltd*. paid Dividend for 1996 Rs. 1,00,000. After this date, capital profit is only Rs. 4,00,000. In August 1997, *Y Ltd.* issued bonus shares of Rs. 2,00,000 out of pre-acquisition profit. After this, capital profit is only Rs. 2,00,000. Thus, by the term capital profit we mean pre-acquisition profit (whether of capital nature or of revenue nature) that is still available. Capital profit is divided between Holding company and Minority.

(ii) **Revenue Profit :** Post-acquisition profit (whether of capital nature or of revenue nature) that is still available, i.e., here we consider such profits which were earned by subsidiary company after its shares were acquired by holding company and which are still available, i.e., available on the date of Consolidated Balance Sheet. Revenue profit is divided between holding company and minority.

(iii) Minority Interest (Outside Shareholders' interest) = Paid up value of Shares held by outside minority + Minority's shares in revenue profit + Minority's share in Capital profit + Minority's shares in proposed dividend of subsidiary company.

(iv) **Cost of Control :** It is the difference between "Cost of the shares of subsidiary company held by holding company" and "Book value of such shares as on date

of acquisition". If cost of share is more than book value, the difference is goodwill and if cost of shares is less than book value, the difference is capital reserve. Cost of control can be calculated by either of two methods of calculations:

Method I :

Gross-cost of Shares of subsidiary company ....
(as held by holding company)

Less :(i) Pre-acquisition dividend received/receivable
(ii) Paid up value of such shares
(iii) Holding company's share in capital
Profit of subsidiary company

If the resultant figure is positive, it is goodwill, if it is negative, it is capital reserve.

Method II :

Gross-cost of shares of subsidiary company ....
(as held by holding company)

Less Book value of such shares,
as on date of acquisition ....

Goodwill or capital Reserve ....

Notes :(i) If 'Gross Cost' less 'Book Value' is positive, it is goodwill, otherwise capital reserve.

(ii) If proposed dividend by subsidiary company was there on the date of acquisition, book value should be cum-dividend.

(AS-21 uses the term 'equity' for what we have referred as book value here)

RULES FOR PREPARING CONSOLIDATED BALANCE SHEET

(i) Aggregate all the real assets and all the outside liabilities (secured loans, unsecured loans, current liabilities and Provisions) of the two companies except "Investment in shares of subsidiary company" as appearing in holding company Balance Sheet. This rule is subject to rule No. 2.

(ii) Eliminate inter-company Owings.

(iii) Take share capital only of holding company.

(iv) Calculate cost of control and show as separate item.

(v) Calculate minority interest and show as separate item.

(vi) Create reserve for unrealized amount of profit included in stock at least to the extent of holding company's Share.

For example, subsidiary company purchased certain goods from outside world for Rs. 1,00,000. Subsidiary company sold these goods to holding company for Rs. 1,25,000. These goods are still in the stock of holding company as on date of Consolidated Balance Sheet In the individual balance sheet of holding company we can show the stock at Rs. 1,25,000 because it is cost for holding company. In the Consolidated balance sheet, we cannot show the stock at Rs. 1,25,000 because Consolidated Balance Sheet is the balance sheet of group as a whole and for group as a whole, cost is not Rs. 1,25,000. Hence, we should create reserve for profit element included in stock. In this connection, there are two opinions: (i) create full Stock Reserve, i.e., Rs. 25,000; (ii) create proportionate Stock Reserve, for example, if holding company is holding 80 per cent shares of subsidiary company, create Stock Reserve of Rs. 20,000. The first approach is recommended by AS-21 (paragraph 16).

(vii) Take reserve and surplus of holding company. Holding company's share in post-acquisition profit of subsidiary company should be added to the appropriate (concerned) account of holding company.

Question No. 2

H Ltd. acquired 80,000 shares of Rs. 10 each is *S Ltd.* on 1.1.1983. The summarized balance sheets of *H Ltd.* and *S Ltd.* on 30.6.1983 were :

S. capital	25,00,000	10,00,000	Machinery	11,00,000	4,50,000

Reserves	1,30,000	1,50,000	Furniture	1,00,000	40,000
P&L A/c	20,000	45,000	Shares in S Ltd.	8,80,000	-----
Debentures	------	2,50,000	Debentures in S Ltd.	80,000	-----
Creditors	4,00,000	2,00,000	Stock	5,20,000	6,50,000
B/P	20,000	10,000	Drs.	1,80,000	2,70,000
			B/R	10,000	15,000
			Cash	2,00,000	2,30,000
Total	30,70,000	16,55,000	Total	30,70,000	16,55,000

B/R of *S Ltd.* include bills for Rs. 7,000 accepted by *H Ltd.* and Creditors of *S Ltd.* include Rs. 20,000 due to *H Ltd.* Stock of *H Ltd.* includes goods of Rs. 10,000 purchased from *S Ltd.* which made a profit of Rs. 2,000 on these goods. The balance in the P&L A/c of *S Ltd.* was nil on 1.7.1982. An amount of Rs. 50,000 was transferred by *S Ltd.* to reserves during the year. Prepare consolidated balance sheet. (Minority Interest Rs.239000 Capital Reserve 38000 Total of consolidated B/s 3736000)

Question No. 3

A Ltd. acquired 60 per cent of equity and 80 per cent of preference share in *B Ltd.* on 1.1.1983 at a total cost of Rs. 5,00,000. The balance sheets on 31st December 1983 when the accounts of both the companies were prepared were as follows :

Balance Sheet of A Ltd. (31.12.83)

Shares Capital	8,50,000	Land & Buildings	6,15,000
Creditors	75,000	Plant	2,60,000
Gen. Reserve (1.1.1983)	5,15,000	Debtors	1,30,000
P&L	4,00,000	Stock	1,70,000
		Investment (Shares of *B*)	5,00,000
		Bank	1,65,000
Total	18,40,000		18,40,000

Creditors of *A Ltd.* include Rs. 60,000 for purchases from *B Ltd.* on which *B Ltd.* made a profit of Rs. 17,500. Stock of *A Ltd.* includes Rs. 15,000 stock (at cost to *A Ltd.*) purchased from *B Ltd.*, part of above-mentioned Rs. 60,000 purchases.

Balance Sheet of B Ltd. (31.12.83)

Equity Capital	1,50,000	Land & Buildings	1,50,500
6% Pref. Capital	1,00,000	Plant & Machinery	1,35,000
Creditors	80,500	Stock	1,01,000
General Reserve (1.1.83)	5,000	Debtors	79,000
P&L A/c	1,85,000	Bank	55,000
Total	5,20,500		5,20,500

The balance of P&L A/c on 1.1.1983 was Rs. 1,80,000 out of which equity dividend (at the rate of 16%) and preference dividend were paid for 1982.

Prepare consolidated balance sheet as on 31.12.1983. (Goodwill 217800 M. Int. 154800 Total of Consolidated B/s 2013925)

Question No. 4 In preparing the consolidated balance sheet of *L Ltd.* as at 31st December 1989 you are required to show clearly what amounts, if any, you would include in respect of *W Ltd.* with regard to :

(a) Cost of control (b) Minority interest

(c) Profit or loss, i.e., holding company's share in post-acquisition profit of subsidiary company.

under each of the following assumptions :

(a) 48,000 of the shares then in issue of *W Ltd.* were acquired at a cost of £ 95,000 on 1st March 1987; *L Ltd.* did not participate in the proposed dividend of £ 8,000.

(b) 40,000 of the shares then in issue of *W Ltd.* were acquired at a cost of £ 90,000 on 31st December, 1987; *L Ltd.* participated in the bonus issue but not in proposed dividend of £ 9,000.

(c) 60,000 of the shares then in issue of *W Ltd.* were acquired at a cost of £ 80,000 on 1st July, 1989; *L Ltd.* participated in the proposed dividend of £ 6,000.

The balance sheet of *W Ltd.* as at 31st December 1989 showed :

Ordinary share of £ 1 each, fully paid £ 80,000

Undistributed profits £20,000

The profits appropriation account, for the years ended 31st December, was as follows :

	1986 (£)	1987 (£)	1988 (£)	1989 (£)
Balance in the beginning of the year	16,000	22,000	43,000	28,000

Bonus issue of 1 for 4 (1.1.88)	-----	------	16,000	-----
			27000	
Profit for the year	14000	30000	7000	(8000)
	30000	52000	34000	20000
Proposed Dividend	8000	9000	6000	Nil
Bal. c/d	22000	43000	28000	20000

The only increase in issued share capital during this period has been from the bonus issue on 1st January 1988. Ans.(a) Goodwill 26750 M. Int. 25000 (b) Goodwill 23125 M. Int. 37500)

Question No. 5

The balance sheets of *S Ltd.* and *T Ltd.* as at 31.3. 1994 were as below:

	S Ltd.	*T Ltd.*
	Rs.	*Rs.*
Liabilities		
Share Capital (Rs. 10 each)	5,00,000	2,00,000
Reserves	2,40,000	1,00,000
Profit and Loss A/c	57,200	82,000
Bank Overdraft	80,000	—
Bills Payable	—	8,400

Creditors	47,100	9,000
	9,24,300	3,99,400
Assets		
Land and Buildings	1,50,000	1,80,000
Plant & Machinery	2,40,000	1,35,000
Investment in *T Ltd.*	3,40,000	—
Stock	1,20,000	36,400
Sundry Debtors	44,000	40,000
Bills Receivable	15,800	—
Cash	14,500	8,000
	9,24,300	3,99,400

S Ltd. had acquired 16,000 shares of *T Ltd.* on 1st October, 1993. The profit and loss account of *T Ltd.* stood at Rs. 30,000 (credit) on 31st March, 1993 out of which a dividend of 10 per cent was paid on 1st November, 1993. *S Ltd.* had credited its share of dividend to its profit and loss account.

S Ltd. had sold an item of machinery to *T Ltd.* on hire-purchase basis. In respect of this machinery, the following were the balances in its books as of 31st March, 1994 : Installments due Rs. 5,000 Installments not due Rs. 2,000

HP Stock Reserve Rs. 400

The above stood included under appropriate heads in the balance sheets. Prepare the consolidated balance sheet of the two companies as on 31st March, 1994. [CA (Final), May 1994]

Working notes : Analysis of profit of T Ltd. as on 31.3.1994:

	Capital profit (pre- 1st Oct.,	Revenue profit

		1993)	(1.10.1993 – 31.3.1994)
General reserve* 1.4.1993		1,00,000	
P & L a/c 1.4.1993 Less dividend for year ended 31.3.1993	30,000 20,000	10,000	
Profit for year ended 31.3.1994		36,000	36,000
Total		1,46,000	36,000
Holding company's share (80%)		1,46,000 x 0.80 = 1,16,800	36,000 x 0.80 = 28,800
Minority's share (20%)		1,46,000 x 0.20 = 29,200	36,000 x 0.20 = 7,200

*Assumed to have been brought down from last year

Minority interest : Paid up value 40000 + capital profit 29200 + revenue profit 7200 = 76400

Cost of control Cost of shares 3,40,000

Less (i) paid up capital -1,60,000

(ii) pre-acquisition div. - 16,000

(iii) capital profit - 1,16,800

Goodwill 47,200

Proposed Dividend of Subsidiary Co. (Three Types of Situations) I case

Proposed dividend of subsidiary company appears in subsidiary company balance sheet but holding company has not passed the entry for the receivable amount of dividend. In this situation proposed dividend should be taken as separate item while making analysis of profit.

Question No. 6

Summarized Balance Sheets of *A Ltd.* and its subsidiary company *B Ltd.* as on 31st March, 1977, are given below :

E. shares (Rs.10)	7,00,000	2,00,000	FA	3,85,000	3,25,000
7% Pref. share capital (Rs.10)	----	1,60,000	15000 equity shares in B	3,30,000	---
G. Reserve	-----	80,000	12000 pref. Shares in B	1,20,000	----
P & L	2,97,000	88,800	Rs.20000 Debs. in B	20,000	----
6% Deb.	-----	40,000	CA	3,82,000	3,48,200
Prop. Div. Pref.	----	11,200			
Prop. Div. equity	*60,000*	20,000			
Deb. Interest accrued (6 months)	-----	1,200			
Crs.	1,80,000	72,000			
Total	1,80,000	6,73,200	Total	12,37,000	6,73,200

Relevant informations:

(a) *A Ltd.* acquired the shares in *B Ltd.* on 31st March, 1976.

(b) The general reserve of *B Ltd.* as on 31st March, 1976 was the same as on 31st March, 1977.

(c) The balance in the profit & loss account of *B Ltd.* is made up as follows: (Rs.)

Balance as on 31st March 1976	56,000
Profit for year ended 31st March 1977	64,000
	120000
Less : Proposed Dividends	31,200
	88,800

(d) The stock of *B Ltd.* as on 31st March 1977 includes Rs. 36,000 in respect of goods purchased from *A Ltd.* on which the later company made a profit of 20 per cent above cost.

(e) The balance in the profit and loss account of *B Ltd.* as on 31st March, 1976 is after providing for the preference dividend of Rs. 11,200 and a proposed equity dividend of Rs. 15,000 both of which were subsequently paid but the proportionate amount due to *A Ltd.* was inadvertently credited by it to its profit & loss account.

(f) No entries had been made in the books of *A Ltd.* in respect of the debenture interest, and the proposed dividends due from *B Ltd.* for the year ended 31st March, 1977.

(g) On 31st March, 1977, *B Ltd.* made an issue of bonus shares for Rs. 80,000 by capitalizing the general reserve and issued pro-rata. The transaction had not yet been shown in the books of *B Ltd.*

Prepared a consolidated balance sheet of *A Ltd.* and its subsidiary *B Ltd.* as on 31st March, 1977. (M. Int. 140000 Con B/S total 1492550 Goodwill 58350)

Proposed Dividend of Subsidiary Co. (Three Types of Situations) II case

Proposed dividend of subsidiary company appears just as a note, i.e., neither subsidiary company has passed the entry proposing the dividend nor holding company has passed the entry for receivable amount of proposed dividend. There are two ways of dealing with this situation: (a) Taking proposed dividend as a separate item; (b) Taking proposed dividend as part of P&L A/c. (Actually in this way, we have to do nothing, we just ignore the note regarding proposed dividend of subsidiary company). We prefer the second way.

Proposed Dividend of Subsidiary Co. (Three Types of Situations) III case

Proposed dividend of subsidiary company appears in subsidiary company balance sheet and holding company has passed the entry for receivable amount of the proposed dividend of subsidiary company. In this case, that proportion of proposed dividend of subsidiary company which is to be received by holding company appears in assets side of holding company balance sheet. Hence, this amount we deduct from both sides of Consolidated balance sheet and the remaining amount of proposed dividend of subsidiary company we may either show as proposed dividend for minorities or add to the amount of minorities interest.

Question No. 7

On 1st January, 1976, *A Ltd.* acquired 8,000 shares of Rs. 10 each of *B Ltd.* at Rs. 90,000. The respective balance sheets on 31st December, 1978 are given below: (Rs.)

	A Ltd.	*B Ltd.*		*A Ltd.*	*B Ltd.*
Share Capital (Rs. 10 each)	2,00,000	1,00,000	Fixed Assets	1,60,000	1,10,000
Reserve	40,000	28,000	Investments	1,00,000	15,000
Profit & Loss A/c	36,000	33,000	Debtors	20,000	18,000
			Stock	25,000	35,000

Creditors	42,000	28,000	Cash & Bank	42,000	31,000
O. Liabilities	29,000	20,000			
	3,47,000	**2,09,000**		**3,47,000**	**2,09,000**

Additional information:

(1) At the time of acquiring shares, *B Ltd.* had Rs. 24,000 in reserve and Rs. 15,000 in profit & loss account.

(2) *B Ltd.* has paid 11 per cent dividend in 1976, 12 per cent in 1977 and 15 per cent in 1978 for 1975, 1976 and 1977 respectively. All dividends received have been credited to the profit and loss account of *A Ltd.*

(3) Proposed dividend of both the companies for 1978 is 12 per cent.

(4) A bonus dividend of one full paid share of 5 held has been declared by *B Ltd.* out of pre-acquisition reserve. No effect has been given to that in the above accounts.

(5) On 1.1.76 building of *B Ltd.* which stood in the books at Rs. 50,000 was revalued at Rs. 60,000 but no adjustment has been made in the books. Depreciation has been charged @ 10 per cent p.a. on reducing balance method.

(6) In 1978, *A Ltd.* purchased from *B Ltd.* goods for Rs. 10,000 on which *B Ltd.* made a profit of 20 per cent on sales, 25 per cent on such goods are lying unsold on 31st December, 1978.

You are required to prepare a consolidated balance sheet as on 31st December, 1978.(Cap. Reserve Rs.29200, M. Int. 33658 Con. B/S total 472790)

Question No. 8 :

A Ltd. made an offer to acquire all the shares in *B Ltd.* at a price of Rs. 25 per share, to be satisfied by the allotment of five shares in *A Ltd.* for every four shares in *B Ltd.* By the date of expiration of the offer, which was January 1, 1978

shareholders owning 60 per cent of the shares in *B Ltd.* had accepted the offer, and the acquisition was effective from that date.

The accounting date of *B Ltd.* was 31st March in each year but to confirm with *A Ltd.*, accounts were prepared to 30th June, 1978, covering the fifteen months to the date.

The draft summarized account of the companies as on 30th June, 1978 which do not include any entries regarding the acquisition of shares in *B Ltd.* were as follows :

Balance Sheet as on 30th June, 1978

		A Ltd.	*B Ltd.*
		Rs.	*Rs.*
Equity shares of Rs. 10 each			
Authorised		3,00,000	75,000
Issued & fully paid		1,50,000	60,000
Reserves & Surplus	*Rs.*		
General Reserve	55,000		
Profit & Loss A/c	2,62,000	3,17,000	20,000
Current Liabilities		27,000	7,000
Provision for taxation		33,000	6,000
		5,27,000	93,000
Freehold Property		2,00,000	38,000
Plant & Machinery		2,32,000	9,000
Quoted Investment at Cost		7,000	—
Stock at cost		32,000	21,000
Debtors		41,000	17,000
Balance at Bank		15,000	8,000

	5,27,000	93,000

Profit & Loss Account — Period ended 30th June

	A Ltd.	*B. Ltd.*
	One year	*15 months*
	Rs.	*Rs.*
Balance brought forward (1.4.1977)	2,14,000	7,500
Profit for the period	80,000	22,500
	———	———
	2,94,000	30,000
	———	———
Taxation for the period	32,000	6,000
Interim dividend paid 30th Nov. 1977	—	4,000
Balance carried forward	2,62,000	20,000
	———	———
	2,94,000	30,000

The directors of *A Ltd.* have recommended a final dividend of 20 per cent to the shareholders on register as on 30th June, 1978. The directors of *B Ltd.* has proposed a final dividend of 12½ per cent payable on 30th September, 1978.

You are required to prepare the consolidated balance sheet of *A Ltd.* on 30th June, 1978.

Answer ; A Ltd purchased 3600 shares of B Ltd (from shareholders of B Ltd.) for Rs.90000 (3600 shares @ Rs.25)

A Ltd issued (3600)x(5/4) i.e. 4500 shares.

	Capital profit (pre 1.1.78)	Revenue profit (1.1.78-

		30.6.78)
Profit b/d	7500	---
Current 15 months post tax profit	16500x(9/15)	16500x(6/15)
Interim dividend	- 4000	-----
Total	13400	6600
Holding co.'s share	13400 x 0.60 =8040	6600 0.60 = 3960
Minority's share holding	13400 x 0.40 =5360	6600 x 0.40

Minority interest		**Cost of control**	
Paid up capital	24000	Cost of shares	90000
Capital profit	5360	Paid up value	-36000
Revenue profit	2640	Capital profit	-8040
Total	**32000**	**Goodwill**	**45960**

Consolidated B/S of A Ltd. and its Subsidiary B Ltd. as on 30.6.1978

S. capital	195000	Goodwill	45960
S. Prem.	45000	Freehold	238000
GR	55000	Plant	241000
P & L 262000 +3960 Prop. Div. of A -39000	226960	Investment	7000
CL	34000	Stock	53000

Tax	39000	Drs.	58000
Prop. Div (A)	39000	Bank	23000
M. Int.	32000		
Total	665960	Total	665960

Question No. 9

H Ltd. purchased on 1.4.1985, 8,000 equity shares of Rs. 100 each in *S Ltd.* when *S Ltd.* had Rs. 10,00,000 share capital. It sold 500 such shares on 1.4.1986 and purchased 1000 shares on 1.4.1987.*S Ltd.* paid 15 per cent dividend each year in September and there was no change in share capital account up to 31.3.1988.

Profit and loss account balances in *S Ltd.* and investments of *H Ltd.* in *S Ltd.* on different dates were as under:

	Profit & Loss Account Balance of S Ltd.	*Investment of H Ltd. in S Ltd.*
	Rs.	*Rs.*
1st April 1985	5,00,000	12,80,000
31st March, 1986	6,20,000	12,80,000
31st March, 1987	7,00,000	11,90,000
31st March, 1988	8,00,000	14,00,000

The amounts shown as investments represent cost price as reduced by sales and increased by further purchase without making any adjustment for profit or loss on sale or for dividend. Calculate cost of control and minority interest on 31st March 1986, 1987 and 1988. (1986 goodwill 80000 M. Int. 324000) (I987 goodwill 75000 M. Int. 425000) (goodwill 115000 M. Int. 270000)

Question No. 10 Study Material Self Examination Questions Q. No. 11 Minor Ltd Page 4.87

Question No. 11

As on 30th June, 1975, the balance sheets of three companies showed the following positions:

Fig Ltd.

		Rs.		*Rs.*	
Share Capital		2,00,000	Land and Buildings		40,000
Capital Reserve		20,000	Plant & Machinery	80,000	
Revenue Reserve		60,000	Share in Run Ltd.		
Current Liabilities			at cost	1,15,000	
Creditors	40,000		Share in Trot Ltd.		
Provision for			at cost	70,000	
taxes	50,000		Stock in hand	57,000	
Proposed			Sundry debtors	83,000	
dividend	1,00,000	1,90,000	Balance at Bank	25,000	
		4,70,000		4,70,000	

Run Ltd.

	Rs.		*Rs.*	
Share Capital	80,000	Land and Buildings		1,00,000
(10 each)		Plant & Machinery	35,000	

Liabilities			Assets		
Capital Reserve		40,000			
Revenue Reserve		42,000	*Current Assets*		
			Stock in hand	65,000	
Current Liabilities			Debtors	40,000	
Creditors	40,000		Bank Balance	60,000	1,65,000
Proposed dividend	80,000			———	
Provision for tax	18,000	1,38,000			
	———	———			———
		3,00,000			3,00,000

Trot Ltd.

		Rs.			Rs.
Share Capital (10 each)		1,00,000	Land and Buildings		65,000
			Plant & Machinery	25,000	
Capital Reserve		—			
Revenue Reserve		32,000	*Current Assets*		
			Stock in hand	60,000	
Current Liabilities			Debtors	40,000	
Creditors	23,000		Bank Balance	10,000	1,10,000
Proposed dividend	10,000			———	
Provision for tax	35,000	68,000			
	———	———			———
		2,00,000			2,00,000

You are also given the following information:

1. *Fig Ltd.* acquired 5,000 shares in *Run Ltd.* in 1970, when the balance on capital reserve had been Rs. 20,000 and on revenue reserve Rs. 16,000. A further 1000 shares were purchased in 1972 when the balance capital reserve and revenue reserve had been Rs. 40,000 and Rs. 24,000 respectively.
2. *Fig Ltd.* had purchased 7,500 shares in *Trot Ltd.* in 1971 when there had been adverse balance on revenue reserve of Rs. 6,000.
3. The proposed dividends from subsidiary companies have been included in the figure for debtors in the accounts of the parent company.

You are required to prepare the consolidated balance sheet of *Fig. Ltd.* and its subsidiaries as on 30th June, 1975, together with your consolidated schedules. (Goodwill 24000 Total of con. B/S 741500)

Question No. 12

On 1.1.1980, *A Ltd.* acquired 90 per cent of the shares in *B Ltd.* and 80 percent of the shares in *C Ltd.* With a view to increase the holding in *C Ltd.* from 80 per cent to 90 per cent, *A Ltd.* sold 10 per cent of shares in *B Ltd.* at Rs. 160 per share on 30.06.1980 crediting the proceeds to investment account and fully utilized the same to acquire 10 per cent of shares in *C Ltd.* The investment account in *A Ltd.* is carried at cost except the account, representing the investment in *B Ltd.* which has been credited with the sale proceeds of 400 shares amounting to Rs. 64,000. The balance sheets are as under, as on 31.12.1980 :

	A. Ltd.	*B. Ltd.*	*C. Ltd.*
	Rs.	*Rs.*	*Rs.*
Share capital (shares of Rs. 100 each)	7,00,000	4,00,000	2,00,000
Other Liabilities	3,77,000	1,35,000	2,00,000
P&L A/c	2,33,000	1,10,000	3,50,000

	13,10,000	6,45,000	7,50,000
Fixed Assets	1,20,000	3,80,000	3,40,000
Current Assets	2,27,000	2,40,000	4,10,000
Loans	95,000	25,000	—
Investments			
B Ltd.	4,40,000	—	—
C Ltd.	4,28,000	—	—
	13,10,000	6,45,000	7,50,000

Profit & Loss Account			
Opening Balance	3,33,000	1,20,000	2,90,000
Add: Profit	40,000	30,000	80,000
	3,73,000	1,50,000	3,70,000
Dividend Paid	1,40,000	40,000	20,000
	2,33,000	1,10,000	3,50,000

Dividends were paid from previous profits in August. Prepare a Consolidated Balance Sheet.(Goodwill 15000 M. Int. 157000 Total of con. B/S 1852000)

Question No. 13

The following summarized balance sheet as on December 31, 1977 as given :
A Ltd. *B Ltd.*

	Rs.	*Rs.*
Share capital (fully paid shares of		
Rs. 100 each)	20,00,000	5,00,000
Reserve & Surplus	6,00,000	2,40,000
Loans from *B Ltd.* (including Int.)	2,25,000	—
Bank Overdraft	—	1,50,000
Sundry Creditors	2,40,000	2,10,000
	30,65,000	11,00,000
Fixed Assets	16,00,000	5,00,000
Investment:		
(i) In *B Ltd.*	4,72,500	
(ii) Other	5,70,000	
Loan to *A Ltd.*		2,00,000
Cash at Bank	1,20,000	16,000
Other current Assets		
(including interest receivable)	3,02,500	3,84,000
	30,65,000	11,00,000

The following other information are available :

1. The reserve of the companies as on January 1, 1977 were : *A Ltd.* Rs. 4,30,000; *B Ltd.* 2,50,000.
2. *B Ltd.* has advanced the loan to *A Ltd.* on January 1, 1977.
3. On July 1, 1977, *B Ltd.* issued fully paid bonus shares at the rate of one share for every four held. On the same date, a dividend of 10 per cent was paid for 1976.

4. *A Ltd.* has purchased 3,500 shares in *B Ltd.* on April 1, 1977 but had disposed of 375 shares on October 31, 1977 at Rs. 140 the sale proceeds of being credited to the concerned investment account which so far has only this entry in addition to that made on the acquisition of the shares.

Prepare consolidated balance sheet. (Total of Cons.B/s 3467500 Capital Reserve 66000 M. Int. 148000)

Chain Holding

Let *A Ltd.* be holding company of *B Ltd.* and *B Ltd.* be holding company of *C Ltd.*, we refer *C Ltd.* as bottom company and *B Ltd.* as middle company. In this case, first we should make analysis of profit of *C Ltd.* and then that of *B Ltd. B Ltd's* share in revenue profit of *C Ltd.* should be added to the revenue profit of *B Ltd.* (Between *B Ltd.* and *C Ltd.*, *B Ltd.* is holding comapny and *C Ltd.* is subsidiary company We studied in Rule (vii) regarding preparing consolidated balance sheet that holding company's share in revenue profit, i.e., post-acquisition profit of subsidiary company should be added to the concerned account of holding company). What about *B Ltd'*s share in capital profit of *C Ltd.*? In this connection there are two opinions. One opinion is that as we transfer revenue profit from *C Ltd.* to *B Ltd.*, on the same basis we should transfer capital profit from *C Ltd.* to *B Ltd.* The other opinion is that we should not transfer capital profit from *C Ltd.* to *B Ltd.* (And this capital profit, i.e., *B Ltd.*'s share in capital profit of *C Ltd.,* should be directly transferred to cost of control). The logic is that between *B Ltd.* and *C Ltd. B Ltd.* is holding company and in case of holding company, we take only its share in post-acquisition profit of its subsidiary.

Question No. 14

From the following data, you are required to prepare the consolidated balance sheet of a group of companies :

Balance Sheet As on 31st December, 1982

	A Ltd Rs.	B Ltd Rs.	C Ltd Rs.		A Ltd Rs.	B Ltd Rs.	C Ltd Rs.
Share capital	250000	200000	120000	FA	56000	110000	75000
Reserves	36000	20000	14400	Shares in B Ltd.	170000	-	-
P & L	32000	4000	10200	Shares in C Ltd.	36000	106000	-
C Ltd	6600	-	-	Stock	24000	-	-
Crs.	14000	10000	-	B Ltd.	16000	-	-
A Ltd	-	14000	-	Drs.	36600	32000	63000
				A Ltd.	-	-	6600
Total	338000	248000	144600	Total	338000	248000	144600

Other particulars are as under :

(i) *A Ltd.* held 1,500 shares of *B Ltd.* and 300 shares of *C Ltd.*

(ii) The share capital of all companies is divided into shares of Rs. 100 each.

(iii) *B Ltd.* held 800 shares of *C Ltd.*

(iv) All investments were made on 30th June, 1982.

(v) There were the following balances on 1st January, 1982 :

	B Ltd.	*C Ltd.*
	Rs.	*Rs.*
Reserves	18,000	12,000
Profit and Loss A/c	2,000	1,680

(vi) Dividends have not been declared by any company during the year nor are any proposed.

(vii) *B Ltd.* sold goods coating Rs. 8,000 to *A Ltd.* at the price of Rs. 8,800 these goods were still unsold on 31.12.1982.

(viii) *A Ltd.* remitted Rs. 2,000 to *B Ltd.* on 30th December, 1982 but the same was not received by *B Ltd.* by 31st December, 1982.
(Goodwill 17955 M. Interest 68960 Total of Conso. B/s 415755)

Chain-Holdings and Different Dates of Acquisitions : Steps

(i) Make analysis of profit of bottom company;

(ii) Note the following dates:

(a) Date(s) on which top company acquired shares in middle company;

(b) Date of Consolidated Balance Sheet.

(iii) Find profit (reserve & surplus) of middle company on the above-mentioned dates. By profit of middle company we mean its own profit and its share in post-acquisition profit of its subsidiary company (i.e., bottom company);

(iv) Make analysis of profit of middle company;

(v) Minority Interest;

(vi) Cost of control

(vii) Consolidated Balance Sheet.

Question No. 15

The following are the balance sheets of *A Ltd., B Ltd.* and *C Ltd.* as at 31st December, 1972 : (Prepare consolidated Balance Sheets).

	A Ltd.	*B Ltd.*	*C. Ltd.*
	Rs.	*Rs.*	*Rs.*
Share capital			
(Rs. 100 each)	10,00,000	5,00,000	2,00,000
General Reserve	2,00,000	36,000	—
Profit & Loss Account	1,70,000	1,19,000	—
Liabilities	1,60,000	3,75,000	1,40,000
	15,30,000	10,30,000	3,40,000
4,000 Shares in *B Ltd*	6,00,000—	—	
500 Shares in *C Ltd*	25,000	—	—
1,500 Shares in *C Ltd.*	—	90,000	—
Profit & Loss Account	—	—	80,000
Other Assets	9,05,000	9,40,000	2,60,000
	15,30,000	10,30,000	3,40,000

The following information are available :

1. *A Ltd.* acquired its investment in *B Ltd.* on 1st January, 1972 on which date the amounts standing to the credit of general reserve and profit and loss account in *B Ltd.* was Rs. 35,000 and 65,000 respectively.

2. *A Ltd.* acquired its investment in *C Ltd.* on 1st January 1972 when the debit balance in the profit and loss account in *C Ltd.*'s book was Rs. 60,000.
3. *B Ltd.* acquired its investment in *C Ltd.* on 1st January 1970 when the debit balance in the profit and loss account in *C Ltd.*'s book was Rs. 20,000. (M. Int. 122000 goodwill 89000 total of con. B/S 2194000)

Question No. 16

The balance sheet of three companies showed the following position as on June 30, 1980 :

	A Ltd.	*B Ltd.*	*C Ltd.*
	Rs.	*Rs.*	*Rs.*
Fixed assets	240000	84000	111000
Shares in *B Ltd.*	1,25,000		
Shares in *C Ltd.*		1,60,000	
Current Assets :			
Stock-in-trade	42,400	50,300	61,200
Debtors	82,390	46,610	44,300
Bank Balance	1,30,400	22,350	77,750
	6,20,190	3,63,260	2,94,250
Share Capital :			
Authorised & Issued E. shares of Rs. 10 each	2,50,000	1,00,000	1,50,000

Reserve and Surplus :			
Capital Reserve	40,000	—	30,000
Revenue Reserve	77,496	61,420	32,425
Current Liabilities and Provisions :			
Creditors	80,194	90,940	16,340
Income-tax	72,500	60,900	35,485
Prop. Dividends	1,00,000	50,000	30,000
	6,20,190	3,63,260	2,94,250

You also obtain the following information (prepare consolidated balance sheet) :

1. *B Ltd.* acquired 12,000 shares in *C Ltd.* in 1976-77 when the balance on capital reserve had been Rs. 20,000 and on revenue reserve Rs. 22,000.
2. *A Ltd.* purchased 7,500 shares in *B Ltd.* in 1977-78 when the balance on the consolidated revenue reserve had been Rs. 25,000. The balance on capital reserve in *C Ltd.* at the time was Rs. 30,000.
3. *A Ltd.* purchased a further 1,500 shares in *B Ltd.* in 1978-79 when the balance on the consolidated revenue reserve had been Rs. 40,000.
4. Proposed dividends from subsidiary companies have been included in the figure for debtors in the accounts of parent companies.(Goodwill 9450 M. Int. 60261 Total con B/s 933150)

Question No. 17

The following are the balance sheet of *A Ltd.*, *B Ltd.*, & *C Ltd.* as on 31.12.1984.

	A Ltd.	*B Ltd.*	*C Ltd.*
Share Capital (Rs. 100)	5,00,000	2,50,000	1,00,000
Capital Reserve	50,000	15,000	10,000
Revenue Reserve	1,00,000	75,000	60,000
Other Liabilities	3,50,000	1,60,000	80,000
	———	———	———
Fixed Assets	3,20,000	1,60,000	30,000
Shares in *B Ltd.*	4,50,000	—	—
Shares in *C Ltd.*	50,000	1,00,000	—
Current Assets	1,80,000	2,40,000	2,20,000

Prepare consolidated balance sheet using following further information:

(i) *B Ltd.* acquired 600 shares in *C Ltd.* on 1.1.1983 when *C Ltd.*'s capital reserve was Rs. 8000 and revenue reserve Rs. 15,000.

(ii) *A Ltd.* acquired 2,000 shares in *B Ltd.* on 1.1.1984 when the consolidated revenue reserve was Rs. 55,000. The balance on capital reserve in *B Ltd.* was Rs. 15,000.

(iii) *A Ltd.* acquired 300 shares in *C Ltd.* on 1.1.1984 when *C Ltd.*'s capital reserve was Rs. 9,000 and revenue reserve Rs. 35,000. (M. Int. 90640 Goodwill 226520 Total of Con. B/s 1376520)

Question No. 18 Study Material Self Examination Questions Q. No. 17 Red Ltd Page 4.90

CONSOLIDATED PROFIT AND LOSS ACCOUNT

Consolidated Profit and Loss Account should be prepared in columnar form. Draw on each side one column for each company, one column for adjustments and one for total. The account may be divided into three parts. In the first part, we determine profits. Second part is concerned with appropriation of profits. Dividends received/receivable by holding company from subsidiary company are also credited to this part. In third part, we make rectification and three consolidation adjustments. In first two parts, inter-company transactions are eliminated.

The rectification in the third part of this account relates to dividend received by holding company out of pre-acquisition profits of subsidiary company, i.e., if holding company's column of this P&L A/c has been credited with pre-acquisition dividend (i.e., dividend out of pre-acquisition profit of subsidiary company) of subsidiary company such dividend should be transferred to 'Investment in shares of Subsidiary A/c's by debiting the amount in holding company column of Consolidated P&L A/c. The three adjustments are:
(i) Minority's share in profits of subsidiary company as appearing in this P&L A/c; (ii) holding company's share in capital profit of subsidiary company, as appearing in this P&L A/c; (iii) Stock reserve.

Interim Dividend of Subsidiary Company

(i) If interim dividend relates to any particular period, charge it against profit of that period.

(ii) If it does not relate to particular period:

 (a) Paid in pre-acquisition period-charge against profits of pre-acquisition period. (Example: Q. No. 8). The reason is that because of this dividend, the book value of shares on the date of acquisition got reduced. To find this reduced book value, we reduce capital profit which can be done by charging this interim dividend against pre-acquisition profit.

(b) Paid in post-acquisition period — we should pro-rata this dividend against profits of current year on the basis of pre-acquisition and post-acquisition profits of current year.

Question No. 19

H Ltd. holds 3000 equity shares of Rs. 100 each in *S Ltd.* whose capital consist of 4,000 equity shares of Rs. 100 each and 6 per cent 1,000 cumulative preference shares of Rs. 100 each. *S Ltd.* has also issued 6 per cent debenture to the extent of Rs. 2,00,000 out of which *H Ltd.* hold Rs. 1,00,000. The following are the profit & loss account of the two companies for the year ending 31st December, 1976.

	H Ltd.	*S Ltd.*		*H Ltd.*	*S Ltd.*
To Adjusted Purchases	15,00,000	6,00,000	By Sales	19,00,000	15,00,000
To Manu. Expenses	—	4,00,000			
To G,P.	4,00,000	5,00,000			
	19,00,000	15,00,000			

To sundry Expenses	1,50,000	2,00,000	By Gross Profit	4,00,000	5,00,000
To Debenture Interest	—	12,000	By Deb Interest	6,000	-----
To Profit C/d	2,98,000	2,88,000	By Interim Dividend	42000	------
	4,48,000	5,00,000		4,48,000	5,00,000
To Income Tax	1,40,000	1,20,000	By Profit B/D	2,98,000	2,88,000
To Preference Dividends		6,000			
To dividend (interim)		56,000			
To Proposed dividend	1,00,000	84,000			
To Bal. c/d	58,000	22,000			
	2,98,000	2,88,000		2,98,000	2,88,000

From the following information prepare consolidated P & L account.

1. The shares were acquired by *H Ltd.* on 1st April, 1976 but the debentures were acquired on 1st January 1976. *S Ltd.* was incorporated on 1st January, 1976.
2. During the year, *S Ltd.* sold to *H Ltd.* goods costing Rs. 1,00,000 at the selling price of Rs. 1,50,000 one-fourth of the goods remained unsold on 31st December, 1976. The goods were valued at cost to the holding company for closing stock purposes.

Question No. 20

On 1st February, 79, *A Ltd.* purchased 2,70,000 equity shares and 9,000 preference shares in *B Ltd.* Both the companies makes up their accounts on 30th June each year. The following figures are extracted from the companies' records for the year ended on 30th June, 79 :

	A Ltd.	*B Ltd.*
	Rs.	*Rs.*
Sales	1,62,00,000	1,53,00,000
Purchase	89,63,820	86,86,440
Selling Expenses	8,10,000	12,15,000
Overhead Expenses	20,70,000	9,45,000
Interim dividend paid on 1.1.79		
On Equity Shares	13,50,000	7,20,000
On Preference Shares	—	81,000
Stock on 30th June, 78	8,93,700	18,05,040
Issued and Paid-up share capital :		
Equity shares of Rs. 10 each	54,00,000	36,00,000
9% Pref. Shares of Rs.100 each	—	18,00,000
P& L A/c: Bal. on 30.6.78	4,81,500	5,76,000

Following additional information are relevant:

1. Stock on hand as on 30th June, 79 were : *A* 15,77,520 *B* 16,71,480 2. Provision for taxation for year is to be made as follows : *A* 27,00,000 *B* 19,44,000
3. *A Ltd.* proposes to pay final dividend on equity shares at 25 %.
4. *B Ltd.* proposes to pay half year's dividend on preference shares and a final dividend on equity shares at 20 per cent.

5. *B Ltd.* sold to *A Ltd.* in March 79 material for Rs. 7,50,000 at cost plus 25 per cent of which *A Ltd.* still had unsold stock of Rs. 5,00,000 (at cost to *A Ltd.*) as on 30th June, 79.

Prepare consolidated profit and loss account of *A Ltd.* and its subsidiary *B Ltd.* for the year ended on 30th June, 79.

Question No. 21

The trial balances of *X Ltd.* and *Y Ltd.* as at 31st December, 1968 are given below:

	X Ltd. Dr. Rs.	X Ltd. Cr. Rs.	Y Ltd. Dr. Rs.	Y Ltd. Cr. Rs.
Equity Share capital	---	10,00,000	---	1,00,000
6% Pref. share capital				1,00.000
Reserves 1.1.68		2,00,000	----	80,000
P. & L. A/c		37,000		20,000

6% Debentures of Y	50,000			1,00,000
Drs.	2,05,940		62,208	
Crs.		1,48,000		92,860
Purchases	4,00,000		3,00,000	
Sales		8,00,000		7,00,000
Opening stock	1.00.000		50,000	
Deb. Int.		3,000	6,000	
Salaries	35,000		20,000	
Gen. exp.	57,000		40,475	
Pref. div.(up to 30.6.68)		1,200	3,000	
Income tax deducted at Source	1,260			2,700
Bank	10,000		8,000	
Equity shares in Y Ltd	2,50,000			
Pref. shares in Y Ltd	40,000			
Fixed assets (Less Dep. @ 10% p.a.)	8,73,000		5,90,040	
Dep. On FA	97,000		65,560	
Wages	70,000		50,000	
Total	2189200	2189200	1195560	1195560

Additional information :

(i) Closing Stock : *X Ltd.* — Rs. 2,00,000; *Y Ltd.* — Rs. 15,000.

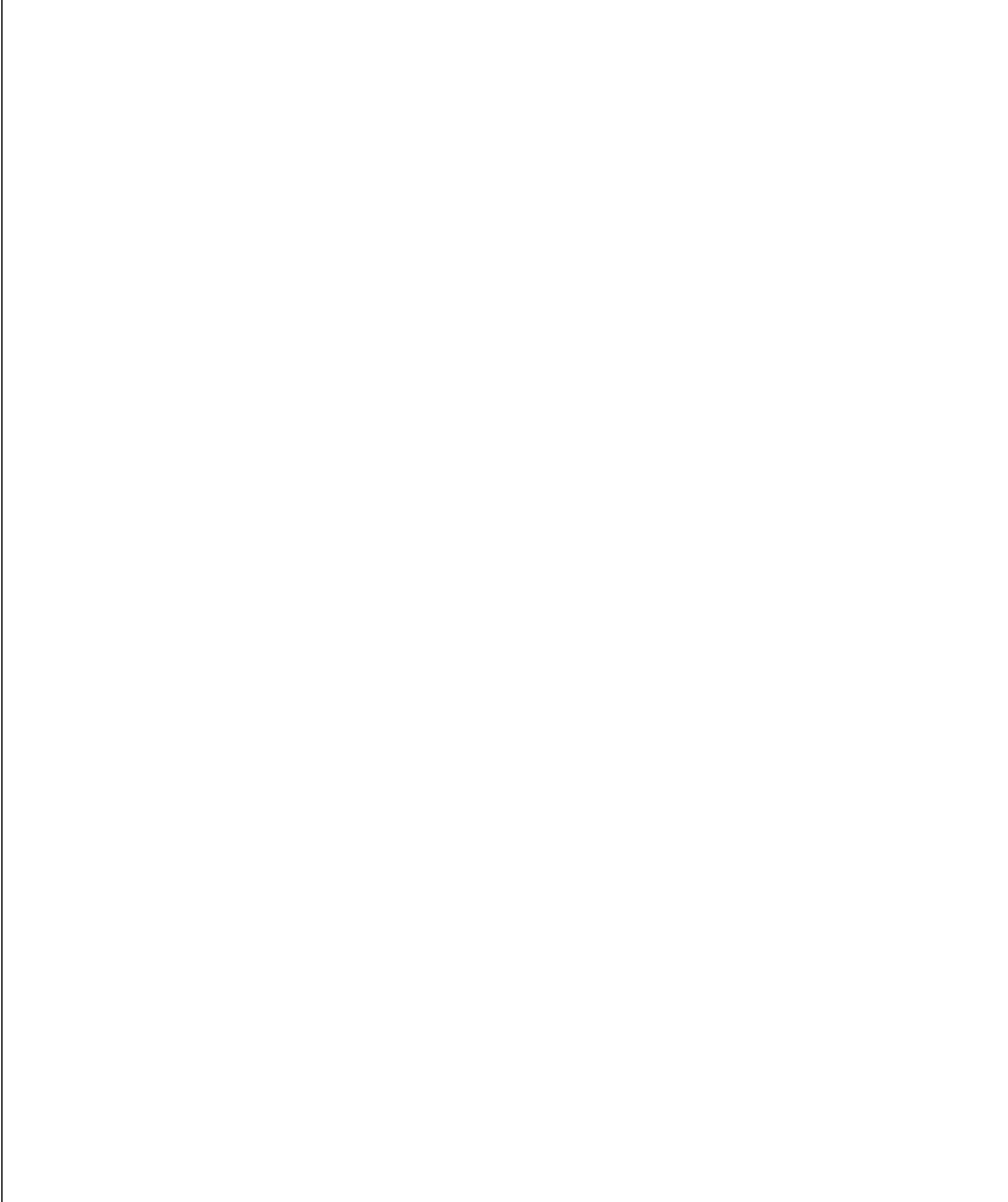
(ii) Shares in *Y Ltd.* were acquired on 1.4.1968 and consisted of 75 per cent of equity capital and 40 per cent or preference capital. Half of the debentures of *Y Ltd.* were acquired by *X Ltd.* on 1.1.1968.

(iii) After acquisition of control *X Ltd.* bought good from *Y Ltd.* at selling price (which is cost plus 25%) valued at Rs. 40,000. One-fourth of these goods was still in the closing stock of *X Ltd.* These goods were valued at cost to *X Ltd.* for valuation of its closing stock.

(iv) Included in the fixed assets of *Y Ltd.* is machinery which stood in the books on 1.1.1968 at Rs. 1,00,000 and on which depreciation had been written off at 10 per cent p.a. It was revalued at Rs. 1,20,000 on the date of acquisition of control, i.e., 1.4.1968. This appreciation in the value of machinery remains unrecorded as yet.

(v) Proposed dividend on equity shares : *X Ltd.* —10 %; *Y Ltd.* — 15%.

Prepare a consolidated profit and loss account of *X Ltd.* and *Y Ltd.* for the year ended 31.12.1968 and a consolidated balance sheet as on that date.



Hint : Cons. B/S

S. capital	10,00,000	Goodwill	49,396
Reserve	2,00,000	FA	14,83,852
P & L a/c	2,78,921	Drs.	2,68,148
Deb.	50,000	Stock less stock reserve	2,13,000
Crs.	2,40,860	Bank	18,000
TDS	2,700	TDS	1,260
Prop. Div. (X)	1,00,000		
Minority interest	1,61,175		
	20,33,656		20,33,656

Question No. 22

The following information was extracted from the books of *A Ltd.* Group as on 3112.80 :

	A Ltd. *Rs.*	*B Ltd.* *Rs.*	*C Ltd.* *Rs.*
Profit and Loss Account —			
Balance on December 31,			
1978 after provision of dividends of 10% in respect of calendar year 1978 but excluding dividend received	50,000	36,000	26,000
Net trading Profit earned in 1979	60,000	42,000	28,000
	1,10,000	78,000	54,000
Less: Dividends of 10% in 1980 in respect of calendar year 1979	40,000	30,000	20,000

	70,000	48,000	34,000
Net trading profit earned in 1980 (before taking into account proposed dividends of 10% in respect of calendar year 1980)	50,000	50,000	30,000
	1,20,000	98,000	64,000
Dividend Received :			
From *B Ltd.* in 1979	20,000		
From *B Ltd.* in 1980	25,000		
From *C Ltd.*		15,000	
Share Capital — Authorised and Full paid, Equity Shares of Re. 1 each	4,00,000	3,00,000	2,00,000
Current Liabilities	20,000	5,000	17,000
	5,85,000	4,18,000	2,81,000

Fixed Assets at cost less Depreciation	2,10,000	1,88,000	2,61,000
Current Assets	60,000	30,000	20,000
Investment at cost — 2,00,000 Equity Shares in *B Ltd.* brought on December 31, 1978	2,50,000		
50,000 Equity shares in *B Ltd.* Bought on December 31, 1979	65,000		
1,50,000 Equity Shares in *C Ltd.* Bought on December 31, 1979		2,00,000	
	5,85,000	4,18,000	2,81,000

All the companies pay dividends of 10 per cent on paid up share capital in March following the end of the accounting year. The receiving companies enter the dividends in their books when the dividends are received. Prepare

consolidated P&L account for year ended 31.12.1980 and consolidated balance sheet as on 31.12.1980.

Note to Question No. 22

A Ltd. acquired 2,00,000 shares of *B* on 31.12.1978. In 1979, *A Ltd.* received Rs. 20,000 as 1978 dividend on these shares. It is appearing as a separate item in balance sheet. We cannot take this item in 1980's P&L account because it is neither 1980's income nor 1980's receipt. It is pre-acquisition dividend. We transfer it to investment account, i.e., cost of control.

A Ltd. acquired additional 50,000 shares of *B* on 31.12.1979. In 1980, *A Ltd.* received Rs. 25,000 as 1979 dividend (Rs. 20,000 for 2,00,000 shares acquired on 31.12.1978 and Rs. 5,000 for 50,000 shares acquired on 31.12.1979). The dividend in respect of 50,000 shares, acquired on 31.12.1979, is pre-acquisition. We transfer it to investment account.

B Ltd. acquired 1,50,000 shares of *C Ltd.* on 31.12.1979. In 1980, *B Ltd.* received Rs. 15,000 as 1979 dividend on these shares. It is pre-acquisition dividend. Hence transfer it to investment account.

Hint :Con. B/s

s. capital	4,00,000	Goodwill	17,500
P & L	2,08,417	FA	6,59,000
CL	42,000	CA	1,10,000
M. Int.	1,36,083		
	7,86,500		7,86,500

Inter-company Holdings

(i) Find capital profit and revenue profit on the basis of simultaneous equation.

(ii) In consolidated balance sheet, we take only that part of share capital of holding company, which is being held by shareholders other than subsidiary company.

(iii) In consolidated balance sheet, we do not take 'Investment in shares of holding company as appearing in subsidiary consolidated balance sheet'.

(iv) Cost of control to be adjusted by difference between "Amount of Investment in shares of holding company as appearing in subsidiary balance sheet and paid value of such shares".

(v) Profits to be reduced by subsidiary company's share in profits of holding company.

Question No. 23

Following are the summarized balance sheets of two companies *H Ltd.* and *S Ltd.* as at 31st December, 1976 :

	H Ltd.	*S Ltd.*		*H Ltd.*	*S Ltd.*
Share Capital			Fixed Assets	18,10,000	13,00,000
(Rs.10 each)	25,00,000	12,50,000	1,00,000 shares in *S Ltd.*	11,00,000	
Reserves	7,50,000	5,00,000	25,000 shares in *H Ltd.*		2,75,000
Creditors	2,25,000	2,00,000	C. Assets	5,65,000	3,75,000
	34,75,000	19,50,000		34,75,000	19,50,000

H Ltd. purchased shares in *S Ltd.* on 1.1.1976 when reserves in *S Ltd.* stood at Rs. 3,00,000 and in *H Ltd.* at Rs. 4,50,000. *S Ltd.* purchased shares in *H Ltd.* on 1.1.1975. Prepare the consolidated balance sheet.

Statement Under Section 212

Under Section 212 of the Companies Act, a statement should be attached to the balance sheet of holding company giving following details in respect of each subsidiary company —

(A) Interest and Profit of holding company in subsidiary company:

(i) The extent of holding company's interest in the subsidiary company as at the end of financial year of subsidiary company;

(ii) The amounts of subsidiary company's profit (less loss) which is attributable to holding company and which has not been dealt with in the accounts of holding company: (a) For the financial year of subsidiary company ending with or within financial year of holding company, (b) For the previous financial year of subsidiary company since it became subsidiary company;

(iii) Information similar to (ii) as to the profits and losses of subsidiary company which have been dealt with in the accounts of holding company.

(B) Where holding company and subsidiary company have different financial years, the following information have to be given in the statement:

(i) The changes, if any, in the holding company's shareholdings in subsidiary company, during the time-gap (from end of financial year of subsidiary company to the date of balance sheet of holding company to which the statement is attached).

(ii) Details of any material changes which have occurred during time gap in respect of subsidiary's fixed assets, investments, lendings and borrowings (other than for the purpose of meeting current liabilities).

Question No. 24

From the following particulars, prepare a statement to be attached to the balance sheet of *X Ltd.* as on 31.3.1988.

(1) *X Ltd.* purchased 2,800 shares of *Y Ltd.* on 1.1.1986 for Rs. 3,50,000. Issued capital of *Y Ltd.* has been 4,000 shares of Rs. 100 each.

(2) On 1.1.1986 *Y Ltd.* had general reserve of Rs. 3,00,000 and P&L A/c *Cr.* Balance of Rs. 1,00,000. *Y*'s accounting year is calendar year.

(3) *Y Ltd.* made profit (post tax) of Rs. 1,00,000 in 1986 and of Rs. 1,10,000 in 1987. (4) *Y Ltd.* declared and paid dividend of 20 per cent for each of these two years. (5) During the period from 1.1.1988 to 31.3.1988, following important transactions have taken place :

(i) *X Ltd.* purchased further 200 shares of *Y Ltd.* on 1.3.1988 for Rs. 30,000.

(ii) *Y Ltd.* issued 13.5 per cent redeemable debentures of Rs. 2,00,000 to finance the purchase of a machine. This machine was purchased and installed in March 1988 at a cost of Rs. 2,10,000.

(iii) *Y Ltd.* purchased shares of *Z Ltd.* for Rs. 10,000.

(iv) *Y Ltd.* advanced a loan of Rs. 10,000 at 18 per cent to *A Ltd. A Ltd.* supplies material to *Y Ltd.*

Answer to question No. 24

X Ltd.

Balance Sheet Dated 31st March, 1988

Statement pursuant to Section 212 of the Companies Act, 1956 relating to subsidiary company *Y Ltd.* (*Y Ltd.*'s financial year ended on 31.12.1987).

1. *X Ltd.*'s interest in *Y Ltd.* as on 31.12.1987 : *X Ltd.* held 2,800 equity shares of *Y Ltd.* (out of 4,000 shares)

2. Amount of *Y Ltd.*'s profit which is attributable to *X Ltd.* and which has not been dealt with in the books of *X Ltd.* for

   (i) Year ended 31.12.1987: Rs. 21,000

   (ii) Other years since acquisition : Rs. 14,000

3. Amount of *Y Ltd.*'s profit which is attributable to *X Ltd.* and which has been dealt with in the books of *X Ltd.* for

   (i) Year ended 31.12.1987: Rs. 56,000

(ii) Other years since acquisition	:	Rs. 56,000
4. Change in *X Ltd.*'s interest in *Y Ltd.* during 1.1.1988-31.3.1988	:	Acquired 200 shares of *Y Ltd.*
5. Material changes during 1.1.1988-31.3.1988 in respect of following items of *Y Ltd.*		
(i) Fixed Assets	:	Machine purchased and installed at a cost of Rs. 2,10,000.
(ii) Investments	:	Shares of *Z Ltd.* Rs. 10,000
(iii) Lendings	:	Advanced 18 per cent Loan of Rs. 10,000 to *A Ltd.*
(iv) Borrowings	:	Issued 13.5 per cent Redeemable Debenture of Rs. 2,00,000.

CONSOLIDATED FINANCIAL STATEMENTS AS-21

The AS prescribes the guidelines for presentation of consolidated financial statements for a group of enterprises under the control of a parent. The standard also applies to the accounting of investments in the subsidiaries in the separate books of a parent. The statement neither requires nor encourages the preparation of the consolidated financial statements, it prescribes that in case a parent presents the consolidated financial statements of its group, it should follow the prescriptions of this accounting standard. The consolidated financial statements should include consolidated B/S, Consolidated P & L a/c, notes to the consolidated financial statements and consolidated Cashflow statement (if the parent presents cash flow statement as a part of its separate financial

statements). The AS clarifies that the consolidated financial statements are not in lieu of separate financial statement of the parent.

Control means the power to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. Control is obtained by one or both of the following two ways

(i) the parent (generally referred as holding company) owns more than 50% of voting right shares of the enterprise either directly or indirectly
(ii) the parent has the right of appointing the majority of directors/governors of the enterprise

ASI – 24 : In a rare situation, when an enterprise is controlled by two enterprises, both the enterprises should consolidate the financial statements of that enterprise as per requirements of AS-21.

The consolidated accounts should include all of the parent's subsidiaries, both domestic and foreign. A subsidiary should be excluded from the consolidation when :

- control is acquired and held with an intention of disposal in near future (the term near future refers to the period not exceeding 12 months).

  ASI – 21 : Where an enterprise owns majority of voting power by virtue of ownership o the shares of another enterprises and all the shares held as stock in trade are acquired and held exclusively with a view to their subsequent disposal in the near future, the control should be considered as temporary.

- The subsidiary operates under severe restrictions regarding transfer of funds to the parent

In this case, the investment in the subsidiary should be accounted for in the consolidated financial statements in accordance with AS-13.

We shall be discussing the accounting procedure in detail in the class. A few points, which need special mention, are as follows:

- **Cost of control** i.e. goodwill / capital reserve (Refer to paragraph 13 of the AS)

" any excess of the cost to the parent of its investments in a subsidiary over the parent's portion of equity of the subsidiary , at the date on which investment in the subsidiary is made, should be described as goodwill to be recognized as an asset in the CFSs"
" when the cost to the parent of its in subsidiary is less than the parent's portion of equity of subsidiary, at the date on which investment in subsidiary is made, the difference should be treated as a capital reserve in the CFSs"

- **Two or more investments** (Refer to paragraph 15 of the AS)

"If an enterprise makes two or more investments in another enterprise at different dates and eventually obtains control of the other enterprise, the consolidated financial statements are presented only from the date on which holding-subsidiary relationship comes in existence. If two or more investments are made over a period of time, the equity of the subsidiary at the date of investment, for the purposes of paragraph 13 above, is generally determined on a step-by-step basis; however, if small investments are made over a period of time and then an investment is made that results in control, the date of the latest investment, as a practicable measure, may be considered as the date of investment."

Question No. 25: Study material Self Examinations Questions Q. No. 23 A Ltd. page 4.96

Answer:(Assumption : the preference shares are cumulative pref. shares)

Minority interest :

Paid up capital (equity) 55,000 (including bonus)

Paid up capital (pref.) 25,000

Capital profit -1,000

Revenue profit (GR) 7,500

------do--- (Pref.) 2,500

_______do---(equity) 91,000 x 0.25 1,11,750

Cost of control : Cost of shares 96000 + 80000 +36000 = 2,12,000

Paid up capital (equity, including bonus) -1,65,000

Paid up capital (pref.) -15,000

Pre-acquisition dividend (dividend for 1999) -7,000

Share in capital profit -(-3000)

Goodwill 28.000

Consolidated B/S of A Ltd. and its subsidiary B Ltd. 31.12.1999

Liabilities	Amount	Assets	Amount
ESC	4,00,000	Goodwill 50000+30000+28000	1,08,000
PSC	80,000	Machinery**	1,21,000
GR 80,000 + 22,500	1,02,500	Vehicles	2,35,000
P & L a/c	1,91,950*	Furniture	1,00,000
BO	50,000	Investment***	83,000
Creditors	1,04,000	Stock 1,00,000 -800	99,200

B/P	2,000	Cash	1,46,000
M. Interest	1,11,750	Drs.	1,50,000
Total	10,42,200	Total	10,42,200

* P & L a/c 1,30,000 Post
acquisition profit (E) +68250 Post
acquisition profit (P) + 1500
Pre-acquisition dividend -7000
Stock reserve -800 1,91,950

Machinery ** 80000 +50000 -10000 + 1000 = 121000

Investment*** 250000 + 45000 - 96000-80000-36000 = 83000

Q. No. 26 : Study Material Illustration 20 Eagle , Garuda and Bird page 4.58

- **Unrealized profit or losses** (Refer to paragraph 16 of AS)

"Intra-group balances and intra-group transactions and resulting un-realised profits should be eliminated in full. Un-realised losses resulting from intra-group transactions should also be eliminated unless cost cannot be recovered." (This is not required , though encouraged, for transactions entered into during accounting periods commencing on or before 31.12.2001.)

- **Uniform policies** (refer to paragraph 20 of the AS)

"Consolidated financial statements should be prepared using uniform accounting policies for like transactions and other events in similar circumstances. If it is not practicable to use uniform accounting policies in preparing the consolidated financial statements, that fact should be disclosed together with the proportions of the items in the consolidated financial statements to which the different accounting policies have been applied."

- **Minority interest** refer to paragraph 25 of the AS)

" Minority interests should be presented in the consolidated balance sheet separately from liabilities and the equity of the parent's shareholders. Minority interests in the income of the group should also be separately presented."

- **Pref. dividend** (refer to paragraph 27 of the As-21)

"If a subsidiary has outstanding cumulative preference shares which are held outside the group, the parent computes its share of profits or losses after adjusting for the subsidiary's preference dividends, whether or not dividends have been declared."

- **Tax expense :** While preparing consolidated financial statements, the tax expense to be shown in the consolidated financial statements should be the aggregate of the amounts of tax expense (comprising current tax & deferred tax) appearing in the separate financial statements of the parent an its subsidiaries.

Disclosure :

- A list containing following details in respect of each subsidiary company should be given : **(i)** name **(ii)** country of incorporation, and **(iii)** proportion of ownership interest proportion of voting right held (if voting right and ownership are not identical)
- nature of relationship between the parent and the subsidiary if the parent does not own more than 50 % voting right shares of the subsidiary (directly or indirectly)
- name(s) of the subsidiary(ies) of which accounting years are different from that of parent company.
- The parent's share in the post acquisition reserves of a subsidiary, forming part of corresponding reserves in the consolidated balance sheet, is not required to be disclosed separately in the consolidated balance sheet.

VALUATION OF GOODWILL AND SHARES

Three categories of methods of Valuation of Goodwill:

(i) Purchase of profit method.

(ii) Methods based on super profit.

(iii) Capitalization of profit method.

PURCHASE OF PROFIT METHOD

Under this method we take profits for a few years of past, we take average of these profits and multiply the average profit with number of years purchase to

find the value of goodwill. We should take profit for such number of years as may reveal future trend of profits. We should take weighted average if profit has clear trend, otherwise we should take simple average. Profit for goodwill purpose means normal trading profit before appropriation. By number of years of purchase, we mean weight or importance we attach to this average profit.

METHODS BASED ON SUPER PROFIT

Super Profit = Future Maintainable Profit – Normal Profit.

Future Maintainable Profit

Buyer of goodwill is interested in future profits of the concern. Hence, for determining value of goodwill, we estimate future maintainable profit on the basis of following points :

(i) Take profits for a few years of past. We take profit for such number of years as reveals the future trend of the profit e.g., if the profit has clear trend we may take profit only for three years but if there is no clear trend, we may take profit for 4 to 7 years.

(ii) Eliminate the effect of non-trade terms. For example: Income from investment of surplus funds.

(iii) Eliminate the effect of abnormal items, for example, loss on account of strike, flood, etc., abnormal profit on account of war, etc.

(iv) Eliminate the effect of such items which occurred in the past but which are not likely to take place in the future.

(v) Take average of profits. If the profits have clear trend, take weighted average, otherwise take simple average.

(vi) Take effect of such transactions into consideration which did not take place in past but which would take place in future.

(vii) Consider Income-Tax.

Normal Profit

Normal Profit = Average capital Employed × Normal Rate of Return

Normal rate of return may be given in the question. Alternatively, we may have to estimate it on the basis of market price of share and dividend per share. Under this approach, we assume that market value of share depends upon dividend rate *vis-a-vis* normal rate.

Hence normal Rate

$$= \frac{\text{Dividend Per Share}}{\text{Market Price per Share}} \times 100$$

If the question neither mentions 'the normal rate' nor 'dividend per share and market price of share', we just assume the normal rate. (We may assume any rate between 10 to 20 per cent).

Capital employed, here, means owners investment in trade assets of the business.

Capital Employed = ESC + PSC + R&S – Misc. Exp.
– P&L A/c *Dr.* Balance if any
– Non-trade assets
= Trade Assets – outside liabilities.

One special point about calculation of capital employed :

When we calculate capital employed for valuation of goodwill, book value of goodwill (if given in the question) is ignored, i.e., capital employed is exclusive of Book value of Goodwill.

$$\text{Average Cap. Emp.} = \frac{\text{Open. Cap. Emp.} + \text{Closing Cap. Emp.}}{2}$$

If opening capital employed is not given in the question, we assume opening capital employed is equal to closing capital employed minus current year post tax profit. Hence average capital employed :

$$= \frac{(\text{Closing C.E.} - \text{Current Year Post Tax Profit}) + \text{Closing C.E.}}{2}$$

= Closing C.E. – Half of Current Year Post Tax profit.

Average capital employed when dividend has been paid at the end of the year: If dividend is paid at the end of the year, it reduces closing capital employed but it won't have much influence over the average capital employed

throughout the year[25]. Hence, in this situation, we calculate average capital employed that would have been there if no dividend was paid (or proposed) at the end of year. Average capital employed:

---

[25] Let's understand this point clearly with the help of an example . A Ltd.'s capital employed on 1.1.2004 was Rs. 500000. It earned a profit of Rs. 365000 during the year 2003. Assume for simplicity that it operates for 365 days in a year and earns the profit evenly. So the profit is Rs. 1000 per day. It paid a dividend of Rs. 100000 on 27th Dec. 2003. What is the average capital employed for the year 2003?

$$\text{Average CE (1.1.2003 -27.12.2003)} = \frac{500000 + 860000}{2} = 680000$$

$$\text{Average CE (28.12.2003-31.12.2003)} = \frac{760000 + 765000}{2} = 762500$$

$$= \frac{\text{Open. C.E. + Clos. C.E. + Dividend paid at year end}}{2}$$

If opening capital employed is not given, we assume that it is equal to closing capital employed plus dividend paid at year end minus current year post tax profit. Hence average capital employed —

$$= \frac{\text{(Clos. C.E. + Dividend paid at year end – Current year Post Tax Profit) + Closing C.E. + Dividend at year and}}{2}$$

= Closing C.E. + Dividend at year end – Half of Current year Post Tax Profit.

An important point from past question papers: If the P&L A/c balance appearing in balance sheet is less than current year's profit, it can be assumed that dividend has been paid. In the absence of amount of dividend, average capital employed cannot be calculated. Hence, normal profit may be calculated on closing capital employed. In other words, if payment of dividend is a fact or assumption and we do not know the amount of dividend, average capital employed cannot be calculated, In this case, we calculate normal profit on the basis of closing capital employed.

Based on super profit, goodwill can be calculated by following methods:

Purchase of Super profit Method:

Goodwill = Super profit × No. of years of purchase

For example, if super profit = Rs. 10,000 and establishment of new business requires 3 years,

Goodwill = Rs. 10,000 × 3 = Rs. 30,000.

Annuity Method: Goodwill = Super Profit × Annuity.

Ave. CE for the year : [(680000x360) + (762500x5)] / 365 = 681130

Had the dividend not been paid , Ave. CE would have been [(500000 + 865000) / (2)] = 682500

The difference between these two figures is negligible. Calculation of Ave. CE by first method is quite typical. Hence, the second method is being followed. In other words, when dividend is paid towards end of the year, we calculate the Ave. CE that would have been there if no such dividend was paid.

Advocates of annuity method put forward the plea that we pay for goodwill now and get its benefits in future. Hence, value of goodwill should not be calculated on the basis of number of years of purchase. (If it is done, the buyer of goodwill suffers loss on account of interest. For example: If a person pays Rs. 30,000 for goodwill today and gets benefit from goodwill of Rs. 10,000 annually for 3 years, i.e., he gets Rs. 10,000 after one year from today, another Rs. 10,000 after two years from today and yet another Rs. 10,000 after three years from today; he paid Rs. 30,000, he got Rs. 30,000 but he suffered loss of interest). They opine that the goodwill should be calculated on the basis of annuity for number of years of purchase so that the buyer does not suffer loss on account of interest:

$$\text{Annuity} = \frac{1}{(1+r)^1} + \frac{1}{(1+r)^2} + \frac{1}{(1+r)^3} + \ldots\ldots$$

If number years of purchase is 3, normal rate of return 10 per cent.

$$\text{Annuity} = \frac{1}{(1+.10)^1} + \frac{1}{(1+.10)^2} + \frac{1}{(1+.10)^3} = 2.487$$

Hence goodwill if super profit is Rs. 10,000 = 10,000 × 2.487 = 24,870

Hence, if the buyer of goodwill pays Rs. 24,870 now, he will get Rs. 10,000 at the end of first, second and third year. Present value of what he gets in three years is equal to 24,870. Hence, the buyer does not suffer loss on account of interest.

Capitalization of Super Profit Method

The central idea of capitalization method is that value of any asset depends upon its earnings *vis-a-vis* normal rate of return. For example, if normal rate of return is 10 per cent, then value of any asset earning Rs. 10 is Rs. 100. Super profit is earned by goodwill (goodwill is defined as super profit earning capacity of a firm). Hence, if normal rate is 10 per cent, it means, for Rs. 10 of super profit, goodwill is Rs. 100. Hence,

$$\text{Goodwill} = \frac{\text{Super Profit}}{\text{Normal Rate}} \times 100$$

(This method is not covered by the study material/suggested answers. Hence, it should be used in the examination only if specifically asked)

CAPITALISATION OF PROFIT METHOD

Under this method, we find value of business :

$$\text{Value of Business} = \frac{\text{Future Maintainable Profit}}{\text{Normal Rate}} \times 100$$

Value of Goodwill = Value of Business – Closing Capital employed.

VALUATION OF SHARES

(i) Intrinsic value method or book value or balance sheet value method.

(ii) Market value method or yield value method.

Intrinsic Value Method

Intrinsic value method assumes liquidation (without liquidation expenses) i.e., we find the amount which the holder of one equity share will get if the company goes into liquidation. It is obtained by dividing (current value of all assets including goodwill and non-trade-assets minus outside liabilities minus P.S.C.) by number of equity shares. A special point about proposed dividend, i.e., whether it is outside liability or not. The answer to this point is if we have to calculate ex-dividend value of shares, proposed dividend should be treated as outside liability. If we have to calculate cum-dividend value of the share, proposed dividend is not outside liability.

If we have to calculate the value of shares as wealth (i.e. no, purchase or sale of shares is taking place), we find cum-dividend value. If the value that we shall determine would be the basis of issuing new shares, we should find ex-dividend value as the proposed dividend appearing in balance sheet shall not be available for new shares to be issued. If purchase/sale/transfer of existing shares is to take place, we find the value from the point of view of buyer. If the buyer will get the proposed dividend, we find cum-dividend value and otherwise ex-dividend value.

If a company has shares of different face values, we find their equivalent number on the basis of any one of the face values. We find the value of shares on the basis of that face value. We find the value of shares of other face values accordingly.

If we are given that shares have different paid up values, we assume that all the shares are to be made fully paid up. We calculate the value of one fully paid up share. Value of partly paid up share = value of fully paid up share minus unpaid amount. Here we should know the Company Law provision that on the liquidation of a company (intrinsic value method assumes liquidation), company's profits/losses are shared by equity shareholders in the ratio of face value of shares (not in the ratio of paid up value of shares).

Market Value method assumes business as a going concern. Under this two approaches are there: (i) based on dividend, and (ii) based on earnings. Based on dividend, two approaches are there, one is based on actual dividend (It is also known as dividend yield approach) and the other is based on maximum possible dividend. Based on earnings also, there are two methods (i) based on EPS (ii) based on return on equity shareholders' fund (ROE).

Market value (based on actual dividend)	$\frac{\text{Actual Dividend Rate}}{\text{Normal Rate}} \times$ paid up value
Market value (Based on Max. possible div.)	$\frac{\text{Max. Possible Div. Rate}}{\text{Normal rate}} \times$ paid up value
Market value (Based on EPS)	$\frac{\text{E.P.S}}{\text{Normal Rate}}$
Market value (Based on ROE)	$\frac{\text{ROE}}{\text{Normal rate}} \times$ Paid up value

Fair Value = Average of Intrinsic value and market value.

CHOICE OF METHOD

1. Fair value method is considered as most appropriate method when the value to be determined is going to affect a fairly large number of shares. Like acquiring controlling interest, amalgamation, etc., conversion of private company to public company. For fair value, yield value may be calculated on the basis of earnings.
2. Intrinsic value method may be applied when current value of goodwill is given or is to be calculated.
3. In all other cases, yield value based on maximum possible dividend may be applied.
4. Sometimes, the choice of method depends upon data/information given in question.

Question No. 1

From the following information supplied to you, ascertain the value of goodwill of *A Ltd.*, which is carrying on business as retail under super profit method:

Balance Sheet as on 31st March, 1982

	Rs.		Rs.
Paid up capital (5000 shares of Rs.100 each fully paid up)	5,00,000	Goodwill at cost	50,000
Bank overdraft	1,16,700	Land and Building	2.20.000
Sundry creditors	1,81,000	Plant and machinery	2.00.000

Provision for taxation	39,000	Stock	3,00,000
P. & L a/c	1,13,300	Debtors	1.80,000
Total	9,50,000		9,50,000

The company commenced operations in 1965 with a paid up capital of Rs. 5,00,000. Profits for recent years (after taxation) have been as follows:

Year ended 31st March	*Rs.*
1978	40,000 (Loss)
1979	88,000
1980	1,03,000
1981	1,16,000
1982	1,30,000

The loss in 1978 occurred due to a prolonged strike.

The income-tax paid so far has been at the average rate of 40 per cent but is likely to be 50 per cent from onwards. Dividends were distributed at the rate of 10 per cent on the paid up capital in 1979 and 1980 and at the rate of 15 per cent in 1981 and 1982. The market prices of shares is ruling at Rs. 125 at the end of the year ended 31st March, 1982. Profits till 1982 have been ascertained after debiting Rs. 40,000 as remuneration to the managing director. The government has approved remuneration of Rs. 60,000 with effect from 1st April, 1982. The company has been able to secure a contract for supply of materials at advantageous price. The advantage has been valued at Rs. 40,000 per annum .

Question No. 2

Negotiation is going on for transfer of *X Ltd.* on the basis of the balance sheet and the additional information as given below:

Balance Sheet of X Ltd. as on 31st March, 1988

	Rs.		Rs.
Share capital (Rs.10 fully paid up)	10.00,000	Goodwill	1,00,000
Reserve and surplus	4,00,000	Land and building	3,00,000
Creditors	3,00,000	Plant and machinery	8,00,000

		Investments	1,00,000
		Stock	2,00,000
		Debtors	1,50,000
		Cash and bank	50,000
	17,00,000		**17,00,000**

Profit before tax for 1987-88 amounted to Rs. 6,00,000 including Rs. 10,000 as interest on investment. However, and additional amount of Rs. 50,000 p.a. shall be required to be spent for smooth running of the business.

Market values of land & buildings and plant & machinery are estimated at Rs. 9,00,000 and Rs. 10,00,000 respectively. In order to match the above figures further depreciation to the extent of Rs. 40,000 should be taken into consideration. Income-tax rate may be taken at 50 per cent. Return on capital at the rate of 20 per cent before tax may be considered normal for this business at the present stage.

It has been agreed that 4 years' purchase of super profit shall be taken as value of goodwill for the purpose of the deal. Value the goodwill.

[Adapted November 1988]

Question No. 3

Below is given the balance sheet of Prosperous Ltd. as 31st March, 1977.

	Rs.		*Rs.*
Share Capital		Land and Building	2,70,000
Authorised & Issued		Plant and Machinery	1,00,000
6,000 shares of Rs. 100		Stock	3,60,000
each fully paid up	6,00,000	Sundry Debtors	1,60,000
Profit & Loss A/c	40,000		
Bank Overdraft	10,000		
Creditors	80,000		
Provision for Taxation	1,00,000		
Proposed Dividend	60,000		
	8,90,000		8,90,000

The net profits of the company, after deducting usual working expenses but before providing for taxation, were as under :

Year	*Rs.*
1972-73	1,70,000
1973-74	2,10,000
1974-75	1,80,000
1975-76	2,20,000
1976-77	2,00,000

On 31st March, 1977, land & building were valued at Rs. 2,80,000 and plant & machinery at Rs. 1,20,000. Sundry debtors, on the same date include Rs. 4,000 as irrecoverable.

Having regard to the nature of the business, a 10 per cent return on net tangible capital invested, is considered reasonable.

You are required to value the company's share ex-dividend. Your own valuation of goodwill may be based on five year's purchase of annual super periods. (The tax rate is to be assumed at 50 per cent).

[Closing CE = 728000, Ave. CE 679000, normal profit 67900, FM Profit 97600, super profit 28700, goodwill 148500, value of share 136.08]

Question No. 4

Balance Sheet of Sound Ltd. as at 31st March 1987 is given below :

Liabilities	*Rs.*	*Assets*	*Rs.*
Share Capital		*Fixed Assets:*	
6,000 Equity share of		Building	1,50,000
Rs. 100 each fully		Machinery	2,20,000
paid up	6,00,000	*Current Assets*	
Profit & Loss A/c	50,000		
Bank overdraft	10,000	Stock	3,00,000
Creditors	60,000	Sundry Debtors	1,60,000
Provision for Taxation	1,10,000	Bank	60,000
Proposed Dividend	60,000		

	8,90,000		8,90,000

The net profits of the company, after deducting usual working expenses but before providing for taxation, were as under :

Year	*Rs.*
1984-85	2,00,000
1985-86	2,40,000
1986-87	2,20,000

On 31st March, 1987, Building was revalued at Rs. 2,00,000 and machineries Rs. 2,50,000. Sundry debtors, on the same date, included Rs. 10,000 as irrecoverable. Having regard to nature of business, a 10 per cent return, on net tangible capital invested, is considered reasonable.

You are required to value the company's share-ex-dividend. Valuation of goodwill may be based on three years' purchase of annual super profits. Depreciation on building — 2 per cent, machineries — 10 per cent. The income-tax rate is to be assumed at 50 per cent. All working should form part of your answer.

[May 1987]

[Closing CE = 785000, Ave. CE 732500, normal profit 73250, FM Profit 106333, super profit 33083, goodwill 99249, value of share 137.38]

Question No. 5

On 31st March, 1991, the balance sheet of Menon Ltd. was as follows:

	Rs.		*Rs.*
Share Capital		Land and Building	2,20,000
Authorised & Issued		Plant and Machinery	95,000
5,000 Equity shares of		Stock	3,50,000
Rs. 100 fully paid	5,00,000	Sundry Debtors	1,55,000
Profit & Loss A/c	1,03,000		
Bank Overdraft	20,000		
Creditors	77,000		
Provision for Taxation	45,000		
Proposed Dividend	75,000		
	8,20,000		8,20,000

The net profits of the company, after deducting all working charges and providing for depreciation and taxation, were as under :

Year ended 31st March	*Rs.*
1987	85,000
1988	96,000
1989	90,000
1990	1,00,000
1991	95,000

On 31st March, 1991, land and building were valued at Rs. 2,50,000 and plant and machinery at Rs. 1,50,000.

In view of the nature of the business, it is considered that 10 per cent is a reasonable return on tangible capital. Tax 35 per cent.

Prepare a valuation of the company's shares after taking into account the revised values of fixed assets and your own valuation of goodwill based on five years' purchase of the super profits based on the average profit of the last five years. [Closing CE = 763000, Ave. CE 715500, normal profit 71550, FM Profit 93200, super profit 21650, goodwill 108250, value of share 159.25 ex-dividend]

Question No. 6

The following is the balance sheet of Moon and Co. Ltd. as on 31.3.1990:

Liabilities	*Rs.*	*Assets*	*Rs.*
Share Capital:		*Fixed Assets:*	
Eq. shares of Rs. 100 each	10,00,000	Machines	6,00,000
Less: Calls in arrear		Factory shed	5,00,000
(Rs. 20 for final call)	1,00,000	Vehicles	2,00,000
	9,00,000	Furniture	50,000
Reserve and Surplus:		*Current Assets:*	
General Reserve	3,00,000	Stock	5,00,000
Profit & Loss A/c	4,00,000	Debtors	6,70,000
Current Liabilities:		Bank	50,000
Bank Overdraft	3,00,000	Miscellaneous Expenditure	
Creditors	7,00,000	(to the extent not written	

		off) Pre. Expenses	30,000
	26,00,000		26,00,000

The following additional information is furnished :

(i) Machinery and factory shed are worth 30 per cent above their book value. Depreciation on appreciated value of machinery and factory shed is not to be considered for valuation of goodwill and share.

(ii) For the purpose of valuation of shares, goodwill is to be considered on the basis of 4 years purchase of super profits based on average profit (after tax) of the last 3 years.

Profit (after tax) are as follows : *Rs.*

For the year ended 31.3.1988 3,60,000
For the year ended 31.3.1989 4,70,000
For the year ended 31.3.1990 3,70,000
In a similar business return on capital employed is 15 per cent (after tax).

(iii) In the year ended 31.3.1988 new addition to factory shed costing Rs. 20,000 charged to profit and loss account. Depreciation charged on factory shed is @ 10 per cent on reducing balance method.

Find out the value of each fully paid and partly paid equity share on net assets basis. Income-tax 50 per cent. Show your workings.

[Closing CE = 1918954, Ave. CE 1734359, normal profit 260154, FM Profit 402430, super profit 142276, goodwill 569104, value of share 258.80 fully paid]

Question No. 7

The following is the balance sheet of Star and Co. Ltd. as at 31st Dec. 1985:

Liabilities	*Rs.*	*Assets*	*Rs.*
Share Capital		Goodwill	1,00,000
Equity Share of		Machinery	5,00,000
Rs. 100 each	10,00,000	Factory shed	5,50,000
Less: Calls in arrear		Vehicles	1,50,000
(Rs. 20 for final call)	1,00,000	Furniture	50,000
	9,00,000	Investments	2,00,000
10% Preference share of		*Current Assets:*	
Rs. 10 each fully paid	4,00,000	Stock-in-Trade	4,00,000
Reserves and Surplus:		Sundry Debtors	7,00,000
General Reserve	4,00,000	Cash at Bank	1,00,000

Profit & Loss A/c	3,00,000	*Misc. Expenditure:*	
Current Liabilities:		Prel.Expenses	50,000
Bank Loan	2,00,000		
Sundry Creditors	6,00,000		
	28,00,000		28,00,000

Additional information are as under :

1. Fixed assets are worth 20 per cent above their book value. Depreciation on appreciated value of fixed assets not to be considered for valuation of goodwill.
2. Of the investment, 60 per cent is non-trading and the balance is trade. All trade investments are to be valued at 25 per cent above cost. A uniform rate of dividend @ 15 per cent is earned on all investments.
3. For the purpose of valuation of shares, goodwill is to be considered on the basis of 4 years' purchase of the super profits based on average profit (after tax) of the last 3 years :

   Profit (after tax) : 1983 Rs.400000; 1984 Rs.4,30,000; Rs.4,50,000

   In a similar business, return on capital employed is 15 per cent (after tax). Tax 50 per cent.
4. In 1983 new machinery costing Rs. 20,000 was purchased but wrongly charged to revenue (no effect has yet been given for rectifying the same).

Depreciation charged on machinery is @ 10 per cent on reducing balance method.

Find out the value of each fully paid and partly paid equity share on net assets basis.

Closing CE = 2017496, normal profit 302624, FM Profit 417795, super profit 115171, goodwill 460684, value of share 229.82 fully paid]

Question No. 8

From the balance sheet of India Trading Company Limited as at 31st March, 1980, the following figures have been extracted:

Share Capital	*Rs.*
9% Preference Shares of Rs. 100 each	3,00,000
10,000 Equity shares of Rs. 10 each (Rs. 5.00 paid up)	50,000
10,000 Equity shares of Rs. 10 each (Rs. 2.50 paid up)	25,000
10,000 Equity shares of Rs. 10 each (fully paid)	1,00,000
	4,75,000
Reserves and Surplus	
General Reserve	2,00,000
Profit and Loss Account	50,000

7,25,000

On a revaluation of assets on 31st March, 1980, it was found that they had appreciated by Rs. 75,000 over their book value in the aggregate.

The articles of association of the company provide that in case of liquidation, preference shareholders would have a further claim to 10 per cent of the surplus assets, if any.

You are required to determine the value of preference share and equity share assuming that a liquidation of the company has to take place on 31st March, 1980, and that the expenses of winding up are nil.

Question No. 9

A Ltd. and its subsidiary *B Ltd.* get their supply of some essential raw materials from *C Ltd.* To coordinate their production on a more profitable basis, *A Ltd.* and *C Ltd.* agreed between themselves each to acquire a quarter of shares in the other's authorised capital by means of exchange of shares. The terms are as follows:

(i) *A Ltd.*'s shares are quoted at Rs. 14, but for the purpose of exchange the value is to be taken at the higher of the two values (a) quoted and (b) on the basis of the balance sheet valuation.

(ii) *C. Ltd.*'s share which are unquoted are to be taken at the higher of the value as on (a) yield basis and (b) the balance sheet basis. The future profits are estimated at Rs. 1,05,000 subject to one-third to be retained for development purposes. Shares of similar companies yield 8 per cent.

(iii) Freehold properties of *C Ltd.* are to be taken at Rs. 4,30,000.

(iv) No cash is to pass and the balance due on settlement is to be treated as loan between the two companies.

The summarized balance sheets of the companies at the relevant date stood as follows:

	A Ltd. Rs.	*B Ltd.* Rs.	*C Ltd.* Rs.
Authorised share capital equity share of Rs. 10 each	12,00,000	5,00,000	10,00,000
Issued and Fully paid	8,00,000	5,00,000	7,50,000
Share Premium	80,000		
7% Debentures	3,00,000		
Profit & Loss A/c	2,30,000	2,10,000	2,00,000
Current Liabilities	2,80,000	1,80,000	2,10,000
Proposed Dividend	1,00,000	50,000	
	17,90,000	9,40,000	11,60,000
	A Ltd.	*B Ltd.*	*C Ltd.*

	Rs.	Rs.	Rs.
Freehold Properties	6,60,000	2,90,000	3,30,000
Plant & Machinery etc.	4,50,000	4,10,000	4,40,000
Investments 40,000 shares in *B Ltd.*	4,70,000		
Current Assets	2,10,000	2,40,000	3,90,000
	17,90,000	9,40,000	11,60,000

You are required to compute the value of the shares according to the terms of the agreement and to present the final settlement showing all the workings.

Question No. 10

The following information relates to Good luck Pvt. Ltd. as at 31st December.

(Rupees in lakhs)

	1977	*1978*	*1979*
10,000 Equity shares of Rs. 100 each	10.00	10.00	10.00
Creditors	3.50	4.50	5.50
General Reserve	4.50	5.50	6.50
Profit & Loss Account Balance	.80	.90	1.20
	18.80	20.90	23.20
Goodwill	4.00	3.00	2.00
Building and Machinery (Less Dep.)	9.00	10.00	10.00
Stock-in-trade etc.	4.00	5.00	6.00
Debtors	.20	.90	2.50
Cash and Bank Balance	1.60	2.00	2.70
	18.80	20.90	23.20

The following assets had been undervalued, their real worth to business being:

(Rs. in lakhs)

Building & Machinery	10.00	11.00	12.50
Stock-in-trade etc.	5.20	6.10	8.00
Net Profit, after writing off Depreciation and Provision for taxation and general reserve, balance (including opening balance)	4.80	5.70	6.10

According to company's articles, directors have declared and paid dividends to its members in December each year out of the profit of the relative year. The cost of goodwill of the company was four lakhs. Capital employed at the

beginning of the year 1977 was Rs. 19,30,000 including the cost of goodwill and balance in profit and loss account at the same time was Rs. 80,000. Tax 50 per cent.

You are requested to prepare statement showing :

(a) Average capital employed during each of the three years.

(b) Goodwill on the basis of four years purchase of the average super profits on a ten per cent yield basis.

(c) Yield value of shares.

	1977	1978	1979	Average
Closing CE	13.50	15.50	20.20	
Op. CE	15.30	13.50	15.50	
Div. paid	4	4.8	4.9	
Ave. CE	16.40	16.90	20.30	
Normal profit	1.64	1.69	2.03	
FM profit	5.60	6.85	7.65	6.70
Super profit	3.96	5.16	5.62	4.91333

Question No. 11

The summarized balance sheet of Jai Pvt. Ltd. as on 31st December, 1976 is as follows:

Liabilities	Rs.	Assets	Rs.
Preference Share		*Fixed Assets*	
(Rs. 100 each)	1,50,000	Goodwill	1,50,000
45000 Equity shares		Freehold Property	3,75,000
(Rs. 10 each)	4,50,000	Plant and Machinery	1,50,000
	6,00,000		6,75,000
P&L A/c	7,50,000	Quoted Investment	3,00,000
5% Debentures 1980	3,00,000	*Current Assets*	
Sundry Creditors	2,39,250	Stock	2,70,000
		Debtors (Net)	2,99,250
		Bank Balance	3,45,000

	18,89,250		18,89,250

A foreign investor shown interest in the company's business. You have been appointed for suggesting the value of equity shares of the company. You gather the following data :

Profits for the three years 1974, 1975 and 1976 after charging debenture interest but before providing for preference dividend, were Rs. 2,20,500, Rs. 3,22,500 and Rs. 2,40,000 respectively.

(a) Preference shares are payable at par on liquidation.

(b) The purchaser wants to acquire all the 45,000 equity shares.

(c) (i)The normal rate of return 10 per cent.

(ii) The goodwill to be calculated at three times the adjusted average super profits of the three years referred to above.

(iii) Debentures will be redeemed at a discount of 25 per cent prior to the sale of the business.

(iv) The value of freehold property is agreed to be ascertained on the basis of 8 per cent return. The current rental value is Rs. 50,400.

(v) A claim of Rs. 8,250 was omitted to be provided in the year 1976.

(vi) Tax 35 per cent.

It is decided to sell the business, you are required to compute the purchase price of equity shares after taking into consideration the following relevant facts:

(vii) Market value of quoted investment was Rs. 3,75,000.

(viii) Non-recurring profits are to be eliminated. 10 per cent of profits for 1975 referred to above arose from a transaction of a non-recurring nature.

(ix) A provision of 5 per cent on sundry debtors was made in 1976 which is no longer required.

Question No. 12

Balance sheet of *A Ltd.* as on 31.12.1987 was as under:

Liabilities	*Rs.*	*Assets*	*Rs.*
Equity Share Capital (Rs. 10)		Buildings	2,00,000
Rs. 10 paid up per share	3,00,000	Plant and Machinery	4,00,000
Rs. 5 paid up per share	2,00,000	Sundry Debtors	2,10,000
9% Preference Share		Stock	2,50,000
Capital (Rs. 100)	1,00,000	Cash and Bank	40,000
Reserve	3,00,000		
Sundry Creditors	2,00,000		
	11,00,000		11,00,000

Profit and dividend in last several years were as under :

Year	*Profit Rs.*	*Equity Dividend*
1987	3,20,000	18%
1986	2,50,000	15%
1985	2,20,000	12%

Land and buildings are worth Rs. 4,00,000. Managerial remuneration is likely to go up by Rs. 20,000 p.a. Income-tax may be provided at 50 per cent. Equity shares of companies in the same industry with dividend rate of 10 per cent are quoted at par.

Find the most appropriate value of an equity share assuming that:

(a) Controlling interest is to be transferred.

(b) Only a few shares are to be transferred.

Ignore goodwill value, depreciation adjustment for revaluation and the need of transfer to general reserve. *[May 1988]*

Question No. 13

Mindtree Ltd. belongs to an industry in which equity shares sell at par on the basis of 9 per cent dividend yield provided the net tangible assets of the company are 300 per cent of the paid up capital and provided that the total distribution of profit does not exceed 50 per cent of the profits. The dividend rate fluctuates from year to year in the industry. The balance sheet of Mindtree Ltd. stood as follows on 31.12.2004:

Liabilities	*Rs.*	*Assets*	*Rs.*
7% Preference Shares full paid (Rs. 100)	6,00,000	Goodwill	1,00,000
		F.A. less Dep.	16,00,000
Equity shares of Rs. 80 paid (F.V. Rs. 100)	8,00,000	Investment	1,50,000
		C.A.	6,30,000
Revenue Reserve	4,00,000	Prel. Expenses	20,000
6% Debentures	4,00,000		
Current Liabilities	3,00,000		
	25,00,000		25,00,000

The company has been earning on the average Rs. 4,00,000 as profit after debenture interest but before tax which may be taken at 50 per cent. The rate of dividend on equity shares has been maintained at 12 per cent in the past year and is expected to be maintained. Determine the probable market value of the

equity shares of the company. The fixed assets may be taken to be worth Rs. 17,20,000.

Answer :Note 1 Net tangible assets = FA 1720000 + Investments 150000 + CA 630000 – Debentures 400000 – CL 300000 = 1800000 Paid up capital = 14, 00, 000

Net assets as a % of paid up capital = (1800000 / 1400000)x100 = 129

It is less than 300 % (which is bench mark for the industry). It is a negative feature of the Mindtree as compared of industry. It should result in reduction of value of Mindtree Ltd. For this purpose, we should raise the normal rate of Mindtree Ltd.

Alternative note : Net tangible assets attributable to equity shareholders= FA 1720000 + Investments 150000 + CA 630000 – Debentures 400000 – CL 300000 – Pref. share capital 600000= 1200000

Paid up equity capital = 8,00, 000

Net assets as a % of paid up capital = 1200000/ 800000 = 150 %

It is less than 300 % (which is bench mark for the industry). It is a negative feature of the Mindtree Ltd. as compared of industry. It should result in reduction of value of Mindtree Ltd. For this purpose, we should raise the normal rate of Mindtree Ltd.

Note 2 :Average Profit of Mindtree Ltd.= 400000 - tax 200000 = 2,00,000

Pref .Div. – 42,000

Equity Div (@ 9 %)[26]	- 72,000
Retained profit	86000

Retained profit is less than 50 % of profit. Lower retained profit means lower growth in future (Remember that Gordon has told that growth depends upon two factors . retained profit is one of those two factors.) It is a negative feature of the Mindtree Ltd. as compared of industry. It should result in reduction of value of Mindtree Ltd. For this purpose, we should raise the normal rate of Mindtree Ltd.

Question No. 14

Following are the information relating to a manufacturing company:

Year	*Average Net Worth (Rs.)*	*Adjusted Taxed Profits (Rs.)*
1975-76	20,00,000	3,00,000
1976-77	22,50,000	3,70,000
1977-78	23,00,000	3,75,000
1978-79	24,00,000	4,00,000

(a) Average net worth does not include investments worth Rs. 3,00,000 (at market value) on the valuation date, the yield in respect of which has been excluded in computing the adjusted tax profits figures.

(b) The company has Rs. 9,00,000 on equity shares of Rs. 100 each and Rs. 4,00,000 in 9 per cent preference shares of Rs. 100 each.

(c) It is the usual practice of similar type of companies to set aside 20 per cent of the taxed profits for rehabilitation purposes.

(d) On the valuation day, the net worth (including investments) amounted to Rs. 25,50,000.

(e) The normal expected rate of return is 10 per cent.

(f) The company has paid dividends regularly within a range of 9 per cent to 11 per cent on equity shares over the past 6 years and expects to maintain the same.

---

[26] Industry retains 50% of profit after paying 9 % dividend. Hence, to find whether Tee retains 50% profit or not, we should consider 9 % equity dividend i.e. we should find whether Tee Ltd can retain 50% profit after paying 9% dividend (which is industry mark). (Industry's 50 % bench mark is based on 9 % equity dividend and not on 12 % dividend). If Tee does not retain 50% profit on the basis of 9% dividend, it a negative point for Tee; if it does not retain 50% on the basis of 12 %, it not a negative point.

Find out the value of equity shares on the basis of productivity. You may use weight factor: 1, 2, 3, 4 for four years, assigning weight 1 to the year 1975-76 and so on.

Answer : The main point of this question is that we have to find the value of share on some date (which has been referred in the question as valuation date), and not on the B/S date. For 1978-79, average CE (average net worth)was 24,00,000 (exclusive of investment amount) , adjusted taxed profit for the year was 400000, it means CE (net worth)on 31.3.1979 was more than 24,00,000. On the date on which we have to find the value of the share (which has been referred in the question as valuation date), the net worth exclusive of investment is Rs.22,50,000 (net worth inclusive of investments 25,50,000; amount of investments 300000; hence net worth exclusive of investments 2250000).

Year	Rate of return
75-76	(300000/2000000) x 100 = 15.00
76-77	(370000/2250000) x 100 = 16.44
77-78	(375000/2300000) x 100 = 16.30
78-79	(400000/2400000) x 100 = 16.67

Average rate of return of the past : {(15x 1) + (16.44 x 2) + (16.30x 3) + (16.67x 4) }/10 = 16.35 %

It is assumed that in the future, the company shall be earning the same rate of return.

Question No. 15

Compute the values of a preference share and an equity share of each of the companies *A* & *B* on the basis of following information:

	A *Rs.*	*B* *Rs.*
Profit After tax	10,00,000	10,00,000
12% Preference Shares (Rs. 100)	10,00,000	20,00,000
Equity Shares (Rs. 10)	50,00,000	40,00,000

Assume market expectation 15 per cent and that 80 per cent of profits are distributed.

Q. No.16 :The B/S of RNR limited as on 31st De. 1999 as follows(Rs. Lakhs)

Liabilities		Assets	
100000 equity shares of Rs. 10 each fully paid	10	Goodwill	5
100000 equity shares of Rs. 6 each fully paid	6	FA	15
Reserve and surplus	4	Other tangible assets	5
Liabilities	10	Intangible assets (market value)	3
		Miscellaneous exp. (Yet to be written off)	2
Total	30	Total	30

Fixed assets are worth Rs. 24 Lakhs. Other tangible assets are revalued at Rs. 3 Lakhs. The company is expected to settle the disputed bonus claim of Rs. 1 Lakhs not provided for in the accounts. Goodwill appearing in the Balance Sheet is purchased goodwill. It is considered reasonable to increase the value of goodwill by an amount equal to average of the book value and a valuation made at 3 years' purchase of average super-profit for the last 4 years. Tax 50%.
After tax profits and dividend rates were as follows :

Year	PAT (Rs. Lakhs)	Dividend %
1996	3.00	11
1997	3.50	12
1998	4.00	13
1999	4.10	14

Normal expectation in the industry to which the company belongs is 10%.

Akbar holds 20,000 equity shares of Rs. 10 each fully paid and 10,000 equity shares of Rs.6 each fully paid . He wants to sell away his holdings.

(i) Determine the break-up value[27] and market value of both kinds of shares

(ii) what should be the fair value of shares, if controlling interest is being sold ?

Hint : Assumption – Dividends referred in the question are proposed dividends. The amount of proposed dividend for the year 1999 is included in the amount of liabilities (Rs. 10 Lakhs) appearing in the B/S.

AMALGAMATION ABSORPTION AND RECONSTRUCTION

Background : In case of amalgamation, two or more companies are wound up and a new company is formed to take over their businesses. (One formation, winding up of two or more). Absorption: In this case, an existing company takes over the business(es) of one or more existing companies. (No new formation, winding up of one or more). For Example, an existing company *A Ltd.* takes over the business of another existing company *B Ltd.* It is absorption. Another example: Let *A Ltd.*, *B Ltd.* and *C Ltd.* be existing companies. *A Ltd.* take over the business of *B Ltd.* and *C Ltd.* It is also absorption. External Reconstruction: In this case, a newly-formed company takes over the business of an existing company. (One formation, one winding up).

	WINDING UP	FORMATION
AMALGAMATION	TWO OR MORE	ONE
ABSORPTION	ONE OR MORE	NO NEW FORMATION
E. Reconstruction	One	One

From the above discussion, we can conclude that whether it is a case of amalgamation or absorption or external reconstruction, there are two types of companies: (i) Purchasing company, (ii) Vendor company.

[27] Intrinsic value

Before passing the entries, we should calculate the purchase consideration (PC). PC is the amount paid by purchasing company to the liquidator of vendor company for shareholders of vender company. There are two methods of calculating P.C. (i) Net payment method, and (ii) Net assets method. Under net payment method, PC is the sum of "Cash and agreed value of shares, debentures and other assets" given by purchasing company to the liquidator of vendor company for shareholders of vendor company. Under net assets method, PC is equal to agreed value of assets (including goodwill) taken over minus agreed value of liabilities taken over.

Two important points about liabilities of vendor company (i) If a liability of vendor company is discharged by purchasing company, then first it should be taken over by purchasing company and then it should be directly discharged by purchasing company. (It should not be paid through liquidator). (ii) Inter-company Owings, i.e., liabilities of vendor company which are assets of purchasing company, should be taken over by purchasing company and then these are cancelled against corresponding assets of purchasing company.

Steps for Realization account (books of vendor company):

1. Transfer all real assets (except cash and bank) to the *Dr.* side of realization a/c at their book values whether taken over by purchasing company or not.
2. Transfer that amount of cash and bank which is taken over by purchasing company to the *Dr.* side of realisation a/c.
3. Transfer all outside liabilities to the credit side of realisation a/c at their book values whether taken over or not.
4. For assets and liabilities taken over by purchasing company, debit the purchasing company account by crediting the realisation account with the amount of purchase consideration (Purchasing company a/c *Dr.* to realisation a/c).
5. Sometimes, a liability is satisfied by transfer of an existing non-cash and bank asset of vendor company (existing non-cash and bank asset of vendor company implies (i) The asset has not been received as part of PC, and (ii) It is other than cash and bank). No entry is passed in this situation. But if the liability is not fully satisfied and some cash is also paid, the entry should be passed for cash paid, i.e., realisation a/c should be debited and cash a/c should be credited with amount of cash paid. If the asset is valued at an amount higher than that of liability, some cash may be received. The entry for such receipt should be passed, i.e., cash a/c should be debited and realisation a/c should be credited with the amount of cash received.
6. For other assets (neither taken over by purchasing company, nor transferred in favour of liabilities): (a) If sold, cash a/c should be debited and realisation a/c should be credited, (b) If transferred to shareholders, shareholders a/c should be debited are realisation a/c should be credited with current value of such assets.
7. For other liabilities (i.e., liabilities which are neither taken over by purchasing company nor satisfied through transfer to existing non-cash and

bank asset of vendor company) (A) If paid for *Dr.* realisation a/c and credit concerned payment account. Concerned payment a/c may be cash or bank, (B) If transferred to shareholders: *Dr.* realisation a/c and *Cr.* shareholders a/c.

8. For realisation expenses paid by vendor company, *Dr.* realisation a/c and *Cr.* cash a/c.
9. Profit/loss on realisation should be transferred to sundry shareholders a/c.

Realisation expenses/winding up expenses of vendor company paid by purchasing company—

(a) Purchasing company should debit goodwill a/c and credit cash/bank a/c.
(b) No entry in the books of vendor company.

VENDER COMPANY HOLDS SHARES OF PURCHASING COMPANY

Net Assets Method

Find PC for assets and liabilities taken over, as the purchasing company cannot take over its own shares, such shares should not be considered for calculation of PC. Such shares should be transferred to shareholders of vendor company through realisation a/c.

Net Payment Method

(a) Find PC that would have been there if purchasing company would have purchased its own shares also. (We do not consider this PC for recording the transactions in the books of accounts, it is not correct amount of PC as it is based on wrong assumption that the purchasing company takes over its own shares).
(b) As purchasing company cannot take over its own shares, the amount calculated above should be reduced by 'No. of shares of purchasing company held by vendor company multiplied by agreed value of each such share'. The resultant figure is PC for the assets and liabilities taken over.

PURCHASING COMPANY HOLDS SHARES OF VENDOR COMPANY

Find PC ignoring the fact that purchasing company holds shares of vendor company. This is the PC for the business taken over. The purchasing company won't have to pay full amount of this PC as it is already part owner of the business. Hence, PC is reduced by the amount which the purchasing company is entitled to get as shareholder of vendor company.

BOTH COMPANIES HOLD SHARES OF EACH OTHER

Net Assets Method

(i) Find value of both businesses with the help of simultaneous equations.
(ii) Find PC for assets and liabilities taken over only. As purchasing company cannot take over its own shares, such shares should not be considered for PC.

(iii) Purchasing company won't pay the full amount of PC calculated above. Hence, the PC calculated above should be reduced by the amount receivable by the purchasing company in the capacity of shareholders of vendor company. The resultant figure is the amount of PC payable by purchasing company to the liquidator of vendor company

Net Payment Methods

(a) Find PC that would have been there if purchasing company would have purchased its own shares also. While finding out this amount we ignore that fact that purchasing company holds shares of vendor company. (We do not consider this PC for recording the transactions in the books of accounts. It is not correct amount of PC as it is based on wrong assumption that the purchasing company takes over its own shares).

(b) As purchasing company cannot take over its own shares, the amount calculated above should be reduced by 'No. of shares of purchasing company held by vendor company multiplied by agreed value of such share.' The resultant figure is PC for assets and liabilities taken over.

(c) Purchasing company won't pay the full amount of PC calculated above. Hence, the PC calculated above should be reduced by the amount receivable by purchasing company in the capacity of shareholder of vendor company. The resultant figure is the amount of PC payable by purchasing company to the liquidator of vendor company.

Internal Reconstruction

In this case there is no winding up no new formation no sale of business no purchase of business. The assets and liabilities are revalued through capital reduction A/c. P&L A/c *Dr.* balance and fictitious assets must be written off against capital reduction a/c even if the question is silent on this point. If the final balance in capital reduction a/c is debit it should be transferred to goodwill a/c, if there is credit balance it should be transferred to capital reserve account.

Question No. 1

White Ltd. agreed to acquire the business of Green Ltd. as on December 31, 1975. The summarized balance sheet of Green Ltd. on that date was as follows:

Liabilities	*Rs.*	*Assets*	*Rs.*
E. Share capital		Goodwill	1,00,000
(Rs. 10 each)	6,00,000	Land Build& Plant	6,40,000
General Reserve	1,70,000	Stock-in-Trade	1,68,000
P&L Account	1,10,000	Debtors	36,000
6% Debentures	1,00,000	Cash	56,000
Creditors	20,000		
	10,00,000		10,00,000

The amount payable by White Ltd. was agreed as follows:

1. A cash payment equivalent to Rs. 2.50 for every Rs. 10 share in Green Ltd.
2. The issue of such an amount of fully paid 5 per cent debentures of White Ltd. at 96 per cent as is sufficient to discharge the 6 per cent debentures of Green Ltd. at a premium of 20 per cent.
3. The issue of 90,000 Rs. 10 shares, fully paid, in White Ltd. having an agree value of Rs. 15 per share.

When computing the agreed consideration, the directors of White Ltd. valued the land, building and plant at Rs. 12,00,000, the stock-in-trade at Rs. 1,42,000 and the debtors at their face value subject to an allowance of 5 per cent to cover doubtful debts. The cost of liquidation (met by White) of Green Ltd. comes to Rs. 5,000. Close the books of Green Ltd. and draft journal entries required in the books of White Ltd.

Ans. **Books of Green Ltd.**

Realization a/c

Goodwill	1,00,000	Creditors	20,000
Land Building	6,40,000	Deb.	1,00,000
Stock	1,68,000	White Ltd.	15,00,000
Drs.	36,000		
Cash	56,000		
Shareholders a/c (Profit on realization)	6,20,000		
Total	16,20,000	Total	16,20,000

Shareholders a/c

Bank	150000	ESC	600000
Shares of white	1350000	G.R.	170000
		P & L	110000
		Realisation a/c (profit)	620000
Total	1500000	Total	1500000

Question No. 2

The following is the balance sheet of Weak Ltd. as on June 30, 1976 :

Liabilities	*Rs.*	*Assets*	*Rs.*
Share Capital :		Goodwill	35,000

(Rs. 100 each)	2,00,000	Land and Building	85,000
Reserve Fund	20,000	Plant and Mach.	1,60,000
5% Debentures	1,00,000	Stock	55,000
Loan from *A* (a director)	40,000	Debtors	65,000
Sundry Creditors	80,000	Cash at Bank	34,000
		Discount on Debentures	6,000
	4,40,000		4,40,000

The business of the company is taken over by Strong Ltd. as on the date, on the following terms :

(a) Strong Ltd. to take over all assets except cash, to value the assets at their book value less 10 per cent except goodwill which was to be valued at 4 years purchase of the excess of average (five years) profits over 8 per cent of the combined amount of share capital and reserves;

(b) Strong Ltd. to take over trade creditors which were subject to a discount of five per cent. Other outside liabilities were discharged by Strong Ltd. at their book values.

(c) The purchase consideration was to be discharged in cash to the extent of Rs. 10,000 and the balance in fully paid equity shares of Rs. 10 each valued at Rs. 12.50 per share.

The average of the five years' profits was Rs. 30,100. The expenses of liquidation amounted to Rs. 4,000. Weak Ltd. had sold prior to 30th June, 1976, goods costing Rs. 30,000 to Strong Ltd. for Rs. 40,000. Debtors include Rs. 20,000 still due from Strong Ltd. on the date of absorption, Rs. 25,000 worth of the goods were still in stocks of Strong Ltd. Show the important ledger accounts in the books of Weak Ltd. and Journal entries in the books of Strong Ltd.

Ans, **Books of Weak Ltd.**

Realization a/c

Goodwill	35,000	Crs.	80,000
L & B	85,000	Loan	40,000
P & M	1,60,000	Deb.	1,00,000
Stock	55,000	Strong Ltd.	1,62,500
Drs.	65,000	Shareholders a/c (loss)	21,500
Cash (exp.)	4,000		
Total	4,04,000	Total	4,04,000

Shareholders a/c

Dis. On Deb.	6000	ESC	200000

Realization a/c	21500	Res.	20000
Bank (34000 + 10000 - 4000)	40000		
Shares of strong	152500		
Total	220000	Total	220000

Question No. 3

B Co. Ltd. had the following Balance Sheet as on 31st March 1978. (Rs.)

Share Capital		Fixed Assets	83,00,000
(Rs. 100 each)	50,00,000	Current Assets	69,00,000
Capital Reserve	8,00,000	Investments	17,00,000
General Reserve	36,00,000	Goodwill	2,00,000
Unsecured Loans	22,00,000		
Sundry Creditors	42,00,000		
Provision for Taxation	11,00,000		
Proposed Dividend	2,00,000		
	171,00,000		171,00,000

B. Co. Ltd. is amalgamated with Beesons Ltd. as on 31st March, 1978, on which date the balance sheet of Beesons Ltd. as follows :

Beesons Ltd.

Liabilities	*Rs.*	*Assets*	*Rs.*
Share Capital		Fixed Assets	160,00,000
(Rs. 10 each)	80,00,000	Current Assets	168,00,000
General Reserves	100,00,000		
Secured Loans	40,00,000		
Sundry Creditors	46,00,000		
Provision for Tax	52,00,000		
Proposed Dividend	10,00,000		
	328,00,000		328,00,000

For the purpose of the amalgamation the goodwill of *B. Co. Ltd.* was considered valueless. There are also arrears of depreciation in *B. Co. Ltd.* amounting to Rs. 4,00,000. The shareholders in *B. Co. Ltd.* are allotted, in full satisfaction of their claims, shares in Beesons in the same proportion as the respective intrinsic values of shares of two companies bear to one another. Pass Journal entires in the books of both the companies to give effect to the above.

Ans. **Books of B co Ltd.**

Realization a/c

FA	8300000	Loan	2200000
CA	6900000	Crs.	4200000
Invest.	1700000	Tax	1100000
Goodwill	200000	Beesons	9000000
		Shareholders a/c (Loss)	600000
Total	17100000	Total	17100000

Shareholders a/c

Realisation a/c (Loss)	600000	ESC	5000000
Shares of Beesons	9000000	CR	800000
		GR	3600000
		Prop. Dividend	200000
Total	9600000	Total	9600000

Question No. 4

The following are the balance sheets of *A Ltd.* and *B Ltd.* as on 31.12.1979.

A Ltd.

Liabilities	*Rs.*	*Assets*	*Rs.*
150000 Equity shares of Rs. 10 each	15,00,000	Fixed Assets	17,00,000
5,000 Pref. shares of Rs. 100 each	5,00,000	Stocks (Pledged with secured Loan holders)	92,00,000
General Reserves	2,00,000	Other Current Assets	18,00,000
Secured Loans (Secured against pledge of stocks)	80,00,000	Profit & Loss A/c	83,00,000
Unsecured Loans	43,00,000		
Current Liabilities	65,00,000		
	210,00,000		210,00,000

B Ltd.

Liabilities	*Rs.*	*Assets*	*Rs.*
50,000 Equity shares of Rs. 10 each	5,00,000	Fixed Assets	34,00,000
Capital Reserves	14,00,000	Current Assets	48,00,000
Secured Loans	40,00,000		

Current Liabilities	23,00,000		
	82,00,000		82,00,000

The two companies go into liquidation and *C Ltd.* is formed to taken over their business. The following information is given :

(a) All the current assets of the two companies except pledged stock are taken over by *C Ltd.* The realizable value of all current assets are 80 per cent of book values in case of *A Ltd.* and 70 per cent for *B Ltd.*

(b) The break-up of current liabilities is as follows:

	A Ltd.	*B Ltd.*
Statutory Liabilities (including Rs. 11,00,000 in case of *A Ltd.* in respect of a claim not having been admitted shown as contingent liability)	36,00,000	5,00,000
Liability of Employees	15,00,000	9,00,000

(c) Secured loans include Rs. 8,00,000 accrued interest in the case of *B Ltd.*

(d) 1,00,000 equity shares of Rs. 10 each are allotted at par against cash payment of entire face value by *C Ltd.* to the shareholders of *A Ltd.* and *B Ltd.* in the ratio of face values of shares held by them in *A Ltd.* and *B Ltd.*

(e) Preference shareholders are issued equity shares worth Rs. 1,00,000 in lieu of present holdings.

(f) Secured loan holders agree to continue the balance amount of their loans to *C Ltd.* after adjusting value of pledged security in case of *A Ltd.* and after waiving 50 per cent of interest due in case of *B Ltd.*

(g) Unsecured loans are taken over by *C Ltd.* at 25 per cent of loan amounts.

(h) Employees are issued fully paid up equity shares in *C Ltd.* at par in full settlement of entire dues.

(i) Statutory liabilities are taken over by *C Ltd.* at full value and miscellaneous creditors are taken over at 80 per cent of the book value.

Show the opening balance sheet of *C Ltd.*

Ans. **Books of A Ltd.**

Realization a/c

FA	17,00,000	CL	65,00,000
Stock	92,00,000	Loan	43,00,000
CA	18,00,000	Loan	80,00,000
Shareholders a/c (profit)	62,00,000	C Ltd	1,00,000
Total	1,89,00,000	Total	1,89,00,000

Shareholders a/c

P & L A/C	83,00,000	ESC	15,00,000

Esc	1,00,000	PSC	5,00,000
		GR	2,00,000
		Real. a/c (profit)	62,00,000
Total	84,00,000	Total	84,00,000

Question No. 5

The Balance Sheet of *X Ltd.* and *Y Ltd.* as on 31.3.1977 are as below :

Balance Sheet as on 31.3.1977

Liabilities	*X*	*Y*	*Assets*	*X*	*Y*
Equity Shares Capital (Rs. 10)	5,00,000	3,00,000	Fixed Assets Other than Goodwill	3,00,000	2,00,000
Reserve	40,000	20,000	Stock	80,000	60,000
P&L A/c	60,000	40,000	Debtors	1,40,000	90,000
Sundry Creditors	50,000	30,000	Bank	1,20,000	35,000
			Preliminary Expenses	10,000	5,000
	6,50,000	3,90,000		6,50,000	3,90,000

Y Ltd. is taken over by *X Ltd.* as on 1.7.1977. No balance sheet of *Y Ltd.* is prepared as on 1.7.1977. But it is estimated that Rs. 20,000 profit has been earned in these three months after charging 10 per cent depreciation p.a. on fixed assets. Profit earned by *X Ltd.* over these three months is estimated at Rs. 40,000 after charging 10 per cent depreciation p.a.

Both the companies have declared and paid 10 per cent dividend in the meantime. Purchase consideration is to be satisfied by *X Ltd.* at par neglecting actual value of its shares. Goodwill of *Y Ltd.* is valued at Rs. 20,000 and fixed assets are valued Rs. 10,000 above the estimated book value. Balance sheet of *X Ltd.* after absorption?

Ans. **Books of Y**

Realization a/c

FA	195000	X Ltd.	375000
WC	150000		
Shareholders' a/c (profit)	30000		
Total	375000	Total	375000

Shareholders' a/c

P. Exp.	5000	ESC	300000
Shares of X Ltd.	375000	Res.	20000

		P & L a/c	30000
		Realization a/c (Profit)	30000
Total	380000	Total	380000

Question No. 6

The summarised balance sheets of *PQ Ltd.* and *XY Ltd.* at 31st December, 1988.

	PQ Ltd.	*XY Ltd.*
	£	£
Authorised Capital :		
7 % cum. preference share of £ 1	—	1,50,000
6% cum. preference shares of £ 1	25,000	
Ordinary shares of £ 0.25	1,50,000	2,00,000
Issued Capital :		
7% cumulative preference shares of £ 1 fully paid	—	1,00,000
6% cumulative preference shares of £ 1 fully paid	25,000	—
Ordinary shares of £ 0.25	1,00,000	1,50,000
Profit and loss account balance	—	15,400
6% Debentures	40,000	—
Trade Creditors	39,000	37,000
Bank overdraft (secured)	24,000	—
Provision for doubtful debts (including £ 3,000 for *PQ Ltd.*)	—	4,000

			2,28,000	3,06,400
Fixed Assets at cost less depreciation				
Buildings	54,000		61,000	
Plant & Machinery	29,000	83,000	73,000	1,34,000
Goodwill		20,000		15,000
Investments :				
50,000 shares of £ 1 in *MN Ltd.* at cost		40,500		—
Rs.9,550 6% Debentures in *PQ Ltd.* at cost		—		9,100
Current Assets:				
Stocks	31,000		28,900	
Debtors	21,500		77,400	
Balance at Bank	—	52,500	42,000	1,48,300
Profit and Loss account bal.		32,000		
		2,28,000		3,06,400

PQ Ltd. owed *XY Ltd.* £ 9,000 on current trading and this is included in the debtors and creditors of the respective companies.

The necessary meetings of debenture holders, creditors and members having been held, it was agreed that *PQ Ltd.* should cease trading at 31st December and go into liquidation on 3rd January, 1989 and *XY Ltd.* should take over the assets and liabilities of *PQ Ltd.* on the following terms and taking into account the following factors:

1. On 2nd January, 1989 *PQ Ltd.* paid into its bank account the following sums :

	£
Collections from trade debtors	2,500
Bad debt recovered	300

2. *MN Ltd.* had gone into liquidation on 31st August 1988 and on January 3rd, 1989 a final repayment of £ 0.1 in the £ was paid to the purchasing company on 3rd January.
3. The assets of *PQ Ltd.* were to be taken over at the following valuation:

	£
Buildings	60,000
Plant	15,000
Stock	19,000
Goodwill	100
Trade Debtors	At book value

4. The Bank overdraft as on 3rd January, 1989 was to be paid off by *XY Ltd.*

5. The debentures of *PQ Ltd.* (other than those held by *XY Ltd.* which were to be cancelled) were to be satisfied by an issue of 7½ per cent debentures in *XY Ltd.* which were to be issued at an agreed value of 102.
6. *PQ Ltd.*'s debt of £ 9,000 to *XY Ltd.* was to be cancelled.
7. In settlement of each £ 1 of their claim the creditors of *PQ Ltd.* were to receive an immediate allotment of two ordinary shares of £ 0.25 fully paid in *XY Ltd.*, followed by £ 0.'3 cash, the latter to be paid by *XY Ltd.* on 1st February, 1989.
8. Preference shareholders in *PQ Ltd.* were to receive two 7 per cent cumulative preference shares of *XY Ltd.* for each five shares of their present holding.
9. Ordinary shareholders in *PQ Ltd.* were to receive one ordinary share in *XY Ltd.* for every fifty shares of their present holding.

You are required to prepare : (i) Ledger accounts of vendor company, (ii) Journal of purchasing company.

Ans. **Books pf PQ**

Realization a/c

Building	54000	Bank Overdraft	21200
P.& M.	29000	Creditors	39000
Goodwill	20000	Deb.	40000
Investment	40500	XY Ltd. (Purchase consideration)	17900
Stock	31000	Shareholders a/c(Loss)	75400
Drs.	19000		
Total	193500	Total	193500

Shareholders a/c

P & L a/c (32000- 300 bad debts recovered)	31700	ESC	100000
Pref. shares of XY	10000	PSC	25000

E. shares of XY	7900		
Realization a/c	75400		
Total	125000	Total	125000

Question No. 7

A *Ltd.* and *B Ltd.* both incorporated on 1.1.1981 decided to amalgamate. Holding company *C Ltd.* is formed on 1.1.1983 to acquire all the shares of both companies. From the information given below, prepare balance sheet of *C Ltd.* after acquiring all shares. Both *A Ltd.* and *B Ltd.* are engaged in similar business activities.

1. The shares of the two companies were acquired on the following terms:
   (a) Rs. 100, 12 per cent debenture for every Rs. 100, of net assets owned by each company on 31st December, 1982, and
   (b) Rs. 100 equity shares based on two years purchase of profit before taxation. The profits are to be average profits of 1981 and 1982 being weighted on 1 : 2 basis.
2. It was agreed that accounts of *B Ltd.*, for the two years ended December 31, 1982 be adjusted, where necessary, to confirm with accounting policies followed by *A Ltd.*
3. The pre-tax profits, included investment income, of the two companies were as follows:

	1981	*1982*
A Ltd.	5,46,000	6,12,000
B Ltd.	5,96,000	8,58,000

4. *A Ltd.* values stock on last-in-first-out basis while *B Ltd.* used first-in-first-out basis. To bring *B Ltd.*'s values in line with those of *A Ltd.* its values will be require to be reduced by Rs. 12,000 at the end of 1981 and Rs. 34,000 at the end of 1982.
5. B. Ltd. deducts 1 per cent from trade debtors as a general provision against doubtful debts.
6. Both companies use straight line method of depreciation.
7. Prepaid expenses in *B Ltd.* include advertising expenditure carried forward of Rs. 60,000 in 1981 Rs. 30,000 in 1982, being part of initial advertising in 1981 which is being written off over three years. Similar expenditure in *A Ltd.* has been fully written off in 1981.

B Limited

Liabilities	*1981 Rs.*	*1982 Rs.*	*Assets*	*1981 Rs.*	*1982 Rs.*
Share Capital			Fixed Assets		

Issued & Subscribed			Cost	3,20,000	3,20,000
5000 equity shares			*Less:* Depre-		
of Rs. 100 each			ciation	48,000	96,000
fully paid	5,00,000	5,00,000			
Revenue				2,72,000	2,24,000
Reserve	2,86,000	7,14,000	Investments		
Sundry			(Market value		
Creditors	4,90,000	4,94,000	4,90,000)	—	4,00,000
Bank overdraft	—	1,70,000	Current Assets:		
Provision for			Stock-in-trade		
taxation	3,10,000	4,30,000	in cost	5,97,000	7,42,000
			Sundry		
			Debtors	5,94,000	8,91,000
			Prepaid Exp.	72,000	48,000
			Cash at Bank	51,000	3,000
	15,86,000	23,08,000		15,86,000	23,08,000

A Limited

Liabilities	*1981 Rs.*	*1982 Rs.*	*Assets*	*1981 Rs.*	*1982 Rs.*
Share Capital			Fixed Assets	2,30,000	2,30,000
(Rs. 100)	4,00,000	4,00,000	*Less:* Dep.	23,000	46,000
Capital Reserve	—	70,000			
Revenue				2,07,000	1,84,000
Reserve	2,66,100	5,58,000	Investments	—	2,60,000
Creditors	5,00,900	6,07,000	Stock	6,10,000	7,25,000
Taxation	2,80,000	3,20,000	Debtors	6,00,000	7,40,000
			Prepaid Exp.	10,000	14,000
			Bank	20,000	32,000
	14,47,000	19,55,000		14,47,000	19,55,000

Working notes and Ans.

$$\text{A's goodwill} = \frac{[(546000 \times 1) + (612000 \times 2)]}{3} \times 2 = 1180000$$

$$\text{B's goodwill} = \frac{[(546000 \times 1) + (885000 \times 2)]}{3} \times 2 = 1544000$$

	Goodwill	Net assets	Total
A	11,80,000	10,28,000	22,08,000
B	15,44,000	12,81,000	28,25,000
Total	27,24,000	23,09,000	50,33,000

B/S of C Ltd as on 1.1.83

ESC	2724000	Investment in shares of A Ltd.	2208000
Deb.	2309000	Investment in shares of B Ltd.	28,25,000
Total	50,33,000	Total	50,33,000

Question No. 8

Following are the balance sheets of two companies, Wye Ltd. and Zee Ltd. as at December 31, 1965.

	Wye Ltd. *Rs.*	*Zee Ltd.* *Rs.*		*Wye Ltd.* *Rs.*	*Zee Ltd.* *Rs.*
Creditors	1,50,000	95,000	1,000 shares in		
Reserve	1,00,000	55,000	Wye Ltd.		1,00,000
Share Capital (Rs. 100)	5,00,000	3,00,000	Sundry Assets	7,50,000	3,50,000
	7,50,000	4,50,000		7,50,000	4,50,000

(a) Wye Ltd. absorbed Zee Ltd. on the basis of intrinsic value of shares.(b) What will be your answer if, all other facts remaining unchanged, entries are to be made at par.

Ans (a) PC = 350000-95000 = 255000

Intrinsic value of share of Wye = (750000 -150000)/5000 = Rs.120

No. of shares of Wye to be issued = 255000 / 120 = 2125

Journal of Wye

Business purchase a/c Dr. 255000

To Liquidator of Zee

S. assets a/c Dr.350000
To Cr. 95000
To Business purchase 255000

Liquidator a/c Dr. 255000
To ESC 212500
To Sec. Premium a/c 42500

Books of Zee

Realization a/c

S. assets	350000	Crs.	95000
Investment	100000	Wye	255000
Shareholders a/c (profit)	20000	Shareholders a/c (1000 shares of Wye)	120000
Total	470000	Total	470000

Shareholders a/c

Realization a/c (1000 shares of Wye)	120000	ESC	300000
Shares of Wye (2125 shares of Wye)	255000	Reserve	55000
		Realisation a/c (profit)	20000
Total	375000	Total	375000

(b) Entries at par :

Net assets :

S. assets 350000
Crs. -95000

255000

Intrinsic value of share of Wye : 120

No. of shares to be issued= 255000/120 = 2125

PC = 2125 shares of Rs. 100 each i.e. 212500

Journal of Wye

Business purchase a/c Dr. 212500
To Liquidator of Zee

S. assets a/c Dr.350000
To Cr. 95000
To Business purchase 212500
To Cap. Reserve 42500

Liquidator a/c Dr. 212500
To ESC 212500

Books of Zee

Realization a/c

S. assets	350000	Crs.	95000
Investment	100000	Wye	212500
		Shareholders a/c (1000 shares of Wye)	100000
		Shareholders a/c (Loss)	42500
Total	450000	Total	450000

Shareholders a/c

Realization a/c (1000 shares of Wye)	100000	ESC	300000
Shares of Wye (2125 shares of Wye)	212500	Reserve	55000
Realization a/c (loss)	42500		
Total	355000	Total	355000

Question No. 9

Balance sheets of *X Ltd.* and *Y Ltd.* as on 31.12.1987 are given below:

	X	*Y*		*X*	*Y*
Share Capital (Rs. 10 each)	4,00,000	2,00,000	S .Assets	6,00,000	3,40,000
9% Debentures	—	1,00,000	5,000 shares of *X Ltd.*	—	50,000
Reserve	1,00,000	40,000			
Creditors	1,00,000	50,000			
	6,00,000	3,90,000		6,00,000	3,90,000

X Ltd. to take over *Y Ltd.* on the following terms (a) For each share of *Y Ltd.*, *X Ltd.* will issue its one share of Rs. 10 at Rs. 11 and pay cash 50 paise, (b) *X Ltd.* to issue such an amount of fully paid 10 per cent debentures at 90 as it sufficient to discharge 9 per cent debentures of *Y Ltd.* at a premium of 8 per cent. Give Journal of *X.* Also give Realization account and Shareholders A/c in the books of *Y Ltd.*

Question No. 10

A Ltd. has acquired, as a current asset, 60,000 shares in *B Ltd.* for Rs. 60,000 on 1st November, 1964. On 1st January, 1966 it agreed to absorb *B Ltd.* the consideration being :

(i) The assumption of its liabilities;

(ii) The discharge of the Rs. 40,000 debentures held outside the company at a premium of 10 per cent by the issue of 6½ per cent. Debentures in *A Ltd.* carrying a full six months interest payable 1st July, 1966;

(iii) A payment in case of Re. 0.50 per share in *B Ltd.*; and

(iv) The issue of shares of Re. 1 each in *A Ltd.* credited as fully paid to the members of *B Ltd.* on the basis of:

Two equity shares (valued at Rs. 1.60 each) and one 7½ cumulative preference share (valued at Rs. 1.10) for every five shares in *B Ltd.*

The summarized balance sheet of *B Ltd.* as on 31st December, 1965 was as follows:

	Rs.		*Rs.*
Share Capital:		Fixed Assets	73,000
1,60,000 shares of Re. 1		Stocks	85,800
each Re. 0.75 paid	1,20,000	Debtors	45,000
General Reserve	75,000	*Investments:*	
Profit & Loss A/c	21,550	On account of	
Insurance Funds*	10,000	Insurance Fund	10,000
5% Debentures	45,000	General Rs. 5000	
Creditors	17,800	5% Debentures	
		in *B Ltd.*	4,800
		Bank Balance	50,750
		Goodwill	20,000
	2,89,350		2,89,350

* The company had been carrying its own insurance risk crediting amounts equivalent to premium to the fund and charging losses thereof.

It was agreed that for absorption purposes, 5 per cent should be written off stocks and provision of 2½ per cent made for doubtful debts. The remaining assets, other than goodwill, are considered to be properly valued for the purpose of absorption.

Before passing entries in respect of the absorption, *A Ltd.* decided to revalue shares in *B Ltd.* on the same basis as that of the absorption.

The absorption was completed on 1st March, 1966 by the issue of necessary shares and debentures in *A Ltd.* and payment of cash *B Ltd.* was thereupon wound up. Expenses amounted to Rs. 750 and were paid by *A Ltd.* Prepare Ledger of *B* and Journal of *A*.

Question No. 11

Assuming the Strong Ltd. purchased 10 per cent shares of Weak Ltd. for Rs. 18,000 sometime before it took over the business of Weak Ltd. revise your answer to Q. No. 2.

Question No. 12

The following balance sheets are given as on 31st March, 1976:

(Rs. in lakhs)

	Best Ltd.	*Better Ltd.*		*Best Ltd.*	*Better Ltd.*
Share Capital			Fixed Assets	25	15
Share of Rs.100			Investment	5	—
each fully paid	20	10	Current Assets	20	5
Reserve &					
Surpluses	10	8			
Liabilities	20	2			
	50	20		50	20

The following further information are given:

(a) Investment of Best Ltd. includes Rs. 3 lakhs representing shares in Better Ltd. having a face value of Rs. 2 lakhs.

(b) Better Ltd. issued Bonus on 1st April 1976, in the ratio of one share for every two held, out of ‘Reserves and Surplus’.

(c) It was agreed that Best Ltd. will take over the business of Better Ltd., on the basis of the Better's balance sheet, the consideration taking the form of allotment of Shares in Best Ltd.

(d) The value of the shares in Best Ltd. was considered to be Rs. 150, and the shares in Better Ltd., were valued at Rs. 100 after the issue of the bonus shares. The allotment of shares is to be made on the basis of these values.

(e) Liabilities of Better Ltd., included Rs. 1 lakh due to Best Ltd. for purchase from it, on which Best Ltd. made a profit of 25 per cent on the cost. Rs. 50,000 out of the said purchases, remained in stock on the date of the above balance sheet.

Make the closing ledger entries in the books of Better Ltd. and the opening journal entries in the books of Best Ltd. and prepare the balance sheet as at 1st April, 1976, after the take over.

Ans. **Journal of Best**

Business Purchase a/c Dr. 1500000
To Liquidator of Better

Liquidator of Better Dr. 1500000
To Investment a/c………300000
To ESC ……………800000
To S. Prem. ……………400000

FA ………………………Dr. 1500000
CA………………………Dr. 500000
To Liabilities 200000
To Business purchase …………….1500000
To Capital reserve ………………….300000

Liabilities a/c ………….Dr.100000
To CA ………..100000

Capital reserve a/c ………..Dr.10000
To Stock………………………10000

Books of Better

Realization A/c

FA	1500000	Liabilities	200000
CA	500000	Best Ltd	1500000
		Shareholders a/c (Loss)	300000
Total	2000000	Total	2000000

Best Ltd.

Realisation a/c	1500000	E. shares of Best	1200000
		Shareholders a/c	300000
Total	1500000	Total	1500000

Shareholders a/c

Realization a/c	300000	ESC	1500000
Best Ltd	300000	Reserve &Surplus	300000
To E. Shares of Best	1200000		
Total	1800000	Total	1800000

Question No. 13

Following are the summarised balance sheets of two companies *P Ltd.* and *N Ltd.* as on 31st December, 1975:

Balance Sheet of P Ltd. and N Ltd. as on 31.12.1975

Liabilities	*P Ltd.* *Rs.*	*N Ltd.* *Rs.*	*Assets*	*P Ltd.* *Rs.*	*N. Ltd.* *Rs.*
Share capital: (Shares of Rs. 10 each)	5,00,000	1,80,000	Shares in *P Ltd.* (10,000)	—	1,00,000
Reserves	1,45,000	—	Shares in *N Ltd.* (4,500)	30,000	
Debentures	—	2,00,000	Debentures in *N Ltd.*	1,00,000	
Trade Creditors	3,00,000	2,00,000	Sundry Assets	8,15,000	4,60,000
			P&L A/c	—	20,000
	9,45,000	5,80,000		9,45,000	5,80,000

The two companies agreed that *P* should take over *N Ltd.* The debenture holders in *N Ltd.* agreed to convert the debentures into 9 per cent redeemable preference shares of Rs. 100 each. Prior to the absorption *P Ltd.* declared a

dividend of 20 per cent the dividend had not yet been paid. Shareholders in *N Ltd.* were to receive share in *P Ltd.* on the basis of the intrinsic value of the shares. The sundry assets of *N Ltd.* had to be written up by Rs. 40,000 and those of *P Ltd.* reduced by Rs. 15,000. Prepare Ledger of *N* and Journal of *P*.

Question No. 14

The following are the balance sheets of *A Ltd.* and *B Ltd.* as on 31.12.1987:

Liabilities	*A*	*B*	*Assets*	*A*	*B*
ESC (Rs. 10)	5,00,000	2,00,000	Fixed Assets	6,00,000	3,50,000
10% PSC (Rs. 100)	1,00,000	1,00,000	4,000 shares in *B*	60,000	—
Reserves & Surplus	2,00,000	1,50,000	3,000 Shares in *A*	—	80,000
12% Deb.	1,00,000	1,00,000	Stock	3,00,000	1,70,000
Creditors	3,40,000	1,60,000	Debtors	1,60,000	90,000
B/P	20,000	20,000	B/R	50,000	10,000
			Bank	90,000	30,000
	12,60,000	7,30,000		12,60,000	7,30,000

Contingent liability for bills discounted 20,000

Fixed assets of both companies are to be revalued at 20 per cent above book value. Both companies pay 10 per cent equity dividend, preference dividend having already been paid.

After the above transactions are given effect to, *A Ltd.* will absorb *B Ltd.* on the basis of following terms:

1. 6 equity shares of Rs. 10 will be issued by *A Ltd.* at par against 5 shares of *B Ltd.*
2. 10 per cent preference shareholders of *B Ltd.* will be paid at 10 per cent discount by issue of 11 per cent preference shares of Rs. 100 each at par in *A Ltd.*
3. Rs. 20,000 is to be paid by *A Ltd.* to *B Ltd.* for liquidation expenses.

Bills receivable discounted by *A Ltd.* were all accepted by *B Ltd.* Creditors of *B Ltd.* include Rs. 30,000 due to *A Ltd.*

Give Journal of *A Ltd.* Also give Equity shareholders A/c, *A Ltd.* A/c and Realisation A/c in the books of *B Ltd.*

Ans. **Journal of A**

Fixed Assets a/c Dr. 120000

To Cap. Reserve

Capital Reserve a/c Dr. 12000

To Investment a/c 12000

P & L a/c Dr. 50000
To Dividend Declared a/c

Dividend declared a/c Dr. 50000
To Bank

Bank a/c Dr. 4000
To Dividend

Dividend a/c Dr. 4000
To P & L a/c

Business Purchase a/c ….Dr. 300000
To Liquidator a/c ……….300000

Liquidator a/c …….Dr. 300000
To Investment 48000
To Pref. share capital 90000
To E. share capital 162000

FA a/c Dr. 420000
Stock a/c Dr.170000
Drs. a/c Dr. 90000
B/R a/c Dr. 10000
Bank a/c Dr. 13000
To Debentures 100000
To Crs. 160000
To Bills payable 20000
To Capital Reserve 123000
To Business purchase 3,00,000

Crs. a/c……………..Dr. 30000
To Drs. a/c

Goodwill a/c Dr 20000
To bank

Books of B Ltd

Realization a/c

FA	420000	B/P	20000
Stock	170000	Crs.	160000
Drs.	90000	Deb.	100000

B/R	10000	A Ltd.	300000
Bank	13000	Shareholders a/c(3000 shares of A Ltd.)	30000
Investment	80000	Shareholders a/c (Loss)	173000
TOTAL	783000	Total	783000

A Ltd.'s a/c

To Realization a/c	300000	E. Shareholders	48000
		E . shares of A Ltd	162000
		P. shares of A Ltd	90000
Total	300000	Total	300000

Pref. shareholders a/c

P. shares of A Ltd	90000	PSC	100000
Equity shareholders a/c	10000		
Total	100000	Total	100000

E. Shareholders a/c

A Ltd.	48000	ESC	200000
E. shares of A Ltd (16200 E. shares of A)	162000	R & S*	203000
Realization a/c (3000 E. shares of A)	30000	Pref. Shareholders a/c	10000
Realization a/c (loss)	173000		
Total	413000	Total	413000

* R& S (given in B/S) 150000
Div. paid -20000
Div, Received +3000
Revaluation of +70000
203000

Question No. 15

Gloria and Swanson Ltd. had to pass the hands of a receiver for debenture holders who held charge on all assets except uncalled capital. The following is the position as prepared by the receiver:

	Rs.
Share Capital	
20,000 shares of Rs. 50 each fully paid up	10,00,000
1,00,000 shares of Rs. 50 each, Rs. 25 per share paid up	25,00,000
First Debentures	25,00,000
Second Debentures	50,00,000
Unsecured Creditors	40,00,000
Bank Balance	30,00,000
Building, Plant and Machinery (estimated to realise Rs. 15,00,000)	40,00,000

The following is the interest of Gloria and Swanson in the company:

	Gloria *Rs.*	*Swanson* *Rs.*
First Debentures	20,00,000	5,00,000
Second Debentures	30,00,000	20,00,000
Unsecured Creditors	6,00,000	9,00,000
	56,00,000	34,00,000
Share Capital:		
Fully paid shares	5,00,000	5,00,000
Partly paid shares	10,00,000	10,00,000

The following scheme of reconstruction is proposed:

1. Gloria is to cancel Rs. 31,00,000 of his total debt, pay cash Rs. 5,00,000 and he would be issued Rs. 30,00,000 first debentures in lieu of first and second debentures to be cancelled.
2. (a) Swanson is to cancel his total debt by accepting Rs. 5,00,000 in cash and Rs. 5,00,000 in first debentures.

   (b) Swanson is to surrender for cancellation Rs. 5,00,000 worth of fully paid up shares.
3. Unsecured creditors, other than Gloria and Swanson, agree to reduce their debt by 20 per cent and accept in lieu thereof, 1,00,000 shares of Rs. 10 each fully paid up and the balance in cash payable in five equal annual installments.
4. Uncalled capital is to be called up in full and Rs. 40 per share to be cancelled, thus marking all shares of Rs. 10 each.

Assuming the scheme is duly approved by all parties interested and by the court, show the reconstructed. Balance sheet and the journal entries in the books of the company.

Question No. 16

Balance sheet of Rundown Ltd. as on 31.12.1993.

Liabilities	*Rs.*	*Assets*	*Rs.*
Authorised Issues and Subscribed Capital:		Goodwill	50,000
30,000 Equity shares of Rs. 10 each	3,00,000	Plant	3,00,000
2,000, 8% Cumulative Preference shares of 100 each fully paid	2,00,000	Loose Tools	10,000
Share Premium	90,000	Debtors	2,50,000
Unsecured Loan (From Director)	50,000	Stocks	1,50,000
Sundry Creditors	3,00,000	Cash	10,000
Outstanding Expenses (including Directors) remuneration 20,000)	70,000	Bank	35,000
		Preliminary Exp.	5,000
		Profit & Loss A/c	2,00,000
	10,10,000		10,10,000

Note : Dividends on cumulative preference shares are in arrears for 3 years.

The following scheme of reconstruction has been agreed upon and duly approved by the court:

1. Equity shares to be converted into 1,50,000 shares of Rs. 2 each.
2. Equity shareholders to surrender to the company 90 per cent of their holding.
3. Preference shareholders agree to forego their right to arrears to dividends. 8 per cent preference shares are to be converted into 9 per cent preference shares.
4. Sundry creditors agree to reduce their claim by one-fifth in consideration of their getting shares of Rs. 35,000 out of the surrendered equity shares.
5. Directors agree to forego loan and remuneration.
6. Surrendered shares not otherwise utilized to be cancelled.
7. Assets to be reduced as under :

Goodwill by	Rs.50,000
Plant by	Rs.40,000
Tools by	Rs.8,000
S/Debtors by	Rs.15,000
Stock by	Rs.20,000

8. Any surplus after meeting the losses should be utilized in writing down the value of the plant further.
9. Expenses of reconstruction amounted to Rs. 10,000.

10. Further 50,000 equity shares were issued to the existing members for increasing the working capital. The issue was fully subscribed and paid up.
11. Authorised capital was suitably increased.

You are required to pass the journal entries for giving effect to the above arrangement and also to draw up the resultant balance sheet of the company.

Ans. Journal of Run Ltd.

(1) ESC a/c Dr. 300000
To Rs.2 ESC

---

(2) Shares surrendered a/c Dr. 270000
To Capital reduction a/c

---

(3) 8 % PSC a/c Dr. 200000
To 9% PSC a/c

---

(4) Crs. a/c Dr. 60000
To Shares surrendered a/c 35000
To capital reduction a/c 25000

---

(5) O/S Exp. a/c Dr. 20000
Unsec. Loan a/c Dr. 50000
To capital reduction a/c

---

(6) Rs.2 ESC a/c Dr. 235000
To Shares surrendered a/c

---

(7) Reconstruction exp. a/c Dr. 10000
to Bank a/c

---

(8) Capital reduction a/c Dr.
To P & L 200000
To P . Exp 5000
To Recons. Exp 10000
To goodwill 50000
To tools 8000
To stock 20000
To Plant 57000 (balancing figure)

---

(9)Bank a/c Dr. 50000x10
To ESC

Q.No. 17 Illustration 1 Study Material AX BX page 2.60
Q.No. 18 Illustration 2 Study Material Long Ltd
Q.No. 19 Illustration 4 Study Material AX TX
Q.No. 20 Illustration 8 Study Material Smith
Q.No. 21 Illustration 9 Study Material Batliboi
Q.No. 22 Illustration 10 Study Material Rich
Q.No. 23 Illustration 11 Study Material Pooh
Q.No. 24 Illustration 12 Study Material A Ltd
Q.No. 25 Illustration 14 Study Material M Ltd.

ACCOUNTING FOR AMALGAMATION AS-14

The term amalgamation for the purpose of AS-14 includes both amalgamation and absorption. There are two conditions for an arrangement to called as amalgamation as per this accounting standard : (i) there is blending of at least two companies and (ii) at least one company goes into liquidation. AS-14 has segregated amalgamation into two broad categories :

(i) Amalgamation in the nature of merger

(ii) Amalgamation in the nature of purchase.

Amalgamation is termed as amalgamation in the nature merger if all of the following five conditions are satisfied :

- The transferee[28] company intends to carry on the business , of the transferor[29] company, after amalgamation.
- After amalgamation, all the assets and liabilities of the transferor company become the assets and liabilities of the transferee company
- Shareholders holding 90 % or more[30] of the face value of equity shares of the transferor (immediately before the transfer) become shareholders of the transferee company by virtue of amalgamation. (For the purpose of this provision, those shares of transferor which were held be transferee or its nominees just immediately before the amalgamation, are not considered). For example, A Ltd. absorbs B Ltd. B Ltd.'s share capital consists of 10,00.000 equity shares of Rs. 10 each. 20% of equity shares of B Ltd, are held by A Ltd. As per this condition, the shareholders (other than A Ltd.) holding at least 72000 shares should become the shareholders of A Ltd after the absorption.

---

[28] Purchasing company
[29] vendor company
[30] The remaining shareholders may be dissenting shareholders.

- Those shareholders of the transferor company who become shareholders of the transferee company should get their consideration by way of equity shares of transferee company (except that on account of fractional shares payment may be made in cash).
- The assets and liabilities should be carried in the books of the transferee at book values of transferor (except that some adjustment may be made for following the uniform accounting policies)

An amalgamation which is not in the nature of merger, is termed as amalgamation in the nature of purchase.

Purchase consideration : PC is what is being paid by the purchasing company to the liquidator of the vendor company for the shareholders of the vendor company.

Accounting for merger is termed as pooling of interest method.

- Under this method, the assets, liabilities and items of reserve and surplus are recognized in the books of transferee at their book values. (The balance of P & L A/c of the transferor is aggregated with the corresponding balance of the transferee company or transferred to general reserve.)
- If the transferor and transferee have been following different accounting policies, uniform policies should be followed after amalgamation. The effects on the financial statements of changes in accounting policies should be reported as per AS-5.
- The difference between the amount recorded as share capital issued (plus any additional consideration)[31] and the amount of share capital of the transferor should be adjusted in the reserves.

Accounting for purchase method :

---

[31] Amount recorded as share capital issued means an amount equal to " No. of shares s issued X issue price". The underlined clause refers to purchase consideration.

- The assets and liabilities, which have been taken over, should be recorded in the books of transferee company at their fair values (if not known, at their book values).
- Difference between "PC and amount at which the net assets are recorded in the books" should be identified as goodwill or capital reserve if any. Goodwill should be amortized over not more than 5 years unless a somewhat longer period can be justified.
- The statutory reserves should be taken over by debiting the Amalgamation Adjustment A/c. This reserve should be shown in the B/S under the heading "Misc. Expenditure". When the maintenance of such reserves is no longer statutorily required, the amount of such reserves should be credited to "Misc. expenditure a/c".

Disclosure

- The following disclosures are required for all the amalgamations :

(I) names and general nature[32] of businesses of transferor companies

(II) effective date of amalgamation

(III) the method of accounting for amalgamation

(IV) particulars of any scheme sanctioned under statute (if any)

- In case of merger :

  (I) description and number of shares issued together with percentage of equity shares of each company exchanged by virtue of amalgamation.

[32] For example retail business, wholesale business, manufacturing business. service providers etc

(II) The amount of any difference between the consideration and the value of net identifiable assets acquired, and the treatment thereof.

- In case of amalgamation in the nature pf purchase :

(I) consideration for amalgamation and description of consideration paid or payable

(II) The amount of any difference between the consideration and the value of net identifiable assets acquired, and the treatment thereof. Treatment of amortization of goodwill to be disclosed.

TEST PAPER-I

Q.No.1)

On April 1, 1980 A Limited paid Rs. 1,10,000 for 90% of the issued capital of B Limited. The assets and liabilities of the two companies as at March 31, 1981 were as follows –

	A Limited Rs.	B Limited Rs.
Fixed Assets	94,000	96,000
Current Assets	30,000	18,000
Investment-at cost	1,56,000	--
Goodwill	20,000	6,000
	3,00,000	**1,20,000**
Issued Shares Capital-(Re. 1 each fully paid)	1,80,000	60,000
General Reserve-April 1, 1980	45,000	20,000
Profit and Loss Account-March 31, 1981	36,000	20,500
Current Liabilities	39,000	9,500
6% Debentures-held by A Limited	--	10,000
	3,00,000	**1,20,000**

(1) On April 1, 1980 the opening credit balance of A Ltd's Profit and Loss Account was Rs. 26,000. Out of this balance, a 10% Dividend was paid subsequently.
(2) The Profit and Loss Account of B Limited showed the following:-

		Rs.
Balance of b/f on April 1, 1980		22,000
Net Profit for the year ended March 31, 1981		12,000
		34,000
Less Dividend Paid-	Rs.	
Final for the year ended March 31, 1980	9,000	
Interim for the half-year ended September 30, 1980	4,500	
		13,500
Balance c/f on March 31, 1981		**20,500**

(3) Included in the stock-trade of B Limited at balance sheet date were goods purchased from A Limited for Rs. 6,000 on which there was a profit of 50% on cost of A Limited.
(4) All Dividends received by A Limited have been correctly recorded in the books of account.

Prepared a Consolidated Balance Sheet as at March 31, 1981 and show your workings.
(CA FINAL) (25 marks) MAY 1981

Q.No.2)
The following are the Balance Sheet of H Limited and S Limited as on 31st March, 1984:-

Liabilities	H Ltd. Rs.	S Ltd. Rs.
Share Capital:		
Equity Shares of Rs. 100 each	10,00,000	7,00,000
Reserve and Surplus:		
General Reserve	2,00,000	3,00,000
Profit and Loss Account	3,00,000	3,00,000
Current Liabilities	5,00,000	9,00,000
	20,00,000	**22,00,000**
Assets:		
Fixed Assets	8,00,000	9,00,000
Investment in S Limited	5,00,000	---
Current Assets	7,00,000	13,00,000
	20,00,000	**22,00,000**

The following further information is furnished:
(1) H Limited acquired 3,000 shares in S Ltd. on 1.4.83 when the Reserve and surplus position of S Limited was as under:
    (a) General Reserve Rs. 5,00,000
    (b) Profit and Loss Account (credit balance) Rs. 2,00,000
(2) On 1.10.83 S Limited issued 2 shares for every 5 shares held, as bonus shares at a face value of Rs. 100 per share. No entry is made, in the books of H Limited for the receipt of these bonus shares.
(3) On 30.6.83 S Limited declared a dividend, out of pre-acquisition profits, of 20% and H Ltd. credited the receipt of dividend to its profit and loss account.
(4) S Limited owed H Limited Rs. 1,20,000 for purchase of stock from H Limited. The entire stock is held by S Limited on 31.3.84.
    H Ltd. made a profit of 20% on cost.
(5) H Limited transferred a machine to S Ltd. for Rs. 1,00,000. The book value of machine to H Limited was Rs. 75,000.
    Prepare Consolidated Balance Sheet as at 31st March, 1984.

(CA FINAL) (20 marks) NOV. 1989

Q.No.3)

A Ltd. acquired 8,000 shares of Rs. 10 each in Omega Ltd on 31st December, 1994. The summarized Balance Sheet of the two companies as on that date were as follows:

Liabilities	A Ltd.	Omega Ltd.
Share Capital		
30,000 Shares of Rs. 10 each	3,00,000	---
10,000 Shares of Rs. 10 each	---	1,00,000
Capital Reserve	---	52,000
General Reserve	25,000	5,000
Profit & Loss Account	38,200	18,000
Loan from Omega Ltd.	2,100	---
Bills Payable (including Rs. 500 to A Ltd.)	---	1,700
Creditors	17,900	5,000
Note on the Balance Sheet of A Ltd. : There is a contingent liability for bills discounted of Rs. 1000.		
	3,83,200	**1,81,700**
Assets		
Fixed Assets	1,50,000	1,44,700
Investment in Omega Ltd. at cost	1,70,000	---
Stock in hand	40,000	20,000
Loan to A Ltd.	---	2,000
Bills Receivable (including Rs. 200 from Omega Ltd.)	1,200	---
Debtors	20,000	10,000
Banks	2,000	5,000
	3,83,200	**1,81,700**

You are given the following information:

(a) Omega Ltd. made a bonus issue on 31st December, 1994 of one share for every two shares held, reducing the capital reserve equivalently, but the transaction is not shown in the above Balance Sheets.

(b) Interest receivable (Rs. 100) in respect of the loan due by A Ltd. to Omega Ltd. has not been credited in the accounts of Omega Ltd.

(c) The directors decided that the fixed assets of Omega Ltd. were over-valued and should be written down by Rs. 5,000.

Prepare the Consolidated Balance Sheet as at 31st December 1994, showing your workings.

(CA FINAL) (15 marks) (MAY, 1995)

Q.No.4)

A Ltd. acquired 8,000 shares of Rs. 100 each in B Ltd. on 30th September 1991. The summarized balance Sheets of the two companies as on 31st March 1992 were as follows:

	A Ltd. Rs.	B Ltd. Rs.
Share Capital: 30,000 Shares of Rs. 100 each	30,00,000	
10,000 Shares of Rs. 100 each		10,00,000
Capital Reserve	---	5,50,000
General Reserve	3,00,000	50,000
Profit and Loss Account	3,82,000	1,80,000
Loan from B Ltd.	21,000	---
Bills Payable (including Rs. 5,000 to A Ltd.)	---	17,000
Creditors	1,79,000	70,000
Note: On the Balance Sheet of A Ltd.: There is a contingent liability for bills discounted of Rs. 6000		
	38,82,000	**18,67,000**
Fixed Assets	15,00,000	14,47,000
Investment in B Ltd. as cost	17,00,000	---
Stock in hand	4,00,000	2,00,000
Loan to A Ltd.	---	20,000
Bills Receivable (including Rs. 5,000 from B Ltd.)	12,000	---
Debtors	2,50,000	1,80,000
Cash and Bank balance	20,000	20,000
	38,82,200	**18,67,000**

You are given the following information:

(1) B Ltd. made a bonus issue on 31st March 1992 of one share for every two shares held, reducing the Capital Reserve equivalently but the accounting effect to this has not been given in the above Balance Sheet.

(2) Interest receivable for the year (Rs. 1,000) in respect of the loan due by A Ltd. to B Ltd. has not been credited in the books of B Ltd.

(3) The credit balance in Profit and Loss Account of B Ltd. as on 1.4.1991 was Rs. 21,000.

(4) The directors decided on the date of acquisition the fixed assets of B Ltd. were over-valued and should be written down by Rs. 50,000. Consequential adjustments on depreciation is to be ignored.

Prepared the Consolidated Balance Sheet as at 31st March 1992 showing your working.
(CA FINAL) (15 marks) (May, 1992)

Q.No.5)

The Balance Sheets of Sun Ltd. and Moon Ltd. as on 31.3.2000 are given below:

Liabilities	Sun Ltd Rs.	Moon Ltd. Rs.	Assets	Sun Ltd. Rs.	Moon Ltd. Rs.
Share Capital (Rs. 10)	1,20,000	1,00,000	Fixed Assets	44,000	84,000
General Reserve	20,0000	36,000	Investment in Moon Ltd 8000 shares	88,000	-----
Profit and Loss A/c	12,000	20,000	Sundry Debtors	6,000	15,000
Bills Payable	2,000	5,000	Bills Receivable	4,000	16,000
Sundry Creditors	4,000	7,000	Stock in Trade	10,000	40,000
			Cash in Bank	6,000	13,000
	1,58,000	**1,68,000**		**1,58,000**	**1,68,000**

Contingent liabilities of SUN LTD.: Bills discounted , not yet matured Rs. 2,500.

Shares were purchased on 1.4.1997. When the shares were purchased, General Reserve & Profit and Loss Account of Moon Ltd. stood at Rs. 30,000 and Rs. 16,000 respectively. Dividends have been paid @ 10% every year after acquisition of shares, first dividend being paid out of pre-acquisition profits. No dividend has been proposed for 1999-2000 as yet and no provision need be made in consolidated Balance Sheet. Sun Ltd. has credited all dividend received to Profit and Loss Account.

On 31.3.2000, Bonus shares has been decided by Moon Ltd. @ 1 fully paid share for 5 held, but no effect has been given to that in the above accounts. The Bonus was declared out of profits earned prior to 1.4.1997 from General Reserve.

When the shares were purchased, agreed evaluations of Fixed Assets of Moon Ltd. was Rs. 1,08,000 although no effect has been given thereto in accounts.

Depreciation has been charged @ 10% p.a. on the book value as on 1.4.1997, (on straight line method), there being no addition or sale since then.

Out of Current Profits Rs. 2,000 has been transferred to general reserve ever year. Bills receivable of Sun Ltd. include Rs. 2,000 bills accepted by Moon Ltd. and bills

discounted by Sun Ltd., but not yet matured include Rs. 1,500 accepted by Moon Ltd. Sundry creditors of Sun Ltd. include Rs. 2,000 due to Moon Ltd. whereas Sundry Debtors of Moon Ltd. include Rs. 4,000 due from Sun Ltd. It is found that Sun Ltd has remitted a cheque of Rs. 2,000 which has not yet been received by Moon Ltd.

Prepare Consolidated Balance Sheet as at 31.3.2000 of Sun Ltd. and its subsidiary.
(MAY 2000) 20 marks (CA FINAL)

TEST PAPER-II

Q.No.6) Study Mat Illustration. 8. A Ltd. acquired 70%
(Holding Company Chapter)

Q.No.7) Study Mat. Illustration. 21. Investment Ltd. (Holding Company Chapter)

Q.No.8) X Ltd. purchased its raw materials from Y Ltd. and sells goods to Z Ltd. In order to ensure regular supply of raw materials and patronage for finished goods, X Ltd. through its wholly owned subsidiary, X Investment Ltd. acquired on 31st December, 1996, 51% of equity capital of Y Ltd. for Rs. 15 crores and 76% of equity capital of Z Ltd. for 30 crores. X Investment Ltd. was floated by X Ltd. in 1990 from which date it was wholly owned by X Ltd.

The following are the Balance Sheet of the four companies as on 31st December, 1996.

(Rs. In crores)	X Ltd. Rs.		X Investment Ltd. Rs.		Y Ltd. Rs.		Z Ltd. Rs.	
Share Capital:								
Equity (fully Paid) Rs. 10 each	25		5		10		15	
Reserves and Surplus	75	100	20	25	15	25	20	35
Loan Funds:								
Secured	15		---		5		20	
Unsecured	10	25	50	50	10	15	15	35
Total Sources		**125**		**75**		**40**		**70**
Fixed Assets: Cost	60		---		15		30	
Less: Depreciation	35	25	---	---	7	8	17	13
Investment at cost in Fully paid Equity Shares of:								
X Investment Ltd.		5		---		---		---
Y Ltd.		---		15		---		---
Z Ltd.		---		30		---		---
Other Companies (Market Value Rs. 116 Cr.)		---		29		---		---
Net Current Assets:								
Current Assets	105		1		96		200	
Current Liabilities	10	95	---	1	64	32	143	57
Total		**125**		**75**		**40**		**70**

There are no inter-company transaction outstanding between the companies.

You are asked to prepare consolidated balance sheet as at 31st December, 1996.
(Part of Q. No. 1) (CA FINAL) (MAY, 97)

Q.No.9)
Following are the Balance Sheets of H Ltd. and S Ltd. as at 31st March, 1990.

Liabilities	H Ltd Rs.	S Ltd. Rs.	Assets	H Ltd. Rs.	S Ltd. Rs.
Equity Share Capital of Rs. 10 each fully paid	6,00,000	1,00,000	Land & Building	2,00,000	1,00,000
General Reserve	50,000	30,000	Machineries	2,80,000	50,000
Profit and Loss A/c	80,000	40,000	7,000 Shares of S Ltd.	1,00,000	---
Sundry Creditors	1,00,000	40,000	Stock	70,000	40,000
Bills Payable	10,000	15,000	Debtors	1,50,000	20,000
			Bills Receivable	10,000	---
			Cash at Bank	30,000	15,000
Total	**8,40,000**	**2,25,000**		**8,40,000**	**2,25,000**

Additional information:

(i) All the Bills Receivable of H Ltd. including those discounted were accepted by S Ltd.

(ii) When 6,000 shares were acquired by H Ltd. in S Ltd., S Ltd. had Rs. 20,000 General Reserve and Rs. 5,000 Credit balance in Profit and Loss Accounts.

(iii) At the time of acquisition of further 1,000 shares by H Ltd., S Ltd. had Rs. 25,000 General Reserve and Rs. 28,000 Credit Balance in Profit and Loss Account from which 20% dividend was paid by S Ltd. and dividend received by H Ltd. on these shares were credited to Profit and Loss Account.

(iv) Stock of S Ltd. include Rs. 20,000 purchased from H Ltd., which has made 25% profit on cost.

(v) Both the Companies has proposed dividend – H Ltd. 10% S Ltd. 15% but no effect has yet been given in the above Balance Sheets.

Prepare Consolidated Balance Sheet as at 31st March, 1990.
(CA FINAL) (20 Marks) NOV 1990

Q.No.10) Illustration.. 18 Study Mat. (Holding Co. Chapter)

TEST PAPER-III

Q.No.11) The following are the Balance Sheet of H Limited and S Limited as on 30th September, 1985:-

Liabilities	H Ltd. Rs.	S Ltd. Rs.
Share Capital:		
Equity Share of Rs. 100 each	5,00,000	2,00,000
12% Preference Shares of Rs. 100 each	1,00,000	50,000
Reserve and Surplus:		
General Reserve	1,00,000	60,000
Profit and Loss Account	1,50,000	90,000
Current Liabilities and Provisions:		
Creditors	60,000	70,000
Income – Tax	70,000	60,000
Total	**9,80,000**	**5,30,000**
Assets:		
Fixed Assets:		
Goodwill	60,000	40,000
Machinery	1,00,000	60,000
Vehicles	1,80,000	70,000
Furniture	50,000	30,000
Shares in S Ltd. at Cost	3,80,000	----------
Current Assets:		
Stock	70,000	1,40,000
Debtors	1,00,000	1,65,000
Bank Balance	40,000	25,000
Total	**9,80,000**	**5,30,000**

The following further information is furnished:-

(i) H Limited acquired 1200 Equity Shares and 400 Preference Shares on 1.10.1984 at a cost of Rs. 2,80,000 and Rs. 1,00,000 respectively.

(ii) The Profit and Loss Account of S Limited had a Credit Balance of Rs. 30,000 as on 1.10.84 and that of General Reserve on that date was Rs. 50,000.

(iii) On 31st December 1984 S Limited declared dividend, out of its pre-acquisition profit, of 12% on its share capital; H Limited credited the receipt of dividend to its profit and Loss Account.

(iv) On 1.4.1985 S Limited issued 1 equity share for every 3 shares held, as bonus shares at a face value of Rs. 100 per share out of its General Reserve. No entry has been made in the books of H Limited for receipt of these bonus shares.

(v) S Limited owed H Limited Rs. 20,000 for purchase of stock from H Limited. The entire stock is held by S Limited on 31.09.1985. H Limited made a profit of 25% on cost.

Prepare a consolidated Balance Sheet as at 30th September 1985.

(CA FINAL) (25 Marks) Nov. 1985

Q.No.12)
The following are the balance sheets of H Ltd., A Ltd. and B Ltd. as on 31.12.1983:-

Liabilities	H Ltd. Rs.	A Ltd. Rs.	B Ltd. Rs.
Shares Capital	10,00,000	2,00,000	1,00,000
Reserves	1,00,000	60,000	60,000
P & L Account	4,00,000	1,20,000	60,000
Creditors	2,00,000	1,20,000	60,000
Bills Payable	---	30,000	---
	17,00,000	**5,30,000**	**2,80,000**
Assets	**Rs.**	**Rs.**	**Rs.**
Sundry Assets	8,00,000	1,20,000	1,00,000
Stock	6,10,000	1,80,000	1,00,000
Debtors	1,30,000	1,70,000	80,000
B/R from A Ltd.	10,000		
Shares in A Ltd.	1,50,000		
Shares in B Ltd.		60,000	
	17,00,000	**5,30,000**	**2,80,000**

H Ltd. purchased 80% of shares in A Ltd. when latter's profit and loss account was Rs. 80,000 and Reserve was Rs. 40,000.
A Ltd. purchased 75% of shares in B Ltd. when latter's profit and loss account was Rs. 40,000 and reserve was Rs. 20,000. Prepare consolidated Balance Sheet of H Ltd. and its subsidiaries A Ltd. and B Ltd. as on 31st December, 1983 together with consolidation schedules.

CA FINAL (25 Marks) MAY 1989

Q.NO.13)
The following is a summary of the Balance Sheet of A Ltd. and its two subsidiaries, Ram Ltd. and Rahim Ltd. as on 31st March, 1991.

	A Ltd. Rs.	Ram Ltd Rs.	Rahim Ltd Rs.
Issued Share Capital:			
Fully paid up Shares of Rs. 10 each	2,00,000	1,60,000	1,00,000
Profit and Loss Account	5,23,500	2,00,100	2,59,400
	7,23,500	**3,60,100**	**3,59,400**
Sundry Assets less Liabilities	5,63,500	2,10,100	3,59,400
10,000 Shares in Ram Ltd. at cost	1,60,000		
90,000 shares of Rahim at cost		1,50,000	
	7,23,500	**3,60,100**	**3,59,400**

When A Ltd. purchased shares in Ram Ltd. on 30th September, 1988, there was a credit balance of Rs. 1,46,500 in the Profit and Loss Account of Ram Ltd. and when Ram Ltd. purchased shares of Rahim Ltd. on 31st March, 1989 there was a credit balance of Rs. 40,000 in the Profit and Loss Account of Rahim Ltd.

Prepare a Consolidated Balance Sheet of the group as on 31st March, 1991, showing your workings. Calculations to be made to the nearest rupee. (Nov. 1991) CA FINAL

Q.No.14)

From the following Balance Sheet of group of companies and the other information provided, draw up the consolidated Balance Sheet as on 31.03.98. Figures given are in Rupees Lakhs:

Balance Sheets as on 31.3.98

	X	Y	Z		X	Y	Z
Share capital (in shares of Rs. 100 each)	300	200	100	Fixed assets less depreciation	130	150	100
Reserves	50	40	30	Cost of Investment in Y Ltd.	180	-	-
Profit & Loss Balance	60	50	40	Cost of Investment in Z Ltd.	40	-	-
				Cost of Investment in Z Ltd.	-	80	-
Bills payable	10	-	5	Stock	50	20	20
Creditors	30	10	10	Debtors	70	10	20
Y Ltd. balance	-	-	15	Bills receivables	-	10	20
Z Ltd balance	50	-	-	Z Ltd. balance	-	10	-
				X Ltd. balance	-	-	30
				Cash and bank balance	30	20	10
Total	**500**	**300**	**200**	**Total**	**500**	**300**	**200**

- X Ltd. holds 1,60,000 shares and 30,000 shares respectively in Y Ltd. and Z Ltd. , Y Ltd. holds 60,000 shares in Z Ltd. These investments were made on 1.7.97 on which date the position was as follows:

	Y Ltd.	Z Ltd.
Reserves	20	10
Profit & Loss Account	30	16

- In December 1997 Y Ltd. invoiced goods to X Ltd. for Rs. 40 Lakhs at cost plus 25%. The closing stock of X Ltd. includes such goods valued at Rs. 5 lakhs.
- Z Ltd. sold to Y Ltd. an equipment costing Rs. 24 lakhs at a profit of 25% on selling price on 1.1.98. Depreciation at 10% per annum was provided by Y Ltd. on this equipment.
- Bills payables of Z Ltd. represent acceptance given to Y Ltd. out of which Y Ltd. had discounted bills worth Rs. 3 lakhs.
- Debtors of X Ltd. include Rs. 5 lakhs being the amount due from Y Ltd.
- X Ltd. proposes dividend at 10%. CA FINAL (MAY, 98) (20 marks)

Q.No.15) Study Mat. Illustration. 17 (Holding Company Chapter)

TEST PAPER – IV

Q. No. 16 : On 31st March, 2004, War Ltd purchased 48,000 shares in Peace Ltd at 50% premium over face value by issue of 8% debentures at 20% premium. The balance sheets of War Ltd and Peace Ltd as on 31.3.2004 were as under :

Liabilities	War Ltd. (Rs.)	Peace Ltd. (Rs.)	Assets	War Ltd. (Rs.)	Peace Ltd.(Rs.)
Share capital (Rs.10)	10,50,000	6,00,000	FA	6,50,000	2,00,000
General reserve	1,20,000	40,000	Stock	3,00,000	1,80,000
P & L a/c	80,000	-------	Drs.	3,20,000	2,00,000
Creditors	1,00,000	60,000	Cash	60,000	30,000
			Preliminary exp.	20,000	10,000
			P & L A/C	------	80,000
TOTAL	13,50,000	7,00,000	TOTAL	13,50,000	7,00,000

Particulars of War Ltd. :

(i) Profit made : 2004-05 ……..Rs.1,60,000; 2005-06……….Rs. 2,00,000

(ii) the above profit was made after charging depreciation of Rs. 60000 and Rs. 40000 respectively.

(iii) Out of profit shown above, every year Rs.20000 had been transferred to general reserve.

(iv) 10% dividend had been paid in both the years.

(v) it has been decided to write down investment to face value of shares in 10 years and to provide for share of loss to subsidiary.

Particulars of Peace Ltd. : The company incurred losses of Rs.40,000 and Rs. 60,000 in 2004-05 and 2005-06 after charging depreciation of 10 % on book value as on 1.4.2004.

Prepare consolidated B/S , as at 31.3.2006, of War Ltd and its subsidiary. (Nov.99 CA Final, Dates changed)

Q. No. 17 : Illustration 11 of the Study Material (Holding co. chapter)

Q. No. 18 : Illustration 15 of the Study Material (Holding co. chapter). Prepare Consolidated B/S by Pooling of interest method.

Pooling of interest method of consolidation : three important points:

(i) No distinction is made between revenue profit and capital profit.

(ii) In Consolidated B/S, we take holding co.'s profit + holding company's share in profit (both pre and post acquisition) of subsidiary company.

(iii) Reserve and surplus in the consolidated B/S is adjusted by difference between PC and paid up value of shares acquired.

Q. No. 19 : Illustration 16 of the Study Material (Holding co. chapter)

Q. No. 20 : Illustration 25 of the Study Material (Holding co. chapter)

TEST PAPER-V

Q.No.21) Illustration. 1 study Mat. Page 4.4.

Q.No.22)

Following are the Balance Sheet of Mumbai Limited Delhi, Limited, Amritsar Limited and Kanpur Limited as at 31st December, 2000.

Liabilities	Mumbai Ltd.	Delhi Ltd.	Amritsar Ltd.	Kanpur Ltd.
Share Capital (Rs. 100 face value)	50,00,000	40,00,000	20,00,000	60,00,000
General Reserve	20,00,000	4,00,000	2,50,000	10,00,000
Profit & Loss Account	10,00,000	4,00,000	2,50,000	3,20,000
	3,00,000	1,00,000	50,000	80,000
Total	**83,00,000**	**49,00,000**	**25,50,000**	**74,00,000**
Assets				
Investment:				
30,000 shares in Delhi Ltd.	35,000,00	---	---	---
10,000 shares in Amritsar Ltd.	11,00,000	---	---	---
5,000 shares in Amritsar Ltd.		5,00,000	---	---
Shares in Kanpur Ltd @Rs.120	36,00,000	18,00,000	6,00,000	---
Fixed Assets		20,00,000	15,00,000	70,00,000
Current Assets	1,00,000	6,00,000	4,50,000	4,00,000
Total	**83,00,000**	**49,00,000**	**25,50,000**	**74,00,000**

Balance in General Reserve a/c and P & L a/c, when shares were purchased in different companies were :

	Mumbai Ltd.	Delhi Ltd.	Amritsar Ltd.	Kanpur Ltd.
General Reserve A/c	10,00,000	2,00,000	1,00,000	6,00,000
Profit & Loss A/c	6,00,000	2,00,000	50,000	60,000

Required: Prepare the consolidated Balance Sheet of the group as at 31st December, 2000 (Calculations may be rounded off to nearest rupee). CA FINAL (MAY 2001) (16 Marks)

Q.No.23

Following are the draft Balance Sheets of two companies A Ltd. and B Ltd. as at 31.03.1996:

				(Rs. In Lakhs)	
Liabilities	A Ltd.	B Ltd.	Assets	A Ltd.	B Ltd.
Share Capital Rs.100 each	6.00	3.00	Fixed Assets	5.00	1.50
Capital Profit	0.80	0.85	Investment:		
Revenue Profit	3.20	0.29	2,400 Shares in B Ltd.	3.00	
Crs.	1.50	0.81	1,200 Shares in A Ltd.	---	2.00
			Debtors	2.00	0.80
			Stock	0.40	0.30
			Cash & Bank	1.10	0.35
	11.50	**4.95**		**11.50**	**4.95**

The following adjustment were not yet made:

1. Stock worth Rs. 5,000 in B Ltd. was found to be obsolete with no value.
2. A Ltd. acquired an asset costing Rs. 50,000 on 31.03.96. No effect has been given for both the purchase and payment.
3. During the year A Ltd. sold an asset for Rs. 60,000 (original cost of Rs. 40,000) The profit was included in the revenue profit.
4. Debtors of A Ltd. included a sum of Rs. 50,000 owed by B Ltd.

You are required to prepare the Consolidated Balance Sheet of both the companies as on 31.03.96 after giving effect to the above adjustments. NOV. 96 (CA FINAL)

Q.No.24)

A Limited is a holding company and B Limited and C Limited are subsidiaries of A Limited. Their Balance Sheets as on 31.12.2000 are given below:

	A Ltd. Rs.	B Ltd. Rs.	C Ltd. Rs.		A Ltd. Rs.	B Ltd. Rs.	C Ltd. Rs.
Share Capital	1,00,000	1,00,000	60,000	Fixed Assets	20,000	60,000	43,000
Reserve	48,000	10,000	9,000	Investment			
Profit & Loss Account	16,000	12,000	9,000	Shares in B Ltd.	95,000		
C Ltd. Balance	3,000			Shares in C Ltd.	13,000	53,000	
Sundry Crs.	7,000	5,000		Stock in Trade	12,000		
A Ltd. balance		7,000		B. Ltd. Balance	8,000		
				Sundry Debtors	26,000	21,000	32,000
				A Ltd. Balance			3,000
Total	**1,74,000**	**1,34,000**	**78,000**	**Total**	**1,74,000**	**1,34,000**	**78,000**

The following particulars are given:

(i) The Share Capital of all companies is dividend into shares of Rs. 10 each.
(ii) A Ltd. held 8,000 shares of B Ltd. and 1,000 shares of C Ltd.
(iii) B Ltd. held 4,000 shares of B Ltd.
(iv) All these investments were made on 30.06.2000.
(v) On 31.12.1999, the position was as shown below:

	B Ltd Rs.	C Ltd. Rs.
Reserve	8,000	7,500
Profit & Loss A/c	4,000	3,000
Sundry Creditors	5,000	1,000
Fixed Assets	60,000	43,000
Stock in Trade	4,000	35,500
Sundry Debtors	48,000	33,000

(vi) 10% dividend is proposed by each company.
(vii) The whole of stock in trade of B Ltd. as on 30.06.2000 (Rs. 4,000) was later sold to A Ltd. for Rs. 4,400 and remained unsold by A Ltd. as on 31.12.2000.
(viii) Cash-in-transit from B Ltd. to A Ltd. was Rs. 1,000 as at the close of business.

You are required to prepare the Consolidated Balance Sheet of the group as on 31.12.2000.
CA FINAL (MAY, 2002) (16 Marks)

Q.No.25

The Balance Sheet of Bat Ltd. and Ball Ltd. as on 31.3.2000 are as follows:

	Bat Ltd. Rs.	Ball Ltd. Rs.	Assets	Bat Ltd. Rs.	Ball Ltd. Rs.
Share Capital (Shares of Rs. 10 each)			Investment: Shares in Ball Ltd.	1,96,000	
	1,60,000	2,00,000	Debtors	---	1,20,000
Profit and Loss account			Stock	----	80,000
	50,000	60,000	Cash at Bank	----	70,000
Creditors	---	16,000	Cash in hand	14,000	6,000
	2,10,000	**2,76,000**		**2,10,000**	**2,76,000**

Particulars of Bat Ltd.:

(1) This company was formed on 1.4.99.

(2) It acquired the shares of Ball Ltd. as under:

Date of Acquisition	No. of Shares	Cost
1.4.99	8,000	1,10,000
31.7.99	6,000	86,000

(3) The shares purchased on 31.7.99 are ex-dividend and ex-bonus from existing holders.

(4) On 31.7.99 dividend at 10% was received from Ball Ltd. and was credited to Profit and Loss Account.

(5) On 31.7.99 it received bonus shares from Ball Ltd. in the ratio of one share on every four shares held.

(6) Bat Ltd. incurred on expenditure of Rs. 500 per month on behalf of Ball Ltd. and this was debited to the Profit and Loss account of Bat Ltd., but nothing has been done in the books of Ball Ltd.

(7) The balance in the Profit and Loss account as on 31.3.2000 included Rs. 36,000 being the net profit made during the year.

(8) Dividend proposed for 1999-2000 at 10% was not provided for as yet.

Particulars of Ball Ltd.:

(1) The balance in the Profit and Loss account as on 31.3.2000 is after the issue of bonus shares made on 31.7.99.

(2) The net profit made during the year is Rs. 24,000 including Rs. 6,000 received from insurance company in settlement of the claim towards loss of stock by fire on 30.6.99 (Cost Rs. 10,800 included in opening stock).

(3) Dividend proposed for 1999-2000 at 10% was not provided for in the accounts.

Prepare the Consolidated Balance Sheet of Bat Ltd. as on 31.3.2000. (16 marks)(Nov. 2000 CA FINAL)

TEST PAPER-VI

Q.No.26)

The Summarized Balance Sheet of A Limited and B Limited are as follows:

Balance Sheets as at 31st December, 2000

	A Ltd. Rs.	B Ltd. Rs.
Sources of Funds:		
Share Capital in equity shares of Rs. 10 each	2,00,000	50,000
Reserves	20,000	5,000
Profit and Loss Account as on 1st January,2000	30,000	10,000
Profit for the year Add: Dividends from B Ltd. Less: Dividends paid	8,000 4,0000 ---	8,000 --- (5,000)
Creditors	30,000	20,000
Total	**2,92,000**	**88,000**
Application of Funds:		
Fixed Assets	2,00,000	80,000
Current Assets	32,000	8,000
Shares in B Ltd. At cost – 3,000 shares	60,000	---
Total	**2,92,000**	**88,000**

A Limited had acquired 4,000 shares in B Limited at Rs. 20 each on 1st January, 2000 and sold 1,000 of them at the same price on 1st October, 2000. The sale is cum dividend. An interim dividend of 10% was paid by B Limited on 1st July, 2000.

Draft the consolidated Balance Sheet as at 31st December, 2000.

(Nov. 2001 CA FINAL)

Q.No.27)

On 31st March, 2002, the Balance Sheets of H Ltd. And S Ltd. Stood as follows:

	H Ltd. Rs.	S Ltd. Rs.
Liabilities:		
Equity Share Capital – Authorised	5,000	3,000
Issued and subscribed in Equity Shares of Rs. 10 each fully paid	4,000	2,400
General Reserve	928	690
Profit and Loss Account	1,305	810
Bills Payable	124	80
Sundry Creditors	487	427
Provision for Taxation	220	180
Other Provisions	65	17
	7,129	**4,604**
Assets.		
Plant and Machinery	2,541	2,450
Furniture and Fittings	615	298
Investment in the Equity Shares of S Ltd.	1,500	---
Stock	983	786
Debtors	700	683
Bills Receivables	120	95
Cash and Bank Balances	410	102
Sundry Advances	260	190
	7,129	**4,604**

Following Additional Information is available:

(a) H Ltd. purchased 90 thousand Equity Shares in S Ltd. on 1st April, 2001 at which date the following balances stood in the books of S Ltd.
General Reserve Rs. 1,500 thousand; Profit and Loss Account Rs. 633 thousand.

(b) On 14th July, 2001 S Ltd. declared a dividend of 20% out of pre-acquisition profits and paid corporate dividend tax (including surcharge) at 11%. H Ltd. credited the dividend received to its Profit and Loss Account.

(c) On 1st November, 2001 S Ltd., issued 3 fully paid Equity Shares of Rs.10 each, for every 5 shares held as bonus shares out of pre-acquisition General Reserve.

(d) On 31st March, 2002, the stock of S Ltd. included goods purchased for Rs.50 thousand from H Ltd., which had made a profit of 25% on Cost. Prepare a consolidated Balance Sheet as on 31st March, 2002. (Nov. 2002 CA FINAL)

Q.No.28)

On 31st March, 1996, P Ltd. acquired 1,05,000 shares of Q Ltd. for Rs. 12,00,000. The Balance Sheet of Q Ltd. on that date was as under:

Liabilities:	Rs.	Assets	Rs.
1,50,000 equity shares of Rs.10 each fully paid	15,00,000	Fixed Assets Current Assets	10,50,000 6,45,000
Pre-incorporation profits	30,000		
Profit and Loss Account	60,000		
Creditors	1,05,000		
	16,95,000		**16,95,000**

On 31st March, 2002 the Balance Sheets of two companies were as follows:

	P Ltd. Rs.	Q Ltd. Rs.		P Ltd. Rs.	Q Ltd. Rs.
Equity shares of			Fixed Assets	79,20,000	23,10,000
Rs. 10 each fully			1,05,000 equity		
paid. (before			Shares in Q Ltd.		
bonus issue)	45,00,000	15,00,000	At cost	12,00,000	---
Securities premium	9,00,000	---	Current Assets	44,10,000	17,55,000
Pre-incorporation					
profits	---	30,000			
General Reserve	60,00,000	19,05,000			
profits and Loss					
Account	15,75,000	4,20,000			
Creditors	5,55,000	2,10,000			
	1,35,30,000	**40,65,000**		**1,35,30,000**	**40,65,000**

Directors of Q Ltd. made bonus issue on 31.3.2002 in the ratio of one equity share of Rs. 10 each fully paid for every two equity shares held on that date.

Calculate as on 31st March, 2002 (i) Cost of Control/Capital Reserve; (ii) Minority Interest; (iii) Consolidated Profit and Loss Account in each of the following cases: (i)Before issue of bonus shares. (ii) Immediately after issue of bonus shares. It may be assumed that bonus shares were issued out of post-acquisition profits by using General Reserve. Prepare a Consolidated Balance Sheet after the bonus issue. (May, 2003 CA)

Q.No.29)

The following are the summarised Balance Sheets of PD Co. Ltd. and SD Co. Ltd. as on 31.3.2004:

Liabilities	PD Co. Ltd.Rs.	SD Co. Ltd. Rs.
Share Capital:	70,00,000	30,00,000
Authorised		
Issued and Subscribed Capital		
Equity shares of Rs. 10 each		
Fully paid	50,00,000	20,00,000
Capital Reserve	5,00,000	3,10,000
Revenue Reserve	8,50,000	75,000
Profit and Loss Account	4,00,000	2,80,000
Sundry Creditors	2,50,000	2,25,000
Bills Payable	1,00,000	10,000
	71,00,000	**29,00,000**
Assets:		
Land and Buildings	20,00,000	15,20,000
Plant and Machinery	20,00,000	8,00,000
Furniture	5,00,000	1,60,000
Investments	16,10,000	---
Stock	3,40,000	1,00,000
Sundry Debtors	3,60,000	2,00,000
Bills Receivable	50,000	40,000
Bank	2,40,000	80,000
	71,00,000	**29,00,000**

PD Ltd. acquired 80% shares of SD Ltd. on 30.9.2003 at a cost of Rs. 18,10,000. On 1.10.03 SD Ltd. declared and paid dividend on Equity shares. PD Ltd. appropriately adjust its shares of dividend in Investment Account.

On 1.4.03, the Capital reserve and Profit and Loss Account stood in the books of SD Ltd. at Rs. 50,000 and Rs. 2,75,000 respectively.

Land and Buildings standing in the books of SD Ltd. at Rs. 16,00,000 on 1.4.03, revalued at Rs. 20,00,000 on 1.10.03. Furniture, which stood in the books at Rs. 2,00,000 on 1.4.03 revalued at Rs. 1,50,000 on 1.10.03. In both the cases the effects have not yet been given in the books.

SD Ltd. bought an item of machinery from PD Ltd. on hire-purchase basis. The following are the balances in respect of this machinery in the books on 31.03.04:

	Rs.
Installment due	20,000
Installment not due	8,000
Hire-purchase stock reserve	1,600

The above item stood included under appropriate heads in Balance Sheet.

Prepare a Consolidated Balance Sheet of PD Ltd. and its subsidiary SD Ltd. as at 31.03.2004, Complying with the requirements of AS-21(Nov. 2004 CA FINAL)

Q.No.30)
The Balance Sheets of Football Ltd. and its subsidiary Hockey Ltd. as on 31st March, 2005 are as under:

Liabilities	Football Ltd. Rs.	Hockey Ltd. Rs.	Assets	Football Ltd. Rs.	Hockey Ltd. Rs.
Equity shares of			Goodwill	4,50,000	3,00,000
Rs. 10 each	48,00,000	20,00,000	Plant & Mach.	12,00,000	5,00,000
10% preference shares of Rs. 10 each	7,00,000	3,80,000	Motor vehicles	9,50,000	7,50,000
General reserve	5,50,000	4,20,000	Furniture &		
P/L A/c	10,00,000	6,00,000	fittings	6,50,000	4,00,000
Bank overdraft	1,20,000	70,000	Investments	26,00,000	4,50,000
Sundry creditors	4,30,000	4,80,000	Stock	4,50,000	7,20,000
Bills payable	---	1,60,000	Cash at bank	2,25,000	2,10,000
			Debtors	9,30,000	7,80,000
			Bills receivable	1,45,000	---
	76,00,000	**41,10,000**		**76,00,000**	**41,10,000**

Details of acquisition of shares by Football Ltd. are as under:

Nature of shares	Nos. acquired	Date of acquisition	Cost of acquisition Rs.
Preference shares	14,250	1.4.2002	3,10,000
Equity shares	80,000	1.4.2003	9,50,000
Equity shares	70,000	1.4.2004	8,00,000

Other information :

(i) On 1.4.2004 Profit and Loss Account and general of Hockey Ltd. had credit balances Rs. 3,00,000 and Rs. 2,00,000 respectively.

(ii) Dividend @10% was paid by Hockey Ltd. for the year 2003-04 out of its P/L balance as on 1.4.2004. Football Ltd. credited its share of dividend to its P/L A/c.

(iii) Hockey Ltd. allotted bonus shares out of general reserve at the rate of 1 share for every 10 shares held. Accounting thereof has not yet been made.

(iv) Bills receivable of Football Ltd. were drawn upon Hockey Ltd.

(v) During the year 2004-05 Football Ltd. purchased goods from Hockey Ltd. of Rs. 1,00,000 at a sale price of Rs. 1,20,000. 40% of these goods remained unsold at close of the year.

(vi) On 1.4.2004 motor vehicles of Hockey Ltd. were overvalued by Rs. 1,00,000. Applicable depreciation rate is 20%.

(vii) Dividends recommended for the year 2004-05 in the holding and the subsidiary companies are 15% and 10% respectively.

Prepare consolidated Balance Sheet as on 31st March, 2005. (May 2005 CA FINAL)

TEST PAPER-VII

Q.No.31) STUDY MATERIAL ILLUSTRATION 3 KUBER LTD. PAGE 2.123

Q.No.32)

The following is the Balance Sheet of Alpha Limited as at 31st December, 1988:-

Liabilities	Rs.	Assets	Rs.
Share Capital:		Fixed Assets:	
Equity shares of		Land and building	4,00,000
Rs. 100 each 10,00,000		Machinery	4,50,000
Less calls in		Motorcar	25,000
arrear (Rs.20		Furniture	25,000
for final call) 1,00,000	9,00,000	Investment (face value)	50,000
Reserve and Surplus:		Current Assets:	
General Reserve	3,50,000	Stock	7,25,000
Profit and Loss Account	2,50,000	Sundry debtors	2,00,000
Current Liabilities:		Cash in Bank	1,05,000
Sundry Creditors	5,00,000	Miscellaneous	
		Expenditure:	
		Preliminary Exp.	20,000
	20,00,000		**20,00,000**

Additional information is as under:-

(1) Fixed Assets are worth:-
    Building Rs. 6,00,000
    Machinery Rs. 5,20,000

(2) All investments are non-trading investments and are to be valued at 20% above cost Dividend at uniform rate of 20% is earned on all investments.

(3) For the purpose of valuation of shares, goodwill is to be valued on the basis of 3 years purchase of super profits based on average profit (after tax) of the last three years.

(4) Depreciation on appreciated value of Land and Building and Machinery is not to be considered for valuation of goodwill.

(5) Profits (after tax) are as follows:

	Rs.
1986	3,80,000
1987	4,20,000
1988	5,00,000

Income-tax 50%. In similar business, return on capital employed is 20% (after tax).

(6) In 1986 machinery (Book value Rs. 20,000) was sold for Rs. 20,000 but the proceeds were wrongly credited to profit and loss account. The mistake has not yet been rectified. Depreciation has been charged on machinery @ 10% per annum on reducing balance method.

Find out the value of each fully paid and partly paid equity share on net assets basis. Note: Trend in profit is to be ignored for the purpose of calculation of average profit.

(CA FINAL) (March 15) MAY 1989

Q.No.33)

Balance Sheet of Major Ltd. as on 31st December, 1982:-

Liabilities	Rs.	Assets	Rs.
Share Capital:		Fixed Assets:	
Equity Shares of		Goodwill	50,000
Rs. 10 each 5,00,000		Machinery	2,30,000
Less:		Factory Shed	3,00,000
Call in arrear		Vehicles	60,000
(Rs. 2 on final call) 10,000	4,90,000	Furniture	25,000
8% preference Share of Rs. 10 each		Investments	1,00,000
Fully paid	2,00,000	Current Assets:	
Reserve and Surplus:		Stock in Trade:	2,10,000
General Reserve	2,00,000	Sundry Debtors	3,50,000
Profit and Loss Account	1,40,000	Cash at Bank	50,000
Current Liabilities:		Preliminary Exp.	25,000
Bank Loan	1,00,000		
Sundry Creditors	2,70,000		
	14,00,000		**14,00,000**

Additional Information:

(1) Fixed Assets are worth 20% above their actual book value, Depreciation on appreciated value of fixed assets to be ignored for valuation of goodwill.

(2) Of the investments, 80% is non – trade and the balance is trade. All trade investments are to be valued at 20% below cost. A uniform rate of dividend of 10% is earned on all investment.

(3) For the purpose of valuation of shares, Goodwill is to be considered on the basis of 4 yeas purchase of the super-profits based on average profit of the last 3 years.
Profit are as follow:

	Rs.
1980	1,90,000
1981	2,00,000
1982	2,10,000

In similar business return on capital employed is 15%. In 1980 new furniture costing Rs. 10,000 was purchased but wrongly charged to revenue. (No effect has yet been given for rectifying the same). Depreciation is charged on furniture @ 10%. Find out the value of each fully paid and party-paid equity share. (CA FINAL) (20 Marks) NOV. 1983

Q.No.34)

Below is given the Balance Sheet of Devta of Ltd. as at 31st December, 1981.

Liabilities		Rs.	Assets	Rs.
Share Capital:			Fixed Assets:	
Equity Shares of			Goodwill	20,000
Rs. 10 each	2,00,000		Machinery	1,10,000
Less calls in arrear			Land & Building	1,20,000
(Rs.2 for final call)	5,000	1,95,000	Furniture & Fixtures	60,000
6% preference Shares	1,00,000		Vehicles	80,000
(Rs. 10 each)			Investments	80,000
Less calls in arrear			Current Assets:	
(Rs.2 for final call)	1,000	99,000	Stock and Trade	55,000
Reserve and Surplus:			Sundry Debtors	90,000
General Reserve		80,000	Cash and Bank	10,000
Profit and Loss Account		16,000	Preliminary Exp.	10,000
Current Liabilities				
Bank Loan		60,000		
Bills Payable		30,000		
Sundry Creditors		1,55,000		
		6,35,000		**6,35,000**

Additional Information:-

(1) For the Purpose of valuation of shares, Goodwill is to be considered on the basis of 2 years' purchase of the super profits based on average profit of last 4 years.
Profits are as follows:-

1978	Rs. 80,000	1980	Rs. 1,05,000
1979	Rs. 90,000	1981	Rs. 1,10,000

(2) In a similar business normal return on capital employed in 15%.

(3) Fixed assets are worth 30% above their actual book value. Stock is over-valued by Rs. 5,000. Debtors are to be reduced by Rs. 1,000. All investment are to be valued at 10% below cost.

(4) Of the investment, 10% is trade and the balance non-trade. Trade investments were purchased on 1.1.1981. 50% of the non-trade investments were acquired on 1.1.80 and the rest on 1.1.79. A uniform rate of dividend of 10% is earned on all investments.

The following further information is relevant:

(1) In 1979 a new machinery costing Rs. 10,000 was purchased but wrongly charged to revenue. (No Rectification has yet been made for above).
(2) In 1980 some old furniture (Book value Rs. 5,000) was disposed of for Rs. 3,000/-
You are required to value each fully paid and partly paid equity share. (Depreciation is charged on machinery @ 10% on reducing system. Ignore Taxation and Dividend). (CA FINAL)(20 marks) MAY 1982

Q.No.35)
The Balance Sheets of X Ltd. are as follows:

		(Rs. In lakhs)
Liabilities	As at 31.3.96	As at 31.3.97
Share Capital	1,000.0	1,000.0
General Reserve	800.0	850.0
Profit and Loss Account	120.0	175.0
Term Loans	370.0	330.0
Sundry Creditors	70.0	90.0
Provision for Tax	22.5	25.0
Proposed Dividend	200.0	250.0
	2,582.5	**2,720.0**
Assets		
Fixed Assets and Investments (Non-trade)	1,600.0	1,800.0
Stock	550.0	600.0
Debtors	340.0	220.0
Cash and Bank	92.5	100.0
	2,582.5	**2,720.0**

Other Information:

1. Current cost of fixed assets excluding non-trade investment on 31.3.96 Rs. 2,200 lakhs and on 31.3.97 Rs. 2,532.8 lakhs.
2. Current cost of stock on 31.3.96 Rs. 670 lakhs and on 31.3.97 Rs. 750 lakhs.
3. Non-trade investments in 10% government securities Rs. 490 lakhs.
4. Debtors include foreign exchange debtors amounting to $ 70,000 recorded at the rate of $ 1 = Rs. 17.50, but the closing exchange rate was $ 1 = Rs. 21.50.
5. Creditors include foreign exchange creditors amounting to $ 1,20,000 recorded at the rate of $ 1 = Rs. 16.50, but the closing exchange rate was $ 1 = Rs. 21.50.
6. Profit included Rs. 120 lakhs being government subsidy which is not likely to recur.
7. Rs. 247 lakhs being the last installment of R and D cost were written off the profit and loss account. This expenditure is not likely to recur.
8. Tax rate during 96-97 was 50%, effective future tax rate is estimated at 40%.
9. Normal rate of return is expected at 15%.

Based on the information furnished, Mr. Iral, a director, contends that the company does not have any goodwill. Examine his contention. (CA FINAL (NOV. 97) (20 marks)

TEST PAPER- VIII

Q.No.36)
The Balance Sheet of Hari Private Ltd. disclose the following position on 31st December 1994.

	Rs.		Rs.
Share Capital		Land and Building	3,00,000
Subscribed:		Plant and Machinery	4,00,000
20,000 5% preference share of		Stock	2,00,000
Rs. 10 each fully paid	2,00,000	Sundry Debtors	2,00,000
30,000 ordinary shares of		Cash at Bank	1,00,000
Rs. 10 each fully paid	3,00,000		
	5,00,000		
General Reserve	2,00,000		
Profit & Loss A/c.	50,000		
Trade Creditors	4,50,000		
	12,00,000		12,00,000

It is proposed to convert Hari Private Ltd. into a public limited company and for this purpose you are asked to value the goodwill of Hari Private Ltd.

The following additional information is supplied to you:

(a) Hari Private was incorporated on 1st January, 1986 and its first accounts were made upto 31st December, 1986.
(b) It manufactures abrasive materials involving technical skill and it has engaged two foreign experts since 1986.
(c) No provision for taxation is required.
(d) The fixed assets of the company have been adequately depreciated.
(e) The present market value of its Land and Building is Rs. 5,00,000 and of Plant and Machinery Rs. 6,00,000.
(f) The profits and losses of the company for the last 3 years after charging depreciation and taxation, have been as follows:

	Rs.
1992	1,01,000
1993	1,50,000
1994	1,69,000

(g) The sales of the company during last 3 year were Rs. 12,99,000 Rs. 13,77,000 and Rs. 18,22,000.

The reasonable return on capital invested in the class of business carried on by Hari Private Ltd. is 10 per cent.

It may be assumed that the company will able to maintain its profits for the next few years on the same level as in the past. Whatever appropriate, you may make further suitable assumptions. All workings should from part of your answer.

(CA FINAL) (15 marks) (May, 1995)

Q.No.37)
STRONG Ltd. have approached you for valuation of their shares in the context of their forthcoming share issue. The company was incorporated on 1.4.1991.
The following information is extracted from their annual reports for the last 3 years.

	(Rs. Lakhs) Year ended 31st March		
	1992	1993	1994
Gross Fixed Assets	200	700	750
Accumulated Depreciation	20	80	150
Net Current Assets	300	600	750
Loans Cr.	nil	500	400
Share Capital			
Equity Shares of Rs. 10 each	400	500	500
Profit before tax	20	60	120
Preliminary Expenses C/F	30	20	10

It is understood that the company has implemented a major project in 1993 which has started yielding results in 1993-94.

Practices of merchant bankers indicate that an average of values based on net assets and on yield is normally adopted in such cases. The normal industry expectation of yield is 15%. Tax rate is 40%.

You are required to compute the value of the client company's equity shares on the basis of the above information showing workings as necessary. (CA FINAL) (NOV. 94)

Q.No.38) Illustration 22 Pages 3.72 Study Material

Q.No.39) Illustration 18 Study Material Page 3.63

Q.No.40) Illustration 19 Study Material Page 3.67

TEST PAPER-IX

Q.No.41) Illustration 13 Study Material Page 3.37
Q.No.42) Illustration 15 Study Material Page 3.43
Q.No.43) Illustration 16 Study Material Page 3.45
Q.No.44) Illustration 17 Study Material Page 3.62
Q.No.45)
Yogesh Ltd. showed the following performance over 5 years ended 31st March, 1997:

Ended 31st March	* Net Profit before tax Rs.		Prior period adjustment Rs.	Remarks
1993	4,00,000		(-)1,00,000	Relating to 1991-92
1994	3,50,000		(-)2,50,000	Relating equally to 1991-92 and 1992-93
1995	6,50,000		(+)1,50,000	Relating to 1993-94
1996	5,50,000		(-)1,75,000	Relating to 1993-94
1997	6,00,000		(-)1,00,000	Relating to 1993-94
			(+) 25,000	Relating to 1995-96

* Net profit before tax is after debiting or crediting the figures of loss (-) or Gains (+) mentioned under the columns for prior period adjustments.

The net worth of the business as per the balance sheet of 31st March, 1992 is Rs. 6,00,000 backed by 10,000 fully paid equity shares of Rs. 10 each. Reserves and surplus constitution the balance net worth. Yogesh Ltd. has not declared any dividend till date.

You are asked to value equity shares on:

(a) Yield basis as on 31.3.1997. Assuming:
(i) 40% rate of tax.
(ii) anticipate after tax yield of 20%.
(iii) Differential weightage of 1 to 5 being given for the five years starting on 1.4.1992 for the actual profits of the respective years.

(b) Net asset basis as per corrected balance sheet for each of the six years ended 31.3.1997.
Looking to the performance of the company over the 5 years period, would you invest in the company? (CA FINAL) (MAY, 97) (15 marks).

Q.No.46)

On the basis of the following information, calculate the value of goodwill of Gee Ltd. at three years' purchase of super profits, if any, earned by the company in the previous four completed accounting years.

Balance Sheet of Gee Ltd. as at 31st March, 2004

Liabilities	Rs. In Lakhs	Assets	Rs. In Lakhs
Share Capital:		Goodwill	310
5 crore equity shares		Land and buildings	1,850
of Rs. 10 each, fully paid up	5,000	Machinery	3,760
Capital Reserve	260	Furniture and Fixtures	1,015
General Reserve	2,543	Patents and Trade Marks	32
Profit & Loss		9% Non-trading Investments	600
(appropriation) A/c	477	Stock	873
Trade Creditors	568	Debtors	614
Provision for Taxation (net)	22	Cash in hand and at Bank	546
Proposed Dividend for 2002-2003	750	Preliminary Expenses	20
Total	9,620	Total	9,620

The profits before tax for the four years have been as follows:

Year ended 31st March	Profit before tax in lakhs of Rupees
2000	3,190
2001	2,500
2002	3,108
2003	2,900

The rate of income tax for the accounting year 1999-2000 was 40%. Thereafter it has been 38% for all the years so far. But for the accounting year 2003-2004 it will be 35%.

In the accounting year 1999-2000, the company earned an extraordinary income of Rs. 1 crore due to a special foreign contract. In August, 2000 there was an earthquake due to which the company lost property worth Rs. 50 lakhs and the insurance policy did not cover the loss due to earthquake or riots.

9% Non-trading investments appearing in the above mentioned Balance Sheet were purchased at par by the company on 1st April, 2001.

The normal rate of return for the industry in which the company is engaged is 20%. Also note that the company's shareholders, in their general meeting have passed a resolution sanctioning the directors an additional remuneration of Rs. 50 lakh every year beginning from the accounting year 2003-2004. (May, 2004 CA FINAL)

TEST PAPER-X

Q.No.47)

The following balances are extracted from the books of Raj Ltd., a real estate company, on 31st March, 1996: (Rs. 000)

	Dr.	Cr.
Sales		2760
Purchases of Materials	1218	
Share Capital Fully Paid		100
Land Purchased in the Year as Stock	73	
Leasehold Premises	42	
Creditors		463
Debtors	735	
Director's Salaries	39	
Wages	111	
Work in Progress on 01.04.95	210	
Sub-Contractors' Cost	894	
Equipment, Fixtures and Fittings at Cost on 01.04.95	264	
Stock on 01.04.95	59	
Profit and Loss Account, Credit Balance on 01.04.95		128
Secured Loans		112
Interest on Loan and Overdraft	22	
Depreciation on Equipment on 01.04.95		164
Administration Expenses	147	
Office Salaries	18	
Bank over draft		105
	3832	**3832**

You also obtain the following information:

(a) On 31st March, 1996, stock on hand including the land acquired during the year, is valued at Rs. 1,42,000. Work in progress at that date is valued at Rs. 1,40,000.

(b) On 1st October, 1995 the company moved to new premises. The premises are on a 12 years lease and the lease premium paid amounted to Rs. 42,000. The company used sub-contract labour of Rs. 40,000 and materials at cost of Rs. 38,000 in the refurbishment of the premises. These are to be considered as part of the cost of leasehold premises.

(c) A review of the debtors reveals specific doubtful debts of Rs. 35,000 and the directors wish to provide for these together with a general provision based on 2% of the balance.

(d) Depreciation on equipment, fixtures and fittings is provided at 15% on the written down value.

(e) Raj Ltd. sued Bright Ltd. for supplying defective materials which has been written off as valueless. The Directors are confident that Bright Ltd. will agree for settlement of Rs. 50,000.

(f) The directors propose a dividend of 25%.

(g) Rs. 20,000 is to be provided as audit fee.

(h) The company will provide 10% of the pre tax profit as bonus to employees in the accounts before charging the bonus.

(i) Income Tax to be provided at 50% of the profits.

You are required:

(i) to prepare the company's financial statements for the year ended 31st March 1996 as near as possible to proper form of company final accounts, and

(ii) to prepare a set of Notes accounts including significant accounting polices.

Notes:- Workings should form part of your answer.
Previous year figures can be ignored.
Figures are to be rounded off to a nearest thousand.

(CA FINAL) (NOV. 96) (20 Marks)

Q.No.48)

The following information has been extracted from the books of account of Jay Ltd. as at 31st March, 1995.

	Dr. (Rs. '000)	Cr. (Rs. '000)
Administration Expenses	240	
Cash at Bank and on Hand	114	
Cash Received on Sale of Fittings		5
Long Term Loan		35
Investments	100	
Depreciation on Fixtures, Fitting, Tools and Equipment (1st April, 1994)		130
Distribution Costs	51	
Factory Closure Costs	30	
Fixtures, Fittings, Tools and Equipment at Cost	340	
Profit & Loss Account (at 1st April, 1994)		40
Purchase of Equipment	60	
Purchases of Goods for Resale	855	
Sales (net of Excise Duty)		1,500
Share Capital (50,000 shares of Rs. 10 each fully paid)		500
Stock (at 1st April, 1994)	70	
Trade Creditors		40
Trade Debtors	390	
	2,250	**2,250**

Additional Information:

(1) The stock at 31st March, 1995 (valued at the lower of cost or net realizable value) was estimated to worth Rs. 1,00,000.

(2) Fixtures, Fittings, tools and equipments all related to administration. Depreciation is charged at a rate of 20% per annum on cost. A full year's depreciation is charged in the year of acquisition, but no depreciation is charged in the year of disposal.

(3) During the year to 31st March, 1995, the Company purchased Rs. 60,000 of equipment. It also sold some fittings (which had originally cost Rs. 30,000) for Rs. 5,000 and for which depreciation of Rs. 15,000 had been set aside.

(4) The average Income Tax for the Company is 50%. Factory closure cost is to be presumed as an allowable expenditure for Income tax purpose.

(5) The company proposes to pay a dividend of 20% of Equity Shares.

Prepare Jay Ltd.'s Profit & Loss Account for the year to 31st March, 1995 and Balance Sheet as at that date in accordance with the Companies Act, 1956 in the Vertical Form alongwith the Notes on Accounts containing only the significant accounting policies. Details of the schedules are not required.

(CA FINAL) (MAY 96) (20 marks)

Q.No.49)

A Company was incorporated on 1st July, 1991 to take over the business of Mr. M as and from 1st April, 1991. Mr. M's Balance Sheet, as at that date was as under:

Liabilities	Rs.	Assets	Rs.
Trade Creditors	36,000	Building	80,000
Capital	1,94,000	Furniture and Fittings	10,000
		Debtors	90,000
		Stock	30,000
		Bank	20,000
	2,30,000		**2,30,000**

Debtors and Bank balances are to be retained by the vender and creditors are to be paid off by him. Realisation of debtors will be made by the company on a commission of 5% on cash collected. The company is no issue M with 10,000 equity shares of Rs. 10 each, Rs. 8 per share paid up and cash of Rs. 56,000.

The company issued to the public for cash 20,000 equity shares of Rs. 10 each on which by 31st March, 1992 Rs. 8 per share was called and paid up except in the case of 1,000 shares on which the third call of Rs. 2 per share had not been realized. In the case of 2000 shares, the entire face value of the shares had been realized. The share issue was under written for 2% commission, payable in shares fully paid up.

In addition to the balances arising out of the above, the following were shown by the books of accounts of the company on 31st March, 1992.

	Rs.
Discount (including Rs. 1,000 allowed on vendor's debtors)	6,000
Preliminary expenses	10,000
Directors' fees	12,000
Salaries	48,000
Debtors (including vendor's debtors)	1,60,000
Creditors	48,000
Purchases	3,20,000
Sales	4,60,000

Stock on 31st March, 1992 was Rs. 52,000 Depreciation at 10% on Furniture and Fittings and at 5% on Building is to be provided. Collections from debtors belonging to the vendor were Rs. 60,000 in the period.

Kindly prepare the Trading and Profit & Loss Account for the period ended 31st March, 1992 of the limited company and its Balance Sheet as at that date.

(CA FINAL) (MAY 1994 25 Marks)

Q.No.50)

With a view to reducing establishment expenses and generally to effect economy in working Divya Ltd. agreed to take over Pranav Ltd. as going concern, both companies being engaged in the same trade.

Divya Ltd. was to pay the debentures and Liabilities of Pranav Ltd. and take over the assets, the consideration being the issue by Divya Ltd. of 4,00,000 fully paid shares of Rs. 10 each at par and payment of Rs. 3,00,000 in cash to Pranav Ltd. Divya Ltd. was to pay the liquidation expenses, which amounted to Rs. 1,40,000.

The Balance in the Books of the respective companies, as on the date of absorption are given hereunder:

	Assets		Liabilities	
	Divya Ltd. Rs.	Pranav Ltd. Rs.	Divya Ltd. Rs.	Pranav Ltd. Rs.
Authorised Capital				
Issued Capital (Rs.)	---	---	1,50,00,000	50,00,000
Unpaid Calls	50,000	10,000	---	---
10% Debentures	---	---	50,00,000	10,00,000
Land & Building	1,03,33000	35,68,200	---	---
Goodwill	30,00,000	5,00,000	---	---
Sundry Debtors & Crds.	7,24,000	3,98,400	8,34,200	4,36,200
Bank Balances	16,84,200	---	---	2,00,000
Stock	17,92,600	7,85,200	---	---
Plant & Machinery	38,76,800	16,43,900	---	---
Bills Receivable	3,62,100	---	---	---
Profit and Loss a/c Balance	---	---	9,88,500	2,69,500
	2,18,22,700	**69,05,700**	**2,18,22,700**	**69,05,700**

Assume that the absorption was duly effected but that the unpaid calls and a book debt of Rs. 40,000 due to Pranav Ltd. proved irrecoverable.

Prepare the Realisation Account and Member Account in the books of Pranav Ltd. and the Balance Sheet of Divya Ltd. after the absorption. Your working should form part of the answer. (CA FINAL) (15 marks) (Nov., 95)

.No.51)

Ksha Ltd. and Yaa Ltd. are two companies. On 31st March, 1999 their Balance Sheet were as under: (Rs. Crores)

	Ksha Ltd		Yaa Ltd.	
	Rs.	Rs.	Rs.	Rs.
Equity Share Capital of Rs. 10 each fully paid up		300		200
Reserve and surplus:	40		20	
Revenue reserves	700		425	
Surplus	10	750	5	450
Owners' funds		1050		650
Loan funds		250		350
Total Sources		**1300**		**1000**
Funds employed in:				
Fixed assets:				
Cost	1000		700	
Less: Depreciation	400	600	300	400
Net current assets:				
Current assets	2000		1500	
Less: Current liabilities	1300	700	900	600
Total funds		**1300**		**1000**

Ksha Ltd. has 2 divisions-very profitable division A and loss making division B. Yaa Ltd. similarly has 2 division-very profitable division B and loss making division A.

The two companies decided to reorganize. Necessary approvals from creditors and members and sanction by High Court have been obtained to the following scheme:

1. Division B of Ksha Ltd. which has fixed assets costing Rs. 400 crores (written down value Rs. 160 crores), Current assets Rs. 900 crores, Current liabilities Rs. 750 crores and loan funds of Rs. 200 crores is to be transferred at Rs. 125 crores to Yaa Ltd.

2. Division A of Yaa Ltd. which has fixed assets costing Rs. 500 crores (depreciation Rs. 200 crores), Current assets Rs. 800 crores, Current liabilities Rs. 700 crores and loan funds of Rs. 250 crores is to be transferred at Rs. 140 crores to Ksha Ltd.

3. The difference in the two considerations is to be treated as loan carrying interest at 15% per annum.

4. The directors of each of the companies revalued the fixed assets taken over as follows:

(i) Division A of Yaa Ltd. taken over : Rs. 325 crores.
(ii) Division B of Ksha Ltd. taken over : Rs. 200 crores.

All the other assets and liabilities are recorded at the balance sheet values.

(a) The directors of both the companies ask you to prepare the balance sheets after reconstruction (showing the corresponding figures before reconstruction).

(b) Master Richie Rich, who owns 50,000 equity shares of Ksha Ltd. and 30,000 equity shares of Yaa Ltd. wants to know whether he has gained or lost in terms of net asset of equity shares on the above reorganization.

(CA FINAL) (MAY 99) (16+4=20 Marks)

TEST PAPER- XI

Q.No.52)

The following are the Balance Sheets as at 31st December, 1991 of X Ltd. and Y Ltd.

	X	Y		X	Y
Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
Share Capital:			Goodwill	30,000	10,000
Equity Shares of			Machinery	1,50,000	1,00,000
Rs. 10 each	4,00,000	3,00,000	Stock	40,000	72,000
Reserve and surplus	60,000	80,000	Debtors	2,10,000	1,20,000
Creditors	40,000	30,000	Bank	60,000	90,000
			Preliminary Exp.	10,000	18,000
Rs.	5,00,000	4,10,000	Rs.	5,00,000	4,10,000

Goodwill of the companies is to be valued of Rs. 50,000 and Rs. 40,000 respectively Machinery of X is worth Rs 2,00,000 and of Y Rs. 90,000. Stock of Y has been shown at 90% of its cost.

It is decided that X will acquire Y, without liquidating the latter, by taking over its business by issue of shares at the intrinsic value.

You are required to draft the Balance Sheet of the two companies after putting through the scheme. (CA Final) (Nov.92) (15 Marks)

Q.No.53)

It has been decided that PURU Ltd. will absorb the entire undertaking of SHO Ltd. and THAM Ltd. as of 1.4.994. the outside shareholders in the latter companies are to be issued equity shares in PURU Ltd. on the basis of an agreed issued price of Rs.20 per share. For this purpose, the interests of such shareholders are to be determined according to the intrinsic value of the shares of the respective companies. AN Ltd. is a subsidiary of THAM Ltd. and is also to be merged into PURU Ltd. appropriately

The Balance Sheet of the companies as at 31.3.1994, stood as under:

(Rs. Lakhs)

	PURU	SHO	THAM	AN
Sources:				
Shares Capital:				
Equity Shares 10 each	1,500	1,000	800	400
Reserves	2,000	540	702	400
Loans	1,600	900	1,000	700
	5,100	2,440	2,502	1,500
Uses				
Land	200	100	50	10
Building	500	400	100	200
Machinery	1,500	800		
Other Fixed Assets	400	100		
Investments:				
40 lakhs Shares of SHO	500	---	---	---
20 lakhs Shares of THAM	300	---	---	---
40 lakhs Shares of AN	---	---	400	---
Other investments	100	---	---	---
Net Current Assets	1,600	1,040	1,252	740
	5,100	**2,440**	**2,502**	**1,500**

For the purpose of the scheme, it is agreed to give effect to the following value appreciation of the assets of the companies to be absorbed:

Land 100% Building 50% Machinery 20%

In order to obtain the consent of the creditors of THAM Ltd., it becomes necessary to accept a claim of Rs. 20 lakhs hitherto classified as contingent. 60% of the claim is accepted by THAM Ltd. and the balance is to be settled by PURU Ltd.

You are required to:

(i) Compute the number of shares to be issued by PURU Ltd. to eligible outsiders, and

(ii) Show the Balance Sheet of PURU Ltd. after the absorption.

(CA FINAL) (20 marks) (Nov. 1994)

Q.No.54)
The following are the Balance Sheet of Major Ltd. and Minor Ltd. as on 31st December 1985.

Assets	Major Ltd. Rs.	Minor Ltd. Rs.
Fixed Assets : Machinery	1,00,000	50,000
Furniture	20,000	5,000
Investment		
Shares in Minor Ltd.	25,000	
Shares in Major Ltd.		12,000
Assets:		
Stock	75,000	45,000
Debtors	60,000	68,000
Cash at Bank	20,000	20,000
	3,00,000	**2,00,000**

	Rs.	Rs.
Liabilities		
Issued, Subscribed, and Paid up capital		
Equity Shares of Rs. 100		
Each fully paid	2,00,000	1,00,000
Reserve and Surplus:		
Profit & Loss Account	60,000	30,000
Current Liabilities and Provisions:		
Sundry Creditors	40,000	70,000
	3,00,000	**2,00,000**

Major Ltd. holds 200 shares in Minor Ltd. and Minor Ltd. holds 100 shares in Major.
The two companies agree on amalgamation on the following basis:-

(1) A new company is to be formed called Hind Ltd.
(2) The Goodwill is valued for Major Ltd. Rs. 50,000 and for Minor Ltd. Rs. 25,000.
(3) The Shares of Hind Ltd. are of nominal value of Rs. 10 each.

Prepare:

(1) Balance sheet of Hind Ltd. resulting from the merger.
(2) Schedule showing fully the shareholdings therein attributable to share-holders of Major Ltd. and Minor Ltd. All costs of amalgamation are to be ignored.

Q.No.55) Study Material Illustration 1 Page 2.112 (Diverse)

Q.No.56) Study Material Illustration 5 page 4.19 (Variety)

TEST PAPER-XII

Q.No.57)

The Balance Sheet of 'S' Ltd. and 'H' Ltd as on 30th June, 1997 were as follows:

				(Rs. in crores)
Liabilities		'S' Ltd.		'H' Ltd.
Equity Share Capital		80		25
Reserve and Surplus		400		75
10% 25 lakhs Debentures of R. 100 each		---		25
Other Liabilities		120		---
		600		**125**
Assets				
Fixed Assets at cost	200		75	
Less: Depreciation	100	100	50	25
Investment in 'H' Ltd.				
2 crores Equity Shares of Rs. 10				
each at cost	32			
10% 25 lakhs Debentures of Rs.100				
each at cost	24	56		
Current Assets	800		300	
Less: Current Liabilities	356	444	200	100
		600		**125**

In a scheme of absorption duly approved by the court, the assets of 'H' Ltd. were taken over at an agreed value of Rs. 130 crores. The liabilities were taken over at par. Outside shareholders of 'H' Ltd. were allotted equity shares in 'S' Ltd. at a premium of Rs. 90 per share in satisfaction of their claims in 'H' Ltd. Fixed assets taken over from 'H' Ltd. were revalued at Rs. 40 crores.

(a) Give journal entries in the books of 'S' Ltd. to record the transactions.

(b) Show the balance Sheet of 'S' Ltd. after absorption of 'H' Ltd.

CA FINAL (NOV. 97) (15 marks)

Q.No.58)

The Balance Sheet of Sunlight Co. Ltd. on 31st December, 1975 stood as follows:-

Share Capital:		Goodwill at cost	2,00,000
(1) 10,000 7% Cumulative Preference Shares of Rs. 100 each	10,00,000	Plants & Machineries (less depreciation)	18,00,000
		Stock	3,00,000
(2) 20,000 Equity Shares of Rs. 100 each	20,00,000	Debtors	4,50,000
6% Debentures	3,00,000	Preliminary Expenses, Commission, etc.	1,00,000
Sundry Creditors	4,00,000	Cash	1,50,000
Bank Overdraft	3,00,000	Profit & Loss A/c	10,00,000
	40,00,000		**40,00,000**

(Pref. Dividends are in arrear for 2 years.)

The company in the past few years had suffered heavily due to slump and labour unrest but since the last quarter of 1975 finds the conditions turning towards and hopes to earn a revenue profit in future to release a reasonable dividend on equity share if adjusted to a reduced value.

A re-organization was agreed to by all parties concerned and you are requested to frame an external scheme of re-construction taking into consideration the following points of agreement and results of revaluation:-

(1) Creditors to forego Rs. 50,000.
(2) Pref. shareholders to forego their claim for arrears of dividend and if loss to Equity share holders tends to exceed 50% to lower their capital claim by 20% at the maximum by reducing the nominal value in consideration of 9% Dividend effective after re-organization.
(3) Bank to convert the overdraft to a term loan to the extent as would raise the current ratio to 2:1.
(4) Debentures will be exchanged according to the existing terms and denomination.
(5) Works, Plants and Machineries will be revalued at Rs. 15,00,000.
(6) Debtors will be written off by Rs. 50,000 being bad.
(7) Equity shares will be exchanged for the same number of Equity Shares in the new Co. at a reduced denomination as would be warranted in the circumstances.

Your Scheme will show the necessary working re: the total loss and its distribution, the reorganization of Shares and Debentures, the revision of working capital and a Performa Balance Sheet of the new company. (CA FINAL) (20 marks) MAY1981

Q.No.59)

A Ltd. has become sick since a few years. The management feels that the company has recently turned the corner. Balance Sheet of company as at 31st march, 1988 and other relevant particulars are given below:-

Balance Sheet of A Ltd. as at 31st March, 1988

Liabilities	Rs.	Assets	Rs.
Equity share capital of		Land & Building	1,00,000
Rs. 10 fully paid up	6,00,000	Plant & Machinery	2,00,000
6% Preference share		Stock	2,00,000
Capital of Rs. 100		Sundry Debtors	2,00,000
fully paid up	2,00,000	Cash and Bank Balance	30,000
9% Debentures of Rs.300		Profit & Loss A/c	
each fully paid	3,00,000	Debit balance	8,20,000
Trade Creditors	4,00,000		
Expense Creditors	50,000		
	15,50,000		**15,50,000**

I Land and Building are worth Rs. 4,00,000
II Stock and sundry debtors are expected to fetch 20% less.
III Equity shares are to be reduced to Rs. 2.50 each, fully paid up.

IV Preference shares are to be reduced to Rs. 50 each, fully paid up, the rate of preference dividend being raised proportionately.
V Debentures are to be reduced to Rs. 200 each fully paid up the rate of interest being raised proportionately.
VI Trade creditors and expense creditors will wait for payment and continue business on existing terms if 20% of their dues is paid forthwith.
VII Directors are willing to bring in Rs. 1,00,000 in the form of equity capital Rs. 20,000 is estimated expenditure for completing the formalities.

Some of the Directors want to go in for capital reduction and some other prefer external reconstruction.

You are requested to prepare Reconstruction Account, Realization Account and two sets of Balance Sheet as may be appropriate under the above alternative schemes effect to the various indicated above. (CA FINAL)

Q.No.60)

The Balance Sheet as at 31st March, 1992 of Sickness Ltd. was as under:

Liabilities	Rs.	Assets	Rs.	Rs.
Share Capital:		Fixed Assets		
8,000 equity shares of		Goodwill at cost	40,000	
Rs. 100 each, Rs. 50 per		Others	8,50,000	
Share paid up	4,00,000		8,90,000	
4,000 11% cumulative		Less: Depreciation	2,70,000	6,20,000
Preference shares of		Investments		25,000
Rs. 100 each, fully paid up	4,00,000	Stock in Trade		2,10,000
Premium received on		Sundry Debtors		2,55,000
Preference shares	40,000	Cash and Bank		1,00,000
General Reserve	60,000			
Current Liabilities	3,10,000			
	12,10,000			**12,10,000**

Contingent liability not Provided: Preference dividends are in a arrears for three years including the year ended 31st March, 1992

The funds of the Company are sufficient to discharge its liabilities including Preference Dividends in arrears. However, the Company does not want to deplete its resources. It would also like to reflect the values of some of its assets in a realistic manner. The Board of Directors of the Company decided and proposed the following scheme of rehabilitation / reconstruction to be effective from 1st April, 1992.

(i) The cumulative preference shareholders are to be issued, in exchange of their holdings. 13% Debentures of the face value of Rs. 100 each at a premium of 10% Fractional holdings are to be paid off in cash.
(ii) Arrears in preference dividends to be converted into equity shares of Rs. 100, Rs. 50 per share paid up.

(iii) After the issue of the equity shares mentioned in (ii) above, the paid up value of all the equity shares is to be reduced to Rs. 25 each.
(iv) The face value of all the equity shares to be reduced to Rs. 50 each and the balance of the unpaid portion is to be called up fully.
(v) Goodwill has lost its value and has to be written off. Market value of other fixed assets is determined, as at 31st March, 1992, at Rs. 5,00,000.
(vi) Investments have no market value and have to be written off.
(vii) Stock in trade is to be valued at 110% of its book value and Sundry Debtors are to be discounted by 5%.

The scheme, as approved by the Directors, is duly accepted by all authorities and put into effect.

During the working for the half year ended 30th September, 1992, it is noticed that the trading for the period has resulted in an increase of bank balances by Rs. 55,100, Drs. by Rs. 40,000, Crs. by Rs. 26000 and stock reduced by Rs. 8,000. Depreciation for the half year on fixed assets at 10% per annum is to be provided. The increase in the bank balances was prior to the company paying the half yearly interest on the debentures and redeeming one half of the debentures on 30th September, 1992.

From the above information, you are required to prepare the Balance Sheet of Sickness Ltd. as at 30th September 1992.

All working notes, including journal entries, ledger accounts etc. are to form part of your answer. (CA FINAL) (20 marks) (May, 1993)

Q.No.61)

A Ltd. decided to re-organise its structure following a period of adverse trading conditions. The Balance Sheet of the company as on 31st March 1992, showed the following:

	Rs.	Rs.		Rs.	Rs.
Share Capital:			Fixed Assets:		
20,000 8% Cumulative Preference Share of Rs. 10 each		2,00,000	Goodwill		55,000
			Freehold property at cost		60,000
15,000 Equity Shares of Rs. 10 each		1,50,000	Leasehold property at cost	1,40,000	
			Less: Dep.	18,000	1,22,000
Share Premium Account		5,000	Plant & Machinery at cost	2,20,000	
9% Debentures (Secured on Freehold property)	60,000		Less: Dep.	60,000	1,60,000
					3,97,000
			Trade Investment		40,000
Add: Accrued Int.	2,700	62,700	Current Assets:		
Creditors		85,000	Stock	30,000	
Bank Overdraft		96,000	Debtors	60,000	90,000
			Preliminary Exp.		2,500
			Profit & Loss A/c		69,200
		5,98,700			**5,98,700**

Note: Preference Dividends are in arrears for four years.

Subsequent to approved by the Court of a scheme for the reduction of capital, the following steps were taken:

(i) The Preference Share were reduced to Rs. 7.5 per share, and the Equity Shares to Rs. 2.0 per share. After reduction, the shares were consolidated into Rs. 10 shares. The authorized capital was restored to 2,00,000 8% Cumulative Preference Share and Rs. 1,50,000 Equity Shares, both of Rs. 10 each.

(ii) I new Equity hare of Rs. 10 was issued for every Rs. 40 of gross preference dividend in arrears.

(iii) The balance on share premium account was utilized.

(iv) The debenture holders took over the freehold property at an agreed figure of Rs. 75,000 and paid the balance to the company after deducing the amount due to them.

(v) Plant and Machinery was written down to Rs. 1,40,000

(vi) Trade Investment was sold for Rs. 32,000.

(vii) Goodwill, Preliminary Expenses, Debts of Rs. 8,600 and obsolete stock of Rs. 10,000 were written off.

(viii) Contingent liability for which no provision had been made was settled at Rs. 7,000 and of the amount Rs. 6,300 was recovered from the insurers.

(ix) Available cash is deposited in Bank Overdraft account.

You are required: (a) to show the Journal entries necessary to record the above transactions in the company's books, (b) to show Capital Reduction Account and Cash Account and (c) to prepare the Balance Sheet after completion of the scheme.

(CA FINAL) (20 marks) (May, 1992)

TEST PAPER- XIII

Q.No.62) Study Material Illustration 2 Page 2.120 (Enterprise)

Q.No.63)
Hamer Limited and Grace Limited proposed to amalgamate:

Their Balance Sheets as on December 31st 1981 were:

Liabilities	Hamer Ltd. Rs.	Grace Ltd. Rs.	Assets	Hamer Ltd. Rs.	Grace Ltd. Rs.
Share Capital:			Fixed Assets (Less Depreciation)	4,00,000	1,00,000
Equity Share of Rs. 10 each	5,00,000	2,00,000	Investment (Face value Rs. 1,00,000 6% tax free G.P. Notes)	1,00,000	
Reserves and Surplus :					
General Reserve	2,00,000	20,000	Current Assets:		
Profit & Loss Account	1,00,000	30,000	Stock	2,00,000	1,30,000
Current Liabilities Creditors	1,00,000	50,000	Debtors	1,70,000	60,000
			Cash and Bank Balance	30,000	10,000
Total	**9,00,000**	**3,00,000**	**Total**	**9,00,000**	**3,00,000**

Net Profit (after taxation)	Hamer Ltd. Rs.	Grace Ltd. Rs.
1979	1,30,000	45,000
1980	1,25,000	40,000
1981	1,50,000	56,000

Goodwill may be taken as 4 years' purchase of average super profits trading on the basis of 15% normal trading profit on closing Capital invested. The stock of Hamer Ltd. and Grace Ltd. to be taken at Rs. 2,04,000 & Rs. 1,42,000 respectively for the purpose of amalgamation. X Ltd. is formed for the purpose of amalgamation of both the companies.

Advise upon Capitalisation of X Ltd. and suggest a scheme of exchange of shares for that purpose.

Draft of Balance Sheet of X Limited (CA FINAL) (20 marks) (NOV. 1982)

Q.No.64)

XYZ Ltd. was incorporated to take over X Ltd., Y Ltd. and Z Ltd. on the basis of their Balance Sheets as on 31.3.87 subject to the following terms and conditions.

(1) Goodwill is to be valued at three years' purchase of average super profit for three years. Such average is to be calculated after adjustment of depreciation at 10% on the amount increase/decrease on revaluation of fixed assets. Income tax is to be ignored.

(2) Assets are to be revalued.

(3) Normal Profit on capital employed is to be taken at 10%, capital employed being considered on the basis of net revaluation amounts of tangible assets.

(4) Equity Shares of Rs. 10 each fully paid on in XYZ Ltd. are to be distributed in the ratio average profit adjustment of depreciation on revaluation as started in (1) above.

(5) 10% Debentures of Rs. 100 each fully paid-up are to be issued by XYZ Ltd. for the balance due.

(6) Issue of Equity Shares and Debentures for this purpose is to be in the ratio of 3:1.

The summarised Balance Sheet as at 31.3.87 and the relevant information are given below:

Assets	X Ltd. Rs.	Y Ltd. Rs.	Z Ltd. Rs.
Net Tangible Block	8,00,000	6,00,000	5,00,000
Goodwill		50,000	
Current Assets	3,00,000	2,50,000	1,00,000
	11,00,000	9,00,000	6,00,000

Liabilities	X Ltd. Rs.	Y Ltd. Rs.	Z Ltd. Rs.
Equity Share Capital (Rs. 10 each)	6,00,000	7,00,000	3,00,000
Reserves	1,00,000	50,000	1,00,000
10% Debentures	2,00,000		1,00,000
Trade and Expense Creditors	2,00,000	1,50,000	1,00,000
	11,00,000	**9,00,000**	**6,00,000**
Revaluation of Tangible Block	10,00,000	5,00,000	6,00,000
Revaluation of Current Assets	3,50,000	1,40,000	80,000
Average Annual Profit for three years before charging Debenture Interest	1,80,000	1,44,000	78,000

(a) Calculate the number of Equity Shares and Debentures to be issued to each of the companies.

(b) Prepare a Draft Balance Sheet of XYZ Ltd. immediately after amalgamation assuming that amounts required for Preliminary Express (Rs. 50,000) and for payment of the existing Debentures in the two companies at par were provided by the promoters against issue of Equity Shares of Rs. 10 each.

(CA FINAL) NOV. 1987

Q.No.65)

The following are the Balance Sheet of Big Ltd. and Small Ltd. for the year ending on 31st March 1998. (Figure in crores of rupees):

	Big Ltd.	Small Ltd.
Equity share capital-in equity shares of Rs. 10 each Preference share capital-in 10% preference shares of Rs. 100 each	50 -	40 60
Reserves and surplus	200	150
	250	250
Loans-Secured	100	100
	350	**350**
Applied for : fixed assets at cost less depreciation	150	150
Current assets less current liabilities	200	200
	350	**350**

The present worth of fixed assets of Big Ltd. is Rs. 200 crores and that of Small Ltd. is Rs. 429 crores. Goodwill of Big Ltd. is Rs. 40 crores and of Small Ltd. is Rs. 75 crores.

Small Ltd. absorbs Big Ltd. by issuing equity shares at par in such a way that intrinsic net worth is maintained.

Goodwill account is not to appear in the books. Fixed assets are to appear to old figures.

(a) Show the Balance Sheet after absorption.

(b) Draft a statement of valuation of shares on intrinsic value basis and prove the accuracy of your workings. (CA FINAL) (MAY 98) (15 marks)

Q.No.66

AB Ltd. and MB Ltd. decide to amalgamate and to form a new company AM Ltd. The following are their balance sheets as at 31.03.1998.

Liabilities	AB Ltd.	MB Ltd.	Assets	AB Ltd.	MB Ltd.
Share Capital (Rs. 100) each	10,00,000	6,00,000	Fixed Assets	7,50,000	2,00,000
General Reserve	1,00,000	50,000	Investments:		
Investment			1500 Sh. In MB	3,50,000	---
Allow. Reserve	40,000	30,000			
12% Debentures (Rs. 100 each)	3,00,000	1,00,000	4,000 Sh. In AB	---	5,00,000
Sundry Creditors	60,000	20,000	Current Assets	4,00,000	1,00,000
Total	**15,00,000**	**8,00,000**		**15,00,000**	**8,00,000**

Calculate the amount of purchase consideration for AB Ltd. and MB Ltd. and draw up the balance sheet of AM Ltd. after considering the following:

(a) Assume amalgamation is in the nature of purchase.
(b) Fixed assets of AB Ltd. are to be reduced by Rs. 50,000 and that of MB Ltd. are to be taken at Rs. 3,00,000.
(c) 12% debenture holders of AB Ltd. and MB Ltd. are discharged by AM Ltd. by issuing such number of its 15% debentures of Rs. 100 each so as to maintain the same amount of interest.
(d) Shares of AM Ltd. are of Rs. 100 each.

Also show, how the investment allowance reserve will be treated in the Financial Statement assuming the Reserve will be maintained for 3 years.

(CA FINAL) (MAY 99) (16 marks)

TEST PAPER-XIV

Q.No.67)

On 1st Nov., 1998 Yash Ltd. was incorporated with an authorities capital of Rs. 1,000 crores. It issued to its promoters equity capital of Rs. 50 crores which was paid for in full. On that day it purchased the running business of Vijay Ltd. for Rs. 200 crores and allotted at par equity capital of Rs. 200 crores in discharge of the consideration. The net assets taken over from Vijay Ltd. were valued as follows: Fixed assets Rs. 150 crores, Inventory Rs. 10 crores, Customers' dues Rs. 70 crores and Creditors Rs. 30 crores.

Yash Ltd. carried on business and the following information is furnished to you:

(a) Summary of cash/bank transactions (for year ended 31st October, 1999)

	Rs. In Cr.	Rs. In Cr.
Equity capital raised:		
Promoters (as shown above)	50	
Others	250	300
Collections from customers		4,000
Sale proceeds of fixed assets (cost Rs. 18 Cr.)		20
		4,320
Payments to suppliers	2,000	
Payments to employees	700	
Payments to expenses	500	3,200
Investments in Upkar Ltd.		100
Payments to suppliers of fixed assets:		
Instalment due	600	
Interest	50	650
Tax payment		270
Dividend		50
Closing cash/bank balance		50
		4,320

(b) On 31st October, 1999 Yash Ltd.'s assets and liabilities were:

	Rs. In Cr.
Inventory at cost	15
Customers dues	400
Prepaid expenses	10
Advances to suppliers	40
Amounts due to suppliers of goods	260
Amount due to suppliers of fixed assets	750
Outstanding expenses	30

(c) Depreciation for the year under:

(i) Companies Act, 1956 Rs. 180 Cr.

(ii) Income-tax for Act, 1961 Rs. 200 Cr.

(d) Provide for tax at 38.5% of "total income". There are no disallowables for the purpose of income taxation. Provision for tax is to be rounded off. Yash Ltd. asks you to prepare:

(i) Revenue statement for the year ended 31st October, 1999 and
(ii) Balance Sheet as on 31st October, 1999, from the above information.

(Nov. 99 CA FINAL) (20 marks)

Q.No.68)

The summarised Balance Sheets of R Ltd. and P Ltd. for the year ending on 31.3.2000 are as under:

	R Ltd. Rs.	P Ltd. Rs.		R Ltd. Rs.	P Ltd. Rs.
Equity Share Capital (in shares of Rs. 10 each)	24,00,000	12,00,000	Assets : Fixed Assets	55,00,000	27,00,000
8% Preference Share Capital (in shares of Rs. 10 each)	8,00,000		Current Assets	25,00,000	23,00,000
10% Preference Share Capital (in shares Of Rs. 10 each)	---	4,00,000			
Reserves	30,00,000	24,00,000			
Current Liabilities	18,00,000	10,00,000			
	80,00,000	**50,00,000**		**80,00,000**	**50,00,000**

The following information is provided:

	R Ltd. Rs.	P Ltd. Rs.
(1) (a) Profit before tax	10,64,000	4,80,000
(b) Taxation	4,00,000	2,00,000
(c) Preference dividend	64,000	40,000
(d) Equity dividend	2,88,000	1,92,000

(2) The equity shares of both the companies are quoted in the market. Both the companies are carrying on similar manufacturing operations.

(3) R Ltd. proposes to absorb P Ltd. as on 31.3.2000. The terms of absorption are as under:

(a) Preference shareholders of P Ltd. will receive 8% preference shares of R Ltd. sufficient to increase the income of preference shareholder of P Ltd. by 10%.

(b) The equity shareholders of P Ltd. will receive equity shares of R Ltd. on the following basis:

(i) The equity shares of P Ltd. will be valued by applying to the earnings per share of P Ltd. 75% of price earnings ratio of R Ltd. based on the results of 1999-2000 of both the companies.

(ii) The market price of equity shares of R Ltd. is Rs. 40 per share.

(iii) The number of shares to be issued to the equity shareholders of P Ltd. will be based on the above market value.

(iv) In addition to equity shares, 8% preference shares of R Ltd. will be issued to the equity shareholders of P Ltd. to make up for the loss

in income arising from the above exchange of shares based on the dividends for the year 1999-2000.

(4) The assets and liabilities of P Ltd. as on 31.3.2000 are revalued by professional valuer as under:-

	Increased by Rs.	Decreased by Rs.
Fixed Assets	1,00,000	---
Current Assets	---	2,00,000
Current Liabilities	---	40,000

(5) For the next two years, no increase in the rate of equity dividend is expected.

You are required to:

(i) Set out in detail the purchase consideration.

(ii) Give the Balance Sheet as on 31.3.2000 after absorption.

Note: Journal entries are not required. (Nov.2000 CA FINAL)

Q.No.69)

The following are the Balance Sheets of RS Ltd. and XY Ltd. as on 31.3.2002.

Rs. in '000s

Liabilities	RS Ltd. Rs.	XY Ltd. Rs.	Assets	RS Ltd. Rs.	XY Ltd. Rs.
Shares Capital:			Fixed Assets net of depreciation	2,700	850
Equity shares of Rs. 100 each fully paid up	2,000	1,00	Investments	700	---
Reserves and Surplus	800	---	Sundry Debtors	400	150
10% Debentures	500	---	Cash & Bank	250	---
Loan from Financial Institutions	250	400	Profit and Loss Account	---	800
Bank Overdraft	---	100			
Sundry Creditors	300	300			
Proposed Dividend	200	---			
Total	**4,050**	**1,800**	**Total**	**4,050**	**1,800**

It was decided that XY Ltd. will acquire the business of RS Ltd. for enjoying the benefit of carry forward of business loss. After acquisition, XY Ltd. will be renamed as XYZ Ltd. The following scheme has been approved for the merger:

(i) XY Ltd. will reduce its shares to Rs. 10 and then consolidate 10 such shares into one shares of Rs. 100 each (New share).

(ii) Financial institutions agreed to waive 15% of the loan of XY Ltd.

(iii) Shareholders of RS Ltd. will be given one new share of XY Ltd. in exchange of every share held in RS Ltd.

(iv) RS Ltd. will cancel 20% holding of XY Ltd. Investments were held at Rs. 250 thousands.

(v) After merger the proposed dividend of RS Ltd. will be paid to the shareholders of RS Ltd.

(vi) Authorised Capital of XY Ltd. will be raised accordingly to carry out the scheme.

(vii) Sundry creditors of XY Ltd. includes payable of RS Ltd. Rs. 1,00,000. Pass the necessary entries to implement the scheme in the books of RS Ltd. and XY Ltd. and prepare a Balance Sheet of XYZ Ltd.

(MAY 2003 CA FINAL)

Q.No.70)

The Balance Sheet of Z Ltd. as 31st March, 2003 is given below. In it, the respective shares of the company's two divisions namely S Division and W Division in the various assets and liabilities have also been shown.

(All amounts in crores of Rupees)

	S Division	W Division	Total
Fixed Assets:			
Cost	875	249	
Less: Depreciation	360	81	
Written-down value	515	168	683
Investments			97
Net Current assets:			
Current Assets	445	585	
Less: Current Liabilities	270	93	
	175	492	667
			1,447
Financed by:			
Loan funds		15	417
Own Funds:			
Equity share capital: shares of Rs. 10 each			345
Reserves and surplus			685
			1,447

Loan funds included, inter alia, Bank Loans of Rs. 15 crore specifically taken for W division and Debentures of the paid up value of Rs. 125 crore redeemable at any time between 1st October, 2002 and 30th September, 2003.

On 1st April, 2003 the company sold all of its investments for Rs. 102 crore and redeemed all the debentures at par, the cash transactions being recorded in the Bank Account pertaining to S Division.

Then a new company named Y Ltd. was incorporated with an authorized capital of Rs. 900 crore divided into shares of Rs. 10 each. All the assets and liabilities pertaining to W Division were transferred to the newly formed company; Y Ltd. allotting to Z Ltd.'s shareholders its two fully paid equity shares of Rs. 10 each at par for every fully paid equity shares of Rs. 10 each held in Z Ltd. as discharge of consideration for the division taken over.

Y Ltd. recorded in its fixed assets at Rs. 218 crore and all other assets and liabilities at the same values at which they appeared in the books of Z Ltd.

You are required to:

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

(ii) Prepare Z Ltd.'s Balance Sheet immediately after the demerger and the initial Balance Sheet of Y Ltd. (Schedules in both cases need not be prepared).

(iii) Calculate the intrinsic value of one share of Z Ltd. immediately before the demerger and immediately after the demerger; and

(iv) Calculate the gain, if any, per share to the shareholders of Z Ltd. arising out of the demerger. MAY 2004 CA FINAL)

Q.No.71)

ABC Ltd. was incorporated in 1/5/2003 to take over the business of DEF and Co. from 1/1/2003. The Profit and Loss Account as given by ABC Ltd. for the year ending 31/12/2003 is as under:

Profit and Loss Account

	Rs.		Rs.
To Rent and Taxes	90,000	By Gross Profit	10,64,000
To Salaries including Manager's salary of Rs. 85,000	3,31,000	By Interest on Investments	36,000
To Carriage Outwards	14,000		
To Printing and Stationery	18,000		
To Interest on Debentures	25,000		
To Sales Commission	30,800		
To Bad Debts (related to sales)	91,000		
To Underwriting Commission	26,000		
To Preliminary Expenses	28,000		
To Audit Fees	45,000		
To Loss on Sale of Investment	11,200		
To Net Profit	3,90,000		
	11,00,000		**11,00,000**

Prepare a Statement showing allocation of pre-incorporation and post incorporation profits after considering the following information:

(i) G.P. ratio was constant throughout the year.

(ii) Sales for January an October were 1 ½ times the average monthly sales while sales for December were twice the average monthly sales.

(iii) Bad Debts are shown after adjusting a recovery of Rs. 7,000 of Bad Debt for a sale made in July, 2000.

(iv) Manager's salary was increased by Rs. 2,000 pm from 1/5/2003.

(v) All investments were sold in April, 2003.[6] (MAY 2004 CA FINAL)

Q.No.72)

Travels & Tours Ltd. has two divisions – 'Inland' and 'International'. The Balance Sheet as at 31st December, 2004 was as under:

	Inland (Rs. crores)	International (Rs. crores)	Total (Rs. crores)
Fixed Assets:			
Cost	600	600	1,200
Depreciation	500	200	700
W.D.V. (written down value)	100	400	500
Net Current Assets:			
Current assets	400	300	700
Less: Current liabilities	200	200	400
	200	100	300
Total	**300**	**500**	**800**
Financed by:			
Loan Funds			
(Secured by a charge on fixed assets)	---	100	100
Own Funds:			
Equity capital (fully paid up Rs.10 shares)			50
Reserves and surplus			650
	?	?	700
Totals	**300**	**500**	**800**

It is decided to form a new company 'IT Ltd.' for international tourism to take over the assets and liabilities of international division.

Accordingly 'IT Ltd.' was formed to takeover at Balance Sheet figures the assets and liabilities of international division. 'IT Ltd.' is to allot 5 crore equity shares of Rs. 10 each in the company to the members of 'Travels & Tours Ltd.' in full settlements of the consideration. The members of Travels & Tours Ltd. are therefore to become members of 'IT Ltd.' as well without having to make any further investment.

(a) You are asked to pass journal entries in relation to the above in the books of 'Travels & Tours Ltd.' and also in 'IT Ltd.'. Also show the Balance Sheets of both the companies as on 1st January, 2005 showing corresponding figures, before the reconstruction also.

(b) The directors of both the companies ask you to find out the net asset value of shares pre- and post-demerger. (c)Comment on the impact of demerger on "Shareholders wealth". (MAY 2005 CA FINAL)

Test Paper – XV

Go through the following theory topics : Mutual Funds, Merchant Bankers, Accounting by Stock Brokers, NBFC, Futures and options, Corporate Social reporting, Corporate Governance, ESPP, ESOP and Environment accounting.

Solutions to Test Paper I (Advanced Accounting)

Q.NO. 1 : Analysis of profit of B Ltd 31.3.1981

		Capital profit (pre- 1st April, 1980)	Revenue profit (1.4.1980 – 31.3.1981)
General reserve 1.4.1980		20,000	
P & L a/c 1.4.1980 Less dividend for year ended 31.3.1980	22,000 9,000	13,000	
Profit for year ended 31.3.1981 Less interim dividend	12,000 -4,500		7,500
Total		33,000	7,500
Holding company's share (90%)		33,000 x 0.90 = 29,700	7,500 x 0.90 = 6,750
Minority's share (10%)		33,000 x 0.10 = 3,300	7,500 x 0.10 = 750

Minority Interest :

Paid up value of shares held by minority	: 6,000	
+ Minority 's share in capital profit	3,300	
+ Minority 's share in revenue profit	750	10,050

Cost of control :

Cost of shares of B Ltd as held by A Ltd.	1,10,000
Less pre acquisition dividend	- 8,100 (9,000 x 0.90)
Paid up value of such shares	- 54,000
A's share in capital profit of B	-29,700
Goodwill	18,200

Consolidated B/S of A Ltd and its subsidiary B Ltd as on 31.3.1981

Liabilities		Amount	Assets		Amount
Share capital		1,80,000	Goodwill		44,200
General reserve		45,000	Other fixed assets		1,90,000
P & L a/c : + share in revenue profit of B - stock reserve	36,000 +6750 - 2000	40,750	CA Less stock reserve	48,000 2,000	46,000
CL		48,500	Investments*		44,100
Minority interest		10,050			
Total		3,24,300	Total		3,24,300

*Total investments of A =	1,56,000
Less shares of B (110000 – 8100)**	-1,01,900
Less debentures of B (Assumption : cost = paid up value)	-10,000
Other investments of A	44,100

** Purchased for Rs. 1,10,000 , later on pre-acquisition dividend was received and credited to Investment a/c (see item No. 4 of the question)

Q.NO. 2 : Analysis of profit of S Ltd 31.3.1984

		Capital profit (pre- 1st April, 1983)	Revenue profit (1.4.1983 – 31.3.1984)
General reserve 1.4.1983 Less bonus shares	5,00,000 -2,00,000	3,00,000	
P & L a/c 1.4.1983 Less dividend for year ended 31.3.1983	2,00,000 1,00,000	1,00,000	
Profit for year ended 31.3.1984			2,00,000
Total		4,00,000	2,00,000
Holding company's share (60%)		2,40,000	1,20,000
Minority's share (40%)		1,60,000	80,000

Minority Interest :

Paid up value of shares held by minority	: 2,80,000	(including bonus shares)
+ Minority 's share in capital profit	1,60,000	
+ Minority 's share in revenue profit	80,000	5,20,000

Cost of control :

Cost of shares of S Ltd as held by H Ltd.	5,00,000	
Less pre acquisition dividend	-60,000	
Paid up value of such shares	- 4,20,000	(including bonus shares)
H's share in capital profit of S	-2,40,000	
Capital reserve	2,20,000	

Consolidated B/S of H Ltd and its subsidiary S Ltd as on 31.3.1984

Liabilities	Amount	Assets	Amount
Share capital	10,00,000	FA	17,00,000
General reserve Capital reserve	2,00,000 2,20,000	CA 20,00,000 Less stock reserve - 20,000 Inter-co.Owings -120000	18,60,000
P & L a/c : 3,00,000 + share in revenue profit of S +1,20,000 - pre-acqus. div. -60,000 - stock reserve - 20,000	3,40,000		
CL 14,00,000 Less inter-co. Owings -1,20,000	12,80,000		
Minority interest	5,20,000		
Total	35,60,000	Total	35,60,000

Q. No. 3 : Assumption : A Ltd. acquired 8000 shares of Omega (before Omega's bonus issue) on cum-bonus basis. In other words, on 31st DEC. 1994, A Ltd. purchased 8000 shares and got 4000 shares of Omega.

Note : There is an error of omission in the books of Omega. Omega is to get Rs. 100 interest from A Ltd. This transaction has not been recorded in the books of Omega. Before preparing the consolidated B/S, we should rectify this error. This will, on one hand, increase the P & L a/c balance of Omega by Rs. 100 and, on the other hand, the amount of "Loan to A Ltd." (as appearing in the B/S of Omega) will also increase by Rs. 100.

Analysis of profit of Omega Ltd. 31.12.1994

		Capital profit (up to 31.12.94)
CAPITAL reserve 31.12.94 Less bonus shares	52,000 -50,000	 2,000
General reserve 31.12.94		5,000
P & L a/c 31.12.94		18,100
Revaluation loss 31.12.94		-5,000
Total		20,100
Holding co.' s share		16,080
Minority interest		4,020

Minority interest :

Paid up value of shares held by minority	:	30,000	(including bonus shares)
+ Minority 's share in capital profit		4,020	34,020

Cost of control :

Cost of shares of Omega a held by A :	1,70,000
Less : (i) paid up value of shares of Omega as held by A (including bonus shares)	-1,20,000
(ii) A' share in capital profit of Omega	-16,080
Goodwill	33,920

Consolidated B/S of A Ltd and its Subsidiary Omega Ltd. as on 31.12.1994

Liabilities	Amount	Assets	Amount
Share capital	3,00,000	Goodwill	33,920
General reserve	25,000	FA	2,89,700
P & L a/c	38,200	Stock	60,000
B/P less inter co. Owings	1,500	B/R less inter-co. Owings	1,000
Crs.	22,900	Drs.	30,000
Minority interest	34,020	Bank	7,000
Total	4,21,620	Total	4,21,620

Contingent liability for Bill discounted Rs. 700.

Q. No. 4 : Notes (i): There is an error of omission in the books of B. B is to get Rs. 1,000 interest from A Ltd. This transaction has not been recorded in the books of B. Before preparing the consolidated B/S, we should rectify this error. This will, on one hand, increase the P & L a/c balance of B by Rs. 1,000 and, on the other hand, the amount of "Loan to A Ltd." (as appearing in the B/S of B) will also increase by Rs. 1,000.

(ii) General Reserve and capital reserve balances have been brought down from last year.

Analysis of profit of B Ltd. as on 31st March, 1992

		Capital profit (pre- 1.10. 91)	Revenue profit (1.10.91 – 31.3.92)
Capital reserve 1.4.91 Less bonus shares	5,50,000 -5,00,000	50,000	
P & L a/c 1.4.1991		21,000	
Profit for year ended 31.3.1992		80,000	80,000
General reserve		50,000	
Revaluation loss		-50,000	
Total		1,51,000	80,000
Holding co.'s share ((80%)		1,20,800	64,000
Minority's share		30,200	16,000

Minority interest :

Paid up capital (including bonus shares)	3,00,000	
Capital profit	30,200	
Revenue	16,000	3,46,200

Cost of control : Cost of shares 17,00,000 Paid up value of shares including bonus shares -12,00,000

Cost of shares	17,00,000	
Paid up value of shares including bonus shares	-12,00,000	
Holding co.'s share in capital profit of B	- 1,20,800	3,79,200

Consolidated B/S of A Ltd and its subsidiary B Ltd. as on 31st March, 1992

Liabilities	Amount	Assets	Amount
Share capital	30,00,000	Goodwill	3,79,200
General reserve	3,00,000	FA	28.97,000
P & L a/c 3,82,000 +64,000	4,46,000	Stock	6,00,000
B/P less inter co. Owings	12,000	B/R less inter-co. Owings	7,000
Crs.	2,49,000	Drs.	4,30,000
Minority interest	3.46.200	Bank	40,000
Total	43,53,200	Total	43,53,200

Contingent liability for Bill discounted Rs. 6,000.

Q.No. 5 : Analysis of profit of Moon Ltd 31.3.2000

	Capital profit (pre- 1.4.97)	Revenue profit (GR) (1.4.1997 – 31.3.2000)	Revenue profit (P & L a/c) (1.4.1997 – 31.3.2000)
General reserve 1.4.1997 30,000 Less bonus shares -20,000 General reserve 1.4.1997-31.3.2000	10,000	6,000	
P & L a/c 1.4.1997 16,000 Less dividend for year ended 31.3.96 10,000	6,000		
Profit 1.4.1997-31.3.2000			14,000
Revaluation loss	-12,000		
Dep written back (1.4.97-31.3.2000)			3,600
Total	4,000	6,000	17,600
Holding co.'s share	3,200	4,800	14,080
Minority' s share	800	1,200	3,520

Cost of control :

Cost of shares	88,000	
Pre- acquisition dividend	-8,000	
Capital profit	-3,200	
Paid up capital	-96,000	(including bonus shares)
Capital reserve	19,200	

Minority interest :

Paid up capital (including bonus)	24,000	
Capital profit	800	
Revenue profit	1,200	
Revenue profit	3,520	29520

Consolidated B/S of Sun Ltd. and its subsidiary Moon Ltd. 31.3.2000

Liabilities	Amount	Assets	Amount
Share capital	1,20,000	FA	1,19,600
General reserve 20000+4800	24,800	Stock	50,000
P & L a/c	18,080*	B/R less inter-co. Owings	18,000
Capital reserve	19,200	Drs. less inter-co. Owings	17,000
B/P less inter co. Owings	5,000	Bank	19,000
Crs. less inter-co. Owings	9,000	Bank in transit	2,000
Minority interest	29,520		
Total	2,25,600	Total	2,25,600

Contingent liability for Bill discounted Rs. 1,000.

* P & L of Holding	12,000	
Less pre- acquisition dividend	-8,000	
Add share in post acquisition P & L of subsidiary	14,080	18,080

Solutions to Test Paper II (Advanced Accounting)
Answer to Q.NO.6 :

	[capital + profit –loss]	30% of [capital + profit – loss]	Minority interest
1.1.93	10,80,000	3,24,000	3,24,000
31.12.93	8,30,000	2,49,000	2,49,000
31.12.94	4,30,000	1,29,000	1,29,000
31.12.95	-70,000	-21,000	Nil
31.12.96	-1,90,000	-57,000	Nil
31.12.97	-1,40,000	-42,000	Nil
31.12.98	-40,000	-12,000	Nil
31.12.99	1,10,000	33,000	33,000

Cost of control : cost of shares 10,00,000
Paid up value -7,00,000
Capital profit -56,000
Goodwill 2,44,000

Working note :Q. No. 7 :
Balance sheet of Investment Ltd. 31.12 1999

Liabilities	Amount	Assets	Amount
S. capital	3,00,000	Investment in A 35,000 Less pre-acqui. Div. -1,500	33,500
P & L a/c : Interim dividend of A 2,400 Interim dividend of B 8,000	10,400	Investment in B	72,000
Payables to A	3,500	Investment in C 92,000 Less pre-acqui. Div. -3,200	88,800
		Bank	1,13,600
		Receivables from B	6,000
Total	3,13,900	Total	3,13,900

Answer to Q. No. 8 :
Consolidated B/s of X Ltd. and its subsidiaries X Investment Ltd, Y Ltd & Z Ltd.

Liabilities	Amount	Assets	Amount
ESC	25.00	Goodwill*	5.65
R&S 75 + 20	95.00	FA	46.00
Loan	125.00	Investment	29.00
Minority interest **	20.65	Net CA	185.00
Total	265.65	Total	265.65

* COST OF SHARES 50
Book value on the date of acquisition: X Invest. -5
Book value on the date of acquisition: Y -25 x 0.51
Book value on the date of acquisition: Z -35 x 0.76
Goodwill 5.65
**Minority interest = (25 x 0.49) + (35 x 0.24) = 20.65

Working notes to Q. No. 9 Analysis of profit of S Ltd. 31.3.1990

	General reserve	P & L a/c
Total	30000	40000
Minority's share	9000	12000
Holding company's share	21000	28000
Pre-acquisition GR [(20000 x 0.60) +(25000 x 0.10)]	14500	
Post acquisition GR	6500	
Pre-acquisition P & L [(5000 x 0.60) +(8000 x 0.10)]		3800
Post-acquisition P & L		24200

Cost of control :

Cost of shares	1,00,000
Paid up capital	-70,000
Capital profit	-14,500
Capital profit	-3,800
Pre-acquisition dividend	-2,000
Goodwill	9,700

Minority interest :

Paid up capital	30,000	
GR	9,000	
P & L	12,000	51,000

Solutions to Test Paper III (Advanced Accounting)
Answer to Q. No. 11 (Assumption : Pref. shares are cumulative)

Analysis of profit of S Ltd 30th Sept. 1985

	Capital profit (pre- 1.10.84)	Revenue profit (GR) (1.10.1984 – 30.9.85)	Revenue profit (P & L a/c) (1.10.1984 – 30.9.85)
General reserve 1.10.84 50,000 Less bonus shares -50,000 General reserve 1.10.84-30.9.85	Nil	60,000	
P & L a/c 1.10.84 30,000 Less dividend for year ended 30.9.84 24,000*	6,000		
Profit 1.10.84 – 30.9.85			84,000
Total	6,000	60,000	84,000
Profit for pref. shareholders	-	-	6,000
Profit for equity shareholders	6,000	60,000	78,000
Holding co.'s share	6,000 x 0.80 =4,800	60,000 x 0.80 =48,000	6000x0.80 + 78000x0.80 =67,200
Minority's share	6,000 x 0.20 = =1,200	60,000 x 0.20 = 12,000	6000x0.20 + 78000 x 0.20 16,800

* Preference dividend 12% on Rs.50,000 and 12% equity dividend on Rs.1,50,000

Cost of control :

Cost of shares	3,80,000
Paid up capital (E) (including bonus)	-1,60,000
Paid up capital (P)	- 40,000
Pre-acquisition dividend (80% of 24000)	- 19,200
Capital profit	- 4,800
Goodwill	1,56,000

Minority interest : Paid up capital (E) including Rs. 10,000 bonus shares	Rs. 40,000
Paid up (pref.)	Rs. 10,000
Capital profit	Rs. 1,200
Revenue profit (GR)	Rs. 12,000
Revenue profit (P & L)	Rs. 16,800
	Rs. 80,000

Consolidated B/S of H Ltd and its subsidiary S Ltd as on 30.9.1985

Liabilities	Amount	Assets	Amount
E. Share capital	5,00,000	Goodwill	2,56,000
P. Share capital	1,00,000	Machinery	1,60,000
G. reserve 100000 +48000	1,48,000	Vehicle	2,50,000
P & L a/c	1,94,000*	Furniture	80,000
Creditors 130000-20000	1,10,000	Stock 210000 – 4000	2,06,000
Tax	1,30,000	Drs. 265000-20000	2,45,000
Minority interest	80,000	Bank	65,000
Total	12,62,000	Total	12,62,000

*Holding co.'s P & L Balance 1,50,000 + H's share in post acquisition profit of S Rs. 67.200 – Stock reserve 4000 – pre-acquisition dividend 19,200 = 1.94.000

Answer to Q. No. 12

Assumption : H acquired 80% shares in A and A acquired 75% shares in B on the same date.

Analysis of profit of B Ltd 31st Dec. 1983

	Capital profit	Revenue profit (GR)	Revenue profit (P & L a/c)
General reserve	20,000	40,000	
P & L	40,000		20,000
Total	60,000	40,000	20,000
A's share	45,000	30,000	15,000
Minority' s share	15,000	10,000	5,000

Analysis of profit of A Ltd 31st Dec. 1983

	Capital profit	Revenue profit (GR)	Revenue profit (P & L a/c)
General reserve	40,000	20,000	
P & L	80,000		40,000
A's share in post acquisition profit of B	Nil	30,000	15,000
Total	1,20,000	50,000	55,000
H's share	96,000	40,000	44,000
Minority's share	24,000	10,000	11,000

Cost of control

Cost of shares (1,50,000 + 60,000)	2,10,000	
Paid up capital (1,60,000 + 75,000)	-2,35,000	
Capital profit (B)	- 45,000	
Capital profit (A)	- 96,000	
CR	1,66,000	
Minority interest : Paid up 40,000 + 25,000	65,000	
B' profit 15000+10000+5000	30,000	
A's profit 24,000+10,000+11,000	45,000	140000

Consolidated B/S of H Ltd and its subsidiaries A Ltd & B Ltd. as on 30.9.1985

Liabilities	Amount	Assets	Amount
S. capital	10,00,000	FA	10,20,000
Reserve 1,00,000 + 40,000	1,40,000	Stock	8,90,000
P & L a/c 4,00,000 + 44,000	4,44,000	Drs.	3,80,000
Capital reserve	1,66,000		
Creditors	3,80,000		
B/P	20,000		
M. Int.	1,40,000		
Total	22,90,000	Total	22,90,000

Answer to Q. No. 13

Analysis of profit of RAHIM as on 31.3.91

	Capital profit (pre- 1.4.89)	Revenue profit (1.4.89 – 31.3.91)
P & L a/c	40,000	2,19,400
Ram's share(90%)	36,000	1,97,460
Minority's share (10%)	4,000	21,940

Profit of Ram (i.e. Ram's own profit and Ram's share in post acquisition profit of Rahim)

	30.9.88	31.3.91
Ram's own P & L a/c	1,46,500	2,10,100
Ram's share in post acquisition profit of Rahim	Nil (Rahim was not subs. of Ram on this date	1,97,460
Total	1,46,500	3,97,560

Analysis of profit of RAM as on 31.3.91

	Capital profit	Revenue profit
P & L a/c	1,46,500	2,51,060
A's share(62.50%)	91,563	1,56,913
Minority's share (37.50%)	54,937	94,147

Minority interest : Paid up	60,000 + 10,000	=	70,000	
Profit of Rahim	4000+21940		25,940	
Profit of Ram	54,937 + 94,147		1,49,084	2,45,024

Cost of control :

Cost of shares	3,10,000
Paid up value	-1,90,000
Capital profit	- 36,000
Capital profit	- 91,563
CR	7,563

Consolidated B/S of A Ltd and its subsidiaries Ram Ltd and Rahim Ltd as on 31.3.91

Liabilities		Amount	Assets	Amount
S. capital		2,00,000	S. Assets	11,33,000
P & L a/c Share in post acquisition profit	5,23,500 +156913	6,80,413		
CR		7,563		
M. Int.		2,45,024		
Total		11,33,000	Total	11,33,000

Solutions to Test Paper IV (Advanced Accounting)
Answer to Q. No. 16:

BALANCE-SHEETS AS ON 31.3.06

	WAR	PEACE		WAR	PEACE
ESC	10,50,000	6,00,000	FA	5,50,000	1,60,000
GR	1,60,000	40,000	Net CA (Bal. fig.)	8,30,000	2.90,000
P & L a/c*	42,000	-----	Investments**	5,92,000	------
Deb.	6,00,000	-----	P & L a/c	-------	1,90,000
Deb. Premium	1.20,000	-----			
Total	19,72,000	6,40,000	Total	19,92,000	6,40,000

*P & L 31.3.04	80,000	
Preli. Exp.	-20,000	
Profit for 2 years	3,60,000	
Transfer to reserve	-40,000	
Div.	-2,10,000	
Loss of subsidiary	- 80,000	
Writing off investments	- 48,000	62,000

**Cost of investments	7,20,000	
Writing off of investments	- 48,000	
Share in the post acquisition Loss of subsidiary	-80,000	5,92,000

Analysis of profit of Peace as on 31.3.06

	Cap. Profit	Rev. Profit
GR	40,000	----
P & L	-80000	-1,00,000
Pre. Exp.	-10000	-----
	-50,000	-1,00,000

Cost of control

Cost of shares	7,20,000	
Capital profit	-(-50000 x 0.80)	
Paid up capital	- 4,80,000	
	2,80,000	
Goodwill written off	- 48,000	2,32,000

Minority interest :

Paid up	120000	
Capital profit	-50000 x 0.20	
Revenue profit	-100000 x 0.20	90,000

Consolidated B/S of War Ltd and its subsidiary Peace Ltd. as on 31.3.06

Liabilities	Amount	Assets	Amount
ESC	10,50,000	Goodwill	2,32,000
GR	1,60,000	FA	7,10,000
P & L	42,000	Net CA	11,20,000
Deb.	6,00,000		
Deb. Premium	1,20,000		
M Int.	90,000		
Total	20,62,000	Total	20,62,000

Working note to Q. No. 17 :

	Capital Profit	Revenue Profit
P & L b/d	15,000	------
P & L current	49,000 x (3/12)	49,000 x (9/12)
Pref. div. paid	- 3500	-3500
Pref. div. proposed	----	-7000
	23,750	26,250
Holding co.'s share	19,000	21,000
Minority's share	4,750	5,250

Working note to Q. No. 19

Assumption : During the period 1.1.99 to 31.3.99, B Ltd had no transaction other than those when are clearly/ impliedly given in the question.

A Ltd.'s a/c

To sales	1,20,000	By purchases	1,80,000
To balance c/d	60,000		
Total	1,80,000	Total	1,80,000

B/S of B Ltd. 31.3.99

Liabilities	Amount	Assets	Amount
S. Capital	5,00,000	FA	4,05,000
R & S 2,05,000 Loss (fire) - 5,000 Profit on goods resold +30000 Debentures int. – 9,750	2,20,250	Stock 3,50,000 Purchases from A +90,000 Fire -20,000	4,20,000
Deb.	3,00,000	Drs.	2,65,000
Creditors 80,000+60000	1,40,000	Bank	1,10,250
Other liabilities	40,000		
Total		Total	

Solutions to Test Paper V (Advanced Accounting)

Working notes to Q. No. 22

(i) Mumbai is holding company of Delhi as Mumbai is holding 75% shares of Delhi directly.

(ii) Mumbai is holding company of Amritsar as Mumbai is holding 75% shares of Amritsar. Mumbai is holding 50% shares of Amritsar directly , it is holding 25% shares of Amritsar through its subsidiary Delhi.

(iii) Mumbai is holding company of Kanpur. Mumbai is holding $83^{1/3}$ % of Kanpur. Details are as follows: (a) Mumbai holds 50% shares of Kanpur directly

(b) Mumbai holds 25% shares of Kanpur through its subsidiary Delhi

(c) Mumbai holds $8^{1/3}$ % shares of Kanpur through its subsidiary Amritsar.

Analysis of profit of Kanpur as on 31st Dec. 2000

	Capital profit	Revenue profit (P & L a/c)	Revenue Profit(GR)
General reserve	6,00,000	------	4,00,000
P & L	60,000	2,60,000	-----
Total	6,60,000	2,60,000	4,00,000
Mumbai's share	3.30,000	1,30,000	2,00,000
Delhi's share	1,65,000	65,000	1,00,000
Amritsar's share	55,000	21,667	33,333
Minority's share	1,10,000	43,333	66,667

<u>Answers</u> Goodwill 6,37,500 Total of Cons. B/s 1,26,87,500 M. Int. 31,25,312

General reserve in Con. B/s : 20,00,000 +2,00,000(Kanpur)+2,59,375(Delhi) +91,667(Amritsar) = 25,51,042

P&L in Cons. B/S : 10,00,000+1,30,000(Kanpur)+1,10,833(Amritsar)+2,40,313(Delhi) = 14,81,146

Answer to Q. No. 23

Let capital profit means pre-acquisition profit that is still available.
Let revenue profit means post-acquisition profit that is still available.

(All figures are in Rs. Lakhs)

Holding company :
Capital profit 0.80 + 0.20 = 1.00
Revenue profit 3.20 – 0.20 = 3.00

Subsidiary company :
Capital profit 0.85
Revenue profit 0.29 – 0.05 = 0.24

Let capital profit of A Ltd. = A

Let capital profit of B Ltd = B

A = 1.00 + 0.80 B ….(i)

B = 0.85 + 0.20 A …….(ii)

Solving the equations : A = 2.00

B = 1.25 A's share 1.00 Minority's share 0.25

Let revenue profit of A Ltd. = x

Let revenue profit of B Ltd = y

x = 3.00 + 0.80 y ….(i)

y = 0.24 + 0.20 x …….(ii)

Solving the equations : x = 3.80

Y = 1.00 A's share 0.80 Minority's share 0.20

Minority Interest :

Paid up capital	0.60	
Revenue profit	0.20	
Capital profit	0.25	1.05

Cost of control

Cost of shares	3.00
Paid up capital	-2.40
Capital profit	-1.00
CR	0.40

Con. B/S of A Ltd and its subsidiary B Ltd. as on 31.3.1996(Rs. Lakhs)

Liabilities	Amount	Assets	Amount
S. capital	4.80	Goodwill **	0.40
R & S*	3.64	FA	7.00
Creditors	1.81	Stock	0.65
M. Int.	1.05	Drs.	2.39
		Bank	0.95
Total	11.30	Total	11.30

* R & S of A	4.00	
A's share in post acquisition profit of B	0.80	
B's share in A's profit counted twice	-1.16	3.64

** Excess of cost of shares of A over their paid up value	0.80
Less CR	-0.40
Goodwill	0.40

Solutions to Test Paper VI (Advanced Accounting)
Working note to Q.No.29 :

Assumption : The balance in Revenue reserve a/c on 1.4.2003 was nil.
(Alternatively it can be assumed that the balance in Revenue reserve a/c on 1.4.2003 was Rs. 75,000)

Analysis of profit of SD on 31.3.2004

	Capital profit (pre-1.10.2003)	Revenue profit (CR) (1.10.2003 to 31.3.2004)	Revenue profit (RR) (1.10.2003 to 31.3.2004)	Revenue profit (P&L) (1.10.2003 to 31.3.2004)
RR current	37,500		37,500	
CR b/d	50,000			
CR current	1,30,000	1,30,000		
P & L b/d 2,75,000 Div. for year Ended 31.3.03 -2,50,000	25,000			
P & L current	1,27,500			1,27,500
Revaluation profit :L&B	4,40,000			
Revaluation loss : Furni.	-30,000			
Dep. on revaluation : L & B Furni.				 -11,000 + 3,000
Total	7,80,000	1,30,000	37,500	1,19,500
Holding co.'s share	6,24,000	1,04,000	30,000	95.600
Minority's share	1,56,000	26,000	7,500	23,900

Cost of control :
Cost of shares 16,10,000 (this amount is net of pre-acquisition dividend recd.)
Paid up value -16,00,000
Capital profit -6,24,000
Capital reserve 6,14,000

Minority interest : Paid up capital	4,00,000	
Profits (1,56,000 + 26,000 + 7,500 + 23900)	2,13,400	6,13,400

Answer to Q. No. 27 :
Analysis of profit of S Ltd 31.3.2002(Rs. '000)

	Capital profit (pre- 1.4.2001)	Revenue profit (P &L) (1.4.01- 31.3.02)	Revenue profit (GR) (1.4.01 - 31.3.02)
General reserve 1.4.2001 1,500 Less bonus shares - 900 General reserve 1.4.01 - 31.3.02	600		90
P & L a/c 1.4.2001 633 Less dividend for year ended 31.3.02 including CDT -333	300		
Profit 1.4.01-31.3.02		510	
Total	900	510	90
Holding co.'s share (60%)	540	306	54
Minority' s share	360	204	36

Minority interest : Paid up 960 + profits 360+204+36 = 1560

Cost of control:

Cost of shares	1500
Pre-acquisition div.	– 180
Paid up	- 1,440 (including Bonus)
Capital profit	- 540
CR	660

Consolidated B/S of H Ltd and its subsidiary S Ltd. 31.3.2002 (Rs.'000)

Liabilities	Amount	Assets	Amount
S. capital	4,000	P & M	4,991
Reserve 928 + 54	982	F & F	913
P & L a/c*	1,421	Stock less stock reserve	1,759
Capital reserve	660	Drs.	1,383
Creditors	914	B/R	215
B/P	204	Cash	512
Tax	400	Advances	450
Other liabilities	82		
M. Int.	1560		
Total	10,223	Total	10,223

* Holding co.'s P & L	1,305	
Pre – acquisition dividend	-180	
Revenue profit	+306	
Stock reserve	-10	1421

Working note to Q. No. 30 : Assumption : Pref. shares are cumulative
Analysis of profit of Hockey Ltd 31.3.2005

	Capital profit (pre-1.4.2004)	Revenue profit (GR) (1.4.04-31.3.05)	Revenue profit (P&L) (1.4.04 - 31.3.05)
General reserve 1.4.2004 2,00,000 Less bonus shares -2,00,000 General reserve 1.4.04 - 31.3.05		2,20,000	
P & L a/c 1.4.2004 3,00,000 Less dividend for year 2003-04 -2,38,000	62,000		
Profit 1.4.04-31.3.05			5,38,000
Revaluation loss	-1,00,000		
Dep. written back on a/c of revaluation loss			+20,000
Total	-38,000	2,20,000	5,58,000
Profit / loss for pref. shareholders	------	------	38,000
Profit/loss for equity shareholders	-38,000	2,20,000	5,20,000
Football's share	-38,000 x .75 = -28500	2,20,000 x .75 =1,65,000	5,20,000 x 0.75 +38,000 x .375 = 4,04,250
Minority's share	-38,000 x 0.25 = - 9,500	2,20,000 x .25 = 55,000	5,20,000 x .25 +38,000 x .625 =1,53,750

Cost of control :

Cost of shares (3,10,000 +9,50,000 + 8,00,000)	20,60,000	
Pre- acquisition dividend*	-70,000	
Paid up (Equity including bonus + Pref.)	-(16,50,000+142500)	
Capital profit	- (-28,500)	2,26,000

M. Int. : Paid up equity (including bonus)	5,50,000	
Paid up Pref.	2,37,500	
Revenue profit	55,000	
Revenue profit	1,53,750	
Capital profit	-9,500	9,86,750

* Dividend for 2003-04 on 70,000 equity shares which were acquired on 1.4.2004.

Solutions to Test Paper X (Advanced Accounting)

Answer to Q. No. 47 (Assumption : Dep. and writing off of lease for income tax purposes : Rs.20)

P & L statement for year ended 31.3.96

Sales		2,760		
Increase in stock		83		
Decrease in WIP		-70		2,773
Purchase material 1218-38			1,180	
Purchase of Land			73	
Wages			111	
Sub-contract			854	
Dep			15	
Writing off of lease			5	
Int.			22	
Director's salaries			39	
O. salaries			18	
A. Exp			147	
Audit			20	
Prov. For DD			49	2,533
Profit before bonus				240
Bonus				-24
PBT				216
Current tax	133			
Deferred tax asset	-25			108
PAT				108
Profit b/d				128
Reserve				-11
Dividend				-25
Profit c/d				200

Balance-sheet as on 31.3.96

Sources of funds:				
(I) S.capital		100		
R & S		211	(P & L 200 + reserve 11)	
(II) S.Loan		112		423
Application of funds :				
FA	384			
Dep	-184	200		
CA	968			
Deferred tax Asset	25			
CL	-770	223		423

CA : Stock 142 + WIP 140 + Drs. 686 = 968

CL : Creditors 463 +O/s Audit fees 20 +BO 105 + Tax 133 + Div 25 + Bonus payable 24 = 770

Answer to Q. No. 48 Assumptions(i) : Dep. for income tax purposes : Rs.84 (ii) the company transfers 10% of profits to reserve through the requirement is only 7.50%

P & L statement for the year ended 31.3.1995 (Rs. 1500)

Sales		1,500	
Increase in Stock		30	1,530
Purchase	855		
Dep	74		
Loss on sale of fixed asset	10		
Dis. cost	51		
AO	240		1,230
			300
Factory closure cost			30
PBT			270
Tax			135
PAT			135
Profit b/d			40
Total profit			175
Reserve			-14
Div.			-100
Profit c/d			61

B/S as on 31.3.1995 S.

Capital 500

Reserve and surplus 75 (P & L 61 + Res. 14) Loan

35 610

FA (370-189) 181

Investments 100

CA :

Stock 100 Drs

390 Bank 114

604 CL & Provisions :

Creditors 40 Div.

100 Tax 135

275 329 610

Working notes and answer to Q.No.49

Entries Regarding vendor's Drs.: (i)

Vendor's Drs. a/c Dr. 90000

To Vendor suspense a/c

(ii) Vendor's suspense a/c Dr. 1,000

To Vendor's Drs. a/c (iii)

Bank a/c Dr. 60,000 To

Vendor's Drs. (iv)

Vendor's Suspense a/c Dr. 60,000 To

Bank 57000

To Com. a/c 3000

PC = 80000 shares + 56000 cash = 136000

Net assets taken over:Building 80000+fur. 10000+stock30,000 =120000 Goodwill = 16,000

Drs. a/c

Sales	4,60,000	Discount	5,000
		Cash (bal. fig.)	3,24,000
		c/d	1,31,000
Total	4,60,000	Total	4,60,000

Creditors a/c

Cash (bal. fig.)	2,72,000	Purchase	3,20,000
c/d	48,000		
Total	3,20,000	Total	3,20,000

Cash a/c

S. capital	1,62,000	Creditors	2,72,000
Drs.	3,24,000	Vendor's suspense a/c	57,000
V. Drs.	60,000	Vendor (Purchase Consideration)	56,000
		P. Exp.	10,000
		D. fees	12,000
		Salaries	48,000
		c/d	91,000
Total	5,46,000	Total	5,46,000

Trading a/c for year ended 31st March, 1992

Op. stock	30,000	Sales	4,60,000
Purchase	3,20,000	C. Stock	52,000
GP	1,62,000		
Total	5,12,000	Total	5,12,000

P & L a/c for year ended 31.3.1992

	Pre-	Post		Pre -	Post
Salaries	12,000	36,000	GP	40,500	1,21,500
D.Fees	-	12,000	Com.		3,000
Discount	1,250	3,750			
Dep. Build.	1,000	3,000			
Dep. fur.	250	750			
Preli. Exp.		10,000			

Underwrit. com.		4,000			
Capital reserve	26,000				
Net profit	-	55,000			
Total	40,500	1,24,500	Total	40,500	1,24,500

B/S of Company as on 31.3.1992

Liabilities	Amount	Assets	Amount
S. Capital : 400 shares of Rs 10 each (other than for cash)	 4,000	Building 80,000 Less dep. -4,000	76,000
10000 shares of Rs.10 Rs. 8 paid (other than cash)	80,000	Furniture 10,000 Less dep. -1,000	9,000
20000 shares of Rs. 10 each Rs.8 called 1,60,000 call in arrear -2,000	 1,58,000 2,42,000	Stock	52,000
Capital reserve 26,000 Less goodwill -16,000	10,000	Drs.	1,31,000
P & L	55,000	Cash	91,000
CL: Call in advance 4,000 Creditors 48,000	 52,000		
Total	3,59,000	Total	3,59,000

Answer to Q. No. 50 : Books of Pranav

Realization a/c

L & B	35,68,200	Debentures	10,00,000
Goodwill	5,00,000	Creditors	4,36,200
Drs.	3,98,400	B.O.	2,00,000
Stock	7,85,200	Divya (Business purchased)	43,00,000
P & M	16,43,900	S. Members a/c (Loss on realization)	9,59,500

Total	68,95,700	Total	68,95,700

S. Members a/c

Unpaid calls	10,000	Share capital	50,00,000
Realisation a/c	9,59,500	P & L a/c	2,69,500
Shares in Divya	40,00,000		
Cash	3,00,000		
Total	52,69,500	Total	52,69,500

Purchase consideration : 43,00,000

Net Assets : L

& B 35,68,200 Drs.

3,58,400 Stock

7,85,200 P& M

16,43,900 Deb. -

10,00,000

Creditors -4,36,200

BO -2,00,000 47,19,500

Capital Reserve (before liquidation expenses) 4,19,500 Liquidation exp,

1,40,000 Capital reserve

2,79,500

B/S of Divya as on ……………(after Absorbtion)

Liabilities	Amount	Assets	Amount

Share capital 1,90,00,000 Less unpaid call – 50,000	1,89,50,000	Goodwill	30,00,000
P & L a/c	9,88,500	L & B	1,39,01,200
Capital reserve	2,79,500	P & M	55,20,700
Debentures	50,00,000	Stock	25,77,800
Liabilities for debentures of Pranav	10,00,000	Debtors	10,82,400
Creditors	8,34,200	B/R	3,62,100
Liabilities for creditors of Pranav	4,36,200	Bank	10,44,200
Total	2,74,88,400	Total	2,74,88,400

Assumption : Divya will pay the liability on account of BO of Pranav immediately and other liabilities will be paid in near future.

Part Answer to Q. No. 51 Journal of Ksha

		Dr.	Cr.
Yaa	Dr.	125	
Dep. Pro. a/c	Dr.	240	
CL	Dr.	750	
Loan	Dr.	200	
To FA			400
To CA			900
To Cap. Res. a/c (Bal. fig.)			15

		Dr.	Cr.
FA a/c	Dr.	325	
CA a/c	Dr.	800	
To CL			700
To Loan			250
To Yaa			140
To Cap. Res. (Bal. fig.)			35

B/S of Ksha as on 31.3.1999 (Rs. crores)

	Before restructure	After restructure
S. capital	300	300
R&S	750	800*
Loan funds	250	315**
Total sources	1,300	1,415
FA Less dep	1,000 -400 600	925*** - 160**** 765
CA CL	2,000 -1300 700	1,900***** -1,250****** 650
Total	1300	1415

* R & S (before restructure) 750
CR (15+35) 50 800
** Loan fund before restructure 250 + Loan acquired from Yaa 250 – Loan transferred to Yaa 200 + payable to Yaa 15 = 315 ***
FA (before restructure) 1000 + FA acquired from Yaa 325 – Gross cost of FA transferred to Yaa -400 = 925
**** Dep pro. (before restructure) 400 – Dep provision of assets transferred to Yaa 240 = 160
***** CA before restructure 2000 + CA acquired from Yaa 800 – CA transferred to Yaa 900 = 1900
******CL Before restructure 1300 + CL acquired from Yaa 700 – CL transferred to Yaa 750 = 1250

Solutions to Test Paper XI (Advanced Accounting)
Working notes and answer to Q. No. 52

Journal of X :

Goodwill a/c Dr. 40,000

Mach. a/c Dr. 90,000
Stock a/c Dr. 80,000
Drs a/c Dr. 1,20,000
Bank a/c Dr. 90,000
To Crs. a/c 30,000
To ESC 3,00,000
To Securities Premium 90,000

Journal of Y :
Shares of X a/c Dr. 3,90,000
Crs. a/c Dr. 30,000
To Goodwill a/c 10,000
To Machine a/c 1,00,000
To Stock a/c 72,000
To Drs. a/c 1,20,000
To Bank a/c 90,000
To P & L a/c 8,000
To Cap. Res. a/c 20,000

B/S of X Ltd. as on 31.12.1991

Liabilities	Amount	Assets	Amount
ESC	7,00,000	Goodwill	70,000
Reserve and surplus : Securities premium 90,000 Other items 60,000	1,50,000	Machinery	2,40,000
Crs.	70,000	Stock	1,20,000
		Drs.	3,30,000
		Bank	1,50,000
		Preliminary exp.	10,000
Total	9,20,000	Total	9,20,000

B/S of Y Ltd. as on 31.12.1991

Liabilities	Amount	Assets	Amount
ESC	3,00,000	Investment	3,90,000
Reserve and surplus : P & L 8,000 CR 20,000 Other items 80,000	1,08,000	Preli. Exp.	18,000
Total	4,08,000	Total	4,08,000

Working notes to Q. No. 53

Net assets taken over (Rs. Lakhs):	SHO	THAM
Land	200	100+20

Building	600	150+300
Mach.	960	600+600
Other FA	100	200+50
Net CA	1040	1252-12+740
Loan	-900	-(1000+700)
PC	2000	2300
Less receivable as shareholder of vendor co	-800	-575
Net payable	1,200	1,725
Issue price	20	20
No. of shares to be issued	1200/20 = 60 Lakhs	1,725/20 = 86.25 Lakhs

Two important entries in the Journal Of Puru

Investment in SHO Dr. 300
Investment in Tham Dr. 275
To Cap. Reserve

———

Capital reserve a/c Dr. 8
To Bank a/c

B/S of Puru as on 1.4.1994 (after absorption)(Rs. Lakhs)

Liabilities	Amount	Assets	Amount
ESC	2,962.50	Land	520.00
Reserve and surplus : Securities prem. 1,462.50 CR 567.00 Other items 2,000.00	4029,50	Building	1,550.00
Loan	4,200.00	Machinery	3,660.00
		Other FA	750.00
		Investment	100.00
		Net CA	4,612.00
Total	11,192.00	Total	11,192.00

Working notes to Q. No. 54

Let the value of all the shares of Major = x

Let the value of all the shares of Minor = y

x = 50,000 +1,00,000 + 20,000 + 0.20 y +75,000 +60,000 + 20,000 -40,000
y = 25,000 +50,000 +5,000 + 0.05x +45,000 +68,000 +20000 – 70,000
Solving the equations, we get, x = 3,16,768 y = 1,58,838

Journal of Hind:

Business purchase a/c	Dr.	4,75,606	
To Liquidator of Major			3,16,768
To Liquidator of Minor			1,58,838

Goodwill a/c	Dr.	75,000	
Mach. a/c	Dr.	1,50,000	
Furniture a/c	Dr.	25,000	
Stock a/c	Dr.	1,20,000	
Drs. a/c	Dr.	1,28,000	
Bank a/c	Dr.	40,000	
Investment in Major	Dr.	3,16,768 X (1/20)	
Investment in Minor	Dr.	1,58,838 X (1 / 5)	
To Crs. a/c			1,10,000
To BP a/c			4,75,606

Liquidator of Major	Dr.	3,16,768	
To Investment in Major			316768 X (1/20)
To ESC			3,00,930

Liquidator of Minor	Dr.	1,58,838	
To Investment in Minor			1,58,838 X (1/5)
To ESC			1.27,070

Ledger of Major
Realization a/c

Mach.	1,00,000	Crs.	40,000
Furniture	20,000	Hind (Business purchase)	3,16,768
Investment	25,000		
Stock	75,000		
Drs.	60,000		
Bank	20,000		
Shareholder a/c (profit)	56,768		
Total	3,56,768	Total	3,56,768

Hind Ltd.

Realization a/c	3,16,768	Shareholders a/c	316768x(1/20)
		Shares of Hind	3,00,930
Total	3,16,768	Total	3,16,768

Shareholders a/c

Hind Ltd	316768x(1/20)	Esc	2,00,000
Shares of Hind	3,00,930	P & L A/C	60,000
		Realization a/c (Profit)	56,768
Total	3,16,768	TOTAL	3,16,768

Solutions to Test Paper XII (Advanced Accounting)

Answer to Q. No. 58

Scheme of external reconstruction

(i) Net worth of the company :

FA	15,00,000	
Stock	3,00,000	
Drs.	4,00,000	
Cash	1,50,000	
Deb.	-3,00,000	
Crs.	-3,50,000	
BO	-3,00,000	14,00,000

Capital invested by shareholders	30,00,000
Loss	16,00,000
Loss for pref. shareholders	2,00,000 (Rs.20 per share)
Loss for equity shareholders	14,00,000 (Rs.70 per share)

(ii) Equity shareholders may be issued 20,000 equity shares of Rs. 30 each and Preference shareholders 10,000 7% Preference shareholders of Rs. 80 each.

(iii) A new company may be formed with authorised capital of 25,000 equity shares of Rs. 30 each and 12,500 preference shares of Rs. 80 each.

(iv) Current ratio = 2 = [(Drs. + Cash + stock)] / [(Creditors + BO)]

2 = [400000 +150000 +300000] /[350000 + BO]

BO = 75,000 . The remaining amount of BO should be converted into loan.

B/S of new company as on ……….

Liabilities	Amount	Assets	Amount
Share capital : Authorised :25000 Equity shares of Rs. 30 each 12500 Pref. shares of Rs. 80 each	 7,50,000 10,00,000	FA	15,00,000
Issued and subscribed : 20000 equity shares of Rs. 30 each fully paid 10,000 9% Pref. shares of Rs.80 each fully paid	 6,00,000 8,00,000 14,00,000	Stock	3,00,000
Deb.	3,00,000	Drs.	4,00,000
Loan	2,25,000	Cash	1,50,000
Crs.	3,50,000		
BO	75,000		
Total	23,50,000	Total	23,50,000

Answer to Q. No. 59: (Internal reconstruction)

Reconstruction a/c (also known as capital reduction a/c)

Drs.	40,000	L & B	3,00,000
Stock	40,000	PSC	1,00,000
Cash(exp. for completing formalities)	20,000	Deb.	1,00,000
P & L	8,20,000	ESC	4,50,000
Capital Reserve (Bal. fig.)	30,000		
Total	9,50,000	Total	9,50,000

B/S of A Ltd (and reduced) as on ………………

Liabilities	Amount	Assets	Amount
ESC	2,50,000	L & B	4,00,000
PSC	1,00,000	P & M	2,00,000
CR	30,000	Stock	1,60,000

Deb.	2,00,000	Drs	1,60,000
Crs.	3,20,000	Bank	20,000
O/s Exp.	40,000		
Total	9,40,000	Total	9,40,000

EXTERNAL RECONSTRUCTION

PC : E. SHARES 60,000 X 2.50
P. Shares 2,000 X 50 2,50,000

Journal of A (New) Ltd.

BP a/c Dr. 2,50,000
To Liquidator of A Ltd. 2,50,000

Liquidator of A Ltd. Dr. 2,50,000
To ESC 1,50,000
To PSC 1,00,000

Bank a/c Dr. 1,00,000
To ESC 1,00,000

Formation exp. a/c Dr. 20,000
To Bank a/c

L&B a/c Dr. 4,00,000
P & M a/c Dr. 2,00,000
Stock a/c Dr. 1,60,000
Drs. a/c Dr. 1,60,000
Bank a/c Dr. 30,000
To Liabilities for Deb. 2,00,000
To Crs. 3,20,000
To Exp. Crs. 40,000
To Liabilities for Crs and exp. crs. a/c 90,000
To Business purchase 2,50,000
To Cap. Reserve (Balancing figure) 50,000

Liabilities a/c Dr. 2,00,000
To 13.50% Deb. a/c

Liabilities for Crs. and Exp. Crs. a/c Dr. 90,000
To Bank

B/S of A (New) Ltd. as on ……….

Liabilities	Amount	Assets	Amount
ESC	2,50,000	L & B	4,00,000
PSC	1,00,000	P & M	2,00,000

CR	50,000	Stock	1,60,000
Deb.	2,00,000	Drs	1,60,000
Crs.	3,20,000	Bank	20,000
O/s Exp.	40,000	Formation exp.	20,000
Total	9,60,000	Total	9,60,000

Vendor's books
Realization a/c

L & B	1,00,000	Deb.	3,00,000
P & M	2,00,000	Crs.	4,00,000
Stock	2,00,000	Exp. Crs.	50,000
Drs.	2,00,000	A (New) Ltd (Business purchased)	2,50,000
Cash	30,000		
Shareholders a/c (profit on Realization)	2,70,000		
Total	10,00,000	Total	10,00,000

Shareholders a/c

P & L	8,20,000	ESC	6,00,000
E shares of A (New)	1,50,000	PSC	2,00,000
P shares of A (New)	1,00,000	Realization a/c	2,70,000
Total	10,70,000	Total	10,70,000

Answer to Q No. 60

Journal

Item (i)

11% PSC	a/c	Dr. 4,00,000	
To 13% Deb.	a/c		3,63,600
To Premium on Deb.	a/c		36,360
To Bank	a/c		40

Item (ii)

Cap. Reduction	a/c	Dr. 1.32.000	

To ESC a/c
(Note : After this entry , there will be 10640 E shares of Rs. 100 each, Rs. 50 paid up)

Item (iii)
ESC a/c Dr. 2,66,000
To Cap. Reduction a/c
(Note : After this entry , there will be 10640 E shares of Rs. 100 each, Rs. 25 paid up)

Item (iv)
ESC a/c Dr. 2,66,000
To Rs.50 ESC a/c
(Note : After this entry , there will be 10640 E shares of Rs. 50 each, Rs. 25 paid up)

Share call a/c Dr. 2,66,000
To Rs.50 ESC a/c

Bank a/c Dr. 2,66,000
To Share call a/c
(Note : After this entry , there will be 10640 E shares of Rs. 50 each, fully paid up)

Items (v), (vi) and (vii)
Capital reduction a/c Dr. 1,57,750
To Goodwill a/c 40,000
To Investments a/c 25,000
To FA a/c 80,000
To Provision for discount on Drs a/c 12,750

Stock a/c Dr. 21,000
To Cap. Reduction a/c

G. Reserve a/c Dr. 2,750
To Capital reduction a/c
(Being the debit balance of capital reduction a/c written off against General Reserve) -----
----

Increase in working capital (1.4.92 to 30.9.92) :
Bank 55,100 + Drs.40,000 - Crs. 26,000 – Stock 8,000 = 61,100.

Increase in WC is on a/c of Profit before "Dep and interest"

Profit = 61,100 – Dep – interest = 61,100 – 25,000 – 23,634 = 12,466

Cash and Bank summary (1.4.92 – 30.9.92)

b/d	1,00,000	PSC	40

S. Call	2,66,000	Interest	23,634
Increase on a/c of operation	55,100	Deb.	1,81,800
		c/d	2,15,626
Total	4,21,100	Total	4,21,100

B/S of Sickness Ltd (and reduced) as on 30.9.92

Liabilities	Amount	Assets		Amount
S. capital	5,32,000	FA		4,75,000
Securities premium	40,000	CA:		
GR	57,250	Stock	2,23,000	
Debenture Premium	36.360	Drs(net)	2,82,250	
P & L A/C	12,466	Bank	2,15,626	7,20,876
Deb.	1.81,800			
CL	3,36,000			
Total	11,95,876	Total		11,95,876

Answer to Q No. 61

Journal of A Ltd

Item (i)

8 % PSC	a/c	Dr.	2,00,000	
To Rs. 7.50 PSC	a/c			1,50,000
To Capital reduction	a/c			50,000

ESC	a/c	Dr.	1,50,000	
To Rs. 2 ESC	a/c			30,000
To Rs. capital reduction	a/c			1,20,000

Rs. 7.50 PSC	a/c	Dr.	1,50,000	
To Rs. 10 PSC	a/c			

Rs 2 ESC	a/c	Dr.	30,000	
To Rs. 10 ESC a/c				

<u>Item (ii)</u>

Capital reduction	a/c	Dr 16000	
To Rs. 10 ESC	a/c		

<u>Item(iii)</u>

Share premium	a/c	Dr. 5,000	
To capital reduction a/c			

<u>Item (iv)</u>

Cash	a/c	Dr. 12,300	
9 % Deb.	a/c	Dr. 60,000	
Acc. Int.	a/c	Dr. 2,700	
To Freehold	a/c		60000
To Cap. Reduction	a/c		15,000

<u>Item (v)</u>

Capital reduction	a/c	Dr. 20,000	
To P & M	a/c		20,000

<u>Item (vi)</u>

Cash	a/c	Dr. 32,000	
Capital reduction	a/c	Dr. 8,000	
To Investment a/c	a/c		

<u>Item (vii)</u>

Capital reduction	a/c	Dr. 76,100	
To Goodwill	a/c		55,000
To Preli. Exp.	a/c		2,500
To Stock	a/c		8,600
To Drs.	a/c		10,000

<u>Item (viii)</u>

Insurance co.	a/c	Dr. 6,300	
Capital reduction	a/c	Dr. 700	
To Cash	a/c		

Cash	a/c	Dr. 6,300	
To Insurance co.			

<u>Item (ix)</u>

BO	a/c	Dr. 43.600	
To cash a/c			-

Capital reduction a/c	a/c	Dr. 69,200	
To P & L a/c			69,200

(After posting of all these entries, the balance in the capital reduction a/c will be nil)

B/S of A Ltd (and reduced) as on 31.3.1992

Liabilities	Amount	Assets	Amount
ESC	1,50,000	Lease-hold	1,22,000
PSC	46,000	P & M	1.40,000
Crs	85,000	Stock	20,000
BO	52,400	Drs.	51,400
Total	3,33,400	Total	3,33,400

Solutions to Test Paper XIII (Advanced Accounting)

Answer to Q. No. 63 : (assumption : Investments are non-trade investments)

Closing capital invested :	Hamer	Grace
Total of assets side of B/S	9,00,000	3,00,000
Investments	-1,00,000	
Crs.	-1,00,000	-50,000
	7,00,000	2,50,000

	Hamer	Grace
Av. Profit	1,35,000	47,000
Non-trade Income	-6,000	---------
Future Maintainable profit	1,29,000	47,000
Normal profit	-700000 x 0.15	- 250000 x 0.15
Super Profit	24000	95000
Goodwill	96000	38000

Purchase consideration :	H	G
Goodwill	96,000	38,000
FA	4,00,000	1,00,000
Investment	1,00,000	-----
Stock	2,04,000	1,42,000
Drs	1,70,000	60,000
Cash	30,000	10,000
Crs.	-100000	-50000
PC	9,00,000	3,00,000
No. of shares of X Ltd.	90,000	30,000

B/S of X Ltd as on 1.1.82

Liabilities	Amount	Assets	Amount
ESC	12,00,000	Goodwill	1,34,000
Crs.	1,50,000	FA	5,00,000
		Investments	1,00,000
		Stock	3,46,000
		Drs.	2,30,000
		Cash	40,000
Total	13,50,000	Total	13,50,000

Answer to Q. No. 64 (a) :

	X	Y	Z
Tangible FA	10,00,000	5,00,000	6,00,000
CA	3,50,000	1,40,000	80,000
Deb. And Crs.	-4,00,000	-1,50,000	-2,00,000
Closing CE	9,50,000	4,90,000	4,80,000

	X	Y	Z
Av. Annual profit after interest	1,60,000	1,44,000	68,000
Dep. on revaluation	- 20,000	+10,000	-10,000
Future maintainable profit	1,40,000	1,54,000	58,000
Normal profit (10% on CCE)	95,000	49,000	48,000
Super Profit	45,000	105000	10,000
Goodwill	135000	315000	30,000

Purchase consideration :

	X	Y	Z	Total
CCE	9,50,000	4,90,000	4,80,000	
Goodwill	1,35,000	3,15,000	30,000	
Total	10,85,000	8,05,000	5.10,000	24,00,000
Shares				
(In the ratio of 140 :154:58)	7,15,900	7,87,500	2,96,600	18,00,000*
Debentures (bal. figure)				

	3,69,100 10,85,000	17,500 8,05,000	2,13,400 5,10,000	6,00,000 24,00,000

*Issue of Equity shares and Debentures for this purpose is to be in the ratio of 3:1. (item no. 6 of the question)

Answer to Q. No. 64 (b) :

B/S of XYZ as on 31.3.87

Liabilities	Amount	Assets	Amount
S. Capital	21,50,000	Goodwill	4,80,000
Deb.	6,00,000	FA	21,00,000
Crs.	4,50,000	CA	5,70,000
		P.exp.	50,000
Total	32,00,000	Total	32,00,000

Answer to Q. No. 65 : Net assets for equity shareholders (Rs. crores)

	Big	Small
Goodwill	40	75
FA	200	429
WC	200	200
Loan	-100	-100
P . Shares	---------	-60
Net assets for equity shareholders	340	544

Intrinsic value of share of purchasing co. (Small) : 544 crores/ 4 crore = 136
Net assets taken over : Rs. 340 Crores.
PC = 340 crores/136 = 2.50 crores shares of Rs. 10 each i.e. Rs. 25 Crores

Journal of Small :
BP a/c Dr. 25
To Liquidator of Big 25

Liquidator of Big Dr. 25
To ESC 25

FA a/c Dr. 150
CA a/c Dr. 200
To Loan 100
To ESC a/c 25
To CR a/c 225 (Bal. fig.)

B/S of Small Ltd as on 31.3.88 (Rs. Crores)

Liabilities	Amount	Assets	Amount
ESC	65	FA	300
PSC	60	CA	400
R & S 150 + 225 (CR)	375		
Loan	200		
Total		Total	700

Intrinsic value of Small (after Business take over)

Goodwill	115
FA	629
WC	400
Loan	-200
P. share	-60
Net assets for equity shareholders	884

Intrinsic value = Rs.884 crores/ 6.50 Crores = Rs. 136

Working Note to Q. No. 66 :

Let the value of all the shares of AB = A
Let the value of all the shares of MB = M

A = (1/4)M + 11,00,000 – 240,000 – 60,000
M =(2/5)A + 4,00,000 – 80,000 – 30,000

Solving the two equations : A = 9,72,222 M = 6,88,889

Journal Of AM

Business Purchase a/c	Dr.	16,61,111	
To Liquidator of AB			9,72,222
To Liquidator of MB			6,88,889

FA a/c	Dr.	10,00,000	
CA a/c	Dr.	5,00,000	
Shares of AB a/c	Dr	9,72,222(2/5)	
Shares of MB a/c	Dr.	6,88,889(1/4)	
To Liabilities For Deb.			3,20,000
To Crs.			80,000
To B P a/c			16,61,111

Liq. Of AB	Dr.	9,72,222
To Shares of AB		9,72,222(2/5)
To ESC		5,83,300
To Cash a/c		33

Liq. Of MB Dr. 6,88,889
To Shares of MB 6,88,889(1/4)
To ESC 5,16,600
To Cash a/c 67

Liability for Deb. a/c Dr. 3,20,000
To 15% Debentures a/c 3,20,000

Amalgamation Adj. a/c Dr. 70000
To Investment Allowance Reserve 70000

LOGARITHMS

Logarithms are of great use in calculations. They simplify typical calculations. With the help of Logarithms, we can make such calculations which other wise are difficult to make. Logarithms are of two types (i) simple Logarithms (mathematically called as log base to 10) (ii) natural log (mathematically called as natural log). In this note we shall be studying simple logarithms.

The logarithm of a number consists of two parts – characteristic and mantissa. Characteristic is determined without any table. Mantissa is determined using log tables.

Finding characteristic of a number 1 or greater than 1 : In this case characteristic is equal to "number of digits before decimal" minus "one".

Number	7	56	567	5678	56432	5670.23	167.89
Character-istic	0	1	2	3	4	3	2

Finding characteristic of a number less than one : In this case characteristic is negative. Negative sign is written in the form of bar . For example -1 is written as 1 , -2 is written as 2 , -3 is written as 3 . Write the number (of which

characteristic is to be determined) in proper decimal form . In this case characteristic is number of zeros before and just after decimal .

Number	.9	.08	.007	.0006	.00006	.00908	.002003
Number in proper Decimal form	0.9	0.08	0.007	0.0006	0.00006	0.00908	0.002003
Characteristic							

MANTISSA is determined using log tables. Mantissa is always positive. For determining Mantissa decimal is ignored. Before finding Mantissa, the number (of which mantissa is to be determined) should be reduced to four digits by approximation.

Number	233	2655	456.8	0.89	0.00902
Characteristic	2	3	2		
Mantissa	.3674	.4240	.6598	.9494	.9552
Logarithms	2.3674	3.4240	2.6598		

ANTILOG is determined using Antilog tables. The table is consulted only for Mantissa part. Place of decimal is "characteristic plus one". This place is counted from left hand side.

Number	233	2655	456.8	0.89	0.00902
Log	2.3674	3.4240	2.6598		
Antilog					

Question 1 : Find log of (i) 2 (ii) 56 (iii) 567 (iv) 5678 (v) 56.78 (vi) 0.543 (vii) 55556.67

Question 2 : Find Antilog of above log values.

CONTENTS

	PAGE
Value Added Statement	1
EVA	19
Accounting for Not-For-Profit Organization	24
Concept of Capital Maintenance	29
Accountant's Report for Prospectus	31
Human Resource Accounting	36
Mutual Funds	41
Merchant Bankers	46
Accounting by Stock Brokers	48
NBFC	50
Futures & Options	62
Corporate Social Reporting	65
ESOP	70
ESPP	72
Corporate Governance	73
Holding Company Accounts	77
Valuation of Goodwill and Shares	121
Amalgamation, Absorption and Reconstruction (Including Corporate Restructuring)	143
Test Papers	174
Hints, Answers and Solutions to Test Papers	225
LOGARITHMS	264