UNIVERSITY OF CALICUT

SCHOOL OF DISTANCE EDUCATION

M.Com

II Semester

CORE COURSE
(2019 ADMISSION ONWARDS)

ADVANCED CORPORATE ACCOUNTING
(MCM2C06)

190606

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STUDY MATERIAL
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UNIVERSITY OF CALICUT
SCHOOL OF DISTANCE EDUCATION
Calicut University P.O. Malappuram,
Kerala, India – 673635

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ADVANCED CORPORATE ACCOUNTING (MCM2C06)

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MODULE I:

GROUP FINANCIAL STATEMENTS

Group financial statements are financial statements that include the financial information for more than one component. A component is an entity or business activity for which financial information is separately prepared, and which is included in the group financial statements. A component is most commonly a subsidiary, but it may also be a function, process, product, service, or geographical location, or even an investment accounted for under the equitymethod.

Group Accounts are the financial statements of a group of companies. These are usually presented in the form of consolidated accounts.They are an example of the 'substance over form' principle in financial reporting. Some large businesses are organised as a single company. If group accounts are not prepared, it would be very difficult to make appropriate comparisons. The purpose of group accounts is to report the results and financial position of the businesses in a way that makes them readily comparable, even though they have different legal structures.

Group Structures: arrangement, and articulation of the members of that group. The group's formation is its overall "design" or "architecture," meaning its general configuration for unifying the constituent elements into a single unit-the group's basic shape. The structure is the underlying pattern of stable relationships among the group members

IFRS 10/ Ind AS 110

IFRS 10 establishes principles for presenting and preparing consolidated financial statements when an entity controls one or more other entities.The primary goal behind this standard is to come up with a single model for control which could be applied to all entities. In other words, IFRS 10 is required in order to have control over an investee by an investor, it must have all three of the following: 1) Power over the investee; 2) Exposure or rights to variable returns from its involvement with the investee; and 3) The ability to use its power over the investee to affect the amount of the investor's returns. IFRS 10 provides guidance on applying this new control model with a view to addressing some of the more complex areas that led to diversity in the past. This includes: when holding a significant but less than a majority of voting rights can give power (i.e. "de facto power"), when potential voting rights should be considered in the assessment of control, what factors should be considered in assessing control for entities not controlled by voting rights (i.e. special purpose entities or structured entities), when an entity is acting as an agent on behalf of others and how this impacts the assessment of control.

In simple, Ind AS 110 establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. The standard defines the principles of control and how to apply the same and explains the accounting requirements for preparing consolidated financial statements.

CONSOLIDATED FINANCIAL STATEMENT

- combine like items of assets, liabilities, equity, income, expenses and cash flows of the parent with those of its subsidiaries
- offset (eliminate) the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary
- eliminate in full intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between entities of the group (profits or losses resulting from intragroup transactions that

are recognized in assets, such as inventory and fixed assets, are eliminated in full).

A reporting entity includes the income and expenses of a subsidiary in the consolidated financial statements from the date it gains control until the date when the reporting entity ceases to control the subsidiary. Income and expenses of the subsidiary are based on the amounts of the assets and liabilities recognized in the consolidated financial statements at the acquisition date.

The parent and subsidiaries are required to have the same reporting dates, or consolidation based on additional financial information prepared by subsidiary, unless impracticable. Where impracticable, the most recent financial statements of the subsidiary are used, adjusted for the effects of significant transactions or events between the reporting dates of the subsidiary and consolidated financial statements. The difference between the date of the subsidiary's financial statements and that of the consolidated financial statements shall be no more than three months.

Non-controlling interests (NCI)

- A parent shall present non-controlling interests in the consolidated balance sheet within equity, separately from the equity of the owners of the parent.
- Changes in a parent’s ownership interest in a subsidiary that do not result in the parent losing control of the subsidiary are equity transactions (i.e. transactions with owners in their capacity as owners).

Non-controlling interest is the equity in a subsidiary not attributable, directly or indirectly, to a parent. For example, when an investor acquires 100% share in a company, then there’s no non-controlling interest, because the investor owns subsidiary’s equity in full. However, when an investor acquires less than 100%, let’s say

80%, then there's non-controlling interest of 20%, as the 20% of subsidiary's net assets belong to someone else.

IFRS 3 permits 2 methods of measuring non-controlling interest:

1. Fair value, or
2. The proportionate share in the recognized acquiree's net assets.

Selection of method for measuring non-controlling interest directly impacts the amount of goodwill recognized.

If a parent loses control of a subsidiary, the parent:

(a) Derecognizes the assets and liabilities of the former subsidiary from the consolidated balance sheet.

(b) Recognizes any investment retained in the former subsidiary at its fair value when control is lost and subsequently accounts for it and for any amounts owed by or to the former subsidiary in accordance with relevant Ind AS. That fair value shall be regarded as the fair value on initial recognition of a financial asset in accordance with Ind AS 39 or, when appropriate, the cost on initial recognition of an investment in an associate or joint venture.

(c) Recognizes the gain or loss associated with the loss of control attributable to the former controlling interest.

IFRS 3/ Ind AS 103 states that financial reporting for Business Combinations should be done as per purchase method of accounting. Under purchase method of accounting, the acquirer identifiable assets and liabilities should be measured at their fair value on the acquisition date, a method that requires significantly more effort than pooling of interests method and will usually result in the recognition of goodwill or negative goodwill on acquisition.

Ind AS 103 "Business Combinations" deals with the accounting for business combinations in standalone as well as consolidated financial statements. A set of assets acquired and liabilities assumed are typically regarded as a business if they can together run independently as a going concern (i.e. it consists of inputs and processes applied to those inputs, which has the ability to create an output). If they do not constitute business, the same shall be accounted as an asset acquisition. Ind AS 103 specifically provides for fair valuation of assets, liabilities and even non-controlling interest, which was earlier described as minority interest and valued at the amount of equity attributable to minority shareholders. One exception to such valuation is Common Control Business Combinations where the items are recorded at their carrying value.

Consolidated financial statements: [IFRS 10:B86]

GOODWILL VALUATION (IFRS 3/ Ind AS 103)

Goodwill is an asset representing the future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognized.

The acquirer shall recognize goodwill as of the acquisition date measured as the excess of (a) over (b) below:

(a) the aggregate of:

(i) the consideration transferred measured in accordance with this Indian Accounting Standard, which generally requires acquisition-date fair value

(ii) the amount of any non-controlling interest in the acquiree measured in accordance with this Indian Accounting Standard; and

(iii) in a business combination achieved in stages, the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree.

(b) the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed measured in accordance with this Indian Accounting Standard. In a business combination in which the acquirer and the acquiree (or its former owners) exchange only equity interests, the acquisition-date fair value of the acquiree's equity interests may be more reliably measurable than the acquisition date fair value of the acquirer's equity interests. If so, the acquirer shall determine the amount of goodwill by using the acquisition-date fair value of the acquiree's equity interests instead of the acquisition-date fair value of the equity interests transferred. To determine the amount of goodwill in a business combination in which no consideration is transferred, the acquirer shall use the acquisition-date fair value of the acquirer's interest in the acquiree determined using a valuation technique in place of the acquisition-date fair value of the consideration transferred.

The objective of IFRS 3 Business Combinations is to improve the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements about a business combination and its effects.

More specifically, IFRS 3 establishes principles and requirements for how the acquirer:

- Recognizes and measures the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree;
- Recognizes and measures the goodwill acquired in the business combination, or a gain from a bargain purchase;
- Determines what information to disclose about the business combination.

What is the difference between IFRS 3 and IFRS 10?

Although it may seem that the IFRS 10 Consolidated Financial Statements and IFRS 3 Business Combinations deal with the same thing, that's not the whole truth. Both standards deal with business combinations and their financial statements. But while IFRS 10 defines a control and prescribes specific consolidation procedures, IFRS 3 is more about the measurement of the items in the consolidated financial statements, such as goodwill, non-controlling interest, etc. It seeks to enhance the relevance, reliability and comparability of information provided about business combinations (e.g. acquisitions and mergers) and their effects. It sets out the principles on the recognition and measurement of acquired assets and liabilities, the determination of goodwill and the necessary disclosures.

INTRA – GROUP TRANSACTIONS

Intra-group transactions are transactions between entities within a group of entities and that group is consolidated into one set of Consolidated Financial Statements. Intra-group transactions are not with third parties outside the scope of consolidation (this means the group of companies consolidated to one unit). In the Consolidated Financial Statements only balances and transactions remain with third parties outside the scope of consolidation.

In the consolidation process all company financial statements of each reporting entity in the scope of consolidation are first combined into a sub-consolidation, then all intra-group transactions are eliminated, sometimes leaving a small (not material) mismatch. Material mismatches have to be investigated and corrected in close collaboration with the two entities involved. Also Intra-company transactions

(transactions with related companies outside the scope of consolidation) may be netted, showing only the remaining receivable or payable with that related company.

Any profits resulting from intra group transactions are eliminated from the consolidated accounts. (For example this would include fixed assets, stocks, investments etc. transferred within the group). Any profits resulting from intra group transactions are eliminated from the consolidated accounts. (For example this would include fixed assets, stocks, investments etc. transferred within the group). The consolidated financial statements are the statements of the group, i.e. an economic entity consisting of a parent and its subsidiaries. These consolidated financial statements then can only contain revenues, expenses, profits, assets and liabilities that relate to parties external to the group. Adjustments must be made for intragroup transactions as these are internal to the economic entity, and do not reflect the effects of transactions with external parties. This is consistent with the entity concept of consolidation, which defines the group as the net assets of the parent, together with the net assets of the subsidiaries. Transactions between these parties internal to the group must be adjusted in full.

What is meant by 'realisation of intragroup profits or losses'?

Profits/losses are realised when an economic entity transacts with another external entity. For a group, this is consistent with the concept that the consolidated financial statements show only the results of transactions with external entities. The consolidated statement of profit or loss and other comprehensive income will thus show only realised profits and realised losses. Profits/losses recognised by group members on sale of assets within the group are unrealised profits/losses to the extent that the assets are still within the group.

Realisation of profits/losses on intragroup transactions involving assets normally occurs when an external party gets involved. With intragroup sales of inventories, involvement of an external party, or realisation, occurs when the inventories are on-sold to an external entity. With intragroup sales of depreciable assets, realisation occurs as the asset is used up, as the benefits are received by the group as a result of use of the asset. The proportion of profits/losses realised in any one period is measured by reference to the depreciation charged on the transferred depreciable asset.

ADJUSTMENT OF UNREALISED PROFIT

Another common adjustment is the removal of unrealised profit. This arises when profits are made on intra-group trading and the related inventories have not subsequently been sold to customers outside the group. Until inventory is sold to entities out with the group, any profit is unrealised and should be eliminated from the consolidated accounts.In the consolidated statement of profit or loss we must always consider two steps:

- Has there been any intra-group trading during the year, irrespective of whether the goods are still included in inventory at the year end?
- Do any of the items remain in inventory at the end of the year?

REVALUATION OF ASSETS AND LIABILITIES

IFRS require fixed assets to be initially recorded at cost, but there are two accounting models – the cost model and the revaluation model.

In the revaluation model, an asset is initially recorded at cost, but subsequently its carrying amount may be increased to account for appreciation in value. The difference between the cost model and revaluation model is that the revaluation model allows both downward and upward adjustment in value of an asset, while the cost model allows only downward adjustment due to impairment loss. This is the model currently adopted by IFRS

BONUS SHARES

The Subsidiary company may issue Bonus shares either at the time of acquisition of shares by the holding company or after the acquisition of shares by the Holding company. For issuing bonus shares, the accumulated profits in the Balance Sheet of the subsidiary company are employed. These profits may be capital or revenue in nature or a combination of both. At the time of bonus issue the share of the Holding company as well as the minorities increases proportionately (in terms of the ration of bonus issue) but the proportion of their ownership remains the same as before. If bonus shares are issued out of capital profits are adjusted accordingly and bonus shares transferred to cost of control. If bonus shares issued out of revenue profit of subsidiary company to that extent revenue profit stand capitalized and will affect capital reserve or goodwill as the case may be.

DIVIDEND ON EQUITY SHARES

The Subsidiary company may declare dividend on its equity shares and the following are the possibilities with respect to it.

a) Intention to propose dividend: In such a case since the proposal has not been approved in the meeting the intention may be ignored and no adjustment is required (in terms of calculation) with respect to this dividend intention.
b) Proposed dividend: It is possible that dividend has been proposed in a meeting on the closing date of the financial year but no notification of this fact has been made in

the books of the Holding company. In such a case, the amount of dividend declared may be added to the profits of the Subsidiary company (assuming this has been deducted) and then the analysis of profits is performed in the usual manner. No adjustment is needed in the books of the Holding company.

c) Dividends Payable: In some cases, the dividends that have been declared by the Subsidiary firm may have been adjusted for in both the books i.e. the Subsidiary and Holding company. In this case adjustment is made in the books of the Subsidiary company. In the books of the Holding company the dividend that are receivable from the Subsidiary company will be credited to Profit and Loss Account of the Holding company (in terms of income receivable on investments).It is possible that these dividends have been paid by the subsidiary firm out of Capital profit, revenue profit, combination of both profit.

- If dividend of subsidiary company have been declared totally out of capital profit, then it is incorrect that this capital income should stand credited to the revenue P/L Account of the holding company. Therefore one adjustment entry is made for remaining dividend from the P/L Account of the holding company and they are transferred to cost of control.

P/L Account (H Ltd.) Dr

To Cost of control/Investment Account

(With the amount of dividend receivable from the Subsidiary firm)

- If the dividend of the subsidiary firm have been declared out of Revenue profit then they should be credited to the P/L A/c. of the Holding Company and of they are already included therein as per our presumption, no adjustment is required.

- The dividend receivable by Holding Company may be partly out of capital profit or out of revenue profit of Subsidiary company. The portion paid out of capital profit will be eliminated form P/L Account of Holding company and transferred to cost of control with respect to the portion of the dividend receivable out of revenue profit no adjustment is required. With respect to the minorities irrespective of the dividend declared by the Subsidiary company being payable out of capital profit or revenue profit will be added to minority interest.

d) Dividend paid: The Subsidiary company may have declared a dividend in the course of the financial year and this fact has been adjusted for in both the books and in fact the cash liability has already been met by subsidiary firm for the purpose of dividend payment. This implies there is no liability outstanding with respect to payment of dividends therefore no addition on account dividends has to be made to minority interest.

- the dividend must have been credited to P/L Account out of capital profit, revenue profit are a combination from the subsidiary company's books. The portion out of capital profit stated earlier will be transferred from the P/L Account of the Holding company to the cost of control.
- Share Premium: The share premium account may appear in the Balance Sheet of the Holding company at the time of consolidation. It will continue as share premium account. However if the holding company has issued some of its own shares to the subsidiary company the share premium due on this share will be adjusted for in the cost of control. If share premium

appears in the books of subsidiary company, it may be prior to the acquisition of shares by the holding company in which case it is treated as capital profit in the analysis of profit. However, the share premium arises after acquisition of share by a company it will continue as share premium in the consolidated Balance Sheet.

- Sale of Share: The holding company may sell some of the share of the subsidiary company that it holds as investment. The P/L on such sale is transfer to cost of control. This changes the proportion of the Holding company and minority interest and requires adjustment in calculation of cost of control, minority interest and an analysis of profit will have to be performed.
- Purchase of shares in instalments: The Holding company may acquire shares in the subsidiary firm not in once single instalment but in a number of instalments.

If the earlier dates of the acquisition may be ignored. If however, shares have been acquired in major instalments, a step by step analysis of profit after taking into consideration the dates of acquisition will have to be performed in the analysis of profit between capital and revenue.

MODULE II

ACCOUNTING FOR CORPORATE RESTRUCTURING

Restructuring is the corporate management term for the act of reorganizing the legal, ownership, operational or other structures of a company for the purpose of making it more profitable or better organized for its present needs. Alternate reasons for restructuringinclude a change of ownership or ownership structure, demerger or a response to a crisis or major change in the business such as bankruptcy, repositioning or buyout. Restructuring may also be described as corporate restructuring, debt restructuring and financial restructuring.

A merger is defined as the joining of two or more companies to form a single legal entity. Generally, the sets of the smaller company are merged into those of the larger, surviving company and shareholders of the target are either bought out or become shareholders in the acquiring corporation. A merger usually requires approval by the shareholders of both the acquiring corporation and the target entity. An acquisition, on the other hand, is the purchase of more than 50% of the voting shares of one firm by another. Following the acquisition of two companies can continue as separate legal entities with the company referred to as the parent company and the target as subsidiary. An acquisition may be structured in one of the four forms: cash purchase of assets, cash purchase of stock, issuance of stock for assets, or issuance of stock for stock. In contrast to a merger, in an acquisition the buyer can negotiate which assets it purchases and which liabilities it assumes. Furthermore, if the transaction is structured as an acquisition of the target's stock, the buyer negotiates only with the target shareholders for the sale of their stock.

Acquisition accounting is a set of formal guidelines describing how assets, liabilities, non-controlling interest and goodwill of an acquired company must be reported by the purchaser. The fair market value of the acquired company is allocated between the net tangibleand intangible assets portion of the balance sheet of the buyer. Any resulting difference is regarded as goodwill. All business combinations must be treated as acquisitions for accounting purposes.

When a company is suffering loss for several past years and suffering from financial difficulties, it may go for reconstruction. In other words, when a company's balance sheet shows huge accumulated losses, heavy fictitious and intangible assets or is in financial difficulties or is to over capitalized, and then the process of reconstruction is restored.

Types of Reconstruction

Reconstruction may be external or internal which are described below:

1. External reconstruction: When a company is suffering losses for the past several years and facing financial crisis, the company can sell its business to another newly formed company. Actually, the new company is formed to take over the assets and liabilities of the old company. This process is called external reconstruction. In other words, external reconstruction refers to the sale of the business of existing company to another company formed for the purposed. In external reconstruction, one company is liquidated and another new company is formed. The liquidated company is called "Vendor Company" and the new company is called "Purchasing Company". Shareholders of

vendor company become the shareholders of purchasing company.

2. Internal reconstruction: refers to the internal re-organization of the financial structure of a company. It is also termed as re-organization which permits the existing company to be continued. Generally, share capital is reduced to write off the past accumulated losses of the company. The accounting procedure of internal reconstruction is distinct from that of amalgamation, absorption and external reconstruction.

ACCOUNTING FOR LIQUIDATION OF COMPANIES

A company comes into being through a legal process and also comes to an end by the law. Liquidation is the legal procedure by which the company comes to an end. Thus a company being a creation of law, cannot die a natural death. A company, when found necessary, can be liquidated. The terms ‘break-up basis’ and ‘liquidation basis’ are not defined terms that are used in IFRS but are ones that are used informally. ‘Break-up basis’ is used in some countries to signify that an entity is at a stage where its assets are being realized or are about to be realized as part of the process of liquidating the entity. In other countries the terms ‘liquidation basis’ or ‘an orderly realisation basis’ are used and are broadly equivalent in nature. An informative description of the preparation basis adopted will often be more important than the label attributed to it. A second point is that each situation needs to be assessed on its own facts and circumstances as some entities in a non-going concern situation will be closer to liquidation or ceasing trading than others. The accounting will typically reflect this. For example, when an entity is in the process of being liquidated or will be liquidated imminently, the financial statements might be prepared under what is sometimes referred to as a 'break-up basis' or 'liquidation basis'. Quantification of the amount of any surplus that may be available for distribution to the shareholders (i.e. what the value of the entity will be when it is 'broken up' into its separate parts on liquidation).

STATEMENT OF AFFAIRS

A Statement of Affairs is a document detailing a company's assets and liabilities. Generally prepared by a liquidator or appointed professional during certain insolvency proceedings, the document is later registered at Companies House, where it becomes available for public view.

The Statement of Affairs includes details of any fixed or floating charges secured on company assets, and provides detailed information for interested parties – generally creditors, shareholders and the Insolvency Practitioner (IP), but the document could also prove to be of interest to potential buyers.

The Statement of Affair is a summary of Company's assets and liabilities. It states a net book value and amount expected to realize at the date of insolvency of the business. Accompanying the balance sheet is a list of creditors and shareholders.

As per Section 454 of the Companies Act, the Officers or Directors of the Company under winding up order, must make out and submit, within 21 days of the court's order, or within such extended time, not exceeding three months' time, as the liquidator or court may allow, a statement containing the following particulars.

(a) The assets of the company, stating separately the cash balance in hand and at the bank, if any, and negotiable securities, if any, held by the company.

(b) Its debts and liabilities.

(c) The names, residences and occupations of its creditors, stating separately the amount of secured and unsecured debts; and in the case of secured debts, particulars of the securities given, whether by the company or an officer thereof, their value and the dates on which they were given.

(d) The debts due to the company and the names, residences and occupations of the persons from whom they are due and the amount likely to be realised on account thereof.

(e) Such further or other information as may be prescribed or as the official liquidator may require.

The statement must be in the prescribed form and properly verified by an affidavit. It should be open for inspection by a creditor, or contributory of the company, on payment of a prescribed fee. The concerned creditor or contributory can also have an extract from it.

DEFICIENCY/SURPLUS ACCOUNT

An account supplementing the balance sheet of a financially weak enterprise showing estimated realization values of assets and their insufficiency to meet creditors' claims and occasionally indicating the causes of the difficulty is called as deficiency account. On the other hand, a surplus is the residual amount of resources remaining after a period of usage. In the accounting area, a surplus refers to the amount of retained earnings recorded on an entity's balance sheet; a surplus is considered to be good, since it implies that there are excess resources available that can be used in the future. An account supplementing the surplus fund is known as surplus account.

LIQUIDATOR’S FINAL STATEMENT OF ACCOUNT

The liquidator’s task is to realize the assets and disburse the amounts among those who have a rightful claim to it; in every case the liquidator has to prepare a statement showing how much he realized and how the amount was distributed.

The following is the order in which disbursements will be made by the liquidator:—

(a) Secured creditors up to their claim or up to the amount realized by sale of securities held by them, whichever is less. The creditors themselves may sell the securities; they will pay to the liquidator any surplus after meeting their claims. Only the surplus is shown as a receipt; the payment to secured creditors is not shown in the liquidator’s final statement of account. The balance left unsatisfied—that is when the claims of the creditors are more than the amount realized by sale of securities—will be added to unsecured creditors.

(b) Legal charges.

(c) Remuneration to the liquidator.

(d) Costs of winding up.

(e) Preferential creditors.

(f) Debenture holders or other creditors having a floating charge on the assets of the company. (While preparing the Liquidator's Statement of Account, payment to preferential creditors is shown, however, after the payment to debenture holders having a floating charge.)

(g) Unsecured creditors. (This may include liability in respect of dividend or amounts due to shareholders on account of profits. In this case, the amount in respect of dividends, etc., shall be paid only after the outsiders are satisfied.)

(h) Preference shareholders,

(i) Equity shareholders. Unless the articles contain provisions to the effect that preference shareholders are entitled to participate in the surplus left after meeting the claims of the equity shareholders in full, the whole of the amount left after payment to preference shareholders will go to the equity shareholders.

The various claims have priority in the order mentioned above. Hence, if the amount available is exhausted after paying, say, the preferential creditors, payment cannot be made to unsecured creditors or anybody else coming after the preferential creditors. The form prescribed by the Supreme Court is given later. While preparing the Liquidator's Statement of Account, it should be noted that there is no double entry involved. It is only a statement although presented in the form of an account. (It is really a summary of the Cash Book after the start of liquidation).

<u>Liquidator's Remuneration.</u> In case of compulsory winding up, the remuneration is fixed by the Court and the amount is payable to the Court since the official liquidator is a salaried employee of the Government. In case of voluntary winding up, the remuneration is fixed by the meeting

which appoints the liquidator. The remuneration once fixed cannot be increased. Usually, the remuneration consists of a commission on assets realized plus a commission on the amount paid to unsecured creditors. Unsecured creditors include preferential creditors unless otherwise stated. The commission on unsecured creditors is on the amount paid and hence care should be exercised in calculating the commission.

RECEIVER'S STATEMENT OF ACCOUNTS

A receiver is generally appointed by the Court to take possession of certain property for protective purposes or for receiving income and profits from the property and for applying it as directed. Sometimes, a mortgagee is also given the power to appoint a receiver in certain circumstances. The debenture-holders may have the power under the Debenture Deed. The Receiver will have the duty of duly accounting for the sums received by him. In case the company is being wound up, the

Receiver (if appointed) will have to observe the rule regarding preferential payments and after paying the mortgagee by whom he is appointed (or paying those persons for whose protection he is appointed by the Court) he will have to hand over the surplus to the Liquidator. There will thus be two accounts: (1) the Receiver's Statement of Account and (2) Liquidator's Final Statement of Account. The Receiver is entitled to recover his expenses and remuneration from sums collected by him.

Problems

1. The following is the draft Balance Sheet of Diverse Lt. having an authorized capital of Rs. 1,000 crores as on 31st March, 2017:

	(Rs. in crores)	
I. Equity and Liabilities		
1. Shareholders' fund		
a) Share Capital		
Equity shares of	250	

10 each fully paid up	750	1,000
b) Reserves and Surplus		
(Revenue)	400	
2. Non-current Liabilities	600	1,000
Long term borrowings		2,000
Secured against: (a)		**4,000**
Fixed assets Rs.300 Cr.		
(b)		
Working Capital Rs. 100 Cr.		
Unsecured		
3. Current Liabilities	800	
	(200)	600
		400
II. Assets		3,000
1. Non – Current Assets		**4,000**
a) Fixed assets		
(i) Tangible Assets		

Gross Block Less: Depreciation b) Investment at Cost (Market Value Rs. 1,000 Cr.) 2. Current Assets		

Capital Commitments: Rs.700 Crores

The company consists of 2 divisions:

i. Established division whose gross block was Rs. 200 Crores and net block was Rs.30 Crores; current assets were Rs. 1,500 Crores And working capital Rs. 1,200 Crores; the entire amount being financed by shareholders' funds.
ii. New project divisions to which remaining fixed assets, current assets and current liabilities related.

The following scheme of reconstruction was agreed upon:

a) Two companies, Sunrise Ltd. And Khajana Ltd. Are to be formed. The authorized capital of Sunrise Ltd. is Rs. 1,000 Crores. The authorized capital of Khajana Ltd. is Rs. 500 Crores.
b) Khajana Ltd. Is to take over investments at Rs. 800 Crores and unsecured loans at balance sheet value. It is to allot equity shares of Rs. 10 each at par to the members of Diverse Ltd. In satisfaction of the amount due under agreement.
c) Sunrise Ltd. is to take over the fixed assets and Net working capital of the new project division along with the secured loans and obligation of capital commitments for which Diverse Ltd. is to continue stand guarantee at book values. It is to allot one crore equity shares of Rs. 10 each as consideration to Diverse Ltd. Sunrise Ltd made an issue of

unsecured convertible debentures of Rs.500 crores carrying interest at 15% per annum and having right to convert into equity shares of Rs.10 each at par on 31.3. 2019. The issue was made to the members of Sunrise Ltd. as a right who grabbed the opportunity and subscribed in full.

d) Diverse Ltd. is to guarantee all liabilities transferred to the 2 companies.

e) Diverse Ltd. is to make a bonus issue of equity shares in the ratio of one equity share for every equity share held by making use of the revenue reserves.

Assume that the above scheme was duly approved by the Honourable High Court and that there are no other transactions. Ignore taxation.

You are asked to:

i. Pass journal entries in the books of Diverse Ltd. , and

ii. Prepare the balance sheet of the three companies and the scheme of arrangement.

Ans:

Journal of Diverse Ltd.

Transactions with Khajana Ltd.

(Rs. in crores)

1	Khajana Ltd. A/c Dr. Unsecured Loans A/c Dr. To Investment A/c To Members A/c (Being transfer to investments at agreed value of Rs. 800 crores, unsecured loans at Rs.600 crores) N.1	200 600	 400 400
2	Members A/c Dr.	200	 200

	To Khajana Ltd. A/c (Being consideration received from Khajana Ltd.)		
3	Members A/c Dr. To Capital Reserve A/c (Being balance in members A/c transferred)		

Transactions with Sunrise Ltd.

(Rs. in crores)

1	Sunrise Ltd. A/c (1 cr. Equity shares x Rs.10 each) Dr. Provision for depreciation A/c (N.2) Dr. Secured loans against fixed	10 30 300 100 1,700	 600

	asset A/c Dr. Secured loans against working capital A/c Dr. Current Liabilities A/c (N.2) Dr. To Fixed Assets A/c (N.2) To Current Assets A/c (N.2) To Capital Reserve A/c (Being assets and liabilities of new project division transferred to Sunrise Ltd. along with capital commitments of Rs.700 crores, the differences between consideration and the book values at which transferred assets and		1,500 40

	liabilities appeared being credited to capital reserve.)		
2	Equity shares of Sunrise Ltd. Dr. To Khajana Ltd. A/c (Being the receipt of one crore equity shares at Rs.10 each from Sunrise Ltd. in full discharge of consideration on transfer of assets and liabilities of new project division)	10	10
3	Investment in Debentures A/c Dr. To Bank A/c (Being issue of unsecured convertible debentures by Sunrise Ltd., subscribed in full)	500	500
4	Revenue Reserves A/c Dr.	250	250

	To Equity Share capital A/c (Being allotment of 25 crores equity shares of Rs.10 each as fully paid bonus shares to the members of the company by using revenue reserves in the ratio of one equity share for every equity share held.		

Diverse Ltd.

Balance Sheet after the scheme of arrangement

		Note No.		*(Rs. in crores)*
I	**Equity and liabilities** (1) **Shareholders'funds**: (a) ShareCapital	1	500	

	(b) Reserves andsurplus	2	740	1,240
	(2) **Currentliabilities**			300
II	Total			1,540
	Assets			
	(1) **Non-current Assets**			
	(a) Fixedassets:	3		30
	(b) Non-currentinvestments	4		510
	(2) **Current assets(1,500 – 500)**			1,000
	Total			1,540
	1. Capital commitments			Nil
	2. Contingent Liability			
	Guarantee given in respect of:			

	Capital commitments by Sunrise Ltd.		700	
	Liabilities transferred to Sunrise Ltd.		2100	
	Liabilities transferred to Khajana Ltd.		600	

Notes to Accounts

(Rs. in crores)

1	**Share capital:** Authorized capital: 00 crores Equity Shares of Rs.10 each Issued, subscribed and paid up capital 50 crores Equity Shares of Rs.10 each fully paid-up Of the above shares, 25 crores fully paid Equity Shares of Rs.10 each have been issued as bonus shares by capitalization of	1,000	500

	revenue reserves.		
2	**Reserves and Surplus:**		
	1. Capital Reserve on transferof:		
	Investments to Khajana Ltd.	200	
	Business of new project division to Sunrise Ltd.	40	240
	2. Surpluses (profit and lossAccount):		
	As per last balance sheet	750	
	Less: Used for issue of fully paid bonus shares	250	500
			740
3	**Fixed assets:**		
	Gross block:		
	As per last balance sheet	800	
	Less: Transfer to Sunrise Ltd.	(600)	200
	Provision for depreciation:		
	As per last balance sheet	200	
	Less: In respect of assets transferred to Sunrise Ltd.	(30)	(170)
			30
4	**Investments (at cost):**		

	Investment in Equity Instruments In wholly owned subsidiary Sunrise Ltd. 1 crore equity shares of `10 each Investment in Debentures and bonds 15% unsecured convertible debentures		10 500 510	

Balance Sheet of Sunrise Ltd. after the scheme of arrangement

		Note No.	*(Rs. in crores)*	
I	**Equity and liabilities** (1)**Shareholders' funds**: (a) Share Capital (2)**Non-current liabilities**: (a)Longterm borrowings	 1		 10

	Secured loans	2	400	
	Unsecured loans	3	500	900
	(3)**Current liabilities**			1700
	Total			2,610
II	**Assets**			
	1. **Non-currentassets**			
	(a)Fixedassets			
	(i) Tangibleassets		570	
	(ii)Intangible assets(Goodwill)		40	610
	(2) **Currentassets**			
	(a) Cash and Cash equivalents		500	
	(b) Other current Asset		1,500	2,000
	Total			2,610
	Capital commitments			

	Guarantee given by Diverse Ltd. in respect of : Capital Commitments Liabilities		700 2,100	

Notes to Accounts

(Rs. in crores)

1	**Share Capital** Authorized Capital 100 crores Equity Shares of Rs.10 each Issued, Subscribed and Paid-up capital 1 crore Equity Shares of Rs.10 each fully paid-up (All the above shares have been issued for consideration	1,000 10

	other than cash, on takeover of new project division from Diverse Ltd. All the above shares are held by the holding company Diverse Ltd.)	
2	**Secured Loans**	
	(a) Against fixed assets	300
	(b) Against working capital	100
		400
3	**Unsecured Loans**	
	15% Unsecured convertible Debentures	500
	- Convertible into equity shares of Rs.10 each at par on 31.3.2019	

Balance Sheet of Khanjana Ltd. after the scheme of arrangement

	Note No.	(Rs. in crores)
I. Equity andliabilities		
(1) **Shareholders'funds:**		
(a)ShareCapital	1	200
(2)**Non-currentliabilities**:		
(a)Long termborrowings		
Unsecured loans		600
Total		800
II. Assets		
Non-current investments		800
Total		800
Guarantee given by Diverse Ltd. in respect of unsecured loans		

Notes to Accounts

		(Rs.in crores)
1	**Share Capital**	
	Authorized	
	50 crores Equity Shares of Rs.10 each	500
	Issued, Subscribed and Paid-up	
	20 crores Equity Shares of Rs.10 each fully paid-up	200
	(All the above shares have been issued to members of Diverse Ltd. for consideration other than cash, on acquisition of investments and taking over of liability for unsecured loans from Diverse Ltd.)	

Working Notes:

1. **Amount Due from KhajanaLtd.**

Investments	800
Less: Unsecured Loans	(600)
Net Consideration	200

2. **Segregation of Assets &Liabilities between Established and NewDivision**

As per information in point (i)

	Particulars	*Total (A)*	*Established Division (B)*	*New Project Division (A-B)*
1	Gross Block	800 (Given)	200 (Given)	600(A-B)
	Net Block	600 (Given)	30(Given)	570(A-B)
	Provision for Depreciation	200	170	30
2	Current Assets	3,000 (Given)	1,500 (Given)	1,500 (A-B)

	Working Capital	1,000 (Given)	1,200 (Given)	(200) (A-B)
	Current Liabilities	2,000	300	1,700

(Rs.in crores)

		Established division	*New Project division*	*Total*
1.	Fixed assets:			
	Gross block	200	600	800
	Less: Depreciation	(170)	(30)	(200)
		30	570	600
	Current assets	1,500	1,500	3,000
	Less:Current liabilities	(300)	(1,700)	(2,000)

2.	Employment of funds	1,200	(200)	1,000
	Guarantee by Diverse Ltd. against:			
	(a) (i) Capital commitments			700
	(ii) Liabilities transferred to Sunrise Ltd.			
	Secured loans against fixed assets		300	
	Secured loans against working capital		100	
	Current liabilities		1,700	2,100
	(b) Liabilities transferred to Khajana Ltd.			600

2.Enterprise Ltd. has 2 divisions Laptops and Mobiles. Division Laptops has been making constant profits while division Mobiles has been invariably suffering losses.

On 31st March, 2017, the division-wise draft Balance Sheet was:

(Rs. in crores)

	Laptops	Mobiles	Total
Fixed assets cost	250	500	750
Depreciation	(225)	(400)	(625)
NetAssets	25	100	125
Current assets:	200	500	700
Less: Current liabilities	(25)	(400)	(425)
(B)	175	100	275
Total (A+B)	200	200	400
Financed by:			

Loan funds	-	300	300
Capital : Equity Rs.10 each	25	-	25
Surplus	175	(100)	75
	200	200	400

Division Mobiles along with its assets and liabilities was sold for Rs.25 croresto Turnaround Ltd. a new company, who allotted 1 croreequity shares of Rs.10 each at a premium of Rs.15 per share to the members of Enterprise Ltd. in full settlement of the consideration, in proportion to their shareholding in the company.

Assuming that there are no other transactions, you are asked to:

(i) Pass journal entries in the books of EnterpriseLtd.

(ii) Prepare the Balance Sheet ofEnterprise Ltd. after the entries in (i).

(iii) Prepare the Balance Sheet of TurnaroundLtd.

Ans.

Journal of Enterprise Ltd.

(Rs. in crores)

			Dr. *Rs.*	*Cr.* *Rs.*
(1)	Turnaround Ltd.	Dr.	25	
	Loan Funds	Dr.	300	
	Current Liabilities	Dr.	400	
	Provision for Depreciation	Dr.	400	
	To Fixed Assets			500
	To Current Assets			500
	To Capital Reserve			125
	(Being division Mobiles along with its assets and liabilities sold to Turnaround Ltd. for Rs.25 crores)			

(2)	Capital Reserve	Dr.	25	
	To Turnaround Ltd.			25
	(Being allotment of 1 crore equity shares of Rs. 10 each at a premium of ` 15 per share to the members of Enterprise Ltd. in full settlement of the consideration)			

Notes:

(1) Any other alternative set of entries, with the same net effect on various accounts, may be given by thestudents.

(2) Profitonsaleofdivisionmay,alternatively,becreditedtoProfitandLossAccountinsteadofCapital Reserve,inaccordancewiththerequirementsofAS5(Revised)onNetProfitorLos

sforthePeriod, Prior Period Items and changes in AccountingPolicies.

Enterprise Ltd.

Balance Sheet after reconstruction

(Rs. in crores)

		Note No.		
I.	**Equity and liabilities**			
	(1)Shareholders'funds			
	(a) Share Capital		25	
	(b)Reserves and surplus	1	175	200
	(2) Current Liabilities			25
	Total			225
II.	**Assets**			
	(1) Non-current assets			
	(a) Fixed assets			25
	(2) Current assets			200
	Total			225

Notes to Accounts

		(Rs. in crores)
1.	**Reserves and Surplus**	75
	Add: Capital Reserve on reconstruction	100
		175

NotetoAccounts:ConsequentontransferofDivisionMobilestonewlyincorporatedcompanyTurnaround Ltd., the members of the company have been allotted 1 crore equity shares of Rs.10 each at a premium of Rs. 15 per share of Turnaround Ltd., in full settlement of the consideration in proportion to their shareholding in thecompany.

Balance Sheet of Turnaround Ltd. *es)*

		Note No.		
I.	**Equity and liabilities**			

	(1)**Shareholders'funds**			
	(a) Share Capital	1	10	
	) Reserves and surplus:			
	Securities Premium		15	25
	(2) **Non-currentliabilities**			
	Long term borrowings			300
	(3) **Currentliabilities**			400
	Total			725
II.	**Assets**			
	(1) **Non-currentassets**			
	Fixed assets			
	(i) Tangibleassets		100	
	(ii) Intangibleassets	2	125	225
	(2) **Currentassets**			500
	Total			725

Notes to Accounts

		(Rs. in crores)
1.	**Share Capital:**	
	Issued and Paid-up capital	
	1 crore Equity shares of ` 10 each fully paid up	10
	(All the above shares have been issued for consideration other than cash, to the members of Enterprise Ltd. on takeover of Division Mobiles from Enterprise Ltd.)	
2.	**Intangibles Assets:**	
	Goodwill (N.1)	125

Working Note

1. **Calculation of Goodwill/Capital Reserve for Turnaround**

Ltd. Assets takenover

Non-Current Assets	100
Current Assets	500
Total Assets (A)	600
Loan Funds	300
Current Liabilities	400
Total Liabilities (B)	700
Net Assets C= (A-B)	(100)
Purchase Consideration (given) (D)	25
Goodwill (D-C)	125

3. Kuber Ltd. a non-listed company, furnishes you with the following draft BalanceSheet as at 31st March,2017:

	(Rs. in crores)	
Equity and liabilities (1) Share holders'funds (a) ShareCapital: Authorized capital		

	100	
Issued, subscribed and paid up capital		
12% Redeemable preference shares of Rs.100 each fully paid	75	100
Equity shares of ` 10 each fully paid	25	
(b) Reserves andsurplus:		
Capital reserve	15	
Securities premium	25	
Surplus (profit and loss account)	260	300
(2) Currentliabilities		40
Assets		440
1. Non-currentassets		
Fixed assets: Cost	100	
Less: Provision for depreciation		Nil
2. Non-current Investments at cost (market value Rs. 400Cr.)	(100)	100
3. Currentassets		340
		440

The company redeemed preference shares on 1st April, 2017. It also bought back 50 lakh equity shares of Rs.10 each at Rs. 50 per share. The payments for the above were made out of the huge bank balances, which appeared as part of current assets.

You are asked to:

(i) Pass journal entries to record theabove

(ii) Prepare balancesheet

(iii) Value equity share on net assetbasis.

Ans.

Journal of Kuber Ltd.

	Dr. *Rs.*	*Cr.* *Rs.*
Redeemable preference share capital Account	75	
To Bank Account		75

(Being redemption of 12% preference shares pursuant to capital re- organisation)		
Revenue reserves Account	75	
To Capital redemption reserve Account		75
(Being amount equal to par value of preference shares redeemed out of profits transferred to capital redemption reserve)		
Equity share capital Account	5	
Securities Premium Account	20	
To Bank Account		25
(Being buy-back of 50 lakh equity sharesof Rs.10		

each from the members at a price of ` 50 per share, premium paid transferred to Securities Premium Account)	5	5
Revenue reserves To Capital redemption reserve		
(Being transfer to capital redemption reserve, on buy-back out of reserves)		

Kuber Ltd.

Balance Sheet (after reconstruction)

		Note No.	*(Rs. in crores)*	
I.	**Equity and liabilities** (1) **Shareholders'funds**			

	(a) Share Capital	1.	20	
	(b) Reserves and Surplus	2.	280	300
	(2) **Currentliabilities**			40
	Total			340
II.	**Assets**			
	(1) **Non-currentAssets**			
	(a) Fixed Assets (100-100)		–	-
	(b) Non-current investments (marketvalue: Rs. 400 crores)			100
	(2) **Currentassets**			240
	Total			340

Notes toAccounts

		(Rs. in crores)	
1.	**Share Capital**		
	1. AuthorisedCapital		100
	2. Issued,Subscribed andPaid-up		
	200 lakhs Equity Shares of ` 10 each fully paid up		20
	(50 lakhs Equity Shares of ` 10 each have been bought back out of Securities Premium account at ` 50 per share and 12% 75 lakhs Redeemable Preference Shares of ` 100 each fully paid up, have been redeemed on 1st April, 2017)		
2.	**Reserves and Surplus**		

	(1) CapitalReserve		15
	(2) Capital RedemptionReserve		
	As per last account		
	Add: Transfer from Revenue Reserves (75 + 5)		80
	(3) Securities Premium Reserve (25 -20)		5
	(4) Surplus (Profit and LossA/c)		
	As per last account	260	
	Less: Transfer to Capital Redemption Reserve (75 + 5)	(80)	180
			280

Net asset value of an equity share

	(Rs.in crores)
Investments (at market value)	400

Net current assets	200
Net assets available to equity shareholders	600
No. of equity shares : 2 crores	
Value of equity shares = $\frac{600 \text{ crores}}{2 \text{ crores}}$ = Rs. 300 crores	

Note: As regards treatment of loss (profit) on buy-back, there is no authoritative pronouncement as to whether the difference between the nominal value and the amount paid should be treated as capital or revenue in nature. In the given case, the debit has been given to Securities premium account. Also, in the absence of any other information, it may be assumed that shares have been bought back out of free reserves. However, the securities premium account has restrictive use. Therefore, the companies may opt to utilize the securities premium account for buy back, if available, rather to use the free reserves which can be used for other purposes infuture.

4. Maxi Mini Ltd. has 2 divisions - Maxi and Mini.The draft Balance Sheet as at 31st October, 2017 was asunder:

	Maxi division Rs.	Mini division Rs.	Total (in crores) Rs.
Fixed assets:			
Cost	600	300	900
Depreciation	(500)	(100)	(600)
W.D.V.	100	200	300
Net current assets:			
Current assets	400	300	700
Less: Current liabilities	(100)	(100)	(200)

(B)	300	200	500	
Total (A+B)	400	400	800	
Financed by :				
Loanfunds (secured by a charge on fixed assets)	–	100	100	
Own funds:				
Equity capital (fully paid up ` 10 shares)			50	
Reserves and surplus			650	
(B)			700	
Total (A+B)	400	400	800	

It is decided to form a new company Mini Ltd. to take over the assets and liabilities of Mini division. Accordingly Mini Ltd. was incorporated to take over at Balance Sheet figures the assets and liabilities of that division. Mini Ltd. is to allot 5 crores equity shares of ` 10 each in the company to the members of Maxi Mini Ltd. in full settlement of the consideration. The members of Maxi Mini Ltd. are therefore to become members of Mini 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 Maxi Mini Ltd. and Mini Ltd. Also show the Balance Sheets of the 2 companies as on the morning of 1st November, 2017, showing corresponding previous year'sfigures.

(b) The directors of the 2 companies ask you to find out the net asset value of equity shares pre and postdemerger.

(c) Comment on the impact of demerger on "shareholderswealth".

Ans.

Demerged Company: Mini Division of "Maxi Mini Ltd.''

Resulting Company: “Mini Ltd.”

(a) Journal of Maxi Mini Ltd. (DemergedCompany)

		(Rs.in crores)	
		Dr. Rs.	Cr. Rs.
Current liabilities A/c	Dr.	100	
Loan fund (secured) A/c	Dr.	100	
Provision for depreciation A/c	Dr.	100	
Loss on reconstruction (Balancing figure)	Dr.	300	
To Fixed Assets A/c			300
To Current assets A/c			300
(Being the assets and liabilities of Mini division taken out of the books on transfer of the division to Mini Ltd., the consideration being allotment to the members of the company of			

one equity share of ` 10 each of that company at par for every share held in the company vide scheme of reorganization)		

Journal of Mini Ltd.

	(Rs. in crores)	
	Dr. Rs.	Cr. Rs.
Fixed assets (300-100) A/c Dr.	200	
Current assets A/c Dr.	300	
To Current liabilities A/c		100
To Secured loan funds A/c		100
To Equity share capital A/c		50
To Capital reserve		250
(Being the assets and liabilities of Mini division of Maxi Mini Ltd. taken over and allotment		

of 5 croresequity shares of Rs.10 each at part as fully paid up to the members of Maxi Mini Ltd.)		

Maxi Mini Ltd.

Balance Sheet as at 1st November, 2017

		Note No.	(Rs. in crores)	
			After reconstruction	Before Reconstruction
I.	**Equity and liabilities**			
	(1)**Shareholder's funds**			
	(a) Share Capital	1	50	50
	(b)Reserves and Surplus		<u>350</u>	<u>650</u>
			400	700

	(2) **Non-current liabilities**			
	Secured loan		-	100
	(3) **Current liabilities**		100	200
	Total		—	
			500	1,000
II.	**Assets**			
	(1) **Non-CurrentAssets**			
	Fixed assets :	2	100	300
	(2) **Currentassets**		400	700
	Total		500	1,000

Notes to Accounts

		After reconstruction	Before reconstructions
1.	Reserves and Surplus	650	650
	Less: Loss on	(300)	—

	reconstruction		
		350	650
2.	Fixed Assets	600	900
	Less: Depreciation	(500)	(600)
		100	300

Note to Accounts: Consequent on reconstruction of the company and transfer of Mini division to newly incorporated company Mini Ltd., the members of the company have been allotted 5 crores equity shares of Rs. 10 each at part of Mini Ltd.

Mini Ltd.

Balance Sheet as at 1 November, 2017

		Note No.	(Rs. in crores)	
I.	**Equity and liabilities**			
	(1) **Shareholder's funds**	1		
	(a) ShareCapital		50	

	(b) Reserves andSurplus		250	300
	(2) **Non-currentliabilities**			
	Secured loans			100
	(3) **Currentliabilities**			100
	Total			500
II.	**Assets**			
	(1) **Non-currentassets**			
	(a) Fixedassets			200
	(2) **Currentassets**			300
	Total			500

Notes to Account

	(Rs. in crores)
1. Share Capital: Issued and paid up : 5 crores Equity shares of `	50

10 each fully paid up (All the above shares have been issued for consideration other than cash, to the members of Maxi Mini Ltd., on takeover of Mini division from Maxi MiniLtd.)	

(b) Net asset value of an equityshare

Pre-demerger

Post- demerger

Maxi Mini Ltd.: <u>Rs.700 crores</u> = Rs. 140

<u>Rs.400 crores</u> = Rs. 80

5 crores

5 crores

Mini Ltd.:

<u>Rs.300 crores</u> = Rs.80

5 crores

(c) Demerger into two companies has had

no impact on "net asset value" of shareholding. Pre- demerger, it was Rs. 140 per share. After demerger, it is Rs.80 plus Rs.60 i.e. Rs.140 per originalshare. It is only yield valuation that is expected to change because of separate focusing on two distinct businesses whereby profitability is likely to improve on account of demerger.

A Ltd. agreed to absorb B Ltd. on 31st March 2017, whose summarized balance sheet stood as follows:

Equity and Liabilities	Rs.	Assets	Rs.
Share Capital 80,000 shares of ` 10 each fully paid	8,00,000	Fixed Assets Investments	7,00,000 –
Reserves &		Current	

Surplus		Assets	
General Reserve	1,00,000	Loans & Advances	
Secured Loan	—	Inventory in trade	1,00,000
Unsecured Loan	—	Trade receivables	2,00,000
Current Liabilities & Provisions			
Trade payables	1,00,000		
	10,00,000		10,00,000

The consideration was agreed to be paid as follows:

(a) A payment in cash of Rs.5 per share in B Ltd. and

(b) The issue of shares of Rs.10 each in A Ltd., on the basis of 2 Equity Shares (valued at Rs.15) and one 10% cumulative preference share (valued at Rs.10) for every five shares held in

B Ltd.

The whole of the share capital consists of shareholdings in exact multiple of five except the following holding.

Chopra	116	
Karki	76	
Amar Singh	72	
Malhotra	28	
Other individuals	8	(eight members holding one shareeach)
	300	

It was agreed that A Ltd. will pay in cash for fractional shares equivalent at agreed value of shares in B Ltd. i.e. ` 65 for five shares of ` 50 paid.

Prepare a statement showing the purchase consideration receivable in shares and cash.

Ans.

(a) Schedule ofFraction

	Holding of Shares (A)	Exchangeable in nearest multiple of five (B)	Exchange in equity (C) = (B) / 5 X 2	Preference Exchangeable (D) = (B) / 5 X 1	Non (E)= (A) – (B)
Chopra	116	115	46	23	1
Karki	76	75	30	15	1
Amarsingh	72	70	28	14	2
Malhotra	28	25	10	5	3
Others	8	-	-	-	8
	300	285	114	57	15

Shares Exchangeable: Equity Shares in ALtd.

		No.		No.
(i)	80,000–300 (Total A above)	79,700	2/5 there of	31,880
	300-15 (Total E Above)	285	2/5 there of	114
		79,985		31,994

Shares Exchangeable: Preference Shares in A Ltd.

Shares held as in b (i)	79,700	1/5 there of	15,940
as in b (ii)	285	1/5 there of	57
	79,985		15,997

(b) **There are 15 shares in B Ltd. which are not capable of exchange into equity and preference shares of A Ltd. they will be paid**

$$150 \times \frac{65}{50} = \text{Rs.}195$$

Purchase Consideration	Rs.
31,994 Equity Shares @ Rs.15 each	4,79,910
15,997 Preference shares @ Rs.10 each	1,59,970
Cash on 79,985 @ Rs.5 each	3,99,925
	10,39,805
Add: Cash for 15 shares	195
	10,40,000

MODULE III

ACCOUNTING FOR TAXATION

It is important to understand how to account for taxation, because it has an impact on the income statement (in the tax expense account) and the balance sheet (in the income tax and deferred tax accounts). The tax expense on the income statement has three components: the tax charge for the period; any under- or over-provision of tax for the previous period; and the increase or decrease in the deferred tax provision.

CURRENT TAX EXPENSE

Current tax is defined as the amount of income taxes payable/ (recoverable) in respect of the taxable profit/ (tax loss) for a period. It is the tax that the entity expects to pay/ (recover) in respect of a financial period

DEFFERED TAX

The tax effect on the timing differences is termed as deferred tax which literally means taxes which are deferred. Deferred tax is recognized on all timing difference – Temporary and Permanent.

These deferred taxes are given effect to in the financial statements through Deferred Tax Asset and Liability as under:

Sl.No	Entity Profit Status	Entity – Current	Entity– Future	Effect
1	Book profit higher than the Taxable profit	Pay less tax now	Pay more tax in future	Creates Deferred Tax Liability (DTL)
2	Book profit is less than the Taxable profit	Pay more tax now	Pay less tax in future	Creates Deferred Tax Asset (DTA)

With respect to timing differences related to unabsorbed depreciation or carry forward losses, DTA is recognized only if there is future virtual certainty. It means DTA can be realized only when the company reliably estimates sufficient future taxable income. This test for virtual certainty has to be done every year on balance sheet date and if the condition is not fulfilled, such DTA/DTL should be written off.

While computing future taxable income, only profits pertaining Business and Professional should be considered and not the income from other sources.

A deferred tax liability as being the amount of income tax payable in future periods in respect of taxable temporary differences. So, in simple terms, deferred tax is tax that is payable in the future. However, to understand this definition more fully, it is necessary to explain the term 'taxable temporary differences'.

Temporary differences are defined as being differences between the carrying amount of an asset (or liability) within the Statement of Financial Position and its tax base i.e. the amount at which the asset (or liability) is valued for tax purposes by the relevant tax authority.Taxable temporary differences are those on which tax will be charged in the future when the asset (or liability) is recovered (or settled). A deferred tax liability is recorded in respect of all taxable temporary differences that exist at the year-end – this is sometimes known as the full provision method.

Within financial statements, non-current assets with a limited economic life are subject to depreciation. However, within tax computations, non-current assets are subject to capital allowances (also known as tax depreciation) at rates set within the relevant tax legislation. Where at the year-end the cumulative depreciation charged and the cumulative capital allowances claimed are different, the carrying value of the asset (cost less accumulated depreciation) will then be different to its tax base (cost less accumulated capital allowances) and hence a taxable temporary difference arises.

Assets:

Financial statement basis > tax basis = TTD

Financial statement basis <tax basis = DTD

Liabilities:

Financial statement basis > tax basis = DTD

Financial statement basis <tax basis = TTD

Taxable Temporary Differences (**TTD**)

- These will result in *taxable* amounts when an asset is recovered or a liability is settled.

- Hence, these result in deferred tax liabilities. This means the company will pay more tax in the future.

Items that give rise to taxable temporary differences are:

- Receivables resulting from sales.
- Prepaid expenses.
- Tax depreciation rates > accounting rates.
- Development costs capitalized and amortized.

Deductible Temporary Differences (DTD)

- These will result in *deductible* amounts when an asset is recovered or a liability is settled.
- Hence, these result in deferred tax assets. This means the company will pay less tax in the future.

Items that give rise to deductible temporary differences are:

- Accrued expenses.
- Unearned revenue.
- Tax depreciation rates < accounting rates.
- Tax losses.

Deferred Tax Liability (DTL) or Deferred Tax Asset (DTA) item forms an important part of your Financial Statements.

The basic difference between deferred tax asset and deferred tax liability is the difference in income that is computed as per the provisions of different laws. Some differences that arise due to application of different provisions of law are temporary differences i.e. the differences that get eliminated over a period of time. These temporary differences are accounted for, recognized and carried forward in the books of accounts and accordingly Deferred tax asset A/c and Deferred tax liability A/c are created. The following table shows the major differences between Deferred Tax Asset and Deferred Tax Liability: -

Deferred Tax Asset		Deferred Tax Liability	
1	When profits as per tax laws is more than profits as per books of accounts, Deferred tax asset is required to be created.	**1**	When profits as per tax laws is less than profits as per books of accounts, Deferred tax liability is required to be created.
2	**Deferred Tax Asset journal entry** Deferred Tax Asset A/C…….Dr To Profit & Loss A/c	**2**	**Deferred Tax liability journal entry** Profit & Loss A/C ……. Dr To Deferred Tax Liability A/c
3	It is shown under	**3**	It is shown under

	the head of Non-Current Assets in the balance sheet.		the head of Non-Current Liability in the balance sheet.

It is important to mention that both the deferred tax asset and deferred tax liability are created for the temporary differences only. These differences are temporary in nature and with the time the impact of these differences gets eliminated. Deferred tax asset items as well as deferred tax liability items are a prominent aspect of every company's financial statements. This difference in timings of both, gives rise to certain variance in the company's accounting. The most generic forms of deferred tax are Deferred Tax Asset and Deferred Tax Liability. Deferred tax assets originate when the amount of tax has either been paid or has been carried forward but it has still not been acknowledged in the statement of income. The actual value of the deferred tax asset is generated by comparing the book income with the taxable income. The biggest benefit of the deferred tax asset is that it causes the company's tax liability to go down tremendously in the future.

The conditions that cause origin of deferred tax asset are as follows:

- The taxing authority takes the expenses into account much before time.
- A tax on the revenue earned is levied before time.
- There is a difference in tax rules for asset and liabilities.

Deferred tax liabilities, on the other hand originate when a company underpays the amount of taxes due, which it would eventually pay in the future. It should be remembered, however, that underpaid does not mean that they have not fulfilled their tax-duties, it's just that the taxes would be paid on a different timescale. It is a tax to be paid in future. In simple words, deferred tax liabilities are the opposite of deferred tax asset, which occur when the taxable income is lesser as compared to the income mentioned in the income statements of the company.

The conditions that cause origin of deferred tax liability are as follows:

- In order to showcase great profits to the shareholders, the companies often push their profits.
- When companies keep more than one copies of the financial statement, for their own personal use or for furnishing the same to tax authorities. This is called dual accounting.
- Sometimes companies also push the current profits into future, this gives them the opportunity to decrease the tax amount. By doing this instead of paying the saved

money as taxes, they use that extra money for making investments.

Deferred Tax Expense" refers to the income tax effect on a balance sheet arising out of difference taxable income calculated on the basis of the company's accounting method and the accounting income calculated on the basis of tax laws. Further, it can also be termed as the income tax effect due to timing differences – temporary or permanent, which is basically taxes that are deferred. Deferred tax is a method of accounting for tax on an accruals basis. Deferred tax expense (income) is the amount of tax expense (income) included in the determination of profit or loss for the period in respect of changes in deferred tax assets and deferred tax liabilities during the period.

MODULE IV

ACCOUNTING FOR REVENUE AND LEASES

IFRS 15/ Ind AS 115

IFRS 15 Revenue from contracts with customers applies to all contracts with customers except for: leases, financial instruments and other contractual rights or obligations within the scope of IFRS 9. A contract with a customer may be partially within the scope of IFRS 15 and partially within the scope of another standard. The core principle of IFRS 15 is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The core principle is delivered in a five step model framework, i.e.

a. Identify the contracts with a customer.
b. Identify the performance obligations in the contract.
c. Determine the transaction price.
d. Allocate the transaction price to the performance obligations in the contract.
e. Recognize the revenue when (or as) the entity satisfies a performance obligation.

Contracts with customers will be presented in an entity's statement of financial position as a contract liability, contract asset or a receivable depending on the relationship between the entity's performance and the customer's payment. A contract liability is presented in the statement of financial position where a customer has paid an amount of consideration prior to the entity performing by transferring the related good or service to the customer. Where the entity has performed by transferring a good or service to the customer and the customer has not yet paid the related consideration, a contract asset or a receivable is presented in the statement of financial position, depending on the nature of the entity's right to consideration. A contract asset is recognized when the entity's right to consideration is conditional on something other than the passage of time, for example future performance of the entity. A receivable is recognized when the entity's right to consideration is unconditional except for the passage of time.

IFRS 15 establishes the principles that an entity applies when reporting information about the nature, amount, timing and uncertainty of revenue and cash flows from a contract with a customer. Applying IFRS 15, an entity recognizes revenue to depict the transfer of promised goods or services to the customer in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

To recognize revenue under IFRS 15, an entity applies the following five steps:

- Identify the contract(s) with a customer.
- Identify the performance obligations in the contract. Performance obligations are promises in a contract to transfer to a customer goods or services that are distinct.
- Determine the transaction price. The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer. If the consideration promised in a contract includes a variable amount, an entity must estimate the amount of consideration to which it expects to be entitled in exchange for transferring the promised goods or services to a customer.
- Allocate the transaction price to each performance obligation on the basis of the

relative stand-alone selling prices of each distinct good or service promised in the contract.

- Recognize revenue when a performance obligation is satisfied by transferring a promised good or service to a customer (which is when the customer obtains control of that good or service). A performance obligation may be satisfied at a point in time (typically for promises to transfer goods to a customer) or over time (typically for promises to transfer services to a customer). For a performance obligation satisfied over time, an entity would select an appropriate measure of progress to determine how much revenue should be recognized.

Under Ind AS 115, entities are required to allocate the transaction price to each performance obligation (or distinct good or service) in proportion to its stand-alone selling price i.e. the price at which an entity would sell the promised good or service separately to a customer.

VARIABLE CONSIDERATION

If a transaction includes a variable amount, an entity should estimate the amount of consideration to which it will be entitled in exchange for transferring the promised goods or services to a customer. Items such as discounts, credits, price concessions, returns and performance bonuses may result in variable consideration.

LONG TERM CONTRACTS

In the construction industry, it is very common for a customer to be required to pay a deposit or portion of the contract price upfront. There can also be cash receipts from customers which do not correspond with the timing of the recognition of revenue. IFRS 15 requires the entity to consider if this represents a financing arrangement. If a financing component is significant, IFRS 15 requires an adjustment to be made for the effect of implicit financing. Similarly, aerospace and defence industry absorb long term contracts.

REVENUE RECOGNITION FROM CONSTRUCTION CONTRACTS

IFRS 15 contains specific, and more precise guidance to be applied in determining whether revenue is recognized over time (often referred to as ‘percentage of completion’ under existing standards) or at a point in time.

The general principle is that revenue is recognized at a **point in time**. However, if any of the criteria in IFRS 15, are met, revenue should be recognized **over time**.

If revenue is recognized at a point in time, the overall principle is that revenue should be recognized at the point in time at which it transfers control of the good or service to the customer.

The following indicators should be considered to determine whether control of an asset or service has been transferred:

- Does the customer have a present right to payment for the asset?
- Does the customer have legal title to the asset?
- Has the entity transferred physical possession of the asset to the customer?
- Does the customer have significant risks and rewards of ownership of the asset?
- Has the customer accepted the asset?

If revenue is recognized over time, the overall principle is that revenue is recognized to the extent that each of the vendor's performance obligations has been satisfied. IFRS 15 permits either **output or input methods** to be used to calculate the amount of revenue to be recognized. An **output method** results in revenue being recognized on the basis of direct measurement of the value of goods or services transferred to date, while **input methods** result in revenue being recognized based on measures such as resources consumed, costs incurred or machine hours.

It is noted explicitly that when input methods are used, there may not be a direct relationship between the inputs being used, and the transfer of goods or services to a customer. Consequently, any inputs that do not relate directly to the vendor's performance in transferring those goods and services are excluded when measuring progress to date.

ACCOUNTING FOR LEASES (IAS 17/Ind AS 17)

Leases prescribes the accounting policies and disclosures applicable to leases, both for lessees and lessors. Leases are required to be classified as either finance leases (which transfer substantially all the risks and rewards of ownership, and give rise to asset and liability recognition by the lessee and a receivable by the lessor) and operating leases (which result in expense recognition by the lessee, with the asset remaining recognized by the lessor).The objective of IAS 17 is to prescribe, for lessees and lessors, the appropriate accounting policies and disclosures to apply in relation to finance and operating leases.

IAS 17 applies to all leases other than lease agreements for minerals, oil, natural gas, and similar regenerative resources and licensing agreements for films, videos, plays, manuscripts, patents, copyrights, and similar items.

However, IAS 17 does not apply as the basis of measurement for the following leased assets:

- property held by lessees that is accounted for as investment property for which the lessee uses the fair value model set out in IAS 40
- investment property provided by lessors under operating leases (IAS 40)

- biological assets held by lessees under finance leases (IAS 41)
- biological assets provided by lessors under operating leases (IAS 41)

Classification of leases

A lease is classified as a finance lease if it transfers substantially all the risks and rewards incident to ownership. All other leases are classified as operating leases. Classification is made at the inception of the lease. Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than the form. Situations that would normally lead to a lease being classified as a finance lease include the following:

- the lease transfers ownership of the asset to the lessee by the end of the lease term
- the lessee has the option to purchase the asset at a price which is expected to be

sufficiently lower than fair value at the date the option becomes exercisable that, at the inception of the lease, it is reasonably certain that the option will be exercised

- the lease term is for the major part of the economic life of the asset, even if title is not transferred
- at the inception of the lease, the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset
- the lease assets are of a specialised nature such that only the lessee can use them without major modifications being made

When a lease includes both land and buildings elements, an entity assesses the classification of each element as a finance or an operating lease separately. In determining whether the land element is an operating or a finance lease, an important consideration is that land normally has an indefinite economic life. However, separate measurement of the land and buildings elements is not required if the lessee's interest in both land and buildings is classified as an investment property in accordance with IAS 40 and the fair value model is adopted.

Finance lease is often used to buy equipment for the major part of its useful life. The goods are financed ex GST and have a balloon at the end of the term. Here, at the end of the lease term, the lessee will obtain ownership of the equipment upon a successful 'offer to buy' the equipment. Traditionally this 'offer' is the balloon amount. On the other hand, an operating lease agreement to finance equipment for less than its useful life, and the lessee can return equipment to the lessor at the end of the lease period without any further obligation.

The major differences between Operating and Financing Leases are:

1. **Title:** In a finance lease agreement, ownership of the property is transferred to the lessee at the end of the lease term. But, in operating lease agreement, the ownership of the property is retained during and after the lease term by the lessor.
2. **Balloon/residual amount:** In finance lease agreement, there is a balloon/residual option for the lessee to purchase the property or equipment at a specific price. But, under an operating lease, the lessee does not have this option.
3. **Running costs & administration:** Under an operating lease all running costs (servicing, registration, tyres, insurance etc) are included in the lease within the designated term and usage km with one set monthly repayment amount. Under a finance lease these are generally not included meaning there can be greater

administration and price fluctuation for the lessee.

4. **Account treatment:** Operating lease are treated as expenses (i.e. off balance sheet items) where as a finance lease is included as an asset for the lessee.

Accounting by lessees

The following principles should be applied in the financial statements of lessees:

- At commencement of the lease term, finance leases should be recorded as an asset and a liability at the lower of the fair value of the asset and the present value of the minimum lease payments (discounted at the interest rate implicit in the lease, if practicable, or else at the entity's incremental borrowing rate).
- Finance lease payments should be apportioned between the finance charge and the reduction of the outstanding liability

(the finance charge to be allocated so as to produce a constant periodic rate of interest on the remaining balance of the liability).

- The depreciation policy for assets held under finance leases should be consistent with that for owned assets. If there is no reasonable certainty that the lessee will obtain ownership at the end of the lease – the asset should be depreciated over the shorter of the lease term or the life of the asset.
- For operating leases, the lease payments should be recognised as an expense in the income statement over the lease term on a straight-line basis, unless another systematic basis is more representative of the time pattern of the user's benefit.

Incentives for the agreement of a new or renewed operating lease should be recognised by the lessee as a reduction of the rental expense over the lease term, irrespective of the incentive's nature or form, or the timing of payments.

Accounting by lessors

The following principles should be applied in the financial statements of lessors:

- At commencement of the lease term, the lessor should record a finance lease in the balance sheet as a receivable, at an amount equal to the net investment in the lease.
- The lessor should recognise finance income based on a pattern reflecting a constant periodic rate of return on the lessor's net investment outstanding in respect of the finance lease.
- Assets held for operating leases should be presented in the balance sheet of the lessor according to the nature of the asset. Lease income should be recognised over the lease term on a straight-line basis, unless another systematic basis is more representative of

the time pattern in which use benefit is derived from the leased asset is diminished.

Incentives for the agreement of a new or renewed operating lease should be recognised by the lessor as a reduction of the rental income over the lease term, irrespective of the incentive's nature or form, or the timing of payments. Initial direct and incremental costs incurred by lessors in negotiating leases must be recognised over the lease term. They may no longer be charged to expense when incurred. This treatment does not apply to manufacturer or dealer lessors where such cost recognition is as an expense when the selling profit is recognised.

NEW STANDARD ON LEASE (IFRS 16/ Ind AS 116)

Leasing is an important and widely used financing solution. It enables companies to access and use property and equipment without incurring large cash outflows at the start. It also provides flexibility and enables lessees to address the issue of obsolescence and residual value risk. In fact sometimes, leasing is the only way to obtain the use of a physical asset that is not available for purchase.

Under existing rules, lessees account for lease transactions either as operating or as finance leases, depending on complex rules and tests which, in practice, use ‘bright-lines’ resulting in all or nothing being recognized on balance sheet for sometimes economically similar lease transactions.The impact on a lessee’s financial reporting, asset financing, IT, systems, processes and controls is expected to be substantial. Many companies lease a vast number of big-ticket items, including cars, offices, power plants, retail stores, cell towers and aircraft.

MAJOR CHANGES IN THE LEASE ACCOUNTING

- The distinction between operating and finance leases is eliminated for lessees, and a new lease asset (representing the right to use the leased item for the lease term) and lease liability (representing the obligation to pay rentals) are recognised for all leases.

- Lessees should initially recognise a right-of-use asset and lease liability based on the discounted payments required under the lease, taking into account the lease term as determined under the new standard. Determining the lease term will require judgment which was often not needed before for an operating lease as this did not change the expense recognition. Initial direct costs and restoration costs are also included.
- Lessor accounting does not change and lessors continue to reflect the underlying asset subject to the lease arrangement on the balance sheet for leases classified as operating. For financing arrangements or sales, the balance sheet reflects a lease receivable and the lessor's residual interest, if any.

- The key elements of the new standard and the effect on financial statements are as follows:
  - A ‘right-of-use’ model replaces the ‘risks and rewards’ model. Lessees are required to recognise an asset and liability at the inception of a lease. All lease liabilities are to be measured with reference to an estimate of the lease term, which includes optional lease periods when an entity is reasonably certain to exercise an option to extend (or not to terminate) a lease.
  - Contingent rentals or variable lease payments will need to be included in the measurement of lease assets and liabilities when these depend on an index or a rate or where in substance they are fixed payments. A lessee should reassess variable lease payments that depend on an index or a rate when the lessee remeasures the lease liability for

other reasons (for example, because of a reassessment of the lease term) and when there is a change in the cash flows resulting from a change in the reference index or rate (that is, when an adjustment to the lease payments takes effect). • Lessees should reassess the lease term only upon the occurrence of a significant event or a significant change in circumstances that are within the control of the lessee.

The new standard will gross up balance sheets and change income statement and cash flow presentation. Rent expense will be replaced by depreciation and interest expense in the income statement (similar to finance leases today). This results in a front-loaded lease expense, which for some might decrease earnings and equity immediately after entering into a lease compared to an operating lease today.

MODULE V

MODERN CONCEPTS IN ACCOUNTING

HUMAN RESOURCE ACCOUNTING

Human resources are considered as important assets and are different from the physical assets. Physical assets do not have feelings and emotions, whereas human assets are subjected to various types of feelings and emotions. In the same way, unlike physical assets human assets never gets depreciated. Therefore, the valuations of human resources along with other assets are also required in order to find out the total cost of an organization. In 1960s, RensisLikert along with other social researchers made an attempt to define the concept of human resource accounting (HRA).

Flamhoitz defines HRA as ‘accounting for people as an organizational resource. It involves mea-suring the costs incurred by organizations to recruit, select, hire, train, and develop human assets. It also involves measuring the economic value of people to the organization'.

According to Stephen Knauf, ' HRA is the measurement and quantification of human organizational inputs such as recruiting, training, experience and commitment'.

Since the beginning of globalization of business and services, the human resources are becoming more important and decisional input for the success of any corporate enterprise. Human resource accounting (HRA) involves accounting for expenditures related to human resources as assets. All the processes of the organisation are operated by human resources, thereby the changes in the HR cost and benefits must be considered. Though it has been accepted that HR is capital resource thereby the valuation of this resource is very necessary and information about the valuation should be given to the investors, the management and others through financial statements. Human resources accounting is basically an information system that tells management what changes are occurring over time to the human resources of the business. Human resources accounting (HRA) is one of the latest concept adopted by few corporations in our country. Most of the corporations have realised that human resources are their most precious resources. So it is required that some measures to develop their human resources but also taken measures to accelerate their values.

Human Resources are invaluable asset in an organization. It is a live asset of any business concern but their value cannot be measured accurately. The value of manpower, present and potential, to the management is conceptually well established. From a macroeconomic view point, the services which people can potentially provide constitute a form of capital. Recently Indian Corporate Sector has shown growing interest in the accounting for human resources.The concept of human resource accounting has been defined by the committee on Human Resource Accounting of the American Accounting Association as “the process of identifying and measuring data about human resources and communication this information to interested parties.”

Need for HRA

The need for human asset valuation arose as a result of growing concern for human relations management in the industry.

Objectives of HRA

RensisLikert described the following objectives of HRA:

1. Providing cost value information about acquiring, developing, allocating and maintaining human resources.

2. Enabling management to monitor the use of human resources.

3. Finding depreciation or appreciation among human resources.

4. Assisting in developing effective management practices.

5. Increasing managerial awareness of the value of human resources.

6. For better human resource planning.

7. For better decisions about people, based on improved information system.

8. Assisting in effective utilization of manpower.

Methods of Valuation of Human Resources

There are certain methods advocated for valuation of human resources. These methods include historical method, replacement cost method, present value method, opportunity cost method and standard cost method. All methods have certain benefits as well as limitations.

Benefits of HRA

1. The system of HRA discloses the value of human resources, which helps in proper interpretation of return on capital employed.
2. Managerial decision-making can be improved with the help of HRA.
3. The implementation of human resource accounting clearly identifies human resources as valuable assets, which helps in preventing misuse of human resources by the superiors as well as the management.
4. It helps in efficient utilization of human resources and understanding the evil effects of labour unrest on the quality of human resources.
5. This system can increase productivity because the human talent, devotion, and skills are considered valuable assets, which can boost the morale of the employees.
6. It can assist the management for implementing best methods of wages and salary administration.

Limitations of HRA

1. The valuation methods have certain disadvantages as well as advantages; therefore, there is always a bone of contention among the firms that which method is an ideal one.

2. There are no standardized procedures developed so far. So, firms are providing only as additional information.

All the processes of the organisation are operated by human resources, thereby the changes in the HR cost and benefits must be considered. Though it has been accepted that HR is capital resource thereby the valuation of this resource is very necessary and information about the valuation should be given to the investors, the management and others through financial statements. Human resources accounting is basically an information system that tells management what changes are occurring over time to the human resources of the business.

The basic objectives of human resource accounting are as under:

(1) HRA facilitates managing the people as one of the resources of the organization.

(2) To help the management for making decision about acquiring, allocating, developing and maintaining human resources in order to keep control on human resource cost as one of the organizational objective.

(3) To provide information to the management regarding human resource cost and value.

(4) To see whether the human resources are effectively utilized or not

(5) To see whether the human resources are producing a return on investment of the persons interested in the organization or not.

(6) Provide human resources accounting detail to outsiders like financers such as bankers, financial institutions and creditors etc.

Methods of Accounting Valuation of Human Resources:

The different approaches invariably denotes the methods or techniques for evaluation of the human resources.

In order to measure the value of HR, there are few decisional aspects to be considered, are as given here:

i. Performance evaluation part for human resources;

ii. Present value of salary/wages payments;

iii. Real capital cost;

iv. Matching the cost of HR with the revenue of organisation.

Generally the methods for HR Accounting with its valuation are:

1. <u>Historical Cost Approach</u>:

This approach was developed by William C. Pyle, which is based on the concept that there are certain cost incurred by the organisation with regard to human resources. Cost is a sacrifice aspect incurred to obtain some anticipated benefits or services. In this approach the actual cost incurred on recruiting, selecting, hiring, training and development of human resources, of the organisation is maintained and a proportion of it is written off to the income of the next and expected useful life of human resources.The approach of the cost of human resources is very similar to the book value of the other physical assets. This method is simple to understand and easy to work out. It is based on traditional accounting concept of matching cost with revenue.

2. Replacement Cost Approach:

This approach was first opined by RensisLikert and was developed by Eric G. Flamholthz. Human resource of an organisation are to be values on the assumption that a new similar organisation has to be created from cut down and what would be the cost to the firm if the existing resources were required to be replaced with other persons of equivalent talents and experience.According to this model the value of employee is estimated as the cost of replacement with a new employee of equivalent ability and efficiency. There are two costs, individual replacement cost and positional replacement cost. The cost of recruiting, selecting, training and development and familiarisation cost are account in individual replacement cost.

When an employee change the present position to another or leave the organisation then the cost of moving, vacancy, carrying and other relevant costs reflect in individual replacement cost. Positional replacement cost refers to the cost of filling different position in an organisation.

3. Opportunity Cost Approach:

This approach analyse the alternative earning sources from the productive capacity of human resources by putting some alternative use. Opportunity cost is the value of an asset (HR) when there is an alternative use of it. The perspective chances of opportunity cost are declined for those employees that are not scarce. But the alternative use of HR within the organisation is restricted and at the same moment, the use of HR with finding out their alternative cost may not be incorporated properly.

4. Standard Cost Approach:

This approach is based on the line and staff as well as functional relationship of employees in an organisation. The employees of an organisation are categorized and divided into different groups with hierarchical levels or positions. Standard cost is fixed for each category of employees and their worthwhile role may be calculated. Due to some of the static position of employees on account of their status and position, it does not take any differences of them put in the same group.

Human resources accounting (HRA) is one of the latest concept adopted by few corporations in our country. Most of the corporations have realised that human resources are their most precious resources. So it is required to taken some measures to develop their human resources but also taken measures to accelerate their values.

FORENSIC ACCOUNTING

Forensic accounting is the assistance of finance professionals to settle disputes concerning allegations, fraudulence, suspicion of fraud and misconduct in business.

What does Forensic Accounting cover?

The two major aspects within forensic accounting practices are:

1. Litigation support services. A forensic accounting expert measures the damages experienced by the parties implicated in legal disputes and can aid in settling conflicts, even before it reaches the courtroom. In the event that a conflict reaches the courtroom, the forensic accounting professional could give evidence as an expert witness

2. Investigative/fact-finding services. A forensic accountant must determine whether illegal matters such as employee felony, securities embezzlement (including tampering and distortion of financial accounts), identity theft and insurance racket have taken place.

Relevance of forensic accounting in an organisation

• Assessing working transactions for compliance with basic operating processes and agreement.
• Performing thorough scrutiny and examination of financial payment dealings in the accounting system to decide if they are standard or beyond company policy.

• Assessing standard ledger and financial reporting system transactions for likely unlawful tampering or falsification of information or accounts and its consequences on the ensuing financial accounts.

•Analysing warranty requests or returns for practices of fraudulence or misuse.
• Assisting in estimating the economic damages and the ensuing insurance demands that arise from catastrophes such as fires or other natural setbacks.
• Assessing or affirming business rating in consolidations and accomplishments.

Forensic accounting is the investigation of fraud or financial manipulationTop Accounting Scandals. The last two decades saw some of the worst accounting scandals in history. Billions of dollars were lost as a result of these financial disasters. Many of these scandals were a result of the excessive greed of the by performing extremely detailed research and analysis of financial information.

SOCIAL RESPONSIBILITY ACCOUNTING

Business is a socio-economic activity and it draws its inputs from the society, hence its objective should be the welfare of the society. It should owe a responsibility towards solving many of the social problems. In the present age of growing technological, economic, cultural and social awareness, the accounting has not only to fulfill its stewardship function for the owners of the enterprise, but also accomplish its social function. Changing environments and social parameters have compelled business enterprises to account and report information with regard to discharge of their social responsibilities. The boundaries of the principles, practices and skills of conventional accounting have been extended to such areas for social disclosure and attestation with regard to the measures of social programmes.

The concept of 'Social Accounting' has gained importance as a result of high level industrialization which has brought prosperity as well as many problems to the society. It has necessitated the corporate sector, with huge amounts of funds at their disposal, to invest substantial amounts in social activities so as to nullify the adverse effects of industrialization. "In modern times, accounting efforts have been extended to the assessment of the state of society and of the social programmes not for the satisfaction of any individual or group but for the application of evaluative procedures in the allocation of resources towards better social well-being as a whole."Social accounting is concerned with the study and analysis of accounting practice of those activities of an organisation. The concept of socialistic pattern of society, civil rights movements, environmental protection and ecological conservation groups, increasing awareness of society towards corporate social contribution, etc. Have contributed towards the growing importance of Social accounting. Social

Accounting, also known as Social Responsibility Accounting, Socio-Economic Accounting, Social Reporting and Social Audit, aims to measure and inform the general public about the social welfare activities undertaken by the enterprise and their effects on the society

Features of Social Accounting:

(i) Social accounting is an expression of a company's social responsibilities.

(ii) Social accounting is related to the use of social resources.

(iii) Social accounting emphasize on relationship between firm and society.

(iv) Social accounting determines desirability of the firm in society.

(v) Social accounting is application of accounting on social sciences.

(vi) Social accounting emphasizes on social costs as well as social benefits.

<u>Need/Benefits of Social Accounting</u>:

(1) A firm fulfills its social obligations and informs its members, the government and the general public to enables everybody to form correct opinion.

(2) It counters the adverse publicity or criticism leveled by hostile media and voluntary social organizations.

(3) It assists management in formulating appropriate policies and programmes.

(4) Through social accounting the firm proves that it is not socially unethical in view of moral cultures and environmental degradation.

(5) It acts as an evidence of social commitment.

(6) It improves employee motivation.

(7) Social accounting is necessary from the view point of public interest groups, social organisations investors and government.

(8) It improves the image of the organization.

(9) Through social accounting, the management gets feedback on its policies aimed at the welfare of the society.

(10) It helps in marketing through greater customer support.

(11) It improves the confidence of shareholders of the firm.

ENVIRONMENTAL ACCOUNTING

Environmental accounting, also called green accounting, refers to modification of the System of National Accounts to incorporate the use or depletion of natural resources. Environmental accounting is a vital tool to assist in the management of environmental and operational costs of natural resources. Environmental accounting principles and practices are mainly used by organizations to more accurately trace environmental costs back to specific activities. Government agencies, private businesses, local communities and individuals all take responsibility for conserving natural resources and operating sustainably in most developed nations. Governmental agencies and businesses are accountable to the public for setting environmentally related efficiency goals that lead to cost reductions and improved operational processes. These organizations are more likely to implement methods from environmental accounting which is a growing subset of traditional accounting. While environmental accounting can focus on environmental management accounting or financial accounting, the most prominent benefits come from the application of environmental management accounting methods. This type of accounting focuses on gathering, estimating and analyzing costs associated with the use of energy and physical materials like timber, metal or coal. Standard accounting practices tended to place these costs in the catch all category of overhead, but environmental management accounting allows accountants to apply activity based cost principles to more accurately associate these costs to various projects or events. Decision makers who can see exactly where these natural resources are used across various projects can locate areas of synergy that allow them to reduce the amount of wasted materials at the program or enterprise level.

Businesses use three generally accepted methods to implement environment accounting: financial accounting, managerial accounting and national income accounting. Financial accounting is the process of preparing financial reports, such as earning statements, for presentation to investors, lenders, governing bodies and other members of the public. In this instance, environmental accounting estimates are presented as part of the financial accounting reports.

INVESTMENT ACCOUNTING

The accounting for investments occurs when funds are paid for an investment instrument. If the investor intends to hold an investment to its maturity date (which effectively limits this accounting method to debt instruments) and has the ability to do so, the investment is classified as held to maturity. Investment means to spend money outside the business in order to earn some income which are non-trading in nature. Usually, money is invested in Government Bonds, Securities, Shares and Debentures of companies etc.

PROACTIVE ACCOUNTING

Proactive accounting manages business finances effectively, make the right decisions and maximise your profits. Most businesses do reactive accounting, i.e. they produce a set of accounts and financial records only when they are legally required to do so. It is important to go deeper into the accounts so as to identify trends and boost profits while avoiding losses. Proactive accounting allows to stay on top of business finances and the take decisions quickly. It allows to identify where money is leaking out of your business. It allows you to see who has been paid, how much and when as well as who has paid, how much and when.

INFLATION ACCOUNTING

Inflation accounting refers to the process of adjusting the financial statements of a company to show the real financial position of the company during the inflationary period. Inflation accounting is a special technique used to factor in the impact soaring or plummeting costs of goods in some regions of the world have on the reported figures of international companies. Financial statements are adjusted according to price indexes, rather than relying solely on a cost accounting basis, to paint a clearer picture of a firm's financial position in inflationary environments. This method is also sometimes referred to as price level accounting. When a company operates in a country where there is a significant amount of price inflation or deflation, historical information on financial statements is no longer relevant. To counter this issue, in certain cases companies are permitted to use inflation-adjusted figures, restating numbers to reflect current economic values.

Techniques of Inflation Accounting:

1. Current Purchasing Power Method: It involves adjustment of financial accounts to price changes. A general price index is used to convert the values of various items. It takes into account the purchasing power of money and ignores the rise and fall in the price of an item.

Conversion factor = Price Index at time of conversion/ Price Index at the date of conversion

CPP Value = Conversion Amount or Historical Value x Conversion Factor

2. Current Cost Accounting: Under this method assets are shown at current costs and profits are determined on the basis of costs at the date of sale rather than the actual cost.

3. Current Value: Under this method all assets and liabilities are measured at current value at which they could be sold or settled at the current price.

4. Replacement Cost Accounting: Under this method all assets and liabilities are recorded on a balance sheet according to the cost of replacing them rather than heir historical costs