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Further, in the Elective Papers which are Case Study based, the solutions have been worked out on the basis of certain assumptions/views derived from the facts given in the question or language used in the question. It may be possible to work out the solution to the case studies in a different manner based on the assumption made or view taken.
PAPER – 6F: MULTI-DISCIPLINARY CASE STUDY

The question paper comprises three case study questions. The candidates are required to answer any two case study questions out of three.

All your workings should form part of your answer.

Question No. I (Contains Part – A and Part – B)

Background

You have recently joined as an Audit Partner in M/s. XYZ & Co., Chartered Accountants ("the Firm") based out of Mohali which has a variety of clients in the Technology, Software and Media segments. All their clients are based out of Mohali and Chandigarh. One of the key clients of the firm is Superstar Group which has several subsidiaries and your Firm does the audit and taxation work for all these entities. You have been assigned to support the Lead Client Service Partner for the Super Star Group, Mr. Madhav Mahajan, Partner, in the audit of Rising Star Limited. You have been provided with the below information to facilitate your audit.

Company Information

Rising Star Limited (the Company), which is a subsidiary of Super Star Limited, a Public Company (unlisted), was incorporated on 1st February, 2007 under the Indian Companies Act, 1956. It specializes in the business of developing graphical images for its various clients spread across the world. The shareholding pattern of the Company as at 31st March, 2017 are as under:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>No. of Shares (in lakhs)**</th>
<th>Total paid up Equity Share Capital (₹In lakhs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Super Star Limited</td>
<td>45.00</td>
<td>450.00</td>
</tr>
<tr>
<td>Mr. Thomas Edison (as a nominee of Super Star Limited)*</td>
<td>32.50</td>
<td>325.00</td>
</tr>
<tr>
<td>Mrs. Morigate Edison (as a nominee of Super Star Limited)*</td>
<td>22.50</td>
<td>225.00</td>
</tr>
<tr>
<td>**Total</td>
<td>100.00</td>
<td>1000.00</td>
</tr>
</tbody>
</table>

*The Company has complied with the requirements of the Companies Act, 1956/2013 with respect to taking note of/filing the beneficial interest of Super Star Limited in the Company with the Registrar of Companies.

**Face Value of ₹10 each.

Whilst the Company was doing well in the initial periods, due to global recession in this segment, the business performance has gone South recently.

The Finance Director of the Company, Mr. Mangesh has requested the Statutory Auditors, M/s. XYZ & Co; Chartered Accountants to take up the audit and issue the audit report before
the Board meeting scheduled in the month of June, 2017 based on which certain critical
decisions impacting the future operations of the Company would be taken including a probable
merger The CEO of the Company, Mr. Stanley is in active discussion with the parent company
and the Board of Directors. This information is proposed to be kept confidential as at this stage.

(A) Key financial data as per Management Information provided for Audit

The Company has also provided you with the management prepared financial statements for
your audit. You have taken charge of this engagement and requested Ms. Manasa Maheswari,
the Audit Manager to support you on this engagement.

The key Financial highlights of the Company as at 31st March, 2017 as per the Management
prepared financial statements are as under:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>As at 31st March, 2017</th>
<th>Particulars</th>
<th>For the year ended 31st March, 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity Share Capital</td>
<td>1,000</td>
<td>Revenue-Net</td>
<td>4,255</td>
</tr>
<tr>
<td>Capital Reserve (not arising on amalgamation)</td>
<td>250</td>
<td>Profit (Loss) After Tax</td>
<td>(124)</td>
</tr>
<tr>
<td>General Reserve</td>
<td>125</td>
<td>Operating cash flows</td>
<td>(452)</td>
</tr>
<tr>
<td>Profit &amp; Loss Account</td>
<td>(238)</td>
<td>Investing cash flows</td>
<td>(230)</td>
</tr>
<tr>
<td>Long Term Borrowings from the Parent Company</td>
<td>20</td>
<td>Financing Cash flows</td>
<td>923</td>
</tr>
<tr>
<td>Net Current Assets</td>
<td>(14)</td>
<td>Extra-ordinary Income</td>
<td>220</td>
</tr>
<tr>
<td>Cash &amp; cash equivalents as at 1/4/2016 (excluding restricted cash and bank balances)</td>
<td>32</td>
<td>Deferred Tax Income</td>
<td>10</td>
</tr>
<tr>
<td>Bank Borrowings</td>
<td>12</td>
<td>Tax paid on Sales Revenue</td>
<td>12</td>
</tr>
<tr>
<td>Off Balance sheet exposure in the form of contingent liabilities to the extent not paid and not provided for</td>
<td>122</td>
<td>Interest expenses</td>
<td>22</td>
</tr>
</tbody>
</table>

(B) Information reported by the Audit Engagement Team:

The Engagement Team lead by Ms. Manasa Maheshwari has reported the following matters to
you based on their field audit :

(1) No physical verification of the assets was carried out during the year ended
31st March, 2017 and the same was due only in the ensuing year ending 31st March, 2018 as per the management policy approved by the Board which was assessed to be acceptable from the audit point of view at the time of policy formulation.

(2) There was no disclosure of outstanding Letter of Credits (LCs) opened for import of certain assets from USA under contingent liabilities in the financials prepared by the Company amounting to ₹ 55 Lakhs.

(3) Gratuity liability was not provided for employees who have joined the Company during the past 3 years, the aggregate amount of which would be ₹ 12.50 Lakhs on the basis that they are yet to complete the stipulated minimum years of service.

(4) Certain computers were received from the parent company free of cost, the value of which is ₹ 0.23 Lakhs and no accounting or disclosure of the same has been made in the notes on accounts.

(5) The loan availed from Chevy Chase Bank remained outstanding to the extent of ₹ 12 Lakhs excluding the penal interest charged by the bank amounting to ₹ 0.23 Lakhs for default in repayment for 2 quarters, pending to be accounted by the Company. The Management has also informed that this is not an information to be disclosed in the financial statements and does not have any bearing on the reporting of Auditors either.

(6) TDS receivable as per books is more than the cumulative balance as per Form 26AS by ₹ 14.50 Lakhs. No valid explanation was made available for the difference amount.

(7) The Company has not provided for any tax expense in the books of accounts due to tax losses. The Company has recognized deferred tax asset on the unabsorbed Business losses based on management assessment.

(8) The Company follows the method of providing depreciation as per Section 123 of the Companies Act, 2013 using the useful lives prescribed as per Schedule II of the Companies Act, 2013. It has provided depreciation on computers which are used during all the 3 shifts using the rates stipulated for continuous process plant since these assets are used for 24 hours (3 shifts).

(9) The amount of restricted bank balances as at 1-4-2016 and 31-3-2017 was ₹ 120 lakhs and the Company does not believe the same as qualifying for disclosure under Cash and Cash Equivalents.

(C) Review of Board Minutes

Whilst the Audit team has identified various matters, they need your advice to conclude on the same. You have asked them to review the Board minutes and other secretarial / regulatory records based on which the following additional matters were brought to your attention:-

(10) The long term borrowings from the parent has no agreed terms and neither the interest nor the principal has been repaid so far.

(11) An amount of ₹ 1.22 Lakhs has been paid under protest against certain tax claims under
dispute where the Company believes it has a fair chance and hence not provided for in the financial statements nor was it disclosed as contingent liabilities. During the discussions, the Company has also mentioned that since they have not provided for the same, this would not be an item in the Companies (Auditor's Report) Order, 2016 (CARO, 2016) reporting by the Auditors as disputed dues.

(12) The Company is in the process of selling its office along with the freehold land available at Chandigarh and is actively on the lookout for potential buyers. Whilst the same was purchased at ₹25 Lakhs in 2008, the current market value is ₹250 Lakhs.

This property is pending to be registered in the name of the Company, due to certain procedural issues associated with the Registration though the Company is having a valid possession and has paid its purchase cost in full. The Company has disclosed this amount under Fixed Assets though no disclosure of non-registration is made in the notes forming part of the accounts.

(13) An amount of ₹3.25 Lakhs per month is paid to M/s. WE CARE Associates, a partnership firm, which is a ‘related party’ in accordance with the provisions of the Companies Act, 2013 for the marketing services rendered by them. Based on an independent assessment, the consideration paid is higher than the arm’s length pricing by ₹0.25 Lakhs per month. Whilst the transaction was accounted in the financial statements based on the amounts’ paid, no separate disclosure has been made in the notes forming part of the accounts highlighting the same as a ‘related party’ transaction.

Ms. Manasa Maheshwari, your Audit Manager has reported that she had asked for certain information relating to another ‘related party’ transaction (quantum likely to be about ₹47 lakhs) and the CFO has refused to provide the same since the same is perceived to be confidential and cannot be shared with Auditors.

(14) The Internal Auditor of the Company has identified a fraud in the recruitment of employees by the HR department wherein certain sums were alleged to have been taken as kick-back from the employees for taking them on board with the Company. After due investigation, the concerned HR Manager was sacked. The amount of such kickbacks is expected to be in the range of ₹12 Lakhs.

(15) Right International Inc., has served a legal notice on the Company claiming ₹250 Lakhs for patent infringement and the Company has challenged the notice through its legal counsel. An ‘independent legal opinion obtained on this matter suggests that the possibility of a cash outflow is more likely than not under the existing legal framework /available evidence as made available to the legal counsel.

(16) The remuneration for the auditors has been fixed by the shareholders as a fixed sum and a percentage based on the profitability of the Company.

(17) CEO of the Company, Mr. Stanley has put forward a proposal to pay dividends to the shareholders notwithstanding the current financial condition. He proposes to manage the cash flows by borrowing from the bank. He would also like to provide for the same in the
financial statements for the year ended 31st March, 2017 on approval by the Board.

(18) The Management has informed that it feels that the market conditions will improve and the Company would be totally profitable in the next 3 years' time and expects new orders/higher revenues in the coming years to fuel higher profitability. During discussions on this topic, Mr. Stanley informed that whilst there are no firm contracts/projects that are available on hand to demonstrate, Management is fully aware of their business environment and their assessment can be taken as sacrosanct.

(D) Findings based on File Review

After a careful consideration of the matters reported by the engagement team, you have also reviewed the financial statements, audit working papers and noted the following additional matters for your conclusion and overall assessment;

(19) An amount of ₹ 0.25 Lakhs paid to M/s. Hemamali Associates, Chartered Accountants (a network firm of XYZ & Co., Chartered Accountants, where Mr. Madhav Mahajan is also a partner) towards various tax representation services has not been disclosed anywhere in the financial statements separately.

(20) Certain unclaimed dividends amounting to ₹ 38 Lakhs pertaining to the prior periods beyond 7 years have been written back to the Statement of Profit & Loss under 'Other income'.

(21) The Market to Market Loss of ₹ 13.74 Lakhs as at 31st March, 2017 on the outstanding forward contracts pertaining to highly probable transactions which have an original tenure of 3 years is proposed to be accounted by the Company as and when the settlement transaction is scheduled which is likely to happen in December 2018. The Company has not adopted hedge accounting consistently.

(22) Extraordinary income arose from the gain on sale of freehold land at Kurukshetra.

(23) The Finance Director of the Company was also enquiring about the applicability of Indian Accounting Standards (IND AS) for the Company. He said that considering the parameters mentioned for applicability of IND AS and the Company's turnover, profit after tax and net worth for the last financial years, it is not applicable for the entity for the financial year 2016-17 and, hence, existing Indian GAAP has been considered by the Company in the preparation of its financial statements. He has also asked you to confirm the same.

(24) During your interactions with Mr. Mangesh, the Finance Director of the Company, he has indicated that he would expect a clean opinion on the financial statements and reference to matters which would have negative perception could be ignored considering the possibility of the merger under evaluation. He has also indicated that he does not expect any further adjustments to the financial statements since the same has been shared with the bankers already.

Based on the above information, you have to provide your inputs on the below aspects to your Lead Client Service Partner to assist him in forming his opinion.
PART-A

Answer the following questions with reasons, in short and appropriate technical references:

(1) Whether Superstar Limited needs to consolidate the financial statements of Rising Star Limited under the Companies Act 2013?
   (A) No
   (B) Yes, for 100%
   (C) Yes, but only to the extent of 45%
   (D) Consolidation requirement itself is not applicable under the Companies Act, 2013 being an unlisted entity. (2 Marks)

(2) What is the Net Worth of the Company as per the Management prepared financial statements as at 31st March, 2017? (₹ in Lakhs)
   (A) 887
   (B) 1137
   (C) 1015
   (D) 1125 (2 Marks)

(3) What is the total amount of contingent liabilities of Rising Star Limited as at 31st March, 2017? (₹ in Lakhs)
   (A) 122
   (B) 178.22
   (C) 123.22
   (D) 213.22 (2 Marks)

(4) What is the amount of Cash and Cash Equivalent to be disclosed in the Cash Flow Statement as at 31st March, 2017? (₹ in Lakhs)
   (A) 241
   (B) 723
   (C) 149
   (D) 273 (2 Marks)

(5) The amount at which the Chandigarh property to be accounted in the books of account as at 31st March, 2017 is ________ (₹ in Lakhs)
   (A) 250
   (B) 275
   (C) 25
(6) Do you think that the "Deferred Tax Asset" recognition on the unabsorbed business losses is appropriate:

(A) Yes
(B) No
(C) Yes, since it is based on Management assessment and the same is as per the AS 22.
(D) It depends/based on the decision to be taken by the CEO regarding the probable merger.

(7) Whether gain on sale of land at Kurukshetra accounted as an extra-ordinary income is acceptable under the Companies Act, 2013 reporting framework?

(A) Yes, it is appropriate.
(B) No, this may be accounted as an exceptional item.
(C) No, this should be accounted as 'income from operations'.
(D) It depends on the decision to be taken by the CEO regarding the probable merger.

(8) Certain information considered as confidential by the Management for sensitive purposes can be rightfully denied to the auditors.

(A) Yes, for valid reasons as assessed by the Management.
(B) No, it cannot be denied; else this would result in possible scope of making audit qualifications for the Auditors.
(C) Can be denied after taking the consent from the Board.
(D) Can be denied after informing the Regulators.

(9) In view of the discussions by the Finance Director with you, reference to unfavourable or qualified answers in the Companies (Auditor's Report) Order, 2016 (CARO, 2016) where applicable may be avoided.

(A) Yes, based on the request from the client.
(B) No, where required, due disclosure as required under the Companies Act, 2013 needs to be made.
(C) Considering the merger possibility, such matters may be reported to the Board and can be avoided in CARO, 2016.
(D) Entire reporting under CARO, 2016 may be dropped.

(10) Whether Auditors’ remuneration as proposed by the shareholders is acceptable to you?

(A) Yes
(B) No
(C) Permissible since the shareholders have approved the remuneration
(D) Cannot decide based on available information. (2 Marks)

PART-B

Answer the following:

(1) Are there any matter(s) that need to be reported with unfavourable response under the Companies (Auditor's Report) Order, 2016-(CARO, 2016)? If so, explain the same with relevant rationale. (8 Marks)

(2) Summarise the material misstatements, if any; on the management prepared financial statements which could impact the true and fair view of the financial statements. Please provide the basis for your assessment briefly. (8 Marks)

(3) What are the disclosure deficiencies, if any, in the Management prepared financial statements that could impact the true and fair view of the financial statements? Please provide the basis for your assessment briefly. (6 Marks)

(4) Provide a brief summary of items to be reported to those in-charge of governance, where applicable, based on your audit findings for Rising Star Limited, duly considering the Auditing Standards and the applicable provisions of the Companies Act, 2013. (4 Marks)

(5) As an auditor of Rising Star Limited, state the matters to be reported under Rule 11 of the Companies (Audit and Auditors) Rules, 2014? What are those matters and how would you report them? (4 Marks)

Answer to Question 1 Part A (MCQs)

(1) Option (B) : Yes for 100 %
Reasoning: As per para 10 of AS 21, the consolidated financial statements are prepared on the basis of financial statements of parent and all enterprises that are controlled by the parent. Here Super Star Ltd. obtains economic benefits by acquiring shares in Rising Star Ltd. through its Nominees, control is assumed. Hence, it will consolidate the financial statements of Rising Star Ltd. for 100%.

(2) Option (B) : ₹ 1137 lakhs
Reasoning: From the definition of Section 2(57), it may be noted that all reserves created out of the profits are included in calculation of 'net worth' even the debit balance of profit and loss account shall be considered in the calculation of net worth.

Accordingly, the net worth of the company shall be calculated as follows:

<table>
<thead>
<tr>
<th>₹ in lakhs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Paid up share capital</td>
</tr>
<tr>
<td>Add: Capital reserve</td>
</tr>
</tbody>
</table>
Add: General reserve | 125
Less: Debit balance of Profit and Loss Account | (238)

1137

(3) Option (C) : ₹ 123.22 lakhs

Reasoning: Calculation of contingent liability:

| ₹ in lakhs |
|Off Balance Sheet exposure in the form of contingent liabilities to the extent not paid and not provided for| 122
Add: Dispute on tax claim | 1.22
| 123.22 |

Note: Letter of Credit opened for import is a liability for the company and not a contingent liability. This can be inferred from the definition given in para 10.2 of AS 29 which states that a liability is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.

(4) Option (D) : ₹ 273 lakhs

Reasoning: Cash flow statement ₹ in Lakhs

| Excluding Restricted cash and bank balances |
|Cash flow from operating activities | (452)
Cash flow from Investing Activities | (230)
Cash flow from Financing Activities | 923
Net cash flows | 241
Add: Opening cash and cash equivalents (30+ 120) | 32
Closing cash and cash equivalents | 273 |

Cash equivalents should be encashable within three months of its origination and the amount that could be encashed should be certain. Here, it is assumed that the period of restriction in more than three months. Cash and bank balances that are restricted for use do not satisfy the definitions of either cash or cash equivalents. Therefore, the treatment by the entity of not considering the cash and bank balance that are restricted for use as part of cash and cash equivalent while preparing cash flow statement is proper.

Further, para 45 states that an enterprise should disclose, together with a commentary by management, the amount of significant cash and cash equivalent balances held by the enterprise that are not available for use by it. According, the entity should disclose the
amount of cash and cash equivalent balances that are restricted for use. The company is required to disclose without including the same in cash flow statement.

(5) Option (C) : ₹ 25 lakhs

Reasoning: As per para 73 of AS 10 Property, Plant and Equipment, Items of property, plant and equipment retired from active use and held for disposal should be stated at the lower of their carrying amount and net realisable value. Any write-down in this regard should be recognised immediately in the statement of profit and loss.

Since the company is in the process of selling its office along with the freehold land and is actively looking for the potential buyer, the company may consider the asset as retired from its active use and held for disposal. In such a situation, the asset shall be carried at lower of carrying value and net realisable value. Therefore, the company shall value its Chandigarh property at ₹ 25 lakhs only.

There is no purpose of revaluing the property which is in the process of sale.

(6) Option (B) : No

Reasoning: Para 17 of AS 22 inter alia states that where deferred tax asset is recognised against unabsorbed depreciation or carry forward of losses under tax laws, it is recognised only to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available against which such deferred tax assets can be realised. Virtual certainty for all practical purposes has to be certain and has to be supported by convincing evidence and not just by forecast and perceptions. Considering that there is no such convincing evidence available in this case, deferred tax asset should not be recognised. Merger, is only at the proposal stage and cannot be the basis for recognition of deferred tax asset.

(7) Option (B): No, this may be accounted as an exceptional item.

Reasoning: Para 12 of AS 5 states that when items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately. Here the gain on sale of land is more than 5% of net-revenue. Hence, based on size and non-recurring nature of the transaction, it is opined that it shall be presented as an exceptional item.

Further, as per para 75 of AS 10, the gain or loss arising from the derecognition of an item of property, plant and equipment should be included in the statement of profit and loss when the item is derecognised. Gains should not be classified as revenue, as defined in AS 9, Revenue Recognition.

(8) Option (B): No, it cannot be denied; else this would result in possible scope of making audit qualification for the auditors.

Reasoning: As per SA 705 “Modifications to the Opinion in the Independent Auditor’s Report”, the auditor’s inability to obtain sufficient appropriate audit evidence (also referred
to as a limitation on the scope of the audit) may arise from limitations imposed by management. Further, law or regulation may require the auditor to communicate about planning and scoping matters in the auditor’s report, or the auditor may consider it necessary to communicate about such matters in an Other Matter paragraph. In the rare circumstance where the auditor is unable to withdraw from an engagement even though the possible effect of an inability to obtain sufficient appropriate audit evidence due to a limitation on the scope of the audit imposed by management is pervasive, the auditor may consider it necessary to include an Other Matter paragraph in the auditor’s report to explain why it is not possible for the auditor to withdraw from the engagement.

(9) Option (B): No, where required, due disclosure as required under the Companies Act, 2013 needs to be made.

Reasoning: The Order requires that the auditor should make a statement on all such matters contained therein as are applicable to the company. The Order further provides that where an auditor is unable to express any opinion, he should indicate such fact. The auditor is also required to give reasons for any unfavourable or qualified answer. Further, where the auditor is unable to express an opinion on any such matter which is applicable to the company, he is also required to indicate in his report such fact together with the reasons as to why he is unable to express any opinion.

(10) Option (B): No.

Reasoning: Clause (10) of Part I to First Schedule to the Chartered Accountants Act prohibits a Chartered Accountant in practice to charges or offers to charge, accepts or offers to accept in respect of any professional employment fees which are based on a percentage of profits or which are contingent upon the findings, or results of such employment, except as permitted under any regulations made under this Act. Thus, auditor’s remuneration which is based on Percentage of Profit is not allowed.

Answer 1

1. Clause (i) (b) of the CARO, 2016 requires “whether the fixed assets have been physically verified by the management at reasonable intervals; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account.”

The Order requires the auditor to report whether the management has verified the fixed assets at reasonable intervals. What constitutes “reasonable intervals” depends upon the circumstances of each case. The factors to be taken into consideration in this regard include the number of assets, the nature of assets, the relative value of assets, difficulty in verification, situation and geographical spread of the location of the assets, etc. The management may decide about the periodicity of physical verification of fixed assets considering the above factors. While an annual verification may be reasonable, it may be impracticable to carry out the same in some cases. Even in such cases, the verification programme should be such that all assets are verified at least once in
every three years. Where verification of all assets is not made during the year, it will be
necessary for the auditor to report that fact, but if he is satisfied regarding the frequency
of verification he should also make a suitable comment to that effect.

In the present case, assets have been physically verified by the management only in the
ensuing year ending on 31-03-2018. No physical verification was carried out during the
year ended on 31-03-2017. The auditor is required to report as per clause (i) (b) of para 3 of
CARO 2016 on physical verification of fixed assets by the management at reasonable interval
and about material discrepancies were noticed, if any subject to verification of the same before
the issuance date of audit report.

2. As per clause (xiii) of para 3 of CARO 2016, the auditor is required to report “whether all
transactions with the related parties are in compliance with sections 177 and 188 of
Companies Act, 2013 where applicable and the details have been disclosed in the
Financial Statements etc., as required by the applicable accounting standards;”

Therefore, the duty of the auditor, under this clause is to report whether related party
disclosures as required by relevant Accounting Standards (AS 18, as may be applicable)
are disclosed in the financial statements.

In the present case, the auditor is required to report as per clause xiii of para 3 of CARO
2016 receipt of computers at free of cost from Parent Company which is transactions with
the related party of which details have not been disclosed in the financial statements as
required by the applicable accounting standard 18.

3. Clause (viii) requires an auditor to report “whether the company has defaulted in repayment
of loans or borrowing to a financial institution, bank, Government or dues to debenture
holders? If yes, the period and the amount of default to be reported (in case of defaults to
banks, financial institutions, and Government, lender wise details to be provided)”

Under this clause, the auditor is required to report whether the company has defaulted in
repayment of loans or borrowings to a financial institution or bank or Government or dues
to debenture holders. If the answer is in the affirmative, the auditor is also required to
mention the period of default and the amount of default, lender wise. In the present case
Rising Star Ltd. defaulted in repayment of loan to Chevy Chase Bank for 2 quarters and levied
penalty interest amounting rupees 0.23 lakh. The auditor is required to report such default of
repayment of loan taken from Chevy Chase bank in accordance with clause (viii) of para 3 of
CARO 2016.

4. As per clause (xiii) of para 3 of CARO 2016, the auditor is required to report “whether all
transactions with the related parties are in compliance with sections 177 and 188 of
Companies Act, 2013 where applicable and the details have been disclosed in the
Financial Statements etc., as required by the applicable accounting standards;”

In the present case, the auditor is required to report as per clause xiii of para 3 of CARO 2016
receipt of long term borrowing from Parent Company which is transactions with the related
party.
5. (i) (c) whether the title deeds of immovable properties are held in the name of the company. If not, provide the details thereof.

In the present case, the Company has office along with freehold land in Chandigarh. Though company has paid its purchase cost in full however, this property is pending to be registered in the name of the company i.e. title deed is not in the name of Company since 2008. Therefore, the auditor is required to report the same in accordance with clause (i)(c) of para 3 of CARO 2016.

6. As per clause (xiii) of para 3 of CARO 2016, the auditor is required to report “whether all transactions with the related parties are in compliance with sections 177 and 188 of Companies Act, 2013 where applicable and the details have been disclosed in the Financial Statements etc., as required by the applicable accounting standards;”

Therefore, the duty of the auditor, under this clause is to report (i) Whether all transactions with the related parties are in compliance with section 177 and 188 of the Companies Act, 2013 (“Act”); (ii) Whether related party disclosures as required by relevant Accounting Standards (AS 18, as may be applicable) are disclosed in the financial statements.

In the present case, the auditor is required to report as per clause xiii of para 3 of CARO 2016, one of related party transaction amounting 3.25 lakhs per month i.e. in lieu of marketing services has been noticed of which amount ₹ 0.25 lakh per month is exceeding the arm’s length price has not been disclosed highlighting the same as related party transactions as per AS 18.

7. As per clause (xiii) of para 3 of CARO 2016, the auditor is required to report “whether all transactions with the related parties are in compliance with sections 177 and 188 of Companies Act, 2013 where applicable and the details have been disclosed in the Financial Statements etc., as required by the applicable accounting standards;”

In the present case, the auditor is required to report as per clause xiii of para 3 of CARO 2016 CFO of the company refused to provide the related party transaction of amounting rupees 47 lakh on the ground that same is perceived to be confidential and cannot be shared with auditors, is not in order.

8. Clause (x) requires. whether any fraud by the company or any fraud on the Company by its officers or employees has been noticed or reported during the year; If yes, the nature and the amount involved is to be indicated.

In the instant case, a fraud has been identified in recruitment of employees by the HR Department wherein certain sums were alleged to have been taken as kickback from the company of amounting rupees approx. 12 lakh. The auditor is required to report on the same as per clause x of para 3 of CARO 2016.

Answer 2.

Material misstatements on the management prepared financial statements which could impact the true and fair view of the financial statements are:
1. No physical verification of the assets was carried out during the year ended on 31-03-2017. There are some discrepancies which are noticed only on physical verification of assets. So, discrepancies could remain unnoticed in the financial statements for want of physical verification of assets.

2. Pending accounting of penal interest of ₹ 0.23 lakh on default repayment of loan for 2 quarters from Chevy Chase Bank may lead to material misstatement impacting the true and fair view of the financial statements.

3. Difference between TDS as per books and TDS as per 26 AS may lead to material misstatement as there is overstatement of revenue by rupees 14.50 lakh and there is no valid explanation available for the difference amount.

4. As per AS 22, deferred tax assets are recognised and carried forward only to the extent that there is a reasonable certainty that sufficient future taxable income will be available against which such deferred tax assets can be realised. Where deferred tax asset is recognised against unabsorbed depreciation or carry forward of losses under tax laws, it is recognised only to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available against which such deferred tax assets can be realised.

In the present case, though management has informed that market conditions will be improved and company would be totally profitable in the next 3 years’ time but as per CEO of the company there is no firm contract/projects that are available on the hand to demonstrate. As per facts given in case, virtual certainty lacking in view of AS 22, therefore recognition of unabsorbed losses based on management assessment as deferred tax assets is not correct and will lead to material misstatement which could impact the true and fair view of the financial statements.

5. The company followed the method of providing depreciation as per section 123 of the Companies Act, 2013 using the useful lives prescribed as per Schedule II of the Companies Act, 2013 is correct, however, they have provided depreciation using the rates stipulated for continuous process plant is not correct. As per Schedule II Computers does not fall in continuous process plant category. Further, computers are included as NESD in Part 2 of Schedule II, which is category of assets in respect of which no extra shift depreciation is permitted. Therefore, though computers are used for 24 hours i.e. triple shift but no extra shift depreciation is permitted on the same. In the instant case, the Company has provided depreciation on computers which are used during all the 3 shifts using the rates stipulated for continuous process plant as per its accounting policy is incorrect and would be misleading resulting into material misstatement and hence impacting true and fair view.

6. As per AS 29 A provision is a liability which can be measured only by using a substantial degree of estimation. Further, a provision should be recognised when (a) an enterprise has a present obligation as a result of a past event; (b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and (c) a reliable estimate can be made of the amount of the obligation. In the instant case, Rising
Star Limited should have made the provision for ₹ 250 lakh for legal notice served by Right International Inc. for patent infringement claiming because as per legal opinion possibility of cash outflow is more than not under the existing legal framework. Therefore, non-provision of rupees 250 lakh may lead to material misstatement and impact true and fair view of financial statements.

7. Pursuant to the provisions of Section 124(5) of the Companies Act, 2013, dividend which remains unpaid or unclaimed for a period of seven years from the date of its transfer to unpaid dividend account is required to be transferred by the Company to Investor Education and Protection Fund (IEPF), established by the Central Government under the provisions of Section 125 of the Companies Act, 2013. The details of unpaid dividend amount should also be disclosed in accordance with the provisions given in the Companies Act, 2013. Rising Star Limited should also transfer the 38 lakh rupees which is unclaimed dividend pertaining to period beyond 7 years and which should be transferred to IEPF. Write back of unclaimed dividend to Statement of Profit & Loss under other income is not correct in view of provisions of the Companies Act, 2013. Therefore, financial statements will lead material misstatement and not present true and fair view.

8. As per AS 11 exchange differences on such a contract should be recognised in the statement of profit and loss in the reporting period in which the exchange rates change. Any profit or loss arising on cancellation or renewal of such a forward exchange contract should be recognised as income or as expense for the period. Thus, non-accounting of mark to market loss of rupees 13.74 lakhs on the outstanding forward contracts pertaining to highly probable transactions during the year will overstate the revenue which will be leading the material misstatements and not present true and fair view.

9. As per AS 15 on “Employee Benefits”, gratuity benefit is a defined benefit obligation as per which actuarial valuation using the projected unit credit method, which recognizes each period of service as giving rise to additional unit of employee benefit entitlement. Thus, even though employee has not completed 5 years of service, liability for gratuity is to be accrued as and when service is rendered by the employees.

Answer 3

1. As per AS 18 If there have been transactions between related parties, during the existence of a related party relationship, the reporting enterprise should disclose the prescribed details. Receipt of free of cost Computers and long term borrowing (on no agreed terms and repayment of interest and principal) from the Parent Company need separate disclosure in financial statements as per AS 18. Therefore, no proper disclosure for transactions with related party would be a disclosure deficiency having impact on the true and fair position of the company.

2. The amount of restricted bank balances as at 1.4.2016 and 31.3.2017 was rupees 120 lakhs and the company does not believe the same as qualifying for disclosure under Cash and Cash Equivalents is not correct as prescribed in para 45 of Accounting Standard 3 “Cash Flow Statement”, an enterprise should disclose, together with a commentary by management, the
amount of significant cash and cash equivalent balances held by the enterprise that are not available for use by it. Therefore, disclosure of restricted bank balances should be done in accordance with AS 3.

3. AS 29 states that a liability is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits. Therefore, payment of rupees 1.22 lakhs under protest in lieu of certain disputed tax claim is required to be disclosed as Contingent Liability. Though Company believes that it has a fair chance and not provided for the same. Non-provision for disputed tax claim is not substitute of non-disclosure of such Current Liability. Therefore, non-disclosure of the same will be constituted as disclosure deficiency impacting true and fair view.

4. Though as per substance over form freehold land appearing in financial statements is correct however, non-registration of the same should be separately disclosed in notes to financial statements. Non-disclosure of the same in notes to accounts will be considered as disclosure deficiency that could impact the true and fair view of financial statements. Further, classification of above land should also be as Assets held for Sale in financial statements.

5. AS 5 states that when items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately. Here the gain on sale of land is more than 5% of net-revenue. Hence, based on size and non-recurring nature of the transaction, it is opined that is shall be presented as an exceptional item. Therefore, separate disclosure as exceptional item is required for gain on sale of freehold land at Kurukshetra in financial statements as per AS 5.

6. **As per AS 18** If there have been transactions between related parties, during the existence of a related party relationship, the reporting enterprise should disclose the same. Therefore, no proper disclosure for transactions with related party would be a disclosure deficiency having impact on the true and fair position of the company. In the present case, one of related party transaction amounting 3.25 lakhs per month i.e. in lieu of marketing services has been noticed of which amount ₹ 0.25 lakh per month is exceeding the arm’s length price has not been disclosed highlighting the same as related party transactions as per AS 18.

7. Default in repayment of borrowing is required to be disclosed in the financial statements of the Company.

8. The amount of 0.25 lakhs paid to a network firm of the statutory auditor needs to be disclosed by way of a footnote as remuneration paid to a network firm of the statutory auditor.

**Answer 4**

As per SA 260, “Communication with Those Charged with Governance”, the auditor shall communicate with those charged with governance:

(a) The auditor’s views about significant qualitative aspects of the entity’s accounting practices, including accounting policies, accounting estimates and financial statement disclosures. When applicable, the auditor shall explain to those charged with governance why the auditor
considers a significant accounting practice, that is acceptable under the applicable financial reporting framework, not to be most appropriate to the particular circumstances of the entity;

(b) Significant difficulties, if any, encountered during the audit;

(c) Unless all of those charged with governance are involved in managing the entity:
   i. Significant matters arising during the audit that were discussed, or subject to correspondence, with management; and
   ii. Written representations the auditor is requesting;

(d) Circumstances that affect the form and content of the auditor’s report, if any; and

(e) Any other significant matters arising during the audit that, in the auditor’s professional judgment, are relevant to the oversight of the financial reporting process.

In the instant scenario, the auditor of Rising Star Limited is required to prepare a brief summary of following items to be reported to those in-charge of governance in accordance with SA 260 as under:

1. The company followed the method of providing depreciation as per section 123 of the Companies Act, 2013 using the useful lives prescribed as per Schedule II of the Companies Act, 2013 is correct, however, they have provided depreciation using the rates stipulated for continuous process plant is not correct. As per Schedule II Computers does not fall in continuous process plant category. Further, computers are included as NESD in Part 2 of Schedule II, which is category of assets in respect of which no extra shift depreciation is permitted. Therefore, though computers are used for 24 hours i.e. triple shift but no extra shift depreciation is permitted on the same.

2. The amount of restricted bank balances as at 1.4.2016 and 31.3.2017 was rupees 120 lakhs and the company does not believe the same as qualifying for disclosure under Cash and Cash Equivalents is not correct as prescribed in para 45 of Accounting Standard 3 “Cash Flow Statement”, an enterprise should disclose, together with a commentary by management, the amount of significant cash and cash equivalent balances held by the enterprise that are not available for use by it. Therefore, disclosure of restricted bank balances should be done in accordance with AS 3.

3. As per AS 18 If there have been transactions between related parties, during the existence of a related party relationship, the reporting enterprise should disclose the name of the transacting related party; a description of the relationship between the parties; a description of the nature of transactions; volume of the transactions either as an amount or as an appropriate proportion; any other elements of the related party transactions necessary for an understanding of the financial statements; the amounts or appropriate proportions of outstanding items pertaining to related parties at the balance sheet date and provisions for doubtful debts due from such parties at that date; and amounts written off or written back in the period in respect of debts due from or to related parties.
(i) One of related party transaction amounting 3.25 lakhs per month i.e. in lieu of marketing services has been noticed of which amount ₹ 0.25 lakh per month is exceeding the arm’s length price has not been disclosed highlighting the same as related party transactions as per AS 18.

(ii) CFO of the company refused to provide the related party transaction of amounting rupees 47 lakh on the ground that same is perceived to be confidential and cannot be shared with auditors, is not in order.

(iii) Receipt of free of cost Computers and long term borrowing (on no agreed terms and repayment of interest and principal) from the Parent Company need separate disclosure in financial statements as per AS 18.

4. Pursuant to the provisions of Section 124(5) of the Companies Act, 2013, dividend which remains unpaid or unclaimed for a period of seven years from the date of its transfer to unpaid dividend account is required to be transferred by the Company to Investor Education and Protection Fund (IEPF), established by the Central Government under the provisions of Section 125 of the Companies Act, 2013. The details of unpaid dividend amount should also be disclosed in accordance with the provisions given in the Companies Act, 2013. Rising Star Limited should also transfer the 38 lakh rupees which is unclaimed dividend pertaining to period beyond 7 years and which should be transferred to IEPF. Write back of unclaimed dividend to Statement of Profit & Loss under other income is not correct in view of provisions of the Companies Act, 2013.

5. As per AS 11 exchange differences on such a contract should be recognised in the statement of profit and loss in the reporting period in which the exchange rates change. Any profit or loss arising on cancellation or renewal of such a forward exchange contract should be recognised as income or as expense for the period. Thus, accounting of mark to market loss of rupees 13.74 lakhs on the outstanding forward contracts pertaining to highly probable transactions to be done on December 2018 on the basis of date of settlement is not in order as per Accounting Standard 11.

6. Para 12 of AS 5 states that when items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately. Here the gain on sale of land is more than 5% of net-revenue. Hence, based on size and non-recurring nature of the transaction, it is opined that is shall be presented as an exceptional item.

Further, as per para 75 of AS 10, the gain or loss arising from the derecognition of an item of property, plant and equipment should be included in the statement of profit and loss when the item is derecognised. Gains should not be classified as revenue, as defined in AS 9, Revenue Recognition.

Further, separate disclosure is required for gain on sale of freehold land at Kurukshtetra in financial statements as per AS 5.
7. Though as per substance over form freehold land appearing in financial statements is correct however, non-registration of the same should be separately disclosed in notes to financial statements. Further such land should be classified as asset held for sale/disposal.

8. Denying for the related part details of ₹ 47 Lakhs is imposing limitation on scope of auditor in view of SA 705.

9. Overstatement of revenue by amounting rupees 14.50 lakhs due to difference in amount of TDS receivable as per books and the cumulative balance as per Form 26 AS.

10. As per AS 29 A provision is a liability which can be measured only by using a substantial degree of estimation and provision should be made when (a) an enterprise has a present obligation as a result of a past event; (b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and (c) a reliable estimate can be made of the amount of the obligation. In the instant case, Rising Star Limited should made the provision for ₹ 250 lakh for legal notice served by Right International Inc. for patent infringement claiming rupees because as per legal opinion possibility of cash outflow is more than not under the existing legal framework.

11. As per section 123 of the Companies Act, 2013, dividend cannot be declared or paid by a company for any financial year except (a) out of profits of the company for that year arrived at after providing for depreciation in accordance with the provisions of Section 123(2), or (b) out of the profits of the company for any previous financial year or years arrived at after providing for depreciation in the manner aforementioned and remaining undistributed, or (c) out of the balances of profit mentioned in (a) and (b) above; or (d) out of money provided by the Central Government or a State Government for the payment of dividend by the company pursuant to the guarantee given by that Government. Therefore, putting forward a proposal to pay dividend to the shareholders notwithstanding the current financial condition which is in loss by CEO of the Company and his proposal to manage the cash flows by borrowing from the bank is not correct in view of section 123 of the Companies Act, 2013.

**Answer 5**

As per section 143 (3) (j) the auditor’s report shall also state such other matters as may be prescribed. Rule 11 of the Companies (Audit and Auditors) Rules, 2014. Rule 11 of CAAR prescribes the other matters to be included in auditor’s report. The auditor's report shall also include their views and comments on the following matters, namely:

(a) whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;

(b) whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts;

(c) whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.
“(d) whether the company had provided requisite disclosures in its financial statements as to holdings as well as dealings in Specified Bank Notes during the period from 8th November, 2016 to 30th December, 2016 and if so, whether these are in accordance with the books of accounts maintained by the company”.

In the instant case, the auditor of Rising Star Limited is required to report the following matters as per Rule 11 of CAAR 2014:

(I) “whether the company has disclosed the impact, if any, of pending litigations on its financial position in its financial statement;”
   (i) Rising Star Limited should disclose the impact of payment made under protest against certain tax claims amounting rupees 1.22 lakhs.
   (ii) Legal notice served by Right International Inc. for patent infringement claiming rupees 250 lakhs.

(II) “whether the company has made provision, as required under any law or accounting standards, for material foreseeable losses, if any, on long term contracts including derivative contracts;”

As per AS 11 exchange differences on such a contract should be recognised in the statement of profit and loss in the reporting period in which the exchange rates change. Any profit or loss arising on cancellation or renewal of such a forward exchange contract should be recognised as income or as expense for the period. Thus, as per Rule 11 of CAAR 2014 the auditor is also required to report on mark to market loss of rupees 13.74 lakhs on the outstanding forward contracts pertaining to highly probable transactions.

(III) “whether there has been any delay in transferring amounts, required to be transferred, to the Investor Education and Protection Fund by the company.”

Pursuant to the provisions of Section 124(5) of the Companies Act, 2013, dividend which remains unpaid or unclaimed for a period of seven years from the date of its transfer to unpaid dividend account is required to be transferred by the Company to Investor Education and Protection Fund (IEPF), established by the Central Government under the provisions of Section 125 of the Companies Act, 2013. The details of unpaid dividend amount should also be disclosed in accordance with the provisions given in the Companies Act, 2013. Rising Star Limited should also transfer the 38 lakh rupees which is unclaimed dividend pertaining to period beyond 7 years and which should be transferred to IEPF. Write back of unclaimed dividend to Statement of Profit & Loss under other income is not correct. The auditor is required to disclose this as per Rule 11 of CAAR 2014.

(IV) “whether the company had provided requisite disclosures in its financial statements as to holdings as well as dealings in Specified Bank Notes during the period from 8th November, 2016 to 30th December, 2016 and if so, whether these are in accordance with the books of accounts maintained by the company”.

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The auditor is also required to report as per Rule 11 of CAAR 2014 on disclosure in its financial statements with respect to holdings as well as dealing in specified bank notes during the prescribed period. The auditor is also required to ensure/report on above specified bank notes that whether these are in accordance with the books of accounts maintained by the company.

Question No. II (Contains Part – A and Part – B)

Background

New Gen Toys and Clothing Limited, is a reputed company which is engaged in two businesses viz.

(i) Manufacture of Soft Toys.

(ii) Fabrics and Cloth business through textile showrooms in various cities and towns.

The manufacture of soft toys started with effect from 01-04-2016 and that of fabric and cloth business with effect from 01-04-2017.

Separate books of accounts as are legally required to be maintained are maintained for the aforesaid businesses. The books of accounts maintained do comply with all significant accounting policies, accounting on the basis of historical cost convention, compliances of Accounting Standards, alignment with generally accepted accounting principles, accrual system of accounting and on the basis of going concern. The books of accounts are also duly audited by a reputed firm of Chartered Accountants. The income tax assessments is also completed up to Assessment year 2016-17 and there are no income tax or any other statutory dues payable by the company.

The Company’s founder and Managing Director has resigned from his position and has inducted in his place his young son, aged 24 years, a research scholar from Harvard University as the new Managing Director after due approval of the Board as well as the shareholders at the annual general meeting of the Company held on 29-09-2016.

The new Managing Director of the Company is desirous of knowing various facets of the provisions of the Income Tax Act, 1961 with special reference to the relevant Sections of the said Act for adopting certain tax planning measures and for other business decision making including, the essential conditions for claiming exemption for newly established units in Special Economic Zones. In this context, he has approached you in the capacity of a Chartered Accountant in practice and also being an expert in the field of direct taxation and has offered you a professional fee. The new Managing Director has provided you with the following information in relation to the soft toys manufacturing business as well as the fabrics and cloth business for the year ended March 31, 2018 and seeks your advice to the questions at the end.
SOFT TOYS MANUFACTURING BUSINESS:

**Net Profit as per Statement of Profit and Loss – ₹ 36,50,000**

**Items debited/credited to Statement of Profit and Loss:**

(i) Bad debts written off in previous year 2016-17 ₹ 2,50,000 of which ₹ 1,80,000 was recovered in July, 2017.

(ii) CSR expenditure by way of putting traffic signal outside the factory ₹ 2 lakhs.

(iii) Donation to registered political party ₹ 70,000. Of this, paid by cash ₹ 30,000 and by cheque ₹ 40,000.

(iv) Amount received as 30% share in an AOP ₹ 1,20,000. The AOP is engaged in the business of plastic mould manufacture.

(v) Long term capital gain on sale of unlisted shares (without indexation) ₹ 50,000.

(\textbf{Note:} With indexation, the long-term capital gain is ₹ 30,000)

(vi) Dividend from domestic companies received during the year ₹ 11,00,000.

(vii) ₹ 20 lakhs was paid to a founder director by way of goodwill, who resigned from the Company on 30-04-2017. No tax was deducted at source on the said payment.

(viii) Depreciation debited ₹ 13,50,000.

(ix) Deferred tax liability debited to profit and loss account ₹ 3 lakhs.

(x) Royalty ₹ 10 lakhs received in respect of Patent developed and registered in India.

FABRICS AND CLOTH BUSINESS:

**Net profit as per Statement of Profit and Loss – ₹ 26,50,000**

**Items debited/credited to Statement of Profit and Loss:**

(i) Income tax debited ₹ 6,60,000.

(ii) Online advertisement charges paid to a foreign company ₹ 2,00,000. No tax was deducted at source.

(iii) Depreciation debited to statement of profit and loss ₹ 24,00,000 (includes ₹ 8 lakhs on account of revaluation of assets).

(iv) Interest on term loan paid during the year ₹ 8,50,000. It includes ₹ 3,20,000 of the financial year 2012-13 which was disputed before the Court and the Court decreed the case in November, 2017.

(v) Group Gratuity Scheme was approved by Commissioner of Income Tax during the year and ₹ 21 lakhs was paid to LIC of India by way of its contribution.

(\textbf{Note:} The payment to employees during the year from the scheme ₹ 3 lakhs)

(vi) Provision made for decrease in value of showroom buildings due to wear and tear ₹ 7,00,000.
Additional Information:

(i) During the year, for the Fabric and Cloth business division, the Company bought generators for ₹ 40 lakhs and for which it got ₹ 5 lakhs by way of subsidy from the Government. This was credited to capital reserve. The Company paid ₹ 3 lakhs by cash and balance ₹ 32 lakhs through net banking channel to the supplier. Though generators were acquired in August, 2017 they were put to use only from 01-12- 2017.

(ii) The Company has not considered interest due of ₹ 2,50,000 from customers of toys division for the delayed payment of bills by them.

(iii) Eligible depreciation under Section 32 in respect of all tangible assets (except generators) is ₹ 87,50,000.

(iv) The Company earned ₹ 2,20,000 by way of sale of carbon credit. This has been credited to capital reserve.

(v) The Company has unabsorbed loss of ₹ 12,50,000 of the assessment year 2016-17 relating to Soft toys manufacturing business. The return was however filed before the ‘due date’ specified in Section 139(1).

(vi) During the year, the Company paid ₹ 4 lakhs to a Director who gave guarantee for securing overdraft facility obtained by Soft toys manufacturing division. This amount is debited to general reserve of the Company.

(vii) The Company employed 30 workers for 9 months during the year 2017-18 by paying salary of ₹ 15,000 per month. The number of employees as on 31-03-2018 has increased by the said recruitment as against the number of employees as on 31-03-2017.

PART-A

Choose the most appropriate alternative for the following and justify the same with reasons in brief:

(1) The Company is eligible to claim depreciation in respect of goodwill at ________ %

(A) 25  
(B) 15  
(C) 100  
(D) NIL  

(2 Marks)

(2) The Company is liable to pay equalization levy at ___% in respect of online advertising paid to non-resident.

(A) 10  
(B) 20  
(C) 8  
(D) 6  

(2 Marks)
(3) The monetary limit for salary per month to new employee for the purpose of claiming deduction under section 80 JJAA under the appropriate provision of Chapter VI-A is
(A) No limit
(B) ₹ 25,000
(C) ₹ 15,000
(D) ₹ 10,000 (2 Marks)

(4) The tax liability due to sale of carbon credit would be
(A) ₹ 67,980 (at 30.9%)
(B) ₹ 45,320 (at 20.6%)
(C) ₹ 22,660 (at 10.3%)
(D) NIL (exempt) (2 Marks)

(5) Amount paid to director for giving guarantee for the Company to secure overdraft facility is chargeable to tax in the hands of Director as
(A) Deemed dividend
(B) Dividend
(C) Income from other sources
(D) Directors’ fee (2 Marks)

(6) In the case of online advertisement charges paid to domestic company, the amount liable for disallowance for non-deduction of tax at source would be:
(A) 10% i.e. 20,000
(B) 30% i.e. 60,000
(C) 100% i.e. 20,000
(D) NIL (2 Marks)

(7) For a domestic company, the long-term capital gain on sale of unlisted shares is taxable at
(A) 10%
(B) 15%
(C) 20%
(D) Fully exempt. (2 Marks)

(8) Interest on term loan is deductible when it is
(A) Paid on or before the 'due date' specified in Section 139(1)
(B) Paid before the 'end' of the previous year.
(C) Paid within 15 days from the date it becomes due.
(D) Due as per the agreement. (2 Marks)

(9) When the assessee has speculation loss, it is eligible for carry forward and set off in the subsequent ____________ assessment years.
(A) 4
(B) 6
(C) 8
(D) Infinite (2 Marks)

(10) The income of the AOP in which the Company is a member is chargeable to tax at_____________ (tax rate).
(A) Individual rate
(B) Maximum marginal rate
(C) 20%
(D) NIL (2 Marks)

**PART-B**

(a) Compute the business income of soft toys manufacturing business for the Assessment Year 2018-19 (7 Marks)

(b) Compute the business income of fabrics and cloth business for the Assessment Year 2018-19 (8 Marks)

(c) Compute total income of the Assessee for the Assessment Year 2018-19. (5 Marks)

(d) Compute the book profit tax under Section 115JB on the assumption that the consolidated figures of two divisions were given in Schedule III to Companies Act, 2013. (5 Marks)

(e) What are the essential conditions for claiming exemption for newly established units in Special Economic Zones? (5 Marks)

**Answer to Question 2 Part A (MCQs)**

1) Option (A) 25 

**Reasoning:** Goodwill is classified as an intangible asset. Intangible assets are eligible for depreciation @ 25% as per section 32 read with Rule 5 of Income-tax Rules, 1962.
(2) Option (D) 6%
Reasoning: As per Chapter VIII of the Finance Act, 2016, when payment exceeding ₹1 lakh is made to a non-resident\(^1\) for online advertisement, it is liable for deduction of equalization levy @6% by the resident-assessee.

(3) Option (B) ₹25,000
Reasoning: The total emoluments of an employee must not exceed ₹25,000 per month for the purpose of qualifying as an “additional employee” for claim of deduction under section 80JJAA

(4) Option (C) ₹22,660 (at 10.3%)
Reasoning: As per section 115BBG, income by way of transfer of carbon credit is chargeable to tax @10.3% (inclusive of education cess and secondary and higher education cess).

(5) Option (C) Income from other sources
Reasoning: Guarantee received by the director is includible in his total income and chargeable to tax under the head “Income from other sources”. Such payment made does not fall in the category of deemed dividend, dividend or director fee.

(6) Option (B) 30% i.e., ₹60,000
Reasoning: Non-deduction of tax at source on online advertisement charges paid to domestic company would attract disallowance @30% under section 40(a)(ia).

(7) Option (C) 20%
Reasoning: As per section 112, long term capital gains on sale of unlisted shares in the hands of domestic company is taxable @ 20%.

(8) Option (A) Paid on or before the ‘due date’ specified in section 139(1).
Reasoning: As per section 43B, interest on term loan is deductible when it is paid during the previous year or before the due date specified in section 139(1)

(9) Option (A) 4
As per section 73(4) the speculation loss is eligible for carry forward upto 4 assessment years for set-off against speculative business income.

(10) Option (B) Maximum marginal rate
As per section 167B, income of the AOP in which the company is a member is chargeable to tax at the maximum marginal rate.

\(^1\)Assuming that the non-resident does not have a permanent establishment in India
PART-B

Answer (a)

Computation of business income of soft toys manufacturing business for the A.Y.2018-19

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net profit as per the statement of profit and loss</td>
<td>36,50,000</td>
</tr>
<tr>
<td><strong>Add:</strong> Expenditure debited to statement of profit &amp; loss but not allowable as deduction or to be considered separately</td>
<td></td>
</tr>
<tr>
<td>(ii) CSR Expenditure incurred</td>
<td>2,00,000</td>
</tr>
<tr>
<td>[As per Explanation 2 to Section 37(1), CSR expenditure incurred by the company as per the Companies Act, 2013 is not deemed to be an expenditure incurred by the company for the purposes of business or profession. Hence, the same is not allowable as deduction. Since the same has been debited to statement of profit and loss, it has to be added back]</td>
<td></td>
</tr>
<tr>
<td>(iii) Donation to registered political party</td>
<td>70,000</td>
</tr>
<tr>
<td>[Donation paid to a political party is not an allowable expenditure under section 37 since it is not laid out wholly or exclusively for the purposes of business or profession. Hence, the same has to be added back while computing business income]</td>
<td></td>
</tr>
<tr>
<td>(vii) Amount paid towards goodwill to a director</td>
<td>20,00,000</td>
</tr>
<tr>
<td>[Goodwill is an intangible asset which is eligible for depreciation under section 32(1) and the amount paid for acquisition of a capital asset is not allowable as deduction. Since the same has been debited to the statement of profit and loss, it has to be added back for computing business income]</td>
<td></td>
</tr>
<tr>
<td>(viii) Depreciation as per books of account</td>
<td>13,50,000</td>
</tr>
<tr>
<td>(ix) Deferred tax liability</td>
<td>3,00,000</td>
</tr>
<tr>
<td>[Deferred tax is an accounting concept and there is no provision in the Income-tax Act, 1961 permitting deduction in respect of the same. Therefore, provision for deferred tax is not an allowable deduction while computing business income. Since the same has been debited to the statement of profit and loss, it has to be added back for computing business income]</td>
<td></td>
</tr>
</tbody>
</table>

<p>|                                                           | 39,20,000  |
|                                                           | 75,70,000  |</p>
<table>
<thead>
<tr>
<th><strong>Add:</strong> Income taxable but not credited to statement of profit and loss</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Al(ii) Interest due from customers</td>
<td>2,50,000</td>
</tr>
<tr>
<td>[Interest due from customers for delayed payment of bills by them is business income. Since the same has been credited to the statement of profit and loss, no further adjustment is required for the same]</td>
<td></td>
</tr>
</tbody>
</table>

**Less:** Items credited to statement of profit and loss, but not includible in business income

| (i) Bad debt recovered | - |
| [The amount of bad debt written off earlier when recovered subsequently, such recovery is taxable under section 41(4). Since the same has been credited to the statement of profit and loss, no further adjustment is required for the same] |  |
| (iv) Share income in AOP | 1,20,000 |
| [Since AOP has to pay tax at the maximum marginal rate or a higher rate, company’s share in the total income of AOP will not be included in his total income and will be exempt. Since the same has been credited to the statement of profit and loss, the same has to be reduced while computing business income] |  |
| (v) Long term capital gain on sale of unlisted shares | 50,000 |
| [The taxability or otherwise of long term capital gain on sale of unlisted shares has to be considered while computing income under the head “Capital Gains”. Since such capital gain has been credited to statement of profit and loss, the same has to be reduced to arrive at the business income.] |  |
| (vi) Dividend received from domestic companies | 11,00,000 |
| [The taxability or otherwise of dividend received has to be considered while computing income under the head “Other Sources”. Since such dividend has been credited to statement of profit and loss, the same has to be reduced to arrive at the business income.] |  |
| (x) Royalty income in respect of patents developed and registered in India | - |
| [Royalty income in respect of patents developed and registered in India is chargeable to tax under section 115BBF can be treated as business income or income from other sources, depending upon the facts of the case.] |  |
In this case, it is assumed that the same is in the nature of business income. Since the amount of ₹10 lakh has already been credited to statement of profit and loss, no further adjustment is necessary.

*Note* – In the alternative, the said income of ₹10 lakhs may be treated as “Income from other sources” and accordingly, reduced the same to compute business income.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less: Expenditure allowable but not debited to statement of profit and loss</td>
<td></td>
</tr>
<tr>
<td>Depreciation</td>
<td></td>
</tr>
<tr>
<td>Depreciation allowable under the Income-tax Act, 1961 on tangible assets of ₹31,50,000 [i.e., ₹87,50,000 x 13,50,000/ 37,50,000] plus Depreciation on goodwill of ₹5,00,000 [i.e., ₹20,00,000 x 25%]</td>
<td>36,50,000</td>
</tr>
<tr>
<td><em>Note</em> – Depreciation allowable under section 32 is given in item (iii) of Additional information. The basis of bifurcation of depreciation between the two businesses is not given in the question. In this solution, the depreciation has been bifurcated between the two businesses of New Gen Toys and Clothing Ltd in the ratio of depreciation already debited as per books of account. It is possible to bifurcate the depreciation on any other reasonable basis.</td>
<td></td>
</tr>
<tr>
<td>Guarantee fees paid to Director</td>
<td>4,00,000</td>
</tr>
<tr>
<td>[Guarantee fee paid to director for securing overdraft facility obtained by the company is an allowable deduction since it is incurred wholly and exclusively for the business purpose.]</td>
<td>40,50,000</td>
</tr>
<tr>
<td>Profits and gains from business and profession</td>
<td>25,00,000</td>
</tr>
</tbody>
</table>

**Answer (b)**

**Computation of business income of fabric and cloth business for the A.Y.2018-19**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net profit as per the statement of profit and loss</td>
<td>26,50,000</td>
</tr>
<tr>
<td><em>Add</em>: Expenditure debited to statement of profit &amp; loss but not allowable as deduction or to be considered separately</td>
<td></td>
</tr>
</tbody>
</table>
### PAPER – 6F: MULTIDISCIPLINARY CASE STUDY

<table>
<thead>
<tr>
<th>(i) Income tax</th>
<th>6,60,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>[Income tax paid is not allowable as deduction from business income as per section 40(a)(ii). Since the same has been debited to the statement of profit and loss, it has to be added back for computing business income]</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(ii) Online advertisement charges paid to foreign company</th>
<th>2,00,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>[Non deduction of equalisation levy on payment of online advertisement charges to a non-resident, by a resident in India who carries on business or profession, would attract disallowance @100% of expenditure. Since the same has been debited to the statement of profit and loss, it has to be added back for computing business income]</td>
<td></td>
</tr>
</tbody>
</table>

**Note** - It is assumed that the foreign company does not have a permanent establishment in India.

<table>
<thead>
<tr>
<th>(iii) Depreciation as per books of account</th>
<th>24,00,000</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>(iv) Interest on term loan</th>
<th>-</th>
</tr>
</thead>
<tbody>
<tr>
<td>[As per section 43B, a deduction of any sum, being interest payable on any loan or borrowing from a public financial institution shall be allowed, if such interest has been actually paid. Since interest related to F.Y. 2012-13 is paid in P.Y. 2017-18, it is allowable as deduction in P.Y. 2017-18. Since the same has been debited to the statement of profit and loss, it has to be added back for computing business income]</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(v) Contribution to gratuity fund</th>
<th>-</th>
</tr>
</thead>
<tbody>
<tr>
<td>[Any contribution to approved gratuity fund is allowable as deduction. Since the contribution of ₹21 lakhs has been debited to the statement of profit and loss, no adjustment is required for the same. Since ₹ 3 lakhs payment to employees is out of the gratuity fund, it has already been allowed as deduction. No separate treatment is required.]</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(vi) Provision for decrease in value of showroom building</th>
<th>7,00,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>[Provision for any asset is not an allowable deduction while computing business income. Since the same has been debited to the statement of profit and loss, it has to be added back for computing business income]</td>
<td></td>
</tr>
</tbody>
</table>

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Add: Subsidy received from Government for acquisition of generator

[Grant/Subsidy received from the Government, other than a grant which is taken into account for determination of actual cost of the asset, is included in the definition of income. In this case, since the grant is received for acquisition of generator, the same has to be adjusted in actual cost.

Since the same has not been credited to the statement of profit and loss, no adjustment is required for the same]

Less: Depreciation

Depreciation allowable under the Income-tax Act, 1961 on tangible assets of ₹ 56,00,000 [i.e., ₹ 87,50,000 x 24,00,000/ 37,50,000] plus Depreciation on generator of ₹ 2,40,000 [i.e., ₹ 32,00,000, being amount paid in cash for generator and the amount of grant, not includible in actual cost x 15% x 50%]

Note – Depreciation allowable under section 32 is given in item (iii) of Additional information. The basis of bifurcation of depreciation between the two businesses is not given in the question. In this solution, the depreciation has been bifurcated between the two businesses of New Gen Toys and Clothing Ltd in the ratio of depreciation already debited as per books of account. It is possible to bifurcate the depreciation on any other reasonable basis.

Profits and gains from business and profession

Profit and gains from business and profession

Answer (c)

Computation of total income of New Gen Toys and Clothing Ltd. for the A.Y. 2018-19

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Profit and gains from business and profession</td>
<td></td>
</tr>
<tr>
<td>Profits and gains of soft toy business</td>
<td>25,00,000</td>
</tr>
<tr>
<td>Profits and gains of fabric and cloth business</td>
<td>7,70,000</td>
</tr>
<tr>
<td></td>
<td>32,70,000</td>
</tr>
<tr>
<td>Particulars</td>
<td>Amount (₹)</td>
</tr>
<tr>
<td>----------------------------------------------------------------------------</td>
<td>------------</td>
</tr>
<tr>
<td><strong>Less: Brought forward business loss</strong></td>
<td>12,50,000</td>
</tr>
<tr>
<td><strong>II. Capital gains</strong></td>
<td></td>
</tr>
<tr>
<td>Long term capital gain on sale of unlisted shares [Chargeable to tax@20% with indexation benefit]</td>
<td>30,000</td>
</tr>
<tr>
<td><strong>III. Income from Other Sources</strong></td>
<td></td>
</tr>
<tr>
<td>Sale of carbon credit</td>
<td>2,20,000</td>
</tr>
<tr>
<td>Dividend from domestic companies [Exempt u/s.10(34)]</td>
<td>2,20,000</td>
</tr>
<tr>
<td><strong>Gross Total Income</strong></td>
<td>22,70,000</td>
</tr>
<tr>
<td><strong>Less: Deduction under Chapter VI-A</strong></td>
<td></td>
</tr>
<tr>
<td>Under section 80JJAA [ (₹15,000 x 30 workers x 9 months) x 30%]</td>
<td>12,15,000</td>
</tr>
<tr>
<td>Under section 80GGC [Donation to registered political party, ₹ 40,000 would be allowed as deduction, since payment is made in a mode other than cash; Donation of ₹ 30,000, paid in cash, would not be allowable as deduction]</td>
<td>40,000</td>
</tr>
<tr>
<td><strong>Total Income</strong></td>
<td>10,15,000</td>
</tr>
</tbody>
</table>

**Answer (d)**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net profit as per statement of profit and loss</td>
<td>63,00,000</td>
</tr>
<tr>
<td>(₹36,50,000 + ₹26,50,000)</td>
<td></td>
</tr>
<tr>
<td><strong>Add: Net profit to be increased by the following amounts as per Explanation 1 to section 115JB:</strong></td>
<td></td>
</tr>
<tr>
<td>- Deferred tax liability debited to statement of profit and loss of toy business</td>
<td>3,00,000</td>
</tr>
<tr>
<td>- Income tax debited to fabric and cloth business</td>
<td>6,60,000</td>
</tr>
<tr>
<td>- Depreciation debited in soft toys manufacturing division</td>
<td>13,50,000</td>
</tr>
<tr>
<td>- Depreciation in respect of fabric and cloth division</td>
<td>24,00,000</td>
</tr>
<tr>
<td>- Provision for diminution in showroom buildings</td>
<td>7,00,000</td>
</tr>
<tr>
<td></td>
<td>54,10,000</td>
</tr>
<tr>
<td></td>
<td>1,17,10,000</td>
</tr>
</tbody>
</table>
Less: Net profit to be decreased by the following amounts as per Explanation 1 to section 115JB:

- Share income of AOP [Since exempt in the hands of company] 1,20,000
- Dividend from domestic companies credited to profit and loss account – exempt u/s 10(34) hence excluded 11,00,000
- Royalty ₹10 lakh received in respect of patent developed and registered in India by the assessee taxable at concessional rate @10% under section 115BBF 10,00,000
- Depreciation in respect of soft toy division 13,50,000
- Depreciation in respect of fabric and cloth division [₹24,00,000 – ₹8,00,000] 16,00,000 51,70,000

Book Profit under section 115JB 65,40,000

Tax on book profit:

18.5% of ₹65,40,000 12,09,900
Add: Education Cess and SHEC@3% 36,297
Total tax on book profit 12,46,197

Tax on book profit (rounded off) 12,46,200

Answer (e)

Conditions for claiming exemption for newly established units in SEZ

<table>
<thead>
<tr>
<th>Particulars</th>
</tr>
</thead>
<tbody>
<tr>
<td>Section 10AA deals with deduction for units located in special economic zone.</td>
</tr>
<tr>
<td>Any unit which begins to manufacture or produce articles or things or provide any service during the period from 01.04.2006 to 31.03.2020 is eligible for claiming tax benefit.</td>
</tr>
<tr>
<td>It should not be formed by splitting up or reconstruction of a business already in existence.</td>
</tr>
<tr>
<td>It should not be formed by the transfer of machinery or plant previously used for any purpose to a new business. However, deduction under section 10AA will be available if total value of the machinery or plant transferred does not exceed 20% of the total value of machinery or plant used in the business.</td>
</tr>
<tr>
<td>For this purpose, any machinery or plant which was used outside India by any person other than the assessee shall not be regarded as machinery or plant previously used for any purpose if the following conditions are fulfilled:</td>
</tr>
<tr>
<td>(a) such machinery or plant was not at any time used in India;</td>
</tr>
<tr>
<td>(b) such machinery or plant is imported into India from any country outside India; and</td>
</tr>
</tbody>
</table>
(c) no deduction on account of depreciation has been allowed in respect of such machinery or plant to any person earlier.

Question No. III (Contains Part – A and Part – B)

Background

You are a leading Mergers and Acquisition (M & A) Practitioner advising corporates on the implications of mergers and amalgamations covering various aspects inter alia on the legal, business, and corporate and tax related matters.

Your Client, Magma Automobiles Limited (the Company), has reached out to you for seeking your advice with respect to their proposal to consider some restructuring in the group in a more robust manner. They have requested you to join their internal brain storming session organized to discuss and decide on the way forward. This meeting will be attended by Yasin Malik, Managing Director, Anirudh, Chief Financial Officer, Aswini, President -Taxation and Mohan Rangarajan, Company Secretary. They have also requested their Financial Controller Subha to join the session. You have agreed to participate and provide your insights in the session.

You will be provided with the brief background of the Company and matters raised by various participants for which your advice will be required. Please note that the Company will decide the way forward based on your advice and, hence, your valuable guidance would be extremely crucial for the ultimate decision making by the Board/Shareholders.

Corporate Information

Magma Automobiles Limited "Magnum" is a listed Company incorporated under the Companies Act, 1956. The shares of the Company are listed in the Bombay Stock Exchange. It specializes in the manufacture of luxury cars and has its plants located at Hyderabad and Mumbai. It also has its own captive power plant at Hyderabad. The shareholding pattern of the Company as at 31st March, 2015 is as under:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>No. of Shares</th>
<th>Amount in ₹Lakhs</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public shareholding</td>
<td>270,000</td>
<td>270</td>
<td>27%</td>
</tr>
<tr>
<td>Promoters</td>
<td>610,000</td>
<td>610</td>
<td>61%</td>
</tr>
<tr>
<td>Institutional Investors</td>
<td>120,000</td>
<td>120</td>
<td>12%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,000,000</strong></td>
<td><strong>1,000</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

The Company has been doing extremely well and its Turnover and Profit After Tax for the past 3 years is given below:

<table>
<thead>
<tr>
<th>Year</th>
<th>Turnover (Amount in ₹Lakhs)</th>
<th>Profit after tax (Amount in ₹lakhs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY 2015</td>
<td>47,021</td>
<td>2,915</td>
</tr>
<tr>
<td>FY 2014</td>
<td>50,406</td>
<td>3,578</td>
</tr>
<tr>
<td>FY 2013</td>
<td>51,918</td>
<td>3,062</td>
</tr>
</tbody>
</table>
The Company was promoted by Rahman Malik, father of Yasin Malik who has set up several ventures as a first generation entrepreneur. Whilst there are 15 such companies promoted by him in different segments which are operational, 'Magnum' is the flagship company of the Malik group (Maliks). 'Magnum' went public in the year 2005 and the shares were oversubscribed by 2.12 times at that time. The Company has been paying dividend to its shareholders consistently and is having a healthy price trend in the Bombay Stock Exchange during the past several years.

The Company has surplus cash and the cash accretion is generally invested in fixed deposits and mutual funds.

The Proposal

Yasin Malik has put forward a proposal to merge 'Magnum' with an unlisted entity ‘Yamuna’ Fitting Works Limited, (“Yamuna”) through an approved restructuring route considering certain business reasons. He has requested the Chief Financial Officer to explain the financial and other details of 'Yamuna' to kick start the discussions further. He has also preferred to go for a capital reduction of 'Yamuna', if permissible under the law along with the Scheme.

Information Provided by Anirudh, CFO

‘Yamuna’ which is an entity promoted by the Maliks, is specializing in the manufacture of engineering products for vehicle manufacture. It was incorporated in 2010 and its plant is located at Pune. Due to various external conditions, 'Yamuna' is not doing well and has recorded huge losses accumulated year on year. Details of shareholding pattern of 'Yamuna' as at 31\textsuperscript{st} March, 2015 is as under:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>No. of Shares</th>
<th>Amount in ₹ Lakhs</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Promoters (same Shareholders as that of ‘Magunum’)</td>
<td>90,000</td>
<td>90</td>
<td>90%</td>
</tr>
<tr>
<td>Friend and Relatives</td>
<td>10,000</td>
<td>10</td>
<td>10%</td>
</tr>
<tr>
<td>Total</td>
<td>100,000</td>
<td>100</td>
<td>100%</td>
</tr>
</tbody>
</table>

The number of shares mentioned above have increased every year by 7,000 shares for the last 7 years continuously, but the proportion of shareholding has remained the same.

The key financial data of ‘Yamuna’ is as under: (₹ in lakhs)

<table>
<thead>
<tr>
<th>Particulars</th>
<th>As at 31\textsuperscript{st} March, 2015</th>
<th>As at 31\textsuperscript{st} March, 2014</th>
<th>As at 31\textsuperscript{st} March, 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity Share Capital</td>
<td>100</td>
<td>93</td>
<td>86</td>
</tr>
<tr>
<td>Capital Reserve</td>
<td>25</td>
<td>25</td>
<td>25</td>
</tr>
<tr>
<td>General Reserve</td>
<td>42</td>
<td>42</td>
<td>42</td>
</tr>
<tr>
<td>Profit &amp; Loss Account</td>
<td>(287)</td>
<td>(211)</td>
<td>(163)</td>
</tr>
</tbody>
</table>
Anirudh has highlighted the following significant matters relating to 'Yamuna':

- 'Magnum' has lent an amount of ₹20,000 Lakhs to 'Yamuna' as an inter-corporate deposit for meeting various working capital requirements in the year 2012 which is being rolled over every 6 months since 'Yamuna' is not in a position to repay the loan as per the agreed tenure. It is also not servicing any interest and the amount of interest payable as per the terms is not recognised in the books of 'Magnum' in view of the uncertainties attached to revenue recognition.

- In addition, 'Yamuna' has also taken loans from Zomi Bank for ₹10,000 lakhs and the same has been guaranteed by 'Magnum'. Due to default in repayment, the bank has classified the loan provided to 'Yamuna' as a Non-Performing Asset. It has also taken certain steps to recover the amount by filing a winding up petition. 'Yamuna' is in the process of discussing One Time Settlement with the Bank through some third party funding arrangement. The gains arising out of one time settlement amounting to ₹2,000 lakhs has already been taken to Revenue on accrual basis in anticipation of the settlement.

- 'Yamuna' is dependent on couple of customers namely Magic Works and Perfection Precision Works. Whilst the operating level margins are positive, at net profit level, these arrangements are not profitable due to its limited size/complication involved in execution.

- Lack of adequate core working capital and higher power cost are the main reasons for the loss in 'Yamuna'.

- Whilst the plant of 'Yamuna' requires renovation, the same can be utilized for carrying out certain activities of 'Magnum' with some additional investment of about Rs 1,000 lakhs.

- The accumulated business loss of 'Yamuna' as per tax is ₹4,500 lakhs and the unabsorbed depreciation loss is ₹1,200 lakhs.
Further Background of the Proposal

Yasin Malik added that it is apparent that 'Yamuna' is going through tough times and all the efforts made by the promoters to revive the entity has become futile and time has come now to fix the problem with the help of 'Magnum'.

He added that a due valuation of both the entities may be carried out and based on the swap ratio as determined by the Valuers, shares can be allotted to the holders of 'Magnum' in 'Yamuna'. He also wanted to understand the process involved under the Companies Act, 2013 listing agreement, as well as SEBI (LODR) Regulations, 2015 as well as other applicable regulations that are significant.

Key Matters raised by Aswini, President, Taxation.

Aswini has suggested that since 'Magnum' is a tax paying entity, through the merger, the possibility of setting off the carry forward losses of 'Yamuna' including the speculative losses, needs to be explored.

He also added that considering the financial position of 'Magnum' and 'Yamuna', based on the valuation, the merger could trigger a goodwill in the hands of 'Yamuna' which can also be considered for tax deduction.

He was skeptical about the acceptance of the scheme by the tax authorities in view of the involvement of the Group Company/related party. He wanted to know if the same would be permissible under the Companies Act, 2013.

Inputs from Mohan Rangarajan, Company Secretary.

Mohan believes that this proposal is completely workable and infact the same needs to be mandatorily pursued through the fast track mechanism available under the regulatory framework. He further added that the ICD which remains as outstanding from 'Yamuna' will, also be eliminated on merger and hence the issue of repayment also does not arise. He wanted some inputs on the various procedural formalities involved in getting the regulatory consent for the scheme.

Mohan also indicated that the creditors meeting is not required if the eligible conditions are satisfied.

Matters raised by Subha, Financial Controller.

Subha raised the issue of accounting for interest on the ICD. Further, Subha also raised the issue of on going settlement with the bankers and the potential impact of the same on this proposal. In addition, Subha raised the issue of the date of giving effect to the proposal in the books of account based on the scheme if approved by the appropriate authority.

Other matters raised during the session

It was agreed that the merger proposal will be pursued based on the scheme to be approved by the Board/Shareholders/other stakeholders/appropriate authority under the Companies Act,
2013 and other applicable legislation duly taking the required professional advise wherever required.

PART-A

Based on the above information, please provide your suitable advice to your client to assist him in forming his opinion to the following questions in short and appropriate technical reference:

1. The proposal put forward by 'Magnum' would be best termed as
   (A) Asset Sale
   (B) Amalgamation
   (C) Slump Sale
   (D) None of the above (2 Marks)

2. Capital Reduction of 'Yamuna' can be carried out along with the proposal of 'Magnum' to merge with 'Yamuna' if approved by all the stakeholders/appropriate authority.
   (A) No
   (B) Yes
   (C) Permissible only under certain circumstances with the approval of Competition Commission of India.
   (D) Permissible only with the consent of all the minority shareholders. (2 Marks)

3. The Scheme, if approved, will be given effect to in the books of account on
   (A) The date of the Order of the Appropriate Authority
   (B) Appointed Date
   (C) Financial year end in which the Order is received.
   (D) The date on which the Order of the Appropriate Authority is filed with the Registrar of Companies. (2 Marks)

4. On giving effect to the Scheme, Inter-company Loan provided by 'Magnum' to 'Yamuna'
   (A) Will remain in the books of 'Yamuna'
   (B) Will re squared off
   (C) Will remain as a memorandum Entry
   (D) Will remain only in the books of 'Magnum' (2 Marks)

5. Whether the proposal of 'Magnum' for the merger needs to be mandatorily pursued under fast track option?
   (A) Yes
   (B) Would vary on a case to case basis depending on the contents of the scheme.
(C) Yes, if it involves capital reduction  
(D) No  

(6) Whether the speculative losses carried forward by 'Yamuna' is available for set off against the profits and gains of business of 'Yamuna' post-merger?  
(A) Yes  
(B) No  
(C) Permissible if it is within the period of 8 years.  
(D) If the Scheme provides for such set off, the same would be permissible.  

(7) The accounting for the one time settlement benefit in the form of anticipated interest waiver by the Bank in the books of account of 'Yamuna' for the year ended 31st March, 2015 is appropriate.  
(A) Yes, it is appropriate.  
(B) No, this should be accounted as an exceptional item.  
(C) No  
(D) Permissible since the entity is going through the merger proposal.  

(8) Meeting of the Creditors cannot be dispensed with under any circumstances under the Companies Act, 2013  
(A) Yes  
(B) No, it can be dispensed with under certain circumstances as stipulated under the Companies Act, 2013.  
(C) Dispensation is possible, if the scheme is approved by the shareholders.  
(D) Dispensation is not possible, if there is a loan taken from the Bank.  

(9) Additional amount of capital expenditure expected to be spent on renovation of 'Yamuna' needs to be accounted in the books of account on  
(A) The Effective Date of the Scheme.  
(B) Date of filing the approved scheme with the Registrar of Companies.  
(C) The day on which the expenditure is incurred.  
(D) End of the financial year in which the order sanctioning the scheme was received.  

(10) Any Merger Scheme which involves 'related parties' would not be approved under the Companies Act, 2013.  
(A) Yes
(B) Permissible if the stipulated requirements of the Act including obtaining the consent from all the intended stakeholders is complied with

(C) Permissible only when the 'related parties' sell off their holding to third parties.

(D) Permissible with the sole approval of the Audit Committee.  (2 Marks)

PART-B

Answer the following:

(a) What are the risk factors to be considered in the matter of merger of 'Magnum' with 'Yamuna'?  (5 Marks)

(b) What are the ideal considerations for a reverse merger and state its relevance to 'Magnum'?  (5 Marks)

(c) If the Reverse Merger scheme is duly approved under the Companies Act, 2013 evaluate the impact of the same under the Income Tax Act, 1961 for 'Yamuna'.  (10 Marks)

(d) Who are the stakeholders impacted because of the Reverse Merger proposal to whom the required notices have to be sent/consent to be taken before the sanctioning of the Scheme?  (5 Marks)

(e) Are there any other options available Instead of Reverse Merger Option? If so, please explain the same with your rationale.  (5 Marks)

Answer to Question 3 Part A (MCQs)

(1) Option (D): None of the Above

Reasoning: The proposal would be in the nature of Reverse Merger. Reverse Merger refers to a merger where the smaller company gains control over a large one. In this case, Magnum (the transferor company) is a larger listed entity which is getting merged into Yamuna (the transferee company), the smaller unlisted loss making entity. Hence, this is a reverse merger.

(2) Option (B): yes.

Reasoning: Explanation to section 230 of the Companies Act, 2013—For the removal of doubts, it is hereby declared that the provisions of section 66 shall not apply to the reduction of share capital effected in pursuance of the order of the Tribunal under this section.

Since reduction of share capital requires an application to Tribunal by company after passing Special Resolution and on confirmation by Tribunal, reduction of share capital gets effected. However, in the case of compromise under section 230 if that results into reduction of capital, compliance of section 66 is not required to be made separately in such cases.
(3) Option (B): Appointed Date.

**Reasoning:** As per section 232, Sub-section (5) & (6), states that every company in relation to which the order is made shall cause a certified copy of the order to be filed with the Registrar for registration within thirty days of the receipt of certified copy of the order. The scheme under this section shall clearly indicate an appointed date from which it shall be effective and the scheme shall be deemed to be effective from such date and not at a date subsequent to the appointed date.

(4) Option (B) : Will be squared off

**Reasoning:** Mutual transactions are eliminated and the intercompany balances are set-off during merger as per general practice followed in Accounting.

(5) Option (D): No

**Reasoning:** As per section 233 of the Companies Act, 2013, a scheme of merger or amalgamation under Fast Track may be entered into between two or more small companies or between a holding company and its wholly-owned subsidiary company or such other class or classes of companies as given in Rule 25 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016. So the proposal of Magnum for the merger need not be required to be pursued under fast track option.

(6) Option (B) No

**Reasoning:** As per section 73(1), a loss in speculation business can be set off only against the profits and gains of any other speculation business and not against any other normal business income.

(7) Option (C) : No

**Reasoning:** Yamuna Ltd. is in process of discussion for One-time Settlement. The deal has not been finalised. As per AS, prudence and conservatism concept did not allow to anticipate and recognise the revenue until and unless the same has been realised or accrued.

Para 37 of the Framework for the preparation and presentation of financial statements defines Prudence as “The preparers of financial statements have to contend with the uncertainties that inevitably surround many events and circumstances, such as the collectability of receivables, the probable useful life of plant and machinery, and the warranty claims that may occur. Such uncertainties are recognised by the disclosure of their nature and extent and by the exercise of prudence in the preparation of the financial statements”.

(8) Option (B): No, it can be dispensed with under certain circumstances as stipulated under the Companies Act, 2013

**Reasoning:** According to section 230(9) of the Companies Act, 2013, the Tribunal may dispense with calling of a meeting of creditor or class of creditors where such creditors or class of creditors, having at least ninety per cent value, agree and confirm, by way of
affidavit, to the scheme of compromise or arrangement. [Sub-section (9)]. So, the meeting of the creditors can be dispensed as per the requirement specified here in the section.

(9) Option (C) : The day on which the expenditure is incurred.

**Reasoning:** Accounting is done when either the expense is incurred or accrued. Accordingly the best appropriate answer should be option c.

(10) Option (D): Permissible with the sole approval of the Audit Committee

**Reasoning:** As per section 177(4) of the Companies Act, 2013, every Audit Committee shall act in accordance with the terms of reference specified in writing by the Board which shall, inter alia, include, approval or any subsequent modification of transactions of the company with related parties.

Provided that the Audit Committee may make omnibus approval for related party transactions proposed to be entered into by the company.

**Descriptive Answers: PART B**

**Answer (a)**

The risk factors to be considered are discussed in the following paragraphs.

Magnum is an entity that is doing extremely well. By merging it with another entity that is not doing well, the combined results may not be beneficial to the shareholders of Magnum. Hence, the need for such a merger from a standalone point of view needs a critical evaluation from the view point of magnum.

Merging an entity with a related party could have its own bias of arm's length valuation/protecting the interest of the minority shareholders.

Magnum is an established name in the market. A reverse merger could result in loss of name and renaming of the entity post the reverse merger may be considered effectively. Considering the outstanding loans to lenders and creditors, there could be an objection to the proposal by these parties.

Such loans could be either settled upfront or appropriately restructured to ensure that the creditors/lenders get the required comfort that the merged entity's ability to generate adequate funds for repayment is higher than that Yamuna can operate on its own.

Considering the above, the Scheme of Merger would need to be drafted carefully from all the above aspects and ensure that the concerns of any of these parties don't remain unaddressed.

**Alternative Answer**

The risk factors to be considered in the matter of merger of 'Magnum' with 'Yamuna' are discussed as below:

(i) A merger is a complicated process and a reverse merger can leave the shareholder with shares in an entity that is loss-making or debt burdened. As Yamuna already has huge debt and is loss making, this is a big risk which has to be seriously considered.
A reverse merger may put more pressure on the company’s accounting books, especially if the smaller firm is unlisted. In the present case, huge losses of Yamuna may make a serious dent in the profitability position of the company.

The additional investment of ₹1000 lakhs for the renovation of the plant of Yamuna may not bring the desired results as anticipated by the merged company. The reason is that the company may not get any substantial return on the investment made. Also, the financing aspect has to be thought off i.e. whether to finance the investment by debt or equity. Too much debt will increase the default risk of the company and too much equity will deprive the company of tax benefits and higher earnings per share to a certain extent. So a balancing act is required in this respect.

Then, there is credit risk as well as reputation risk if one time settlement with the bank doesn’t fructify well. The merged entity may struggle to make the required payment which may further damage the reputation of the company.

Lastly, there is legal risk as lawsuits for various reasons are very common during the reverse merger. Also, the company may fumble to meet the various compliance requirements relating to merger which further increases it’s compliance risk. So, there may not be any increase in value for the shareholders as promised during the reverse merger process.

**Answer (b)**

In ordinary cases, the company taken over is the smaller company; in a ‘reverse merger’, a smaller company gains control of a larger one. Reverse Merger is also known as ‘back door listing’. Thus, the ideal considerations for a reverse merger are explained as follows:

- **Easy access to capital market**: Magnum is a listed company and reverse merger is an easy route for Yamuna to get access to capital market.

- **Increase in visibility of the company in corporate world**: Again, Yamuna will get the required exposure of the corporate world by associating with a successful company like Magnum.

- **Cheaper and easier route to go for a public issue**: This kind of merger can be an alternative for Yamuna to go for public issue without incurring huge expenses and passing through cumbersome process.

**Further, the relevance of merger to Magnum has been explained as below:**

- Tax benefits on carry forward of losses of the acquired company - Magnum can **carry forward the losses and can thus, reduce its tax liability**.

- The reverse merger may create a positive impact on the competition in the market. Magnum may be **able to compete more efficiently after the merger.**
- It results in efficient use of available resources. Magnum can take advantage of the **specialization** which Yamuna got in manufacture of engineering products for vehicle manufacture.
- The reverse merger **adds value to the business** and enhances its future sustainability. After the merger, Magnum will be a bigger company having an additional expertise in manufacture of engineering products for vehicle manufacture.

**Alternative Answer**

Reverse merger typically is a case where a smaller company gains control over a larger one as against the ordinary mergers where the company taken over is a larger one. The key considerations for a reverse merger with the situation at Magnum are analyzed below:

<table>
<thead>
<tr>
<th>Considerations for Reverse Merger</th>
<th>Relevance to Magnum</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Involves a smaller company gaining control over a larger one.</td>
<td>Magnum is a listed entity and a larger one whereas Yamuna is an unlisted entity that is smaller. Magnum is proposed to be merged with Yamuna thereby resulting in a reverse merger situation.</td>
</tr>
</tbody>
</table>
| (2) A reverse merger typically has three tests to be fulfilled which are as below:  
  - The assets of the transferor company are greater than the transferee company.  
  - Equity capital to be issued by the transferee company pursuant to the acquisition exceeds the original issued capital.  
  - The change of control in the transferee company through the introduction of a minority holder or group of holders. | As can be noted, assets of Yamuna is much lesser compared to that of Magnum.  
Yes  
Yamuna’s shareholders prior to the reverse merger were 90% promoter group and 10% friends and relatives. Pursuant to the reverse merger, all shareholders in Magnum are now shareholders in Yamuna having minority shareholders including public shareholders and institutional investors. |
| (3) Reverse merger provides the following benefits to the acquiring company:  
  - Easy access to capital market.  
  - Increase in visibility of the company in the corporate world. | Yamuna was an unlisted entity earlier under financial stress. The reverse merger results in easier access to capital market for Yamuna.  
Yamuna was an entity wasn’t known in the market and this creates visibility.  
Yamuna has significant losses which can be utilized post-merger.  
Applicable in the case of Yamuna. |
Tax benefit on carry forward losses to the acquired company.
Cheaper and easier route to become a public company.

Answer (c)

(1) **Transfer of capital asset by Magnum Ltd. to Yamuna Ltd. at the time of merger**

“Amalgamation”, in relation to companies, under Income-tax Act, 1961 means the merger of one or more companies with another company or the merger of two or more companies to form one company (the company or companies which so merge being referred to as the amalgamating company or companies and the company with which they merge or which is formed as a result of the merger, as the amalgamated company) in such a manner that -

(i) all the property of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of the amalgamation;

(ii) all the liabilities of the amalgamating company or companies immediately before the amalgamation become the liabilities of the amalgamated company by virtue of the amalgamation;

(iii) shareholders holding not less than three-fourth in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by, or by a nominee for, the amalgamated company or its subsidiary) become shareholders of the amalgamated company by virtue of the amalgamation, otherwise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first mentioned company.

If Magnum Ltd. merges into Yamuna Ltd. by satisfying all the above conditions, any transfer of a capital asset by the Magnum Ltd., the amalgamating company to Yamuna Ltd., the amalgamated company, being an Indian company, would not be regarded as transfer as per section 47. From the information given in the question, the promoters holding 61% of shares of Magnum Ltd. would become shareholders of the amalgamated company. If out of the remaining shareholders of Magnum Ltd., shareholders holding at least 14% of shares opt to become shareholders of Yamuna Ltd., then, the third condition would be fulfilled. Assuming that conditions (i) and (ii) are also fulfilled in this case, the transfer of capital asset would not be subject to capital gains tax.

(2) **Transfer of shares held by the shareholders of Magnum Ltd.**

Transfer of shares held by the shareholders in Magnum Ltd. in consideration of the allotment to them of any share in Yamuna Ltd., an Indian company, would not be regarded as transfer as per section 47, if the amalgamation fulfills all the above conditions.
(3) **Carry forward and set-off of losses of Yamuna Ltd. post-merger:**

As per section 72A, accumulated losses and unabsorbed depreciation of the amalgamating company would be deemed to be the loss or depreciation, as the case may be, of the amalgamated company for the previous year in which the amalgamation took place. However, in the present case, since, amalgamating company i.e., Magnum Ltd. is a profit making company, section 72A would not be relevant in this case.

As per section 79, in the case of a company in which the public are not substantially interested, no loss incurred in any year prior to the previous year shall be carried forward and set-off against the income of the previous year, unless on the last day of the previous year, the shares of the company carrying not less than 51% of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less than 51% of the voting power on the last day of the year or years in which the loss was incurred.

In the present case, since Yamuna Ltd. is a company in which public are not substantially interested, it would not be allowed to set-off its brought forward losses, if on the last day of the previous year 2017-18, the shares of the company carrying not less than 51% of the voting power were not beneficially held by persons, who beneficially held shares of the company carrying not less than 51% of the voting power on the last day of the year or years in which the loss was incurred.

However, it would be allowed to set-off its brought forward losses, if on the last day of the previous year 2017-18, the shares of the company carrying not less than 51% of the voting power were beneficially held by persons, who beneficially held shares of the company carrying not less than 51% of the voting power on the last day of the year or years in which the loss was incurred.

This condition, however, does not apply in respect of set-off of unabsorbed depreciation.

(4) **Treatment of Depreciation on reverse merger:** Depreciation @25% of the value of goodwill would be allowed to Yamuna Ltd. considering it as intangible asset.

In case of amalgamation, the depreciation would be first computed as if the amalgamation has not taken place and thereafter, it has to be bifurcated between the amalgamating company, i.e., Magnum Ltd. and the amalgamated company i.e., Yamuna Ltd. in the ratio of the number of days for which the assets were used by them.

**Answer (d)**

As per the provisions given in section 230 (3), (4) & (5) of the Companies Act, 2013, where a meeting is proposed to be called in pursuance of an order of the Tribunal under section 230 (1), a **notice of such meeting shall be sent to the following:**

- all the creditors or class of creditors, and
- to all the members or class of members and
- the debenture-holders of the company,
individually at the address registered with the company accompanied with relevant documents as prescribed in section 230(4).

Provided that such notice and other documents shall also be placed on the website of the company, if any, and in case of a listed company, these documents shall be sent to the Securities and Exchange Board and stock exchange where the securities of the company are listed, for placing on their website and shall also be published in newspapers in such manner as prescribed under Rule 8 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

Provided further that where the notice for the meeting is also issued by way of an advertisement, it shall indicate the time within which copies of the compromise or arrangement shall be made available to the concerned persons free of charge from the registered office of the company.

The persons to whom the notice is sent as per the above provision, they are entitled to vote in the meeting to the adoption of the compromise or arrangement within one month from the date of receipt of such notice. Provided that any objection to the compromise or arrangement shall be made in compliance to the provision.

A notice shall also be sent to the-

- Central Government,
- the income-tax authorities,
- the Reserve Bank of India,
- the Securities and Exchange Board,
- the Registrar,
- the respective stock exchanges,
- the Official Liquidator,
- the Competition Commission of India under the Competition Act, 2002, if necessary, and
- such other sectoral regulators or authorities which are likely to be affected by the compromise or arrangement, and

shall require that representations, if any, to be made by them shall be made within a period of thirty days from the date of receipt of such notice, failing which, it shall be presumed that they have no representations to make on the proposals.

Answer (e)

As per section 230(7) of the Companies Act, 2013, the other options available instead of reverse merger option vide an order made by the Tribunal shall provide for all or any of the following matters, namely:—
(a) where the compromise or arrangement provides for conversion of preference shares into equity shares, such preference shareholders shall be given an option to either obtain arrears of dividend in cash or accept equity shares equal to the value of the dividend payable;

(b) the protection of any class of creditors;

(c) if the compromise or arrangement results in the variation of the shareholders’ rights, it shall be given effect to under the provisions of section 48;

(d) if the compromise or arrangement is agreed to by the creditors under section 230(6), any proceedings pending before the Board for Industrial and Financial Reconstruction (BIFR) established under section 4 of the Sick Industrial Companies (Special Provisions) Act, 1985 shall abate;

(e) such other matters including exit offer to dissenting shareholders, if any, as are in the opinion of the Tribunal necessary to effectively implement the terms of the compromise or arrangement.

Provided that no compromise or arrangement shall be sanctioned by the Tribunal unless a certificate by the company’s auditor has been filed with the Tribunal to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under section 133.

Yasin Malik has put forward a proposal to merge 'Magnum' with an unlisted entity 'Yamuna' Fitting Works Limited, ("Yamuna") through an approved restructuring route considering certain business reasons. He has requested the Chief Financial Officer to explain the financial and other details of 'Yamuna' to kick start the discussions further. He has also preferred to go for a capital reduction of ‘Yamuna’, if permissible under the law along with the Scheme.

**Information Provided by Anirudh, CFO**

‘Yamuna’ which is an entity promoted by the Maliks, is specializing in the manufacture of engineering products for vehicle manufacture. It was incorporated in 2010 and its plant is located at Pune. Due to various external conditions, ‘Yamuna’ is not doing well and has recorded huge losses accumulated year on year. Details of shareholding pattern of 'Yamuna' as at 31\textsuperscript{st} March, 2015 is as under:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>No. of Shares</th>
<th>Amount in ₹ Lakhs</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Promoters (same Shareholders as that of ‘Magnum’)</td>
<td>90,000</td>
<td>90</td>
<td>90%</td>
</tr>
<tr>
<td>Friend and Relatives</td>
<td>10,000</td>
<td>10</td>
<td>10%</td>
</tr>
<tr>
<td>Total</td>
<td>100,000</td>
<td>100</td>
<td>100%</td>
</tr>
</tbody>
</table>