Skillshort

Self-Study Preparation Pack

CS EXECUTIVE

Paper 4: Corporate Accounting and Financial Management (CAFM)

Mock Test 2 – Full Paper with Model Answers

ICSI Syllabus 2022 pattern: 100 marks · 3 hours (+15 minutes' reading) · Part I Corporate Accounting (60 marks) Q1–Q4 · Part II Financial Management (40 marks) Q5–Q6 · all questions compulsory · internal choice in Q4/Q4A and Q6/Q6A · Original Skillshort questions, all figures verified in Python

Time: 3 hours | Max marks: 100 | Answer ALL questions | Show working notes | Model answers follow the paper

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This subject pack has 6 parts

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Prepared by Skillshort for self-study. Original explanations and questions; not an official ICSI publication. Items marked VERIFY should be checked against the latest official material.

Question Paper

Answer ALL questions. Show working notes. Assume tax at 25% where not given.

Part I – Corporate Accounting (60 marks)

Q1 Case study. Zenith Engineering Ltd.'s balance sheets (₹ lakh):

Particulars	31-3-2025	31-3-2026
Equity share capital (₹10 shares)	400	500
General reserve	100	130
Surplus in profit and loss	60	110
10% debentures	200	150
Trade payables	90	110
Provision for tax	40	50
Total	**890**	**1,050**
Fixed assets (net)	500	620
Non-current investments	80	60
Inventory	120	150
Trade receivables	140	170
Cash and bank	50	50
Total	**890**	**1,050**

Additional information for 2025-26: depreciation ₹60 lakh; a machine with book value ₹30 lakh was sold for ₹25 lakh; investments costing ₹20 lakh were sold for ₹26 lakh; tax provided ₹55 lakh; dividend paid ₹40 lakh; debentures of ₹50 lakh were redeemed at par on 1 April 2025 and interest was paid on the balance; new shares were issued at par for cash.

(i) Compute net profit before tax for 2025-26 (working notes for profit, tax paid and fixed assets purchased). **(3 marks)**

(ii) Compute net cash from operating activities (indirect method). **(3 marks)**

(iii) Compute net cash from investing activities. **(3 marks)**

(iv) Compute net cash from financing activities and reconcile with the cash balance. **(3 marks)**

(v) How are interest and dividends paid and received classified by a non-financial company under AS 3? **(3 marks)**

Q2 (a) Tara Ltd. issued 50,000 equity shares of ₹10 at a premium of ₹5: ₹3 on application, ₹7 on allotment (including premium), ₹5 on call. Applications were received for 80,000 shares: applications for 10,000 shares were rejected and refunded; the rest were allotted pro rata, and excess application money was adjusted towards allotment. Compute the amount due and receivable on allotment and pass the entries up to receipt of allotment money (all paid). **(5 marks)**

(b) Sonal Ltd. redeemed 20,000 10% preference shares of ₹100 each at a premium of 10%. For this, it issued 1,00,000 equity shares of ₹10 each at par. It has securities premium ₹3,00,000 and general reserve ₹15,00,000. Pass journal entries for redemption. **(5 marks)**

(c) Divya Ltd. took over assets of ₹4,50,000 and liabilities of ₹60,000 of Neel Ltd. for ₹4,40,000, paid ₹80,000 in cash and the balance by issue of equity shares of ₹10 each at ₹12. Pass journal entries in Divya Ltd.'s books. **(5 marks)**

Q3 (a) On 1 April 2025 Ravi Ltd. issued 5,000 9% debentures of ₹1,000 each at a discount of 5%, redeemable at a premium of 10% after 5 years. Pass entries for the issue and compute the amount of loss on issue to be written off each year. **(5 marks)**

(b) H Ltd. bought 80% of S Ltd. for ₹4,00,000 when S Ltd. had share capital ₹3,00,000 and reserves ₹50,000. Since then S Ltd. has earned profit of ₹1,00,000. H Ltd. sold goods to S Ltd. at cost plus 25%; goods of ₹50,000 (at

invoice price) are in S Ltd.'s closing inventory. H Ltd.'s trade receivables include ₹30,000 due from S Ltd. Compute goodwill, NCI and the adjustments for unrealised profit and mutual owings. **(5 marks)**

(c) Prepare a summarised balance sheet from: sales ₹36 lakh (all credit); gross profit 20% of sales; inventory turnover (on cost of goods sold) 8 times; average collection period 1 month; current ratio 2.5; quick ratio 1.5; fixed-asset turnover (on sales) 3 times; net worth ₹15 lakh; the balance is long-term debt. **(5 marks)**

Q4 Answer the following (3 marks each):

(i) What do AS 2 and Ind AS 2 exclude from the cost of inventories?

(ii) Profit after tax ₹60 lakh; 20 lakh equity shares; 1,00,000 8% convertible debentures of ₹100, each convertible into 5 equity shares. Compute basic and diluted EPS.

(iii) What is firm underwriting, and how does it affect an underwriter's liability?

(iv) How are bonus shares issued when the company has partly paid shares?

(v) State the role of the escrow account in a buy-back through the open-market or tender-offer route.

OR Q4A Answer the following (3 marks each):

(i) Distinguish the research phase and the development phase under AS 26.

(ii) State three key differences between AS and Ind AS.

(iii) State the conditions for issue of sweat equity shares under s.54.

(iv) What interest can a company charge on calls in arrears and pay on calls in advance under Table F?

(v) Distinguish financial forecasting and budgeting.

Part II – Financial Management (40 marks)

Q5 Case study. Orion Electricals Ltd. has 10 lakh equity shares of ₹10 each and no debt. It needs ₹50 lakh for expansion, after which EBIT is expected to be ₹40 lakh. Options: **Plan A** – equity shares at ₹25 each; **Plan B** – 12% debentures; **Plan C** – 10% preference shares. Tax 25%.

(i) Compute EPS under each plan. **(5 marks)**

(ii) Compute the EBIT at which Plans A and B give the same EPS, and verify. **(5 marks)**

(iii) Compute the financial break-even point and the degree of financial leverage under each plan. **(5 marks)**

(iv) Advise the company, considering risk and the indifference points. **(5 marks)**

Q6 (a) A company has 5 lakh shares at ₹100; cost of equity 12%; expected dividend ₹6 a share; net income ₹40 lakh; new investment ₹60 lakh. Using the MM model, compute the price at year end and the new shares to be issued if (i) the dividend is paid, (ii) it is not paid; show that the value of the firm is the same. **(5 marks)**

(b) Sales ₹8 lakh give a profit of ₹80,000; sales ₹10 lakh give a profit of ₹1,40,000. Compute P/V ratio, fixed cost, BEP, sales for a profit of ₹2,00,000 and margin of safety at ₹10 lakh. **(5 marks)**

(c) Prepare a cash budget for March–May: opening cash ₹25,000; sales (₹'000) Jan 80, Feb 90, Mar 100, Apr 120, May 110 – 50% collected in the month of sale and 50% the next month; purchases 60% of sales, paid the next month; wages ₹15,000 and rent ₹5,000 a month; advance tax ₹20,000 in April; machine ₹40,000 in May. The bank requires a minimum balance of ₹40,000. **(5 marks)**

(d) Distinguish fundamental analysis and technical analysis. **(5 marks)**

OR Q6A (a) Raw-material storage 30 days, WIP 15 days, finished goods 20 days, debtors 45 days, creditors 30 days; annual cost of sales ₹73 lakh. Compute the operating cycle and working capital. **(5 marks)**

(b) Capital budget ₹10 lakh. Projects (outlay, NPV in ₹ lakh): A (4, 1.2), B (5, 1.0), C (3, 0.9), D (6, 1.5). Select projects if they are (i) divisible, (ii) indivisible. **(5 marks)**

(c) Risk-free rate 6.5%, market return 12%. Share X: beta 0.8, expected return 11%; share Y: beta 1.5, expected return 14%. Using CAPM, state whether each share is under- or over-valued. **(5 marks)**

(d) Explain the risk-adjusted discount rate and the certainty-equivalent method. **(5 marks)**

Model Answers

SOLUTION **Q1 Zenith Engineering Ltd. (₹ lakh)**

(i) Working notes

Profit after tax = increase in surplus 50 + transfer to general reserve 30 + dividend paid 40 = 120

Net profit before tax = 120 + tax provided 55 = **175**

Tax paid = 40 + 55 − 50 = **45**

Fixed assets purchased = 620 − (500 − 60 − 30) = **210**

Debenture interest = 10% × 150 = **15** (redeemed on 1 April 2025).

(ii) Operating activities

Particulars	₹ lakh
Net profit before tax	175
Add depreciation	60
Add loss on sale of machine (30 − 25)	5
Less profit on sale of investments (26 − 20)	(6)
Add interest on debentures	15
Operating profit before working-capital changes	249
Increase in inventory	(30)
Increase in trade receivables	(30)
Increase in trade payables	20
Cash generated from operations	209
Less income tax paid	(45)
Net cash from operating activities	**164**

(iii) Investing activities: purchase of fixed assets (210) + sale of machine 25 + sale of investments 26 = **(159)**

(iv) Financing activities: issue of shares 100 − redemption of debentures (50) − interest (15) − dividend (40) = **(5)**

Net change in cash = 164 − 159 − 5 = **0** → opening cash 50 = closing cash 50 ✓

(v) For a **non-financial company** (AS 3): interest and dividends **paid** are **financing** activities; interest and dividends **received** are **investing** activities. For a financial enterprise, interest paid and interest and dividends received are operating. Taxes are operating unless specifically identified with investing or financing.

SOLUTION Q2 (a) Pro-rata allotment

- Application money received 80,000 × 3 = **₹2,40,000**; refund 10,000 × 3 = **₹30,000**.
- Excess from pro-rata applicants: 70,000 × 3 − 50,000 × 3 = **₹60,000** – adjusted on allotment.

Due on allotment = 50,000 × 7 = **₹3,50,000** (capital ₹2,00,000 + premium ₹2,50,000)

Receivable in cash = 3,50,000 − 60,000 = **₹2,90,000**

Particulars	Dr ₹	Cr ₹
Bank A/c Dr	2,40,000	
To Share application A/c		2,40,000
Share application A/c Dr	2,40,000	
To Share capital A/c (50,000 × 3)		1,50,000
To Share allotment A/c (excess)		60,000
To Bank A/c (refund)		30,000
Share allotment A/c Dr	3,50,000	
To Share capital A/c (50,000 × 2)		1,00,000
To Securities premium A/c (50,000 × 5)		2,50,000
Bank A/c Dr	2,90,000	
To Share allotment A/c		2,90,000

SOLUTION Q2 (b) Redemption of preference shares

Amount payable = 20,000 × ₹110 = **₹22,00,000** (premium ₹2,00,000)

CRR (s.55) = nominal value redeemed 20,00,000 − proceeds of fresh issue 10,00,000 = **₹10,00,000**

Particulars	Dr ₹	Cr ₹
Bank A/c Dr	10,00,000	
To Equity share capital A/c		10,00,000
10% Preference share capital A/c Dr	20,00,000	
Premium on redemption A/c Dr	2,00,000	
To Preference shareholders A/c		22,00,000
Securities premium A/c Dr	2,00,000	
To Premium on redemption A/c		2,00,000
General reserve A/c Dr	10,00,000	
To Capital redemption reserve A/c		10,00,000
Preference shareholders A/c Dr	22,00,000	
To Bank A/c		22,00,000

SOLUTION Q2 (c) Purchase of business

Net assets = 4,50,000 − 60,000 = 3,90,000 → goodwill = 4,40,000 − 3,90,000 = **₹50,000**

Shares issued = (4,40,000 − 80,000) ÷ 12 = **30,000 shares** → capital ₹3,00,000; premium ₹60,000

Particulars	Dr ₹	Cr ₹
Sundry assets A/c Dr	4,50,000	
Goodwill A/c Dr	50,000	
To Sundry liabilities A/c		60,000
To Neel Ltd. (vendor) A/c		4,40,000
Neel Ltd. A/c Dr	4,40,000	
To Bank A/c		80,000
To Equity share capital A/c		3,00,000
To Securities premium A/c		60,000

SOLUTION Q3 (a) Debentures at discount, redeemable at premium

Particulars	Dr ₹	Cr ₹
Bank A/c (5,000 × 950) Dr	47,50,000	
Loss on issue of debentures A/c Dr	7,50,000	
To 9% Debentures A/c		50,00,000
To Premium on redemption of debentures A/c		5,00,000

Loss on issue = discount 2,50,000 + premium on redemption 5,00,000 = **₹7,50,000**

As the debentures are redeemed in one lot after 5 years, write off **₹1,50,000 a year** (first from securities premium, if any, then profit and loss). Premium on redemption is shown under non-current liabilities until paid.

SOLUTION Q3 (b) Consolidation

Goodwill = 4,00,000 − 80% × (3,00,000 + 50,000) = 4,00,000 − 2,80,000 = **₹1,20,000**

Post-acquisition profit to group = 80% × 1,00,000 = **₹80,000**

NCI = 20% × (3,00,000 + 50,000 + 1,00,000) = **₹90,000**

Unrealised profit = 50,000 × 25 ÷ 125 = **₹10,000** – deduct from consolidated inventory and from consolidated profit (downstream sale by H, so all borne by the group)

Mutual owings: cancel ₹30,000 from consolidated trade receivables and trade payables.

SOLUTION Q3 (c) Balance sheet from ratios (₹ lakh)

Cost of goods sold = 36 × 80% = 28.8 → inventory = 28.8 ÷ 8 = **3.6**

Receivables = 36 × 1/12 = **3.0**

Current liabilities = current ratio − quick ratio = 2.5 − 1.5 = 1.0 × CL = inventory 3.6 → CL = **3.6**; current assets = 2.5 × 3.6 = **9.0**

Cash = 9.0 − 3.6 − 3.0 = **2.4**; fixed assets = 36 ÷ 3 = **12.0**

Liabilities	₹ lakh	Assets	₹ lakh
Net worth	15.0	Fixed assets	12.0
Long-term debt (balancing)	2.4	Inventory	3.6
Current liabilities	3.6	Receivables	3.0
		Cash	2.4
Total	**21.0**	**Total**	**21.0**

SOLUTION Q4

(i) Excluded from cost (expensed): **abnormal** wastage of materials, labour or other costs; **storage** costs (unless needed in production before a further stage); **administrative overheads** not related to bringing inventory to its present location and condition; **selling and distribution** costs. Under AS 2, **interest** is generally excluded, but Ind AS 2 allows borrowing costs for qualifying inventories under Ind AS 23.

(ii)

Basic EPS = 60 ÷ 20 = **₹3.00**

Diluted EPS = (60 + 8 × 0.75) ÷ (20 + 5) = 66 ÷ 25 = **₹2.64**

Interest saved after tax = ₹8 lakh × 75% = ₹6 lakh; potential shares = 1,00,000 × 5 = 5 lakh. The debentures are dilutive (₹2.64 < ₹3.00).

(iii) In **firm underwriting** the underwriter agrees to take up a stated number of shares **in any case**, whether or not the public subscribes. Unless the question says otherwise, firm applications are **treated like marked applications** – they reduce the underwriter's gross liability. The underwriter must then take its firm shares **plus** any net shortfall computed after this credit VERIFY. Commission is payable on the whole amount underwritten, including the firm portion.

(iv) First make the partly paid shares **fully paid** by making a **final call** out of capitalised profits (via a bonus to existing members: Bonus to shareholders A/c Dr; To Share final call A/c), or capitalise only on fully paid shares as allowed. Under s.63(3), **partly paid shares must be made fully paid** before bonus is issued. Then issue fully paid bonus shares from free reserves / securities premium / CRR, with the resolution and articles' authority.

(v) Under the SEBI (Buy-back of Securities) Regulations, 2018, a company making a tender offer or open-market buy-back opens an **escrow account** (cash, bank guarantee or approved securities) of at least **25% of consideration up to ₹100 crore + 10% of the excess** for tender offers (open market: **25%** of the amount earmarked). It assures payment to shareholders; on default the merchant banker can forfeit the escrow VERIFY.

SOLUTION Q4A

(i) Research phase: original investigation to gain new knowledge – no intangible asset is recognised; all expenditure is **expensed**. **Development phase:** application of research to a plan or design before commercial production – an intangible asset is **recognised** only if the six criteria are shown (technical feasibility, intention, ability to use or sell, probable future benefits, adequate resources, reliable measurement).

(ii) (1) **Fair value** is used widely in Ind AS; AS is largely historical cost. (2) Ind AS has **Other Comprehensive Income** and a full Statement of Changes in Equity; AS does not. (3) Ind AS requires **substance over form** for financial instruments (e.g. redeemable preference shares as liabilities); proposed dividends are not provided in either. Ind AS is converged with IFRS, AS is not.

(iii) Sweat equity (s.54): issued to **directors or employees** for know-how or value additions; authorised by a **special resolution**; issued to a class of shares already issued (the one-year waiting period was removed by the 2017 amendment); for listed companies, under SEBI SBEB and Sweat Equity Regulations; valued by a **registered valuer**; locked in for **3 years** (unlisted companies); limit 15% of paid-up capital in a year or ₹5 crore, whichever is higher, and 25% overall.

(iv) Table F: interest on **calls in arrears** up to **10% p.a.** from the due date to the date of payment (the Board may waive) VERIFY; interest on **calls in advance** up to **12% p.a.**; calls in advance carry no voting or dividend rights until called.

(v) Forecasting estimates future financial outcomes (sales, assets, funds needed) from assumptions – it is a planning tool and not binding. **Budgeting** turns the forecast into an approved, quantified plan with targets and responsibilities, used for **control** (variance analysis). Forecasting comes first; a budget is a commitment.

SOLUTION Q5 Orion Electricals Ltd. (₹ lakh)

(i)

Particulars	Plan A (equity)	Plan B (12% debt)	Plan C (10% pref.)
EBIT	40.00	40.00	40.00
Interest	–	6.00	–
EBT	40.00	34.00	40.00
Tax 25%	10.00	8.50	10.00
PAT	30.00	25.50	30.00
Preference dividend	–	–	5.00
Earnings for equity	30.00	25.50	25.00
Shares (lakh)	12 (10 + 50/25)	10	10
EPS (₹)	**2.50**	**2.55**	**2.50**

(ii)

Indifference A vs B = EBIT × 0.75 ÷ 12 = (EBIT − 6) × 0.75 ÷ 10

Solving = 10 EBIT = 12 EBIT − 72 → **EBIT = ₹36 lakh**

Verify: A = 36 × 0.75 ÷ 12 = ₹2.25; B = 30 × 0.75 ÷ 10 = ₹2.25 ✓. (A vs C: 7.5 EBIT = 9 EBIT − 60 → ₹40 lakh, which is why A and C give the same EPS now.)

(iii)

Financial BEP = A: 0; B: interest **₹6 lakh**; C: 5 ÷ (1 − 0.25) = **₹6.67 lakh**

DFL = A: **1.00**; B: 40 ÷ 34 = **1.18**; C: 40 ÷ (40 − 6.67) = **1.20**

(iv) Expected EBIT ₹40 lakh is above the A–B indifference point (₹36 lakh), so **debt (Plan B) gives the highest EPS** (₹2.55). Interest cover = 40 ÷ 6 = 6.7 times – comfortable. Plan C has the highest DFL with no EPS gain, because preference dividend is not tax-deductible. **Advice: Plan B**, provided EBIT is unlikely to fall below ₹36 lakh; if EBIT is uncertain, equity (Plan A) is safer.

SOLUTION Q6 (a) MM dividend irrelevance

P1 = P0(1 + ke) − D1 → with dividend 100 × 1.12 − 6 = **₹106**; without dividend **₹112**

New shares (with dividend) = [60 − (40 − 30)] lakh ÷ 106 = 50,00,000 ÷ 106 = **47,170 shares**

New shares (no dividend) = (60 − 40) lakh ÷ 112 = **17,857 shares**

Value check = [(n + Δn)P1 − I + E] ÷ (1 + ke) = **₹500 lakh** in both cases (5 lakh × ₹100)

The value of the firm is unaffected by dividend policy under MM assumptions.

SOLUTION Q6 (b) CVP

P/V ratio = change in profit 60,000 ÷ change in sales 2,00,000 = **30%**

Fixed cost = 8,00,000 × 30% − 80,000 = **₹1,60,000**

BEP = 1,60,000 ÷ 30% = **₹5,33,333**

Sales for ₹2,00,000 profit = 3,60,000 ÷ 30% = **₹12,00,000**

Margin of safety = 10,00,000 − 5,33,333 = **₹4,66,667** (46.7%)

SOLUTION Q6 (c) Cash budget (₹'000)

Particulars	March	April	May
Opening balance	25	46	56
Collections (50% current + 50% previous)	95	110	115
Purchases paid (60% of last month's sales)	(54)	(60)	(72)
Wages and rent	(20)	(20)	(20)
Advance tax / machine	–	(20)	(40)
Closing balance	**46**	**56**	**39**

Against the minimum of ₹40,000, an **overdraft of ₹1,000** is needed in May; March and April have surpluses.

SOLUTION Q6 (d) Fundamental vs technical analysis

Basis	Fundamental	Technical
Focus	Intrinsic value – economy, industry, company (EIC)	Price and volume patterns
Tools	Financial statements, ratios, DCF, management quality	Charts, moving averages, RSI, Dow theory
Horizon	Long-term investing	Short-term trading and timing
Assumption	Price moves to intrinsic value	History repeats; trends persist

SOLUTION **Q6A**

(a)

Operating cycle = 30 + 15 + 20 + 45 − 30 = **80 days**

Working capital = 73 lakh ÷ 365 × 80 = **₹16 lakh**

(b) PI = (outlay + NPV) ÷ outlay: A 1.30, B 1.20, C 1.30, D 1.25.

- **Divisible:** rank by PI – A (4) + C (3) + half of D (3) → NPV = 1.2 + 0.9 + 0.75 = **₹2.85 lakh**.
- **Indivisible:** test combinations within ₹10 lakh – A + D (10) gives NPV **₹2.7 lakh**, the highest (A + C 2.1; C + D 2.4; A + B 2.2). Select **A and D**.

(c)

Required return X = 6.5 + 0.8 × (12 − 6.5) = **10.9%** < expected 11% → **under-valued: buy**

Required return Y = 6.5 + 1.5 × 5.5 = **14.75%** > expected 14% → **over-valued: sell**

(d) RADR: add a risk premium to the risk-free rate for riskier projects and discount expected cash flows at that higher rate – simple, but assumes risk grows with time. **Certainty equivalent:** convert each risky cash flow into its certain equivalent (cash flow × coefficient α between 0 and 1) and discount at the **risk-free rate** – adjusts for risk year by year, but α is subjective.