CA FINAL

FINANCIAL REPORTING

COMPILER

RAHUL MALKAN

VERSION 3.0

: KEY FEATURES :

- Covers RTP and Past Papers
- Chapter wise
- Along with Solutions
- All Chapters Covered

INDEX

INTRODUCTION TO ACCOUNTING STANDARDS (AS) & INDIAN ACCOUNTING STANDARD (IND AS)

CHAPTER - 1

Question 1 : May 2022 – RTP

Fresh Vegetables Limited (FVL) was incorporated on 2nd April, 20X1 under the provisions of the Companies Act, 2013 to carry on the wholesale trading business in vegetables. As per the audited accounts of the financial year ended 31st March, 20X7 approved in its annual general meeting held on 31st August, 20X7 its net worth, for the first time since incorporation, exceeded Rs. 250 crore. The financial statements since inception till financial year ended 31st March, 20X6 were prepared in accordance with the Companies (Accounting Standards) Rules 2006. It has been advised that henceforth it should prepare its financial statements in accordance with the Companies (Indian Accounting Standards) Rules, 2015.

The following additional information is provided by the Company:

- FVL has in the financial year 20X2-20X3 entered into a 60:40 partnership with Logistics Limited and incorporated a partnership firm 'Vegetable Logistics Associates' (VLA) to carry on the logistics business of vegetables from farm to market.
- FVL also has an associate company Social Welfare Limited (SWL) that was incorporated in July, 20X5 as a charitable organization and registered under section 8 of the Companies Act, 2013. Social Welfare Limited has been the associate company of FVL since its incorporation.

Examine the applicability of Ind AS on VLA & SWL.

Solution :

Applicability of Ind AS in general:

- Currently Ind AS is applicable to the following companies except for companies other than banks and Insurance Companies, on mandatory basis:
  - (a) All companies which are listed or in process of listing in or outside India on Stock Exchanges.
  - (b) Unlisted companies having net worth of Rs. 250 crore or more but less than Rs. 500 crore.
  - (c) Holding, Subsidiary, Associate and Joint venture of above.
- Companies listed on SME exchange are not required to apply Ind AS on mandatory basis.
- Once a company starts following Ind AS either voluntarily or mandatorily on the basis of criteria specified, it shall be required to follow Ind AS for all the subsequent financial statements even if any of the criteria specified does not subsequently apply to it.

- Application of Ind AS is for both standalone as well as consolidated financial statements if threshold criteria met or adopted voluntarily.
- Companies meeting the thresholds for the first time at the end of an accounting year shall apply Ind AS from the immediate next accounting year with comparatives.
- Companies not covered by the above roadmap shall continue to apply existing Accounting Standards notified in the Companies (Accounting Standards) Rules, 2006.

Since the net worth of FVL in immediately preceding year exceeded Rs. 250 crore, Ind AS is applicable to it. The entity VLA and SWL have to be examined as they may fall in criteria (c) above.

Applicability of Ind AS on VLA

Joint arrangement can be either joint operation or joint venture. However, for the purpose of identifying the applicability of Ind AS, the Act defines Joint venture (as an explanation to section 2(6) of the Companies Act, 2013), as follows:

"The expression "joint venture" means a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement".

Accordingly, if an entity is classified as joint operation and not joint venture, then Ind AS would not be applicable to such entity.

In the case of VLA, if partners conclude that they have rights in the assets and obligations for the liabilities relating to the partnership firm then this would be a joint operation. However, Ind AS would not be applicable on VLA in such a case since it is the case of joint operation (and not a joint venture).

Alternatively, if partners conclude that they have joint control of the arrangement and have rights to the net assets of the arrangement relating to the partnership firm, then this would be a joint venture. In such a case, Ind AS would be applicable to them.

Applicability of Ind AS on SWL

Social Welfare Limited (SWL) is the associate company of FVL. Accordingly, Ind AS would be applicable on SWL too irrespective of the fact that SWL has been incorporated as a charitable organisation.

Thanks ….

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IND AS – 1 PRESENTATION OF FINACIAL STATEMENTS

CHAPTER - 2

Question 1 : May 2018 – RTP

Company A has taken a long term loan arrangement from Company B. In the month of December 20X1, there has been a breach of material provision of the arrangement. As a consequence of which the loan becomes payable on demand on March 31, 20X2. In the month of May 20X2, the Company started negotiation with the Company B for not to demand payment as a consequence of the breach. The financial statements were approved for the issue in the month of June 20X2. In the month of July 20X2, both company agreed that the payment will not be demanded immediately as a consequence of breach of material provision.
Advise on the classification of the liability as current / non –current.

Solution :

As per para AS 1 "Presentation of Financial Statements" where there is a breach of a material provision of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand on the reporting date, the entity does not classify the liability as current, if the lender agreed, after the reporting period and before the approval of the financial statements for issue, not to demand payment as a consequence of the breach.
In the given case, Company B (the lender) agreed for not to demand payment but only after the financial statements were approved for issuance. The financial statements were approved for issuance in the month of June 20X2 and both companies agreed for not to demand payment in the month of July 20X2 although negotiation started in the month of May 20x2 but could not agree before June 20X2 when financial statements were approved for issuance.
Hence, the liability should be classified as current in the financial statement for the year ended March 31, 20X2.

Question 2 : May 2018 – RTP

A Ltd. is an entity who prepares its financial statements based on Accounting Standards.
Following is the draft financial statement for the year ended on 31st March, 20X1:

(Note all figures are Rs.in million)

Balance Sheet

Particulars	Note	As at March 31, 20X1
EQUITY AND LIABILITIES		
Shareholders' funds		
Share capital (shares of Rs.10 each)		2,000

Reserves and surplus	1	4,000
Non-current liabilities		
Long-term borrowings	2	11,110
Deferred tax liabilities	3	400
Current liabilities		
Trade payables		600
Short-term provisions		500
Other current liabilities	4	300
TOTAL		**18,910**
ASSETS		
Non - Current assets		
Fixed Assets		11,310
Deferred Tax Assets	3	1,000
Current assets		
Inventories		2,000
Trade receivables	5	2,200
Cash and bank balances		2,400
TOTAL		**18,910**

Note 1: The Company has achieved a major breakthrough in its consultancy services in South Asia following which it has entered into a contract of rendering services with Floral Inc. for Rs.12 Billion during the year. The termination clause of the contract is equivalent to Rs.14 Million and is payable in case transition time schedule is missed from 15th December 20X5. The management however is of the view that the liability cannot be treated as onerous.

Note 2 : The Company is not able to assess the final liability for a particular tax assessment pertaining to the assessment year 20X1-20X2 wherein it has received a demand notice of Rs.12 Million. However, the company is contesting the same with CIT (Appeals) as on the reporting date.

Statement of Profit & Loss

Particulars	**Note**	**Year ended March 31, 20X1**
Revenue from operations		11,000
Expenses		
Employee Benefit Expense		2,400
Operating Costs		4,400
Depreciation		1,998
Total Expenses		8,798
Profit before tax		2,202
Tax Expense		(300)
Profit after tax		1,902

Notes to Accounts:

Note 1 : Reserves and Surplus **(INR in millions)**

Capital Reserve		1,000
Surplus from P & L		
Opening Balance	98	
Additions	1,902	2,000
Reserve for foreseeable loss		1,000
Total		**4,000**

Note 2 : Long Term Borrowings

Term Loan from Bank	11,110
Total	11,110

Note 3 : Deferred Tax

Deferred Tax Asset	1,000
Deferred Tax Liability	(400)
Total	600

Note 4 : Other Current Liabilities

Unclaimed dividends	6
Billing in Advance	294
Total	300

Note 5 : Trade Receivables

Considered good (outstanding within 6 months)	2,130
Considered doubtful (due from past 1 year)	80
Provision for doubtful debts	(10)
Total	2,200

Additional Information:

(a) Share capital comprises of 200 million shares of Rs.10 each

(b) Term Loan from bank for Rs.11,110 million also includes interest accrued and due of Rs.1,110 million as on the reporting date.

(c) Reserve for foreseeable loss is created against a service contract due within 6 months.

Required :

(i) Evaluate and report the errors and misstatements in the above extracts; and,

(ii) Prepare the corrected Balance Sheet & Statement of Profit and Loss.

Solution :

(a) On evaluation of the financial statements, following was observed:

1. For foreseeable loss provision is made and not reserves. Hence, reserve for foreseeable loss for INR 1000 million, (due within 6 months), should be a part of

provision. Therefore, it needs to be regrouped. If it was also a part of previous year's comparatives, then a note should be added in the notes to account for regrouping done this year.

2. Interest accrued and due of INR 1,110 million on term loan will be a part of current liabilities since it is supposed to be paid within 12 months from the reporting date. Hence, it should be shown under the heading "Other Current Liabilities".

3. It can be inferred from Note 3, that the deferred tax liabilities and deferred tax assets relate to taxes on income levied by the same governing taxation laws. Hence, these shall be set off, in accordance with AS 22. The net DTA of INR 600 million shall be shown in the balance sheet.

4. The note to trade receivables was incorrectly presented. The rectified note would be as follows:

Trade receivables (Unsecured)	**INR in million**
(a) Over six months from the date they were due for payment	
i. Considered good	0
ii. Considered doubtful	80
Less: Provision for doubtful debts	(10)
(A)	70
(b) Others	
i. Considered good	2,130
ii. Considered doubtful	0
Less: Provision for doubtful debts	0
(B)	2,130
Total (A + B)	2,200

5. It is common to have a termination clause in service contracts. Just by having a termination clause, a company cannot create a liability. Para 14 of AS 29 inter alia states that a provision will be recognized when an enterprise has a present obligation as a result of a past event.

   Since there is nothing to show that there is a present obligation, no provision will be made.

   As per para 27 of AS 29, a contingent liability is recognized only where the possibility of an outflow of resources embodying economic benefits is not remote. Since there is no onerous liability as on the reporting date, the possibility of an outflow becomes remote. Therefore, no contingent liability will arise. In fact, the management has wrongly worded it as 'onerous liability' in its notes to accounts. Onerous liability arises only when the unavoidable costs of meeting the obligation under the contract exceeds the economic benefits expected to be received from it. This note should be eliminated.

6. The demand notice from the tax department (that is under litigation) is a clear instance of a 'contingent liability'. Accordingly, the note should be revised as –

   'Contingent Liability:

There is a demand notice INR 12 Million, which is under CIT (Appeals) as on the reporting date.

7. The Statement to Profit and Loss needs to represent earnings per share, as per AS 20.

(b) Revised extracts of the financial statements

Balance Sheet **(INR in Million)**

	Note No.	As at March 31, 20X1
EQUITY AND LIABILITIES		
Shareholders' funds		
Share capital		2,000
Reserves and surplus	1	3,000
Non-current liabilities		
Long-term borrowings	2	10,000
Current liabilities		
Trade payables		600
Short-term provisions		1,500
Other current liabilities	4	1,410
TOTAL		**18,510**
ASSETS		
Non - current assets		
Fixed Assets		11,310
Deferred Tax Assets	3	600
Current assets		
Inventories		2,000
Trade receivables	5	2,200
Cash and Cash Equivalents		2,400
TOTAL		**18,510**

Statement of Profit and Loss
(INR in Million)

	Note No.	Year ended March 31, 20X1
Revenue from operations		11,000
Expenses		
Operating Costs		4,400
Employee Benefit Expense		2,400
Depreciation		1,998
Total Expenses		8,798
Profit Before Tax		2,202
Tax Expense		300
Profit for the period		1,902

Earnings Per Equity Share		
Basic		9.51
Diluted		9.51
Number of equity shares (face value of Rs.10 each)		200 million

Revised Notes (wherever applicable):

Note on Reserves and Surplus **(INR in Million)**

Capital Reserve		1,000
Surplus from P & L		
Opening Balance	98	
Additions	1,902	2,000
Total		**3,000**

Note on Long Term Borrowings

Term Loan from Bank	10,000
Total	10,000

Note on Other Current Liabilities

Unclaimed dividends	6
Interest on Term Loan	1,110
Billing in Advance	294
Total	1,410

Question 3 : Nov 2018 – RTP

Mr. X, is the financial controller of ABC Ltd., a listed entity which prepares consolidated financial statements in accordance with Ind AS. Mr. X has recently produced the final draft of the financial statements of ABC Ltd. for the year ended 31st March, 2018 to the managing director for approval. Mr. Y, who is not an accountant, had raised following queries from Mr. X after going through the draft financial statements:

(a) One of the notes to the financial statements gives details of purchases made by ABC Ltd. from PQR Ltd. during the period. Mr. Y own 100% of the shares in PQR Ltd.. However, he feels that there is no requirement for any disclosure to be made in ABC Ltd.'s financial statements since the transaction is carried out on normal commercial terms and is totally insignificant to ABC Ltd., as it represents less than 1% of ABC Ltd.'s purchases.

(b) The notes to the financial statements say that plant and equipment is held under the 'cost model'. However, property which is owner occupied is revalued annually to fair value. Changes in fair value are sometimes reported in profit or loss but usually in 'other comprehensive income'. Also, the amount of depreciation charged on plant and equipment as a percentage of its carrying amount is much higher than for owner occupied property. Another note states that property owned by ABC Ltd. but rent out to others is depreciated annually and not fair valued. Mr. Y is of the opinion that there is no consistent treatment of PPE items in the accounts. Elucidate how all these treatments comply with the relevant Ind AS.

(c) In the year to March, 2018, ABC Ltd. spent considerable amount on designing a new product. ABC Ltd. spent the six months from April, 2017 to September, 2017 researching into the feasibility of the product. Mr. X charged these research costs to profit or loss. From October, 2017, A Ltd. was confident that the product would be commercially successful and A Ltd. is fully committed to finance its future development. A Ltd. spent remaining part of the year in developing the product, which is expected to start from selling in the next few months. These development costs have been recognised as intangible assets in the Balance Sheet. State whether the treatment done by Mr. X is correct when all these research and development costs are design costs. Justify your answer with reference to relevant Ind AS.

Provide answers to the queries raised by the managing director Mr. Y as per Ind AS.

Solution :

Ongoing through the queries raised by the Managing Director Mr. Y, the financial controller Mr. X explained the notes and reasons for their disclosures as follows:

(a) Related parties are generally characterised by the presence of control or influence between the two parties.

Ind AS 24 'Related Party Disclosures' identifies related parties as, inter alia, key management personnel and companies controlled by key management personnel. On this basis, PQR Ltd. is a related party of ABC Ltd.

The transaction is required to be disclosed in the financial statements of ABC Ltd. since Mr. Y is Key Management personnel of ABC Ltd. Also at the same time, it owns 100% shares of PQR Ltd. ie. he controls PQR Ltd. This implies that PQR Ltd. is a related party of ABC Ltd.

Where transactions occur with related parties, Ind AS 24 requires that details of the transactions are disclosed in a note to the financial statements. This is required even if the transactions are carried out on an arm's length basis.

Transactions with related parties are material by their nature, so the fact that the transaction may be numerically insignificant to ABC Ltd. does not affect the need for disclosure.

(b) The accounting treatment of the majority of tangible non-current assets is governed by Ind AS 16 'Property, Plant and Equipment'. Ind AS 16 states that the accounting treatment of PPE is determined on a class by class basis. For this purpose, property and plant would be regarded as separate classes. Ind AS 16 requires that PPE is measured using either the cost model or the revaluation model. This model is applied on a class by class basis and must be applied consistently within a class. Ind AS 16 states that when the revaluation model applies, surpluses are recorded in other comprehensive income, unless they are cancelling out a deficit which has previously been reported in profit or loss, in which case it is reported in profit or loss. Where the revaluation results in a deficit, then such deficits are reported in profit or loss, unless they are cancelling out a surplus which has previously been reported in other comprehensive income, in which case they are reported in other comprehensive income.

According to Ind AS 16, all assets having a finite useful life should be depreciated over that life. Where property is concerned, the only depreciable element of the property is the buildings element, since land normally has an indefinite life. The estimated useful life of a building tends to be much longer than for plant. These two reasons together explain why the depreciation charge of a property as a percentage of its carrying amount tends to be much lower than for plant.

Properties which are held for investment purposes are not accounted for under Ind AS 16, but under Ind AS 40 'Investment Property'. As per Ind AS 40, investment properties should be accounted for under a cost model. ABC Ltd. had applied the cost model and thus our investment properties are treated differently from the owner occupied property which is annually to fair value.

(c) As per Ind AS 38 'Intangible Assets', the treatment of expenditure on intangible items depends on how it arose. Internal expenditure on intangible items incurred during research phase cannot be recognised as an asset. Once it can be demonstrated that a development project is likely to be technically feasible, commercially viable, overall profitable and can be adequately resourced, then future expenditure on the project can be recognised as an intangible asset. The difference in the treatment of expenditure upto 30th September, 2017 and expenditure after that date is due to the recognition phase i.e. research or development phase.

Question 4 : Nov 2019 – RTP

An entity has taken a loan facility from a bank that is to be repaid within a period of 9 months from the end of the reporting period. Prior to the end of the reporting period, the entity and the bank enter into an arrangement, whereby the existing outstanding loan will, unconditionally, roll into the new facility which expires after a period of 5 years.

(a) Should the loan be classified as current or non-current in the balance sheet of the entity?

(b) Will the answer be different if the new facility is agreed upon after the end of the reporting period?

(c) Will the answer to (a) be different if the existing facility is from one bank and the new facility is from another bank?

(d) Will the answer to (a) be different if the new facility is not yet tied up with the existing bank, but the entity has the potential to refinance the obligation?

Solution :

Ind AS 1 defines current liabilities as follows:

An entity shall classify a liability as current when:

(i) it expects to settle the liability in its normal operating cycle;

(ii) it holds the liability primarily for the purpose of trading;

(iii) the liability is due to be settled within twelve months after the reporting period; or

(iv) it does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.

An entity shall classify all other liabilities as non-current.

Accordingly, following will be the classification of loan in the given scenarios:

(a) The loan is not due for payment at the end of the reporting period. The entity and the bank have agreed for the said roll over prior to the end of the reporting period for a period of 5 years. Since the entity has an unconditional right to defer the settlement of the liability for at least twelve months after the reporting period, the loan should be classified as non-current.

(b) Yes, the answer will be different if the arrangement for roll over is agreed upon after the end of the reporting period because as per Ind AS 1, "an entity classifies its financial liabilities as current when they are due to be settled within twelve months after the reporting period.

(c) Yes, loan facility arranged with new bank cannot be treated as refinancing, as the loan with the earlier bank would have to be settled which may coincide with loan facility arranged with a new bank. In this case, loan has to be repaid within a period of 9 months from the end of the reporting period, therefore, it will be classified as current liability.

(d) Yes, the answer will be different and the loan should be classified as current. This is because, as per Ind AS 1, when refinancing or rolling over the obligation is not at the discretion of the entity (for example, there is no arrangement for refinancing), the entity does not consider the potential to refinance the obligation and classifies the obligation as current.

Question 5 : Nov 2019 – PAPER

Following are the Financial statements of Abraham Ltd. :

Balance Sheet

Particulars	**Note**	**As at March 31, 2019 (Rs. in lakhs)**
Equity and Liabilities		
Shareholder's funds		
Share capital (Shares of Rs.10 each)	1	1,000
Reserves and surplus		2,400
Non-current liabilities		
Long-term borrowings	2	5,700
Deferred tax liabilities	3	400
Current liabilities		
Trade payables		300
Short-term provisions		300
Other current liabilities	4	200
Total		10,300
Assets		
Non-current assets		
Fixed Assets		5,000
Deferred Tax Assets	3	700

Current assets		
Inventories		1,500
Trade receivables	5	1,100
Cash and bank balances		2,000
Total		**10,300**

Statement of Profit & Loss :

Particulars	**Note**	**As at March 31, 2019 (Rs. in lakhs)**
Revenue from operations		**6,000**
Expenses :		
Employees Benefit Expense		1,200
Operating Costs		3,199
Depreciation		450
Total Expenses		**4,849**
Profit before tax		1,151
Tax Expense		201
Profit after tax		**950**

Notes to Account :

Note 1 : Reserve and surplus

(Rs. in lakhs)

Capital Reserve		500
Surplus from P & L		
Opening Balance	550	
Additions	950	
Reserves for foreseeable loss		400
Total		**2,400**

Note 2 : Long Term Borrowings

Term Loan from Bank	5,700
Total	**5,700**

Note 3 : Deferred Tax

Deferred Tax Asset	700
Deferred Tax Liability	400
Total	**300**

Note 4 : Other Current Liabilities

Unclaimed dividends	10

Billing in Advance	150
Other Current Liabilities	40
Total	**200**

Note 5 : Trade Receivables

Considered good (outstanding within 6 months)	1,065
Considered doubtful (due from part 1 year)	40
Provision for doubtful debts	(5)
Total	**1,100**

Additional Information :

(i) Share capital comprises of 100 Lakh shares of Rs.10 each.

(ii) Term Loan from bank for Rs.5,700 lakhs also includes interest accrued and due of Rs.700 Lakhs as on the reporting date.

(iii) Reserve for foreseeable loss is created against a service contract due within 6 months.

(iv) Inventory should be valued at cost Rs.1,500 Lakhs, NRV as on date is Rs.1,200 Lakhs.

(v) A dividend of 10% was declared by the Board of directors of the company.

(vi) Accrued Interest income of Rs.300 Lakhs in not booked in the books of the company.

(vii) Deferred taxes related to taxes on income levied by the same governing tax laws.

Identify and report the errors and misstatements in the above extracts and prepare corrected Balance Sheet and Statement of Profit and Loss and where required the relevant notes to the accounts with explanations thereof.

Solution :

A) Following adjustments / rectification should be done

1) Interest accrued and due of Rs.700 on term loan should be disclosed as current liability.
2) Reserve for foreseeable loss should be provision and not reserve.
3) As per AS 2 inventory should be reported at lower of cost or NRV. Since NRV is lower the reported value should be decreased by Rs.300 lakh (1500 – 1200) and the same should be added to cost of operation.
4) Assuming that dividend is declared. After balance sheet date no adjustment is to done.
5) Accrued interest not recorded should be recorded. It should be shown under the head "Other Income" and "Other Current Assets".
6) Since deferred tax is related to same govt. As per IND AS 12 it should be set of. The Net DTA of 300 lakh should be reported in Balance Sheet.
7) The presentation of the Notes to "Trade Receivable" will be modified as per requirements of Division II of she schedule III.
8) As per IND AS 33 EPS should be reported at end of profit and loss a/c.

B) **Balance Sheet of Arbraham Ltd.**
as on 31/3/2019

		Rs.
	<u>Assets</u>	
1)	Non Current Assets	
	Property, Plant & Equipment	5,000
	Deferred Tax Asset	300
2)	Current Assets	
	Inventory	1,200
	Financial Assets	
	Trade Receivable	1,100
	Cash & Cash Equivalent	2,000
	Other Financial Assets (Accrued Int.)	300
	Total	9,900
	<u>Equity & Liability</u>	
1)	Equity	
	Equity Share Capital	1,000
	Other Equity	2,000
2)	Non Current Liability	
	Financial Liability	
	Buy term Borrowing	5,000
3)	Current Liability	
	Financial Liability	
	Trade payable	300
	Others	710
	Short term provision	700
	Other Current Liability	190
	Total	9,900

C) **Statement of Profit and Loss A/c.**
for the year ended 31/3/2019

Particular	**Note No.**	**Amount. (Rs. in lakh)**
Revenue from operations		6,000
Other Income (Interest Accrued)		300
Total Income		6,300
<u>Expenses</u>		
Operating Cost		3,199
Changes in Inventory		300

Employee benefit		1,200
Depreciation		450
Total Expenses		5,149
Profit Before Tax		1,151
Tax Expenses		201
Profit After Tax		950
Basis EPS (950)/100		9.5
No. of Shares of Rs.10 each		100

D) Statement for changes in equity

1) Equity capital

	OP.	Changes	Closing
Sh. of 10 each	1,000	-	1,000

2) Reserve

	(Rs. in lakh)
Capital Reserve	500
P & L A/c (5500 + 950)	1,500
	2,000

E) Deferred Tax Asset

	(Rs. in lakh)
DTA	700
– DTL	400
	300

F) Trade Receivable

		(Rs. in lakh)
Considered good		1,065
With Significant Risk	40	
Less : Provision	(5)	35
		1,100

G)

	(Rs. in lakh)
Long Term Borrowing (5,700 – 700)	5,000

H) Other Financial Liability

	(Rs. in lakh)
Unclaimed dividend	10
Interest on term loan	700
	710

I) Short Term Provision

	(Rs. in lakh)
Provisions	300
Foreseeable Loss	400
	700

J) Other Current Liabilities

	(Rs. in lakh)
Billing in Advance	150
Other	40
	190

Question 6 : Nov 2020 – RTP

Deepak started a new company Softbharti Pvt. Ltd. with Iktara Ltd. wherein investment of 55% is done by Iktara Ltd. and rest by Deepak. Voting powers are to be given as per the proportionate share of capital contribution. The new company formed was the subsidiary of Iktara Ltd. with two directors, and Deepak eventually becomes one of the directors of company. A consultant was hired and he charged Rs.30,000 for the incorporation of company and to do other necessary statuary registrations. Rs.30,000 is to be charged as an expense in the books after incorporation of company. The company, Softbharti Pvt. Ltd. was incorporated on 1st April 2019.

The financials of Iktara Ltd. are prepared as per Ind AS.

An accountant who was hired at the time of company's incorporation, has prepared the draft financials of Softbharti Pvt. Ltd. for the year ending 31st March, 2020 as follows:

Statement of Profit and Loss

Particulars	**Amount (Rs.)**
Revenue from operations	10,00,000
Other Income	1,00,000
Total Revenue (a)	**11,00,000**
Expenses:	
Purchase of stock in trade	5,00,000
(Increase)/Decrease in stock in trade	(50,000)
Employee benefits expense	1,75,000
Depreciation	30,000
Other expenses	90,000
Total Expenses (b)	**7,45,000**

Profit before tax (c) = (a)-(b)	**3,55,000**
Current tax	1,06,500
Deferred tax	6,000
Total tax expense (d)	**1,12,500**
Profit for the year (e) = (c) – (d)	**2,42,500**

Balance Sheet

Particulars	**Amount (Rs.)**
EQUITY AND LIABILITIES	
(1) Shareholders' Funds	
(a) Share Capital	1,00,000
(b) Reserves & Surplus	2,27,500
(2) Non-Current Liabilities	
(a) Long Term Provisions	25,000
(b) Deferred tax liabilities	6,000
(3) Current Liabilities	
(a) Trade Payables	11,000
(b) Other Current Liabilities	45,000
(c) Short Term Provisions	1,06,500
TOTAL	**5,21,000**
ASSETS	
(1) Non Current Assets	
(a) Property, plant and equipment (net)	1,00,000
(b) Long-term Loans and Advances	40,000
(c) Other Non Current Assets	50,000
(2) Current Assets	
(a) Current Investment	30,000
(b) Inventories	80,000
(c) Trade Receivables	55,000
(d) Cash and Bank Balances	1,15,000
(e) Other Current Assets	51,000
TOTAL	**5,21,000**

Additional information of Softbharti Pvt Ltd.:

i. Deferred tax liability of Rs.6,000 is created due to following temporary difference: Difference in depreciation amount as per Income tax and Accounting profit

ii. There is only one property, plant and equipment in the company, whose closing balance as at 31st March, 2020 is as follows:

iii. Pre incorporation expenses are deductible on straight line basis over the period of five years as per Income tax. However, the same are immediately expensed off in the books.

iv. Current tax is calculated at 30% on PBT - Rs.3,55,000 without doing any adjustments related to Income tax. The correct current tax after doing necessary adjustments of allowances / disallowances related to Income tax comes to Rs.1,25,700.

v. After the reporting period, the directors have recommended dividend of Rs.15,000 for the year ending 31st March, 2020 which has been deducted from reserves and surplus. Dividend payable of Rs.15,000 has been grouped under 'other current liabilities' alongwith other financial liabilities.

vi. There are 'Government statuary dues' amounting to Rs.15,000 which are grouped under 'other current liabilities'.

vii. The capital advances amounting to Rs.50,000 are grouped under 'Other non-current assets'.

viii. Other current assets of Rs.51,000 comprise Interest receivable from trade receivables.

ix. Current investment of Rs.30,000 is in shares of a company which was done with the purpose of trading; current investment has been carried at cost in the financial statements. The fair value of current investment in this case is Rs.50,000 as at 31st March, 2020.

x. Actuarial gain on employee benefit measurements of Rs.1,000 has been omitted in the financials of Softbharti private limited for the year ending 31st March, 2020.

The financial statements for financial year 2019-2020 have not been yet approved.

You are required to ascertain that whether the financial statements of Softbharti Pvt. Ltd. are correctly presented as per the applicable financial reporting framework. If not, prepare the revised financial statements of Softbharti Pvt. Ltd. after the careful analysis of mentioned facts and information.

Solution :

If Ind AS is applicable to any company, then Ind AS shall automatically be made applicable to all the subsidiaries, holding companies, associated companies, and joint ventures of that company, irrespective of individual qualification of set of standards on such companies.

In the given case it has been mentioned that the financials of Iktara Ltd. are prepared as per Ind AS. Accordingly, the results of its subsidiary Softbharti Pvt. Ltd. should also have been prepared as per Ind AS. However, the financials of Softbharti Pvt. Ltd. have been presented as per accounting standards (AS).

Hence, it is necessary to revise the financial statements of Softbharti Pvt. Ltd. as per Ind AS after the incorporation of necessary adjustments mentioned in the question.

The revised financial statements of Softbharti Pvt. Ltd. as per Ind AS and Division II to Schedule III of the Companies Act, 2013 are as follows:

STATEMENT OF PROFIT AND LOSS
for the year ended 31st March, 2020

Particulars	Amount (Rs.)
Revenue from operations	10,00,000
Other Income (1,00,000 + 20,000) (refer note -1)	1,20,000
Total Revenue	**11,20,000**

Expenses:	
Purchase of stock in trade	5,00,000
Increase) / Decrease in stock in trade	(50,000)
Employee benefits expense	1,75,000
Depreciation	30,000
Other expenses	90,000
Total Expenses	**7,45,000**
Profit before tax	**3,75,000**
Current tax	1,25,700
Deferred tax (W.N.1)	4,800
Total tax expense	**1,30,500**
Profit for the year (A)	**2,44,500**
OTHER COMPREHENSIVE INCOME	
Items that will not be reclassified to Profit or Loss:	
Remeasurements of net defined benefit plans	**1,000**
Tax liabilities relating to items that will not be reclassified to Profit or Loss	
Remeasurements of net defined benefit plans (tax) [1000 x 30%]	(300)
Other Comprehensive Income for the period (B)	**700**
Total Comprehensive Income for the period (A+B)	**2,45,200**

BALANCE SHEET
as at 31st March, 2020

Particulars	**Amount (Rs.)**
ASSETS	
Non-current assets	
Property, plant and equipment	1,00,000
Financial assets	
Other financial assets (Long-term loans and advances)	40,000
Other non-current assets (capital advances) (refer note-2)	50,000
Current assets	
Inventories	80,000
Financial assets	
Investments (30,000 + 20,000) (refer note -1)	50,000
Trade receivables	55,000
Cash and cash equivalents/Bank	1,15,000
Other financial assets (Interest receivable from trade receivables)	51,000
TOTAL ASSETS	**5,41,000**
EQUITY AND LIABILITIES	
Equity	

Equity share capital	1,00,000
Other equity	2,45,200
Non-current liabilities	
Provision (25,000 – 1,000)	24,000
Deferred tax liabilities (4800 + 300)	5,100
Current liabilities	
Financial liabilities	
Trade payables	11,000
Other financial liabilities (Refer note 5)	15,000
Other current liabilities (Govt. statuary dues) (Refer note 3)	15,000
Current tax liabilities	1,25,700
TOTAL EQUITY AND LIABILITIES	**5,41,000**

STATEMENT OF CHANGES IN EQUITY
For the year ended 31st March, 2020

A. EQUITY SHARE CAPITAL

	Balance (Rs.)
As at 31st March, 2019	-
Changes in equity share capital during the year	1,00,000
As at 31st March, 2020	1,00,000

B. OTHER EQUITY

	Reserves & Surplus Retained Earnings (Rs.)
As at 31st March, 2019	-
Profit for the year	2,44,500
Other comprehensive income for the year	700
Total comprehensive income for the year	2,45,200
Less: Dividend on equity shares (refer note – 4)	-
As at 31st March, 2020	2,45,200

DISCLOSURE FORMING PART OF FINANCIAL STATEMENTS:
Proposed dividend on equity shares is subject to the approval of the shareholders of the company at the annual general meeting and not recognized as liability as at the Balance Sheet date. (refer note-4)

Notes:

1. Current investment are held for the purpose of trading. Hence, it is a financial asset classified as FVTPL. Any gain in its fair value will be recognised through profit or loss. Hence, Rs.20,000 (50,000 – 30,000) increase in fair value of financial asset will be recognised in profit and loss. However, it will attract deferred tax liability on increased value (Refer W.N).

2. Assets for which the future economic benefit is the receipt of goods or services, rather than the right to receive cash or another financial asset, are not financial assets.
3. Liabilities for which there is no contractual obligation to deliver cash or other financial asset to another entity, are not financial liabilities.
4. As per Ind AS 10, 'Events after the Reporting Period', If dividends are declared after the reporting period but before the financial statements are approved for issue, the dividends are not recognized as a liability at the end of the reporting period because no obligation exists at that time. Such dividends are disclosed in the notes in accordance with Ind AS 1, Presentation of Financial Statements.
5. Other current financial liabilities:

	(Rs.)
Balance of other current liabilities as per financial statements	45,000
Less: Dividend declared for FY 2019 - 2020 (Note – 4)	(15,000)
Reclassification of government statuary dues payable to 'other current liabilities'	(15,000)
Closing balance	15,000

Working Note:

Calculation of deferred tax on temporary differences as per Ind AS 12 for financial year 2019 – 2020

Item	**Carrying amount (Rs.)**	**Tax base (Rs.)**	**Difference (Rs.)**	**DTA / DTL @ 30% (Rs.)**
Property, Plant and Equipment	1,00,000	80,000	20,000	6,000-DTL
Pre-incorporation expenses	Nil	24,000	24,000	7,200-DTA
Current Investment	50,000	30,000	20,000	6,000-DTL
			Net DTL	4,800-DTL

Question 7 : Jan 2021 – Paper

Entity A had obtained a long-term bank loan during January 2019, which is subject to certain financial covenants. One of such covenants states that during the tenure of the loan, debt equity ratio of 65:35 is to be maintained at all time. In case of breach of this covenant, the loan will be repayable immediately. The loan agreement also states that these covenants will be assessed at the end of each quarter and reported to the bank within a month from the end of each quarter. If the covenants are breached at this time, the loan will be repayable immediately. The entity closes its annual accounts as on 31st March every year.

You are required to show how the loan will be classified as on 31st March 2020, if:

(i) At the financial year end, Entity A determines that it is not in breach of any of the covenants;

(ii) At the quarter ending 31st December 2019, Entity A's debt equity ratio became 75:25 and thus breaches the covenant, however it obtains a waiver from the bank. The terms of the waiver specify that if Entity A rectifies the breach within a period of 12 months from the reporting date then the bank cannot demand repayment immediately on account of the breach during this period. Entity A expects to rectify the breach by raising additional equity capital by means of a rights issue to the existing shareholders and expects that the issue will be fully subscribed;

(iii) Considering the same facts as in (ii) above, except obtaining the waiver clause, what would be your answer?

Solution :

Para 74 of Ind AS 1 'Presentation of Financial Statements', states that where there is a breach of a material provision of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand on the reporting date, the entity does not classify the liability as current, if the lender agreed, after the reporting period and before the approval of the financial statements for issue, not to demand payment as a consequence of the breach.

However, an entity classifies the liability as non-current, if the lender agreed by the end of the reporting period to provide a period of grace ending at least twelve months after the reporting period, within which the entity can rectify the breach and during which the lender cannot demand immediate repayment.

(i) The entity has obtained a long-term loan during January, 2019. Since repayment period of the loan is not mentioned in the question, it is assumed that on 31st March 2020, the repayment period of the loan is more than 12 months. Further, the entity has not breached the covenants specified in the loan; therefore, as at 31st March, 2020, the loan will be classified as 'non-current liability.

(ii) In the second case, though there is a breach of covenant on 31st December, 2019 i.e. before reporting date of 31st March, 2020, yet the bank had agreed to provide a period of grace for twelve months from the reporting period, within which the entity A can rectify the breach and during this period bank cannot demand immediate repayment. Also, entity A has intention to rectify the breach. Thus, entity A will classify the liability of bank loan as non-current liability in its books as at 31st March, 2020.

(iii) Since the covenant for the bank loan has been breached during the quarter ended 31st December, 2019 and reported to the bank within one month from the end of the quarter i.e. by 31st January, 2020, the bank loan becomes repayable immediately. Therefore, it will be presented as current liability in the books of entity A as on 31st March, 2020.

Question 8 : May 2021 – RTP

An entity has the following trial balance line items. How should these items be classified, i.e., current or non-current as per Ind AS 1?

(a) Receivables (viz., receivable under a contract of sale of goods in which an entity deals)

(b) Advance to suppliers

(c) Income tax receivables [other than deferred tax]

(d) Insurance spares

Solution :

(a) As per Ind AS 1, an entity shall classify an asset as current when it expects to realise the asset, or intends to sell or consume it, in its normal operating cycle.

Paragraph 68 provides the guidance that current assets include assets (such as inventories and trade receivables) that are sold, consumed or realised as part of the normal operating cycle even when they are not expected to be realised within twelve months after the reporting period.

In accordance with above, the receivables that are considered a part of the normal operating cycle will be classified as current asset.

If the operating cycle exceeds twelve months, then additional disclosure as required by Ind AS 1 is required to be given in the notes.

(b) As discussed in point (a) above, advances to suppliers for goods and services would be classified in accordance with normal operating cycle if it is given in relation to the goods or services in which the entity normally deals. If the advances are considered a part the normal operating cycle, it would be classified as a current asset. If the operating cycle exceeds twelve months, then additional disclosure as required by paragraph 61 of Ind AS 1 is required to be given in the notes.

(c) Classification of income tax receivables [other than deferred tax] will be driven by Ind AS 1, i.e., based on the expectation of the entity to realise the asset. If the receivable is expected to be realised within twelve months after the reporting period, then it will be classified as current asset else non-current asset.

(d) Ind AS 16 states that items such as spare parts, stand-by equipment and servicing equipment are recognised in accordance with this Ind AS when they meet the definition of property, plant and equipment. Otherwise, such items are classified as inventory.

Accordingly, the insurance spares that are treated as an item of property, plant and equipment would normally be classified as non-current asset whereas insurance spares that are treated as inventory will be classified as current asset if the entity expects to consume it in its normal operating cycle.

Question 9 : July 2021 – Paper

Charm Limited (the 'Company') is a manufacturing company, which is into manufacturing of wires and cables and has assessed its operating cycle to be 15 months. The Company has some trade receivables which are receivable within a period of 12 months from the reporting date i.e. 31st March, 2021.

With respect of the following transactions, which took place during the financial year 2021-21, give your opinion based on relevant Ind AS :

- The Company has received a contract of Rs.10 crores on 31st March 2021. The terms of the contract value with the customer. The Company made a security deposit of Rs.2 crores on

31st March 2021. This contract will be completed in about 14 months 70% of the deposit will be refunded immediately and the balance 30% of the deposit will be refunded after 3 months from the completion of the contract. The company wants to present the security deposit of Rs.2 crores as non-current. Is the management's decision correct?

- The Company has some trade receivables that are due after 14 months from the date of the balance sheet; the management of the Company expects to receive the amount within the period of the operating cycle. Despite the fact that these are receivables in 14 months, the management would like to present these as current. Is the management's decision correct?
- In the normal course of business, the Company has given 2 contracts and received a total security deposit of Rs.4 crores. Rs.3 crores in received from X Limited and Rs.1 crore received from Y Limited on 31st March 2021. These ar repayable on completion of the contract. However, of the contract is cancelled within the contract term of 18 months, then the deposit becomes payable immediately. The Company is positive about the contract with X Limited but is in doubt about the contract received from Y Limited. The Company wants to present the amount of Rs.3 crores as non-current and Rs.1 crore as current in the balance sheet. Is the management's decision correct?
- The Company is planning to replace a machinery. It has given an advance of Rs.1 crores for purchase of new machinery which will be delivered in 6 months from the date of the balance sheet. It has sold the old machinery for Rs.0.5 crores, the payment of which is due in 10 months from the date of the balance sheet. The Company wants to present both these amounts as current since they will be settled within twelve months from the end of the reporting period. Is the management's decision correct?

Solution :

Operating cycle of Charm Limited = 15 months

(i) The security deposit made by the Company with the customers be classified as current assets to the extent of 70% (Rs. 2 crore x 70% = Rs. 1.40 crore) as it will be refunded immediately on completion of 14 months of contract i.e. within the operating cycle of 15 months.

However, 30% of the security deposit will be refunded after 3 months of completion of the contract (14+3 = 17 months) i.e. after 2 months of operating cycle (Operating cycle of the Company is 15 months). Hence, it will be classified as non-current. Therefore, management's decision is not correct. (Refer Para 66 of Ind AS 1)

(ii) Yes, the Company's decision of presenting the trade receivables as Current Assets is correct despite the fact that these are receivables in 14 months' time since the operating cycle of the company is 15 months and any event arising due to trade will be considered as current if its settlement is within the tenure of operating cycle. Additionally, the

Company also need to disclose amounts that are receivable within a period of 12 months and after 12 months from the reporting date. (Refer Para 60 and 61 of Ind AS 1)

(iii) Paragraph 69(d) of Ind AS 1 states that an entity shall classify a liability as current when it does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period.

Although it is expected that X Limited will fulfil the contract and the deposit will not be refunded, but in case of cancellation within the contract term, refund of security deposit is a condition that is not within the control of the entity. Hence, Charm Limited does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period. Accordingly, the deposit will have to be classified as current liability in case of both X and Y Limited.

(iv) Yes, the management decision to classify the payment of Rs. 0.5 crore as a current asset is correct since the payment will be realised in less than twelve months from the end of the reporting period.

Capital advances are advances given for procurement of Property, Plant and Equipment etc. Typically, companies do not expect to realize them in cash. Rather, over the period, these get converted into non-current assets. Hence, capital advances should be treated as other non-current assets irrespective of when the Property, Plant and Equipment is expected to be received.

Under Ind AS Schedule III, Capital Advances are not to be classified under Capital Work in Progress since they are specifically to be disclosed under other non-current assets.

Accordingly, advance of Rs. 1 crore given for purchase of machinery is 'Capital advance' which will be classified as non-current as it relates to acquisition of non-current item i.e., machinery. Hence, management decision to classify it as current is incorrect.

Question 10 : Nov 2021 – RTP

Is offsetting permitted under the following circumstances?

(a) Expenses incurred by a holding company on behalf of subsidiary, which is reimbursed by the subsidiary - whether in the separate books of the holding company, the expenditure and related reimbursement of expenses can be offset?

(b) Whether profit on sale of an asset against loss on sale of another asset can be offset?

(c) When services are rendered in a transaction with an entity and services are received from the same entity in two different arrangements, can the receivable and payable be offset?

Solution :

(a) As per paragraph 33 of Ind AS 1, offsetting is permitted only when the offsetting reflects the substance of the transaction.

In this case, the agreement/arrangement, if any, between the holding and subsidiary company needs to be considered. If the arrangement is to reimburse the cost incurred by the holding company on behalf of the subsidiary company, the same may be presented net. It should be ensured that the substance of the arrangement is that the payments are actually in the nature of reimbursement.

(b) Paragraph 35 of Ind AS 1 requires an entity to present on a net basis gains and losses arising from a group of similar transactions. Accordingly, gains or losses arising on disposal of various items of property, plant and equipment shall be presented on net basis. However, gains or losses should be presented separately if they are material.

(c) Ind AS 1 prescribes that assets and liabilities, and income and expenses should be reported separately, unless offsetting reflects the substance of the transaction. In addition to this, as per paragraph 42 of Ind AS 32, a financial asset and a financial liability should be offset if the entity has legally enforceable right to set off and the entity intends either to settle on net basis or to realise the asset and settle the liability simultaneously.

In accordance with the above, the receivable and payable should be offset against each other and net amount is presented in the balance sheet if the entity has a legal right to set off and the entity intends to do so. Otherwise, the receivable and payable should be reported separately.

Question 11 : May 2022 – RTP

An entity manufactures passenger vehicles. The time between purchasing of underlying raw materials to manufacture the passenger vehicles and the date the entity completes the production and delivers to its customers is 11 months. Customers settle the dues after a period of 8 months from the date of sale.

(a) Will the inventory and the trade receivables be current in nature?

(b) Assuming that the production time was say 15 months and the time lag between the date of sale and collection from customers is 13 months, will the answer be different?

Solution :

Inventory and debtors need to be classified in accordance with the requirement of paragraph 66(a) of Ind AS 1, which provides that an asset shall be classified as current if an entity expects to realise the same or intends to sell or consume it in its normal operating cycle.

(a) In this case, time lag between the purchase of inventory and its realisation into cash is 19 months [11 months + 8 months]. Both inventory and the debtors would be classified as current if the entity expects to realise these assets in its normal operating cycle.

(b) No, the answer will be the same as the classification of debtors and inventory depends on the expectation of the entity to realise the same in the normal operating cycle. In this case, time lag between the purchase of inventory and its realisation into cash is 28 months [15 months + 13 months]. Both inventory and debtors would be classified as current if the entity expects to realise these assets in the normal operating cycle.

Additional information as required by paragraph 61 of Ind AS 1 will be required to be made by the entity, which provides "Whichever method of presentation is adopted, an entity shall disclose the amount expected to be recovered or settled after more than twelve months for each asset and liability line item that combines amounts expected to be recovered or settled:

(a) No more than twelve months after the reporting period, and

(b) More than twelve months after the reporting period."

Thanks ….

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IND AS – 2 INVENTORIES

CHAPTER - 3

Question 1 : May 2018 – RTP

On 31 March 20X1, the inventory of ABC includes spare parts which it had been supplying to a number of different customers for some years. The cost of the spare parts was Rs.10 million and based on retail prices at 31 March 20X1, the expected selling price of the spare parts is Rs.12 million. On 15 April 20X1, due to market fluctuations, expected selling price of the spare parts in stock reduced to Rs.8 million. The estimated selling expense required to make the sales would Rs.0.5 million. Financial statements were authorised by Board of Directors on 20th April 20X1.

As at 31st March 20X2, Directors noted that such inventory is still unsold and lying in the warehouse of the company. Directors believe that inventory is in a saleable condition and active marketing would result in an immediate sale. Since the market conditions have improved, estimated selling price of inventory is Rs.11 million and estimated selling expenses are same Rs.0.5 million.

What will be the value inventory at the following dates:

(a) 31st March 20X1

(b) 31st March 20X2

Solution :

As per Ind AS 2 'Inventories', inventory is measured at lower of 'cost' or 'net realisable value'. Further, as per Ind AS 10: 'Events after Balance Sheet Date', decline in net realisable value below cost provides additional evidence of events occurring at the balance sheet date and hence shall be considered as 'adjusting events'.

(a) In the given case, for valuation of inventory as on 31 March 20X1, cost of inventory would be Rs.10 million and net realisable value would be Rs.7.5 million (i.e. Expected selling price Rs.8 million- estimated selling expenses Rs.0.5 million). Accordingly, inventory shall be measured at Rs.7.5 million i.e. lower of cost and net realisable value. Therefore, inventory write down of Rs.2.5 million would be recorded in income statement of that year.

(b) As per Ind AS 2, a new assessment is made of net realizable value in each subsequent period. It Inter alia states that if there is increase in net realizable value because of changed economic circumstances, the amount of write down is reversed so that new carrying amount is the lower of the cost and the revised net realizable value. Accordingly, as at 31 March 20X2, again inventory would be valued at cost or net realisable value whichever is lower. In the present case, cost is Rs.10 million and net realisable value would be Rs.10. 5 million (i.e. expected selling price Rs.11 million – estimated selling expense Rs.0.5 million). Accordingly, inventory would be recorded at Rs.10 million and inventory write down carried out in previous year for Rs.2.5 million shall be reversed.

Question 2 : May 2020 – RTP

The following is relevant information for an entity :

- Full capacity is 10,000 labour hours in a year.
- Normal capacity is 7,500 labour hours in a year.
- Actual labour hours for current period are 6,500 hours.
- Total fixed production overhead is Rs.1,500.
- Total variable production overhead is Rs.2,600.
- Total opening inventory is 2,500 units.
- Total units produced in a year are 6,500 units.
- Total units sold in a year are 6,700 units.
- The cost of inventories is assigned by using FIFO cost formula.

How overhead costs are to be allocated to cost of goods sold and closing inventory?

Solution :

1) As per AS 2 fixed overheads should be absorbed at actual overheads or budgeted overhead which is lower.

Actual $= \frac{1500}{6500}$ = Rs.0.23/hour

Budgeting $= \frac{1500}{7500}$ = Rs.0.2/hour

i.e. 6500 $\times$ 0.2 = Rs.1300

The balance of fixed overhead

i.e. 1500 – 1300 = 200 should be changed to P & L

2) Variable overheads = $\frac{2600}{6500}$ = Rs.0.4/hr.

3) Closing stock (units)

= Opening stock	2500
+ Production	6500
– Sold	6700
	2300 units

4) Time take to product 1 unit

$= \frac{6500 \text{ hrs}}{6500 \text{ units}}$ i.e. 1 hr./unit

5) Closing stock = 2300 units $\times$ 1 hr./unit $\times$ (0.2 + 0.4)

6) Cost of goods sold

Total overheads (1500 + 2600)	4100
– Closing stock	1380

– Cost charged to P & L	200
	2520

Question 3 : Nov 2020 – RTP

A company normally produced 1,00,000 units of a high precision equipment each year over past several years. In the current year, due to lack of demand and competition, it produced only 50,000 units. Further information is as follows:

Material = Rs.200 per unit;

Labour = Rs.100 per unit;

Variable manufacturing overhead = Rs.100 per unit;

Fixed factory production overhead = Rs.1,00,00,000;

Fixed factory selling overhead = Rs.50,00,000;

Variable factory selling overhead = Rs.150 per unit.

Calculate the value of inventory per unit in accordance with Ind AS 2. What will be the treatment of fixed manufacturing overhead?

Solution :

1) As per AS 2 fixed overhead should be absorbed at Actual CPU or budgeted CPU whichever is low

Actual $= \frac{1,00,00,000}{50,000} =$ Rs.200/unit

Budgeted $= \frac{1,00,00,000}{1,00,000} =$ Rs.100/unit

i.e. it should be absorbed at Rs.100/unit

2)

Inventory value	Rs.
Raw material	200/unit
Labour	100/unit
Variable manufacture O/H	100/unit
Fixed production O/H	100/unit
Total	500/unit

3) Balance fixed factory O/H

i.e. 1,00,00,000 – (50,000 × 100) = 50,00,000 and selling cost should be charged to Profit and Loss A/c.

Question 4 : May 2021 – RTP

On 1 January 20X1 an entity accepted an order for 7,000 custom-made corporate gifts.

On 3 January 20X1 the entity purchased raw materials to be consumed in the production process for Rs. 5,50,000, including Rs. 50,000 refundable purchase taxes. The purchase price was funded by raising a loan of Rs. 5,55,000 (including Rs. 5,000 loan-raising fees). The loan is secured by the inventories.

During January 20X1 the entity designed the corporate gifts for the customer.
Design costs included:

- cost of external designer = Rs. 7,000; and
- labour = Rs. 3,000.

During February 20X1 the entity's production team developed the manufacturing technique and made further modifications necessary to bring the inventories to the conditions specified in the agreement. The following costs were incurred in the testing phase:

- materials, net of Rs. 3,000 recovered from the sale of the scrapped output = Rs. 21,000;
- labour = Rs. 11,000; and
- depreciation of plant used to perform the modifications = Rs. 5,000.

During February 20X1 the entity incurred the following additional costs in manufacturing the customised corporate gifts:

- consumable stores = Rs. 55,000;
- labour = Rs. 65,000; and
- depreciation of plant used to manufacture the customised corporate gifts = Rs. 15,000.

The customised corporate gifts were ready for sale on 1 March 20X1. No abnormal wastage occurred in the development and manufacture of the corporate gifts.
Compute the cost of the inventory? Substantiate your answer with appropriate reasons and calculations, wherever required.

Solution :

Statement showing computation of inventory cost

Particulars	Amount (Rs.)	Remarks
Costs of purchase	5,00,000	Purchase price of raw material [purchase price (Rs. 5,50,000) less refundable purchase taxes (Rs. 50,000)]
Loan-raising fee	–	Included in the measurement of the liability
Costs of purchase	55,000	Purchase price of consumable stores
Costs of conversion	65,000	Direct costs—labour
Production overheads	15,000	Fixed costs—depreciation
Production overheads	10,000	Product design costs and labour cost for specific customer
Other costs	37,000	Refer working note
Borrowing costs	–	Recognised as an expense in profit or loss
Total cost of inventories	**6,82,000**	

Working Note:

Costs of testing product designed for specific customer:

Rs. 21,000 material (ie net of the Rs. 3,000 recovered from the sale of the scrapped output) + Rs. 11,000 labour + Rs. 5,000 depreciation.

Question 5 : Nov 2021 – RTP

Whether the following costs should be considered while determining the Net Realisable Value (NRV) of the inventories?

(a) Costs of completion of work-in-progress;

(b) Trade discounts expected to be allowed on sale; and

(c) Cash discounts expected to be allowed for prompt payment

Solution :

Ind AS 2 defines Net Realisable Value as the "estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale."

Costs of completion of work-in-progress are incurred to convert the work-in-progress into finished goods. Since these costs are in the nature of completion costs, in accordance with the above definition, the same should be deducted from the estimated selling price to determine the NRV of work-in-progress.

Trade Discount is "A reduction granted by a supplier from the list price of goods or services on business considerations other than for prompt payment". Trade discount is allowed either expressly through an agreement or through prevalent commercial practices in the terms of the trade and the same is adjusted in arriving at the selling price. Accordingly, the trade discount expected to be allowed should be deducted to determine the estimated selling price.

Cash Discount is "A reduction granted by a supplier from the invoiced price in consideration of immediate payment or payment within a stipulated period." These types of costs are incurred to recover the sale proceeds immediately or before the end of the specified period or credit period allowed to the customer. In other words, these costs are not incurred to make the sale, therefore, the same should not be considered while determining NRV.

Thanks ....

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IND AS – 16 PROPERTY, PLANT & EQUIPMENT

CHAPTER - 4

Question 1 : May 2018 – RTP

A Ltd. purchased some Property, Plant and Equipment on 1st April, 2011, and estimated their useful lives for the purpose of financial statements prepared on the basis of Ind AS: Following were the original cost, and useful life of the various components of property, plant, and equipment assessed on 1st April, 2011

Property, Plant and Equipment	Original Cost	Estimated useful life
Building	1,50,00,000	15 years
Plant and Machinery	1,00,00,000	10 years
Furniture and Fixture	35,00,000	7 years

A Ltd. uses the straight-line method of depreciation. On 1st April, 2014, the entity reviewed the following useful lives of the property, plant, and equipment through an external valuation expert

Buildings	10 years
Plant and Machinery	7 years
Furniture and Fixture	5 years

There were no salvage values for the three components of the property, plant, and equipment either initially or at the time the useful lives were revised.

Compute the impact of revaluation of useful life on the Statement of Profit and Loss for the year ending 31st March, 2014.

Solution :

1. Depreciation for year ended 2012, 2013 and 2014

PPE	Original Cost	Estimated life	Depreciation PA
Building	1,50,00,000	15 years	10,00,000
Plant and Machinery	1,00,00,000	10 years	10,00,000
Furniture and Fixture	35,00,000	7 years	5,00,000
Total Depreciation			25,00,000

2. Depreciation for year ended 2015

PPE	Original Cost	Depre (3 years)	Carrying amount (1/4/14)	Revised Life	Depre
Building	1,50,00,000	30,00,000	1,20,00,000	10 years	12,00,000
Plant	1,00,00,000	30,00,000	70,00,000	7 years	10,00,000

Furniture	35,00,000	15,00,000	20,00,000	5 years	4,00,000
Total					**26,00,000**

Depreciation charge to Profit and Loss shall increase by Rs.1,00,000. As per IND AS 16, Property, Plant and Equipment entity shall review the estimated useful life estimated residual value atleast at the end each financial year. Any changes should be accounted for as change in estimate as per IND AS 8, Accounting Policy, changes in accounting estimates and errors.

Question 2 : May 2018 – PAPER

Stars Ltd. is a multinational entity that owns three properties. All the three properties were purchased on 1st April 2016. The details of purchase price and the market values of the properties are given as follows:

Particular	**Property 1**	**Property 2**	**Property 3**
	Factory	**Factory**	**Let-out Building**
Purchase Price	30,000	20,000	24,000
Market Value (31-03-2017)	32,000	22,000	27,000
Life	10 years	10 years	10 years
Subsequent Measurement	Cost Model	Revaluation Model	Revaluation Model

Property 1 and 2 are occupied by Stars Ltd, whilst property 3 is let out to a non-related party at a market rent. The management presents all three properties in balance sheet as' 'Property, plant and equipment'.

The company does not depreciate any of the properties on the basis that the fair values are exceeding their carrying amount and recognise the difference between purchase price and fair value in Statement of Profit and Loss.

Evaluate whether the accounting policies adopted by the Stars Ltd. in relation to these properties is in accordance of relevant Indian Accounting Standards (Ind AS). If not, advise the correct treatment along with workings.

Solution :

(i) For classification of assets

As per Ind AS 16 'Property, Plant and Equipment' states that Property, plant and equipment are tangible items that are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes.

As per Ind AS 40 'Investment property', investment property is a property held to earn rentals or for capital appreciation or both, rather than for use in the production or supply of goods or services or for administrative purposes; or sale in the ordinary course of business.

According, to the facts given in the questions, since Property 1 and 2 are used as factory buildings, their classification as PPE is correct. However, Property 3 is held to earn rentals; hence, it should be classified as Investment Property. Thus, its classification as PPE is not correct. Property 3 shall be presented as separate line item as Investment Property as per Ind AS 40.

(ii) For valuation of assets

Ind AS 16 states that an entity shall choose either the cost model or the revaluation model as its accounting policy and shall apply that policy to an entire class of property, plant and equipment. Also, Ind AS 16 states that If an item of property, plant and equipment is revalued, the entire class of property, plant and equipment to which that asset belongs shall be revalued.

However, for investment property, Ind AS 40 states that an entity shall adopt as its accounting policy the cost model to all of its investment property. Ind AS 40 also requires that an entity shall disclose the fair value of investment property.

Since property 1 and 2 is used as factory building, they should be classified under same category or class ie. 'factory building'. Therefore, both the properties should be valued either at cost model or revaluation model. Hence, the valuation model adopted by Stars Ltd. is not consistent and correct as per Ind AS 16.

In respect to property 3 being classified as Investment Property, there is no alternative of revaluation model i.e. only cost model is permitted for subsequent measurement. However, Stars Ltd. is required to disclose the fair value of the investment property in the Notes to Accounts.

(iii) For changes in value on account of revaluation and treatment thereof

Ind AS 16 states that if an asset's carrying amount is increased as a result of a revaluation, the increase shall be recognised in other comprehensive income and accumulated in equity under the heading 'revaluation surplus'. However, the increase shall be recognised in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognised in profit or loss. Accordingly, the revaluation gain shall be recognised in other comprehensive income and accumulated in equity under the heading of revaluation surplus.

(iv) For treatment of depreciation

Ind AS 16 states that depreciation is recognised even if the fair value of the asset exceeds its carrying amount, as long as the asset's residual value does not exceed its carrying amount. Accordingly, Stars Ltd. is required to depreciate these properties irrespective of that their fair value exceeds the carrying amount.

(v) Rectified presentation in the balance sheet

As per the provisions of Ind AS 1, Ind AS 16 and Ind AS 40, the presentation of these three properties in the balance sheet should be as follows:

Case 1: If Stars Ltd. has applied the Cost Model to an entire class of property, plant and equipment.

Balance Sheet extracts as at 31st March 2017

Assets		Rs.
Non-Current Assets		
Property, Plant and Equipment		
Property 1 (30,000 – 3,000)	27,000	
Property 2 (20,000 – 2,000)	18,000	45,000
Investment Property		

Property 3 (Fair value being Rs.27,000) (Cost = 24,000-2,400)	21,600

Case 2: If Stars Ltd. has applied the Revaluation Model to an entire class of property, plant and equipment.

Balance Sheet extracts as at 31st March 2017

Assets		**Rs.**
Non-current Assets		
Property, Plant and Equipment		
Property 1 (30,000 – 3,000 + 5,000)	32,000	
Property 2 (20,000 – 2,000 + 4,000)	22,000	54,000
Investment Properties		
Property 3 (Fair value being 27,000) (Cost = 24,000-2,400)		21,600
Equity and Liabilities		
Other Equity		
Revaluation Reserve *		
Property 1 (32,000 – 27,000)	5,000	
Property 2 (22,000 –18,000)	4,000	9,000

* Revaluation reserve should be routed through Other Comprehensive Income (OCI) (subsequently not reclassified to Profit and Loss) in the Statement of Profit and Loss and shown as a separate column in the Statement of Changes in Equity.

Question 3 : Nov 2018 – RTP

On 1st October, 2017, A Ltd. completed the construction of a power generating facility. The total construction cost was Rs.2,00,00,000. The facility was capable of being used from 1st October, 2017 but A Ltd. did not bring the facility into use until 1st January, 2018. The estimated useful life of the facility at 1st October, 2017 was 40 years. Under legal regulations in the jurisdiction in which A Ltd. operates, there are no requirements to restore the land on which power generating facilities stand to its original state at the end of the useful life of the facility. However, A Ltd. has a reputation for conducting its business in an environmentally friendly way and has previously chosen to restore similar land even in the absence of such legal requirements. The directors of A Ltd. estimated that the cost of restoring the land in 40 years' time (based on prices prevailing at that time) would be Rs.1,00,00,000. A relevant annual discount rate to use in any discounting calculations is 5%. When the annual discount rate is 5%, the present value of Rs.1 receivable in 40 years' time is approximately 0.142.

Analyse and present how the above events would be reported in the financial statements of A Ltd. for the year ended 31st March, 2018 as per Ind AS.

Solution :

1) As per Ind AS 16 PPE should be depreciated from when it ready for use and not from when it is put to use. i.e. Dep. Should start from 1/10/17.

2) As per Ind AS 37, provision should be made over if company has constructive obligation so A Ltd. should provide for site restoration.

3) Cost of PPE on 1/10/17

Construction Cost	2,00,00,000	
Site Restoration	14,20,000	(1,00,00,000 x 0.412)
	2,14,20,000	

4) Dep. For 17-18 to be charged to P&L

$\frac{2,14,20,000}{40} \times \frac{6}{12}$ = Rs.2,67,750

5) Closing PPE = 2,14,20,000

– Dep. 2,67,750

2,11,52,250

6) Finance cost on provision to be charged to P&L

$14,20,000 \times 5\% \times \frac{6}{12}$ = 35,500

7) Provision at end of year

= 14,20,000 + 35,500 = 14,55,500

8) Extracts of Balance Sheet

Asset		**Liability**	
NCA		NCL	
PPE	2,11,52,250	Provision	14,55,500

Question 4 : Nov 2018 – RTP / Nov 2019 – Paper

ABC Ltd is setting up a new refinery outside the city limits. In order to facilitate the construction of the refinery and its operations, ABC Ltd. is required to incur expenditure on the construction/development of railway siding, road and bridge. Though ABC Ltd. incurs (or contributes to) the expenditure on the construction/development, it will not have ownership rights on these items and they are also available for use to other entities and public at large. Whether ABC Ltd. can capitalise expenditure incurred on these items as property, plant and equipment (PPE)? If yes, how should these items be depreciated and presented in the financial statements of ABC Ltd. as per Ind AS?

Solution :

Ind AS 16 states that the cost of an item of property, plant and equipment shall be recognised as an asset if, and only if:

(a) it is probable that future economic benefits associated with the item will flow to the entity; and

(b) the cost of the item can be measured reliably.

In the given case, railway siding, road and bridge are required to facilitate the construction of the refinery and for its operations. Expenditure on these items is required to be incurred in order to get future economic benefits from the project as a whole which can be considered as the unit of measure for the purpose of capitalisation of the said expenditure even though the company cannot restrict the access of others for using the assets individually. It is apparent that the aforesaid expenditure is directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.

In view of this, even though ABC Ltd. may not be able to recognize expenditure incurred on these assets as an individual item of property, plant and equipment in many cases (where it cannot restrict others from using the asset), expenditure incurred may be capitalised as a part of overall cost of the project. From this, it can be concluded that, in the extant case the expenditure incurred on these assets, i.e., railway siding, road and bridge, should be considered as the cost of constructing the refinery and accordingly, expenditure incurred on these items should be allocated and capitalised as part of the items of property, plant and equipment of the refinery.

Question 5 : Nov 2018 – PAPER

On 1st April, 2017 Good Time Limited purchased some land for Rs.1.5 crore (including legal cost of Rs.10 lakhs) for the purpose of constructing a new factory. Construction work commenced on 1st May, 2017. Good Time Limited incurred the following costs in relation to its construction.

	Rs.
Preparation and levelling of the land	4,40,000
Purchase of materials for the construction	92,00,000
Employment costs of the construction workers (per month)	1,45,000
Overhead costs incurred directly on the construction of the factory (per month)	1,25,000
Ongoing overhead costs allocated to the construction project (using the company's normal overhead allocation model) per month	75,000
Costs of relocating employees to work at new factory	3,25,000
Costs of the opening ceremony on 1st January, 2018	2,50,000
Income received during the temporary use of the factory premises as a store during the construction period.	60,000

The construction of the factory was completed on 31st December, 2017 and production began on 1st February, 2018. The overall useful life of the factory building was estimated at 40 years from the date of completion. However, it is estimated that the roof will need to be replaced 20 years after the date of completion and that the cost of replacing the roof at current prices would be 25% of the total cost of the building.

At the end of the 40 years period, Good Time Limited has a legally enforceable obligation to demolish the factory and restore the site to its original condition. The company estimates that the cost of demolition in 40 year's time (based on price prevailing at that time) will be Rs.3 crore. The annual risk adjusted discount rate which is appropriate to this project is 8%. The present value of Rs.1 payable in 40 years time at an annual discount rate of 8% is 0.046.

The construction of the factory was partly financed. by a loan of Rs.1.4 crore taken out on 1st April, 2017. The loan was at an annual rate of interest of 9%. During the period 1st April, 2017 to 30th September, 2017 (when the loan proceeds had been fully utilized to finance the construction), Good Time Limited received investment income of Rs.1,25,000 on the temporary investment of the proceeds.

You are required to compute the cost of the factory and the carrying amount of the factory in the Balance Sheet of Good Time Limited as at 31st March, 2018.

Solution :

Computation of the cost of the factory

	Rs.
Purchase of land	1,50,00,000
Preparation and levelling	4,40,000
Materials	92,00,000
Employment costs of construction workers (1,45,000 x 8 months)	11,60,000
Direct overhead costs (1,25,000 x 8 months)	10,00,000
Allocated overhead costs	Nil
Income from use of a factory as a store	Nil
Relocation costs	Nil
Cost of the opening ceremony	Nil
Finance costs $(1,40,00,000 \times 9\% \times \frac{9}{12})$	9,45,000
Investment income on temporary investment of the loan proceeds	(1,25,000)
Demolition cost recognised as a provision (3,00,00,000 x 0.046)	13,80,000
Total	**2,90,00,000**

Computation of carrying amount of the factory as at 31st March, 2018

Rs.

		Land (Non-depreciable asset)	**Factory (Depreciable asset)**
Cost of the asset (Total cost 2,90,00,000)		1,50,00,000	1,40,00,000
Less: Depreciation			
On Land		Nil	
On Factory			
Depreciation on roof component (1,40,00,000 × 25% × 1/20 x 3/12)	43,750		
Depreciation on remaining factory (1,40,00,000 × 75% × 1/40 × 3/12)	65,625		(1,09,375)
Carrying amount of depreciable asset ie factory		1,50,00,000	1,38,90,625
Total cost			2,88,90,625

Note:

1. Interest cost has been capitalised based on nine month period. This is because, purchase of land would trigger off capitalisation.
2. All of the net finance cost of Rs.8,20,000 (Rs.9,45,000 – Rs.1,25,000) has been allocated to the depreciable asset i.e Factory. Alternatively, it can be allocated proportionately between land and factory.

Question 6 : May 2019 – RTP / May 2020 – RTP

Company X performed a revaluation of all of its plant and machinery at the beginning of 2018-2019. The following information relates to one of the machinery:

	Amount ('000)
Gross carrying amount	Rs.200
Accumulated depreciation (straight-line method)	Rs.80
Net carrying amount	Rs.120
Fair value	Rs.150

The useful life of the machinery is 10 years and the company uses Straight line method of depreciation. The revaluation was performed at the end of the 4th year.

How should the Company account for revaluation of plant and machinery and depreciation subsequent to revaluation?

Solution :

As per Ind AS 16 PPE can be revalued by using any one of the following 2 methods.

1) Adjust the gross carrying amount.

	Current	Revised
Gross	200	250
– Dep.	80	100
Net	120	150

		Dr	Cr
JE	PPE	50	
	To PFD		20
	To Revaluation Res.		30

2) Adjust the Net Carrying Amount

		Dr	Cr
JE	PFD	80	
	To Asset		80
	Asset	30	
	To Revaluation Res.		30

Note : 1) Revaluation Reserve will be routed through OCI.

2) Dep. For shall be 25 i.e. $\frac{250}{10}$ or $\frac{150}{6}$

Question 7 : Nov 2020 – RTP

Entity X has a warehouse which is closer to factory of Entity Y and vice versa. The factories are located in the same vicinity. Entity X and Entity Y agree to exchange their warehouses. The carrying value of warehouse of Entity X is Rs.1,00,000 and its fair value is Rs.1,25,000. It exchanges its warehouse with that of Entity Y, the fair value of which is Rs.1,20,000. It also receives cash amounting to Rs.5,000. How should Entity X account for the exchange of warehouses?

Solution :

As per IND AS 16, Asset acquired in exchange of Non-monetary Asset or combination of monetary and Non-monetary asset should be recorded at fair value unless
(a) the exchange lacks commercial substance or
(b) the fair value of asset received or given up is not available.
Also, in evaluating if exchange lacks commercial substance entity should evaluate the extent to which future cash flow shall be impacted. The exchange has commercial substance if
(a) The future cash flow from Asset received differs from that of Asset given.
(b) The entity operations are affected.
(c) The difference in (a) or (b) is to significant relative to fair value of Asset exchanged.
In the given case, the future cash flow or the operation want be affected and therefore transactions lacks commercial substance. The entity should record the Asset received at carrying amount of Asset given up. Cash received should be used to reduce the cost of Asset received.
Journal Entry

Asset A/c	Dr.	95,000	
Cash A/c	Dr.	5,000	
To Asset A/c.			1,00,000

Question 8 : Jan 2021 – Paper

On 1st April 2019, an entity purchased an office block (building) for Rs.50,00,000 and paid a non-refundable property transfer tax and direct legal cost of Rs.2,50,000 and Rs.50,000 respectively while acquiring the building.
During 2019, the entity redeveloped the building into two-story building. Expenditures on re-development were:

- Rs.1,00,000 Building plan approval;
- Rs.10,00,000 construction costs (including Rs.60,000 refundable purchase taxes); and
- Rs.40,000 due to abnormal wastage of material and labour.

When the re-development of the building was completed on 1st October 2019, the entity rents out Ground Floor of the building to its subsidiary under an operating lease in return for rental payment. The subsidiary uses the building as a retail outlet for its products. The entity kept first floor for its own administration and maintenance staff usage. Equal value can be attributed to each floor.
How will the entity account for all the above mentioned expenses in the books of account?
Also, discuss how the above building will be shown in Consolidated financial statement of the entity as a group and in its separate financial statements as per relevant Ind AS.

Solution :

In accordance with Ind AS 16, all costs required to bring an asset to its present location and condition for its intended use should be capitalised. Therefore, the initial purchase price of the building would be:

Particulars	Amount (Rs.)
Purchase amount	50,00,000
Non-refundable property tax	2,50,000

Direct legal cost	50,000
	53,00,000
Expenditures on redevelopment:	
Building plan approval	1,00,000
Construction costs (10,00,000 – 60,000)	9,40,000
Total amount to be capitalised at 1st October 2019	63,40,000

Treatment of abnormal wastage of material and labour:

As per Ind AS 16, the cost of abnormal amounts of wasted material, labour, or other resources incurred in self-constructing an asset is not included in the cost of the asset.

It will be charged to Profit and Loss in the year it is incurred. Hence, abnormal wastage of Rs. 40,000 will be expensed off in Profit & Loss in the financial year 2019-2020.

Accounting of property- Building

When the property is used as an administrative centre, it is not an investment property, rather it is an 'owner occupied property'. Hence, Ind AS 16 will be applicable.

When the property (land and/or buildings) is held to earn rentals or for capital appreciation (or both), it is an Investment property. Ind AS 40 prescribes the cost model for accounting of such investment property.

Since equal value can be attributed to each floor, Ground Floor of the building will be considered as Investment Property and accounted as per Ind AS 40 and First Floor would be considered as Property, Plant and Equipment and accounted as per Ind AS 16.

Cost of each floor = Rs.63,40,000 / 2 = Rs.31,70,000

As on 1st October 2019, the carrying value of building vis-à-vis its classification would be as follows:

(i) **In Separate Financial Statements:** The Ground Floor of the building will be classified as investment property for Rs.31,70,000, as it is property held to earn rentals. While First Floor of the building will be classified as item of property, plant and equipment for Rs.31,70,000.

(ii) **In Consolidated Financial Statements:** The consolidated financial statements present the parent and its subsidiary as a single entity. The consolidated entity uses the building for the supply of goods. Therefore, the leased-out property to a subsidiary does not qualify as investment property in the consolidated financial statements. Hence, the whole building will be classified as an item of Property, Plant and Equipment for Rs.63,40,000.

Question 9 : May 2021 – RTP

An entity has the following items of property, plant and equipment:

- Property A — a vacant plot of land on which it intends to construct its new administration headquarters;
- Property B — a plot of land that it operates as a landfill site;
- Property C — a plot of land on which its existing administration headquarters are built;
- Property D — a plot of land on which its direct sales office is built;
- Properties E1–E10 — ten separate retail outlets and the land on which they are built;

- Equipment A — computer systems at its headquarters and direct sales office that are integrated with the point of sale computer systems in the retail outlets;
- Equipment B — point of sale computer systems in each of its retail outlets;
- Furniture and fittings in its administrative headquarters and its sales office;
- Shop fixtures and fittings in its retail outlets.

How many classes of property, plant and equipment must the entity disclose?

Solution :

To answer this question one must make a materiality judgement.

A class of assets is defined as a grouping of assets of a similar nature and use in an entity's operations.

The nature of land without a building is different to the nature of land with a building.

Consequently, land without a building is a separate class of asset from land and buildings. Furthermore, the nature and use of land operated as a landfill site is different from vacant land. Hence, the entity should disclose Property A separately. The entity must apply judgement to determine whether the entity's retail outlets are sufficiently different in nature and use from its office buildings, and thus constitute a separate class of land and buildings.

The computer equipment is integrated across the organisation and would probably be classified as a single separate class of asset.

Furniture and fittings used for administrative purposes could be sufficiently different to shop fixtures and fittings in retail outlets. Hence, they should be classified in two separate classes of assets.

Question 10 : Nov 2021 – RTP

Heaven Ltd. had purchased a machinery on 1.4.2X01 for Rs. 30,00,000, which is reflected in its books at written down value of Rs. 17,50,000 on 1.4.2X06. The company has estimated an upward revaluation of 10% on 1.4.2X06 to arrive at the fair value of the asset. Heaven Ltd. availed the option given by Ind AS of transferring some of the surplus as the asset is used by an enterprise.

On 1.4.2X08, the machinery was revalued downward by 15% and the company also re-estimated the machinery's remaining life to be 8 years. On 31.3.2X10 the machinery was sold for Rs.9,35,000. The company charges depreciation on straight line method.

Prepare machinery account in the books of Heaven Ltd. over its useful life to record the above transactions.

Solution :

In the books of Heaven Ltd.

Machinery A/c

Date	Particulars	Amount	Date	Particulars	Amount
1.4.2X01	To Bank / Vendor	30,00,000	31.3.2X02	By Depreciation (W.N.1)	2,50,000
			31.3.2X02	By Balance c/d	27,50,000
		30,00,000			**30,00,000**
1.4.2X02	To Balance b/d	27,50,000	31.3.2X03	By Depreciation	2,50,000
			31.3.2X03	By Balance c/d	25,00,000
		27,50,000			**27,50,000**

1.4.2X03	To Balance b/d	25,00,000	31.3. 2X04 31.3.2X04	By Depreciation By Balance c/d	2,50,000 22,50,000
		25,00,000			**25,00,000**
1.4.2X04	To Balance b/d	22,50,000	31.3.2X05 31.3.2X05	By Depreciation By Balance c/d	2,50,000 20,00,000
		22,50,000			**22,50,000**
1.4.2X05	To Balance b/d	20,00,000	31.3.2X06 31.3.2X06	By Depreciation By Balance c/d	2,50,000 17,50,000
		20,00,000			**20,00,000**
1.4.2X06 1.4.2X06	To Balance b/d To Revaluation Reserve @ 10%	17,50,000 1,75,000	31.3.2X07 31.3.2X07	By Depreciation (W.N.2) By Balance c/d	2,75,000 16,50,000
		19,25,000			**19,25,000**
1.4.2X07	To Balance b/d	16,50,000	31.3.2X08 31.3.2X08	By Depreciation By Balance c/d	2,75,000 13,75,000
		16,50,000			**16,50,000**
1.4.2X08	To Balance b/d	13,75,000	1.4.2X08 31.3.2X09 31.3.2X09 31.3.2X09	By Revaluation Reserve (W.N.4) By Profit and Loss A/c (W.N.5) By Depreciation (W.N.3) By Balance c/d	1,25,000 81,250 1,46,094 10,22,656
		13,75,000			**13,75,000**
1.4.2X09 31.3.2X10	To Balance b/d To Profit and Loss A/c (balancing figure)	10,22,656 58,438*	31.3.2X10 31.3.2X10	By Depreciation By Bank A/c	1,46,094 9,35,000
		10,81,094			**10,81,094**

Working Notes:

1. Calculation of useful life of machinery on 1.4.2X01

Depreciation charge in 5 years = (30,00,000 – 17,50,000) = Rs. 12,50,000

Depreciation per year as per Straight Line method = 12,50,000 / 5 years
= Rs. 2,50,000

Remaining useful life = Rs. 17,50,000 / Rs. 2,50,000 = 7 years

Total useful life = 5 years + 7 years = 12 years

2. Depreciation after upward revaluation as on 31.3.2X06

	Rs.
Book value as on 1.4.2X06	17,50,000
Add: 10% upward revaluation	1,75,000
Revalued amount	19,25,000

Remaining useful life 7 years (Refer W.N.1)

Depreciation on revalued amount = 19,25,000 / 7 years = Rs. 2,75,000 lakh

3. Depreciation after downward revaluation as on 31.3.2X08

	Rs.
Book value as on 1.4.2X08	13,75,000
Less: 15% Downward revaluation	(2,06,250)
Revalued amount	11,68,750

Revised useful life 8 years

Depreciation on revalued amount = 11,68,750 / 8 years = Rs. 1,46,094

4. Amount transferred from revaluation reserve

Revaluation reserve on 1.4.2X06 (A) Rs. 1,75,000

	Remaining useful life 7 years	
	Amount transferred every year (1,75,000 / 7)	Rs. 25,000
	Amount transferred in 2 years (25,000 x 2) (B)	Rs. 50,000
	Balance of revaluation reserve on 1.4.2X08 (A-B)	Rs. 1,25,000
5.	**Amount of downward revaluation to be charged to Profit and Loss Account**	
	Downward revaluation as on 1.4.2X08 (W.N.3)	Rs. 2,06,250
	Less: Adjusted from Revaluation reserve (W.N.4)	(Rs. 1,25,000)
	Amount transferred to Profit and Loss Account	Rs. 81,250

Question 11 : May 2022 – RTP

On 1st January, 20X1 an entity purchased an item of equipment for Rs. 600,000, including Rs. 50,000 refundable purchase taxes. The purchase price was funded by raising a loan of Rs. 605,000. In addition, the entity has to pay Rs. 5,000 in loan raising fees to the Bank. The loan is secured against the equipment.

In January 20X1 the entity incurred costs of Rs. 20,000 in transporting the equipment to the entity's site and Rs. 100,000 in installing the equipment at the site. At the end of the equipment's 10-year useful life the entity is required to dismantle the equipment and restore the building housing the equipment. The present value of the cost of dismantling the equipment and restoring the building is estimated to be Rs. 100,000.

In January 20X1 the entity's engineer incurred the following costs in modifying the equipment so that it can produce the products manufactured by the entity:

- Materials – Rs. 55,000
- Labour – Rs. 65,000
- Depreciation of plant and equipment used to perform the modifications – Rs. 15,000

In January 20X1, the entity's production staff were trained in how to operate the new item of equipment. Training costs included:

- Cost of an expert external instructor – Rs. 7,000
- Labour – Rs. 3,000

In February 20X1 the entity's production team tested the equipment and the engineering team made further modifications necessary to get the equipment to function as intended by management. The following costs were incurred in the testing phase:

- Materials, net of Rs. 3,000 recovered from the sale of the scrapped output – Rs. 21,000
- Labour – Rs. 16,000

The equipment was ready for use on 1st March, 20X1. However, because of low initial order levels the entity incurred a loss of Rs. 23,000 on operating the equipment during March. Thereafter the equipment operated profitably.

What is the cost of the equipment at initial recognition?

Solution :

Description	Calculation or reason	Rs.
Purchase price	Rs. 600,000 purchase price minus Rs. 50,000 refundable purchase taxes	550,000

Loan raising fee	Offset against the measurement of the liability	-
Transport cost	Directly attributable expenditure	20,000
Installation costs	Directly attributable expenditure	100,000
Environmental restoration costs	The obligation to dismantle and restore the environment arose from the installation of the equipment	100,000
Preparation costs	Rs. 55,000 materials + Rs. 65,000 labour + Rs. 15,000 depreciation	135,000
Training costs	Recognised as expenses in profit and loss account. The equipment was capable of operating in the manner intended by management without incurring the training costs.	-
Cost of testing	Rs. 21,000 materials (ie net of the Rs. 3,000 recovered from the sale of the scrapped output) + Rs. 16,000 labour	37,000
Operating loss	Recognised as expenses in profit and loss account	-
Borrowing costs	Recognised as expenses in profit and loss account	-
Cost of equipment		**9,42,000**

Thanks ....

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IND AS – 40
INVESTMENT PROPERTY

CHAPTER - 5

Question 1 : Nov 2018 – RTP

X Ltd. is engaged in the construction industry and prepares its financial statements up to 31st March each year. On 1st April, 2013, X Ltd. purchased a large property (consisting of land) for Rs.2,00,00,000 and immediately began to lease the property to Y Ltd. on an operating lease. Annual rentals were Rs.20,00,000. On 31st March, 2017, the fair value of the property was Rs.2,60,00,000. Under the terms of the lease, Y Ltd. was able to cancel the lease by giving six months' notice in writing to X Ltd. Y Ltd. gave this notice on 31st March, 2017 and vacated the property on 30th September, 2017. On 30th September, 2017, the fair value of the property was Rs.2,90,00,000. On 1st October, 2017, X Ltd. immediately began to convert the property into ten separate flats of equal size which X Ltd. intended to sell in the ordinary course of its business. X Ltd. spent a total of Rs.60,00,000 on this conversion project between 30th September, 2017 to 31st March, 2018. The project was incomplete at 31st March, 2018 and the directors of X Ltd. estimate that they need to spend a further Rs.40,00,000 to complete the project, after which each flat could be sold for Rs.50,00,000.
Examine and show how the three events would be reported in the financial statements of X Ltd. for the year ended 31st March, 2018, as per IND AS.

Solution :

1) From 1st April, 2013, the property would be regarded as an investment property since it is being held for its investment potential rather than being owner occupied or developed for sale.
   The property would be measured under the cost model. This means it will be measured at Rs.2,00,00,000 at each year end.
2) On 30th September, 2017, the property ceases to be an investment property. X Ltd. begins to develop it for sale as flats. The increase in the fair value of the property from 31st March, 2017 to 30th September, 2017 of Rs.30,00,000 (Rs.29,00,000 –Rs.26,00,000) would be recognised in P/L for the year ended 31st March, 2018.
   Since the lease of the property is an operating lease, rental income of Rs.10,00,000 (Rs.20,00,000 x 6/12) would be recognised in P/L for the year ended 31st March, 2018.
   When the property ceases to be an investment property, it is transferred into inventory at its then fair value of Rs.2,90,00,000. This becomes the initial 'cost' of the inventory.
3) The additional costs of Rs.60,00,000 for developing the flats which were incurred up to and including 31st March, 2018 would be added to the 'cost' of inventory to give a closing cost of Rs.3,50,00,000.

The total selling price of the flats is expected to be Rs.5,00,00,000 (10 x Rs.50,00,000). Since the further costs to develop the flats total Rs.40,00,000, their net realisable value is Rs.4,60,00,000 (Rs.5,00,00,000 – Rs.40,00,000), so the flats will be measured at a cost of Rs.3,50,00,000.

The flats will be shown in inventory as a current asset

Question 2 : Nov 2020 – RTP

Shaurya Limited owns Building A which is specifically used for the purpose of earning rentals. The Company has not been using the building A or any of its facilities for its own use for a long time. The company is also exploring the opportunities to sell the building if it gets the reasonable amount in consideration.

Following information is relevant for Building A for the year ending 31st March, 2020:

Building A was purchased 5 years ago at the cost of Rs.10 crore and building life is estimated to be 20 years. The company follows straight line method for depreciation.

During the year, the company has invested in another Building B with the purpose to hold it for capital appreciation. The property was purchased on 1st April, 2019 at the cost of Rs.2 crore. Expected life of the building is 40 years. As usual, the company follows straight line method of depreciation.

Further, during the year 2019-2020, the company earned / incurred following direct operating expenditure relating to Building A and Building B:

Rental income from Building A	=	Rs.75 lakh
Rental income from Building B	=	Rs.25 lakh
Sales promotion expenses	=	Rs.5 lakh
Fees & Taxes	=	Rs.1 lakh
Ground rent	=	Rs.2.5 lakh
Repairs & Maintenance	=	Rs.1.5 lakh
Legal & Professional	=	Rs.2 lakh
Commission and brokerage	=	Rs.1 lakh

The company does not have any restrictions and contractual obligations against buildings - A and B. For complying with the requirements of Ind AS, the management sought an independent report from the specialists so as to ascertain the fair value of buildings A and B. The independent valuer has valued the fair value of property as per the valuation model recommended by International valuation standards committee. Fair value has been computed by the method by streamlining present value of future cash flows namely, discounted cash flow method.

The other key inputs for valuation are as follows:

The estimated rent per month per square feet for the period is expected to be in the range of Rs.50 - Rs.60. It is further expected to grow at the rate of 10 percent per annum for each of 3 years. The weighted discount rate used is 12% to 13%.

Assume that the fair value of properties based on discounted cash flow method is measured at Rs.10.50 crore on 31st March, 2020.

What would be the treatment of Building A and Building B in the balance sheet of Shaurya Limited? Provide detailed disclosures and computations in line with relevant Indian accounting standards. Treat it as if you are preparing a separate note or schedule, of the given assets in the balance sheet.

Solution :

1) As per IND AS 40, Investment Property is defined as property held to earn rentals or for capital appreci0ation or both rather than for use in production or supply of goods or services or for administrative purpose or sale in ordinary course of businesss.

2) Investment property should be initially measured at cost and subsequently should be measured at cost as per IND AS 16, cost model.

3) Investment property for year ended 31/3/2020.

Building A	–	Cost	10 Cr.
	–	Accumulated dep.	2.5 Cr.
			7.5 Cr.
Building B	–	Cost	2 Cr.
	–	Accumulated dep.	0.05 Cr.
			1.95 Cr.

4) Income statement for year 19-20

Rentals Income (75 + 25)	100
– Direct Expenses (5 + 1 + 2.5 + 1.5 + 2 + 1)	13
	87
– Deprecation (0.5 + 0.05)	55
	32

5) Disclosure

(a) Fair value of investment property 10.5 Cr. as per independent valuer, who are specialist in valuing investment properties.

(b) The company has no restrictions on the realisability of its investment properties and no contractual obligations to purchase. Construct or develop investment properties or for repairs, maintenance and enhancement.

(c) Description of valuation of techniques method – Discounted cash flow method

= Estimated Rental / sq.ft.	=	Rs.50 to Rs.60
= Rental growth	=	10% every 3 years
= Discount Rate	=	12% to 13%

Question 3 : May 2021 – RTP

X Ltd owned a land property whose future use was not determined as at 31 March 20X1. How should the property be classified in the books of X Ltd as at 31 March 20X1?

During June 20X1, X Ltd commenced construction of office building on it for own use. Presuming that the construction of the office building will still be in progress as at 31 March 20X2

(a) How should the land property be classified by X Ltd in its financial statements as at 31 March 20X2?

(b) Will there be a change in the carrying amount of the property resulting from any change in use of the investment property?

(c) Whether the change in classification to, or from, investment properties is a change in accounting policy to be accounted for in accordance with Ind AS 8, Accounting Policies, Changes in Accounting Estimates and Errors?

(d) Would your answer to (a) above be different if there were to be a management intention to commence construction of an office building for own use; however, no construction activity was planned by 31 March 20X2?

Solution :

As per paragraph 8(b) of Ind AS 40, any land held for currently undetermined future use, should be classified as an investment property. Hence, in this case, the land would be regarded as held for capital appreciation. Hence the land property should be classified by X Ltd as investment property in the financial statements as at 31 March 20X1.

As per Para 57 of the Standard, an entity can change the classification of any property to, and from, an investment property when and only when evidenced by a change in use. A change occurs when the property meets or ceases to meet the definition of investment property and there is evidence of the change in use. Mere management's intention for use of the property does not provide evidence of a change in use.

(a) Since X Ltd has commenced construction of office building on it for own use, the property should be reclassified from investment property to owner occupied as at 31 March 20X2.

(b) As per Para 59, transfers between investment property, owner occupied and inventories do not change the carrying amount of the property transferred and they do not change the cost of the property for measurement or disclosure purposes.

(c) No. The change in classification to, or from, investment properties is due to change in use of the property. No retrospective application is required and prior period's financial statements need not be re-stated.

(d) Mere management intentions for use of the property do not evidence change in use. Since X Ltd has no plans to commence construction of the office building during 20X1-20X2, the property should continue to be classified as an investment property by X Ltd in its financial statements as at 31 March 20X2.

Question 4 : July 2021 – Paper

Special Limited is a multinational entity that owns 3 properties. All 3 properties were purchased on 1st April, 2020. The following details were furnished :

Particulars	Property 1	Property 2	Property 3
Purchase price	Rs.750,000	Rs.1,050,000	Rs.1,200,000
Estimated life	10 years	15 years	15 years

Fai value as on 31st March, 2021	Rs.800,000	Rs.950,000	Rs.1,300,000

The Company uses Property 1 and Property 2 for its business purposes. The Company is exploring the opportunity to sell Property 3 if it gets reasonable consideration. Till the time it is not sold, the company has rented the property.

It has adopted revaluation model for subsequent measurement of these properties. The depreciation is charged on straight line method. However, the Company has not charged any depreciation on Property 1 and Property 3 for the current year since the fair value of properties exceeds their carrying amount. The difference between their fair value and carrying amount has been recognized in the statement of profit and loss. The properties are shown under the head Property, plant and equipment in the Balance sheet.

Analyze whether the accounting policies adopted by the Company in relation to the given properties are in accordance with Ind AS. If not, advise the correct treatment and present an extract of the Balance Sheet for the year ended 31st March, 2021.

Solution :

(a) Preamble:

The given issue needs to be examined in the umbrella of the provisions given in Ind AS 1 'Presentation of Financial Statements', Ind AS 16 'Property, Plant and Equipment' in relation to property '1' and '2' and Ind AS 40 'Investment Property' in relation to property '3'.

Guidance given in relevant Ind AS:

1. Property '1' and '2'

Definition and applicability:

As per Ind AS 16, Property plant and equipment are tangible items that:

(a) are held for use in the production or supply of goods or services or for administrative purposes; and

(b) are expected to be used during more than one period.

Hence, property 1 and 2 are held for use in the business, therefore Ind AS 16 shall apply in respect of these two properties.

Accounting Principles:

- If an asset's carrying amount is increased as a result of a revaluation, the increase shall be recognised in other comprehensive income and accumulated in equity under the heading of revaluation surplus. However, the increase shall be recognised in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognised in profit or loss.
- If an asset's carrying amount is decreased as a result of revaluation, the decrease shall be recognised in profit and loss statement.

2. Property '3'

Definition and applicability:

As per Ind AS 40, Investment property is property held to earn rentals or for capital appreciation or both, rather than for:

- Use in the production of goods or services or for administrative purposes; or
- Sale in the ordinary course of business.

Therefore, property 3 is an investment property and company shall follow cost model for its subsequent measurement.

Accounting Principles:

- An entity shall adopt as its accounting policy the cost model to all of its investment property; and (Refer paragraph 30 of Ind AS 40)
- requires that an entity shall disclose the fair value of investment property. (Refer paragraph 79 (e) of Ind AS 40

Further, paragraph 54 (2) of Ind AS 1 'Presentation of Financial Statements' requires that as a minimum, the balance sheet shall include line items that present the following amounts:

a. Property, Plant and Equipment
b. Investment Property.

Analysis:

As per the facts given in the question, Special Ltd. has

a. Presented all three properties in balance sheet as 'property, plant and equipment';
b. Not charged depreciation to Property '1' and '3';
c. Upward revaluation is recognised in the statement of profit and loss as profit; and
d. Applied revaluation model to Property '3' being classified as Investment Property.

The above accounting treatment is neither correct nor in accordance with provision of Ind AS 1, Ind AS 16 and Ind AS 40.

Accordingly, Special Ltd. shall depreciate Property 1 irrespective of the fact that, their fair value exceeds the carrying amount. The revaluation gain shall be recognised in other comprehensive income and accumulated in equity under the heading of revaluation surplus.

There is no alternative of revaluation model in respect to property '3' being classified as Investment Property and only cost model is permitted for subsequent measurement. However, Special Ltd. is required to disclose the fair value of the property in the Notes to Accounts. Further, Property '3' shall be presented as separate line item as Investment Property and depreciation should be charged on it as well.

Therefore, as per the provisions of Ind AS 1, Ind AS 16 and Ind AS 40, the presentation of these three properties in the balance sheet will be as follows:

Balance Sheet (extracts) as at 31st March, 2021

Assets	**Rs.**
Non-Current Assets	

Property, Plant and Equipment		
Property '1'	8,00,000	
Property '2'	9,50,000	17,50,000
Investment Properties		
Property '3' (1,200,000 – 80,000)		11,20,000
Equity and Liabilities		
Other Equity		
Revaluation Reserve		
Property '1' [8,00,000 – (7,50,000 – 75,000)]		1,25,000

The revaluation reserve should be routed through Other Comprehensive Income (subsequently not reclassified to Profit and Loss) and shown in a separate column under Statement of Changes in Equity.

Working Notes:

Particulars	**Property 1**	**Property 2**	**Property 3**
Purchase Price	Rs. 7,50,000	Rs. 10,50,000	Rs. 12,00,000
Estimated Life	10 years	15 years	15 years
Depreciation for the year	Rs. 75,000	Rs. 70,000	Rs. 80,000
Carrying Value as on 31st March, 2021	Rs. 6,75,000	Rs. 9,80,000	Rs. 11,20,000
Fair Value as on 31st March, 2021	Rs. 8,00,000	Rs. 9,50,000	Rs. 13,00,000
Subsequent Measurement	Fair Value	Fair Value	Cost
Revaluation Surplus / (Deficit)	Rs. 1,25,000	(Rs. 30,000)	

Thanks ....

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IND AS – 38
INTANGIBLE ASSETS

CHAPTER - 6

Question 1 : Nov 2018 – RTP

A Ltd. intends to open a new retail store in a new location in the next few weeks. It has spent a substantial sum on a series of television advertisements to promote this new store. It has paid for advertisements costing Rs.8,00,000 before 31st March, 2018. Rs.7,00,000 of this sum relates to advertisements shown before 31st March, 2018 and Rs.1,00,000 to advertisements shown in April, 2018. Since 31st March, 2018, A Ltd. has paid for further advertisements costing Rs.4,00,000. The accountant charged all these costs as expenses in the year to 31 March 2018. However, CFO of A Ltd. does not want to charge Rs.12,00,000 against 2017-2018 profits. He believes that these costs can be carried forward as intangible assets because the company's market research indicates that this new store is likely to be highly successful.
Examine and justify the treatment of these costs of Rs.12,00,000 in the financial statements for the year ended 31st March, 2018 as per Ind AS.

Solution :

Ind AS 38 specifically prohibits recognising advertising expenditure as an intangible asset. Irrespective of success probability in future, such expenses have to be recognized in profit or loss. Therefore, the treatment given by the accountant is correct since such costs should be recognised as expenses.
However, the costs should be recognised on an accruals basis.

(a) For Year 17 - 18

Total Amt. paid = Rs.8,00,000 out of which Rs.7,00,000 should be charged to P&L for year 17-18 and Rs.1,00,000 should be show as prepaid expenses.

(b) For year 18-19

Further Amt. paid was Rs.4,00,000. Total Rs.5,00,000 should be charged to P&L for year 18-19.

Question 2 : May 2019 – RTP

As part of its business expansion strategy, KK Ltd. is in process of setting up a pharma intermediates business which is at very initial stage. For this purpose, KK Ltd. has acquired on 1st April, 2018, 100% shares of ABR Ltd. that manufactures pharma intermediates. The purchase consideration for the same was by way of a share exchange valued at Rs.35 crores. The fair value of ABR Ltd.'s net assets was Rs.15 crores, but does not include:

(i) A patent owned by ABR Ltd. for an established successful intermediate drug that has a remaining life of 8 years. A consultant has estimated the value of this patent to be Rs.10

crores. However, the outcome of clinical trials for the same are awaited. If the trials are successful, the value of the drug would fetch the estimated Rs.15 crores.

(ii) ABR Ltd. has developed and patented a new drug which has been approved for clinical use. The cost of developing the drug was Rs.12 crores. Based on early assessment of its sales success, the valuer has estimated its market value at Rs.20 crores.

(iii) ABR Ltd.'s manufacturing facilities have received a favourable inspection by a government department. As a result of this, the Company has been granted an exclusive five-year license to manufacture and distribute a new vaccine. Although the license has no direct cost to the Company, its directors believe that obtaining the license is a valuable asset which assures guaranteed sales and the value for the same is estimated at Rs.10 crores.

KK Ltd. has requested you to suggest the accounting treatment of the above transaction under applicable Ind AS.

Solution :

As per Ind AS 103 'Business Combination', the acquirer's application of the recognition principle and conditions may result in recognising some assets and liabilities that the acquiree had not previously recognised as assets and liabilities in its financial statements. This may be the case when the asset is developed by the entity internally and charged the related costs to expense.

Based on the above, the company can recognise following Intangible assets while determining Goodwill / Bargain Purchase for the transaction:

(i) **Patent owned by ABR Ltd.:** The patent owned will be recognised at fair value by KK Ltd. even though it was not recognised by ABR Ltd. in its financial statements. The patent will be amortised over the remaining useful life of the asset i.e. 8 years.

Since the company is awaiting the outcome of the trials, the value of the patent cannot be estimated at Rs.15 crore and the extra Rs.5 crore should only be disclosed as a Contingent Asset and not recognised.

(ii) **Patent internally developed by ABR Ltd.:** As per para 18 of Ind AS 103 'Business Combination', the acquirer shall measure the identifiable assets acquired and the liabilities assumed at their acquisition date fair values. Since the patent developed has been approved for clinical use, it is an identifiable asset, hence the same will be measured at fair value i.e. Rs.20 crore on the acquisition date.

(iii) **Grant of Licence to ABR Ltd. by the Government:** As regards to the five-year license, applying para 18 of Ind AS 103, grant asset will be recognised at fair value on the acquisition date by KK Ltd. On acquisition date, the fair value of the license is Rs.10 crore. However, since the question does not mention about the fair value of the identifiable liability with respect to grant of license for the acquirer, it is assumed that no conditions with respect to compliance of grant (if any) have been passed to the acquirer. Hence, the fair value of the liability with respect to grant, for acquirer would be nil. Only, the grant asset (license) would be recognised at Rs.10 crore in the books of acquirer KK Ltd.

Hence the revised working would be as follows:

Fair value of net assets of ABR Ltd.	Rs.15 crore
Add: Patent (10 + 20)	Rs.30 crore

Add: License	Rs.10 crore
Less: Grant for License	(Nil)
	Rs.55 crores
Purchase Consideration	(Rs.35 crores)
Bargain purchase	Rs.20 crore

Question 3 : Nov 2019 – PAPER

MNC Ltd. is in process of setting up a medicine manufacturing business which is at very initial stage. For this purpose, MNC Ltd. as part of its business expansion strategy acquired on 1st April, 2019, 100% shares of Akash Ltd., a company that manufactures pharmacy products. The purpose consideration for the same was by way of a share exchange valued at Rs.38 crores. The fair value of Akash Ltd.'s assets and liabilities were Rs.68 crores and Rs.50 crores respectively, but the same does not include the following :

(i) A parent owned by Akash Ltd. for an established successful new drug that has a remaining life of 6 years. A consultant has estimated the value of this patent to bee Rs.8 crores. However, the outcome of clinical trials for the same are awaited. If the trails are successful, the value of the drug would fetch the estimated Rs.12 crores.

(ii) Akash Ltd. has developed and patented another new drug which has been approved for clinical use. The cost of developing the drug was Rs.13 crores. Based on early assessment of its sales success, a reputed values has estimated is market value at Rs.19 crores. However, there is no active market for the patent.

(iii) Akash Ltd.'s manufacturing facilities have received a favourable inspection by a government department. As a result of this, the company has been granted an exclusive five-year license on 1st April, 2018 to manufacture and distribute a new vaccine. Although the license has no direct cost to the Company, its directors believe that obtaining the license is a valuable asset which assures guaranteed sales and the cost to acquire the license is estimated at Rs.7 crores for remaining period of life. It is expected to generate at least equivalent revenue.

Suggest the accounting treatment of the above transactions with reasoning under applicable Ind AS in e books of MNC Ltd.

Solution :

As per Ind AS 103 'Business Combination', the acquirer's application of the recognition principle and conditions may result in recognising some assets and liabilities that the acquiree had not previously recognised as assets and liabilities in its financial statements. This may be the case when the asset is developed by the entity internally and charged the related costs to expense.

Based on the above, the company can recognise following Intangible assets while determining Goodwill / Bargain Purchase for the transaction:

(i) **Patent owned by Akash Ltd.:** The patent owned will be recognised at fair value by MNC Ltd. even though it was not recognised by Akash Ltd. in its financial statements. The patent will be amortised over the remaining useful life of the asset i.e. 6 years. Since the company is awaiting the outcome of the trials, the value of the patent should be valued at Rs.8 crore.

It cannot be estimated at Rs.12 crore and the extra Rs.4 crore should only be disclosed as a contingent asset and not recognised.

(ii) **Patent internally developed by Akash Ltd.:** As per para 18 of Ind AS 103 'Business Combination', the acquirer shall measure the identifiable assets acquired and the liabilities assumed at their acquisition date fair values. Since the patent developed has been approved for clinical use, it is an identifiable asset, hence the same will be measured at fair value i.e. Rs.19 crore on the acquisition date.

(iii) **Grant of Licence to Akash Ltd. by the Government:** As regards to the five-year license, applying para 18 of Ind AS 103, grant asset will be recognised at fair value on the acquisition date by MNC Ltd. On acquisition date, the fair value of the license asset is Rs.7 crore. However, since the question does not mention about the fair value of the identifiable liability with respect to grant of license for the acquirer, it is assumed that the fair value of the liability with respect to grant, for acquirer is nil. Therefore, only, the grant asset (license) would be recognised at Rs.7 crore in the books of acquirer MNC Ltd.

Hence the revised working would be as follows:

Fair value of net assets of Akash Ltd. (68-50)	Rs.18 crore
Add: Patent (8 + 19)	Rs.27 crore
Add: License	Rs.7 crore
Less: Grant for License	(Nil)
	Rs.52 crore
Purchase Consideration	(Rs.38 crore)
Capital Reserve	Rs.14 crore

Question 4 : May 2020 – RTP

One of the senior engineers at XYZ has been working on a process to improve manufacturing efficiency and, consequently, reduce manufacturing costs. This is a major project and has the full support of XYZ's board of directors. The senior engineer believes that the cost reductions will exceed the project costs within twenty four months of their implementation. Regulatory testing and health and safety approval was obtained on 1 June 20X5. This removed uncertainties concerning the project, which was finally completed on 20 April 20X6. Costs of Rs.18,00,000, incurred during the year till 31st March 20X6, have been recognized as an intangible asset. An offer of Rs.7,80,000 for the new developed technology has been received by potential buyer but it has been rejected by XYZ. Utkarsh believes that the project will be a major success and has the potential to save the company Rs.12,00,000 in perpetuity. Director of research at XYZ, Neha, who is a qualified electronic engineer, is seriously concerned about the long term prospects of the new process and she is of the opinion that competitors would have developed new technology at some time which would require to replace the new process within four years. She estimates that the present value of future cost savings will be Rs.9,60,000 over this period. After that, she thinks that there is no certainty about its future. What would be the appropriate accounting treatment of aforesaid issue?

Solution :

Ind AS 38 'Intangible Assets' requires an intangible asset to be recognised if, and only if, certain criteria are met. Regulatory approval on 1 June 20X5 was the last criterion to be met, the other criteria have been met as follows:

- Intention to complete the asset is apparent as it is a major project with full support from board
- Finance is available as resources are focused on project
- Costs can be reliably measured
- Benefits are expected to exceed costs – (in 2 years)

Amount of Rs.15,00,000 (rs.18,00,000 x 10/12) should be capitalised in the Balance sheet of year ending 20X5-20X6 representing expenditure since 1 June 20X5.

The expenditure incurred prior to 1 June 20X5 which is Rs.3,00,000 (2/12 x Rs.18,00,000) should be recognised as an expense, retrospective recognition of expense as an asset is not allowed.

Ind AS 36 'Impairment of assets' requires an intangible asset not yet available for use to be tested for impairment annually.

Cash flow of Rs.12,00,000 in perpetuity would clearly have a present value in excess of Rs.12,00,000 and hence there would be no impairment. However, the research director is technically qualified, so impairment tests should be based on her estimate of a four-year remaining life and so present value of the future cost savings of Rs.9,60,000 should be considered in that case.

Rs.9,60,000 is greater than the offer received (fair value less costs to sell) of Rs.7,80,000 and so Rs.9,60,000 should be used as the recoverable amount.

So, the carrying amount should be consequently reduced to Rs.9,60,000.

Calculation of Impairment loss:

Particulars	**Amount Rs.**
Carrying amount (Restated)	15,00,000
Less: Recoverable amount	9,60,000
Impairment loss	5,40,000

Impairment loss of Rs.5,40,000 is to be recognised in the profit and loss for the year 20X5-20X6.

Necessary adjusting entry to correct books of account will be:

		Rs.	**Rs.**
Operating expenses- Development expenditure	Dr.	3,00,000	
Operating expenses–Impairment loss of intangible assets	Dr.	5,40,000	
To Intangible assets – Development expenditure			8,40,000

Question 5 : Nov 2020 – RTP

ABC Pvt. Ltd., recruited a player. As per the terms of the contract, the player is prohibited from playing for any other entity for coming 5 years and have to in the employment with the company and cannot leave the entity without mutual agreement. The price the entity paid to acquire this right is derived from the skills and fame of the said player. The entity uses and develops the player through participation in matches. State whether the cost incurred to obtain the right regarding the player can be recognised as an intangible asset as per Ind AS 38?

Solution :

As per Ind AS 38, for an item to be recognised as an intangible asset, it must meet the definition of an intangible asset, i.e., identifiability, control over a resource and existence of future economic benefits and also recognition criteria.

With regard to establishment of control, paragraph 13 of Ind AS 38 states that an entity controls an asset if the entity has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits. The capacity of an entity to control the future economic benefits from an intangible asset would normally stem from legal rights that are enforceable in a court of law. In the absence of legal rights, it is more difficult to demonstrate control. However, legal enforceability of a right is not a necessary condition for control because an entity may be able to control the future economic benefits in some other way.

Further, paragraph 15 of Ind AS 38 provides that an entity may have a team of skilled staff and may be able to identify incremental staff skills leading to future economic benefits from training. The entity may also expect that the staff will continue to make their skills available to the entity. However, an entity usually has insufficient control over the expected future economic benefits arising from a team of skilled staff and from training for these items to meet the definition of an intangible asset. For a similar reason, specific management or technical talent is unlikely to meet the definition of an intangible asset, unless it is protected by legal rights to use it and to obtain the future economic benefits expected from it, and it also meets the other parts of the definition.

Since the right in the instant case is contractual, identifiability criterion is satisfied. Based on the facts provided in the given case, the player is prohibited from playing in other teams by the terms of the contract which legally binds the player to stay with ABC Ltd for 5 years.

Accordingly, in the given case, the company would be able to demonstrate control. Future economic benefits are expected to arise from use of the player in matches. Further, cost of obtaining rights is also reliably measurable. Hence, it can recognise the costs incurred to obtain the right regarding the player as an intangible asset. However, careful assessment of relevant facts and circumstances of each case is required to be made.

Question 6 : Jan 2021 – Paper

Super Sounds Limited had the following transactions during the Financial Year 2019-2020.

(i) On 1st April 2019, Super Sounds Limited purchased the net assets of Music Limited for Rs.13,20,000. The fair value of Music Limited's identifiable net assets was Rs.10,00,000. Super Sounds Limited is of the view that due to popularity of Music Limited's product, the life of goodwill is 10 years.

(ii) On 4th May 2019, Super Sounds Limited purchased a Franchisee to organize musical shows from Armaan TV for Rs.80,00,000 and at an annual fee of 2% of musical shows revenue. The Franchisee expires after 5 years. Musical shows revenue were Rs.10,00,000 for financial year 2019-2020. The projected future revenues for financial year 2020-2021 is Rs.25,00,000 and Rs.30,00,000 p.a. for remaining 3 years thereafter.

(iii) On 4th July 2019, Super Sounds Limited was granted a Copyright that had been applied for by Music Limited. During financial year 2019-2020, Super Sound Limited incurred

Rs.2,50,000 on legal cost to register the Patent and Rs.7,00,000 additional cost to successfully prosecute a copyright infringement suit against a competitor.
The life of the Copyright is for 10 years.

Super Sound Limited follows an accounting policy to amortize all intangible on SLM (Straight Line Method) basis or any appropriate basis over a maximum period permitted by relevant Ind AS, taking a full year amortization in the year of acquisition.

You are required to prepare:

(i) A Schedule showing the intangible section in Super Sound Limited Balance Sheet as on 31st March 2020, and

(ii) A Schedule showing the related expenses that would appear in the Statement of Profit and Loss of Super Sound Limited for the year ended 2019-2020.

Solution :

(i) Super Sounds Limited

Balance Sheet (Extract relating to intangible asset) as at 31st March 2020

	Note no.	Rs.
Assets		
(1) Non- current asset		
Intangible assets	1	69,45,000

(ii) Super Sounds Limited

Statement of Profit and Loss (Extract)

for the year ended 31st March 2020

	Note no.	Rs.
Revenue from Operations		10,00,000
Total Revenue		
Expenses:		
Amortization expenses	2	16,25,000
Other expenses	3	7,20,000
Total Expenses		

Notes to Accounts (Extract)

1. Intangible Assets

		Gross Block (Cost)			Accumulated amortisation			Net Block	
		Opening balance Rs.	Additions Rs.	Closing Balance Rs.	Opening balance Rs.	Additions Rs.	Closing Balance Rs.	Opening balance Rs.	Closing Balance Rs.
1	Goodwill* (W.N.1)	-	3,20,000	3,20,000	-	-	-	-	3,20,000
2	Franchise** (W.N.2)	-	80,00,000	80,00,000	-	16,00,000	16,00,000	-	64,00,000
3	Copyright (W.N.3)	-	2,50,000	2,50,000	-	25,000	25,000	-	2,25,000

		-	85,70,000	85,70,000	-	16,25,000	16,25,000	-	69,45,000

*As per Ind AS 36, irrespective of whether there is any indication of impairment, an entity shall test goodwill acquired in a business combination for impairment annually. This implies **that goodwill is not amortised annually but is subject to annual impairment, if any**.

**As per the information in the question, the limiting factor in the contract for the use is time i.e., 5 years and not the fixed total amount of revenue to be generated. Therefore, an amortisation method that is based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate and amortisation based on time can only be applied.

2	**Amortization expenses**		
	Franchise (W.N.2)	16,00,000	
	Copyright (W.N.3)	25,000	16,25,000
3	**Other expenses**		
	Legal cost on copyright	7,00,000	
	Fee for Franchise (10,00,000 x 2%)	20,000	7,20,000

Working Notes:

		Rs.
(1)	**Goodwill on acquisition of business**	
	Cash paid for acquiring the business	13,20,000
	Less: Fair value of net assets acquired	(10,00,000)
	Goodwill	**3,20,000**
(2)	**Franchise**	80,00,000
	Less: Amortisation (over 5 years)	(16,00,000)
	Balance to be shown in the balance sheet	**64,00,000**
(3)	**Copyright**	2,50,000
	Less: Amortisation (over 10 years as per SLM)	(25,000)
	Balance to be shown in the balance sheet	**2,25,000**

Question 7 : May 2021 – RTP

PQR Ltd. is a gaming developer company. Few years back, it developed a new game called 'Cloud9'. This game sold over 10,00,000 copies around the world and was extremely profitable. Due to its popularity, PQR Ltd. released a new game in the 'Cloud9' series every year. The games continue to be the bestseller. Based on Management's expectations, estimates of cash flow projections for the 'cloud9 videogame series' over the next five years have been prepared. Based on these projections, PQR Ltd. believes that cloud9 series brand should be recognised at INR 20,00,000 in its financial statement. PQR Ltd. has also paid INR 10,00,000 to MNC Ltd. to acquire rights of another video game series called the 'Headspace' videogame series. The said series have huge demand in the market.

Discuss the accounting treatment of the above in the financial statements of PQR Ltd.

Solution :

In order to determine the accounting treatment of 'cloud9 videogame series' and 'Headspace', definition of asset and intangible asset given in Ind AS 38 may be noted:

"An asset is a resource:

(a) controlled by an entity as a result of past events; and

(b) from which future economic benefits are expected to flow to the entity."

"An intangible asset is an identifiable non-monetary asset without physical substance."

In accordance with the above, for recognising an intangible asset, an entity must be able to demonstrate that the item satisfies the criteria of identifiability, control and existence of future economic benefits.

In order to determine whether 'cloud9 videogame series' meet the aforesaid conditions, following provisions of Ind AS 38 regarding Internally Generated Intangible Assets may be noted:

As per paragraph 63 and 64 of Ind AS 38, internally generated brands, mastheads, publishing titles, customer lists and items similar in substance should not be recognised as intangible assets. Expenditure on such items cannot be distinguished from the cost of developing the business as a whole. Therefore, such items are not recognised as intangible assets.

Accordingly, though the cash flow projections suggest that the cloud9 brand will lead to future economic benefits, yet the asset has been internally generated; therefore, the Cloud9 brand cannot be recognised as intangible asset in the financial statements.

In order to determine whether 'Headspace' meet the aforesaid conditions, following provisions of Ind AS 38 regarding 'Separately acquired Intangible Assets' should be analused.

As per paragraphs 25 and 26 of Ind AS 38, normally, the price an entity pays to acquire separately an intangible asset will reflect expectations about the probability that the expected future economic benefits embodied in the asset will flow to the entity. In other words, the entity expects there to be an inflow of economic benefits, even if there is uncertainty about the timing or the amount of the inflow. Therefore, the probability recognition criterion in paragraph 21(a) is always considered to be satisfied for separately acquired intangible assets. In addition, the cost of a separately acquired intangible asset can usually be measured reliably. This is particularly so when the purchase consideration is in the form of cash or other monetary assets.

The Headspace game has been purchased for INR 10,00,000 and it is expected to generate future economic benefits to the entity. Since Headspace game is a separately acquired asset and the future benefits are expected to flow to the entity, therefore, an intangible asset should be recognised in respect of the 'Headspace' asset at its cost of INR 10,00,000. After initial recognition, either cost model or revaluation model can be used to measure headspace intangible asset as per guidance given in paragraphs 74-87 of Ind AS 38. In accordance with this, Headspace intangible asset should be carried at its cost/revalued amount (as the case may be) less any accumulated amortisation and any accumulated impairment losses.

Question 8 : Nov 2021 – RTP

X Ltd. purchased a franchise from a restaurant chain at a cost of Rs. 1,00,00,000 under a contract for a period of 10 years. Can the franchise right be recognised as an intangible asset in the books of X Ltd. under Ind AS 38?

Solution :

Ind AS 38 'Intangible Assets', defines asset and intangible asset as under:

An asset is a resource:

(a) controlled by an entity as a result of past events; and

(b) from which future economic benefits are expected to flow to the entity.

An intangible asset is an identifiable non-monetary asset without physical substance.

In accordance with the above, for considering an asset as an intangible asset, an entity must be able to demonstrate that the item satisfies the criteria of identifiability, control over a resource and existence of future economic benefits.

In the given case, the franchise right meets the identifiability criterion as it is arising from contract to purchase the franchise right for 10 years. In addition, X Ltd. will have future economic benefits and control over them from the franchise right. Accordingly, the franchise right meets the definition of intangible asset. The same can be recognised if the following recognition criteria laid down in para 21 of Ind AS 38 is met:

An intangible asset shall be recognised if, and only if:

(a) it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity; and

(b) the cost of the asset can be measured reliably.

In the instant case, identifiability criterion is fulfilled, future economic benefits from franchise right are expected to flow to the entity and cost can also be measured reliably, therefore, X Ltd. should recognise the franchise right as an intangible asset.

Question 9 : May 2022 – RTP

D Ltd. a leading publishing house, purchased copyright of a book from its author for publishing the same. As per the terms of the contract, if D Ltd. chooses to make the payment upfront then, copyright consideration of Rs. 80,00,000 is to be paid (which is in line with general practice in such arrangements). However, the contract also provided that, in case D Ltd. chooses to pay the consideration after 2 years, then it will be required to pay Rs. 1,00,00,000. At what value should the intangible asset be recognised as per Ind AS 38?

Solution :

As per paragraph 32 of Ind AS 38, "If payment for an intangible asset is deferred beyond normal credit terms, its cost is the cash price equivalent. The difference between this amount and the total payments is recognized as interest expense over the period of credit unless it is capitalized in accordance with Ind AS 23, Borrowing Costs.”

In the given case, if the payment for an intangible asset i.e. copyright is deferred beyond normal credit terms, the cash price equivalent Rs. 80,00,000 should be considered as its cost and the intangible asset will be recorded initially at this value.

The difference of Rs. 20,00,000 between cash price equivalent (i.e. Rs. 80,00,000) and the total payment (i.e. Rs. 1,00,00,000) should be recognised as interest expense over the period of credit (i.e. 2 years in this case), unless it is eligible for capitalisation in accordance with Ind AS 23, Borrowing Costs.

Thanks ….

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IND AS – 105
NON CURRENT ASSETS & HELD FOR SALE & DISCONTINUING OPERATIONS

CHAPTER - 7

Question 1 : May 2018 – RTP

Following is the extract of the consolidated financial statements of A Ltd. for the year ended on:

Asset / Liability	**Carry amount as on 31st March, 20X1**
	(In Rs.000)
Attributed goodwill	200
Intangible assets	950
Financial asset measured at fair value through other comprehensive income	300
Property, plant & equipment	1100
Deferred tax asset	250
Current assets – inventory, receivables and cash balances	600
Current liabilities	(850)
Non-current liabilities – provisions	(300)
Total	**2,250**

On 15th September 20X1, Entity A decided to sell the business. It noted that the business meets the condition of disposal group classified as held for sale on that date in accordance with Ind AS 105. However, it does not meet the conditions to be classified as discontinued operations in accordance with that standard.

The disposal group is stated at the following amounts immediately prior to reclassification as held for sale.

Asset / Liability	**Carry amount as on 15th September 20X1**
	(In Rs.000)
Attributed goodwill	200
Intangible assets	930
Financial asset measured at fair value through other comprehensive income	360
Property, plant & equipment	1020
Deferred tax asset	250

Current assets – inventory, receivables and cash balances	520
Current liabilities	(870)
Non-current liabilities – provisions	(250)
Total	**2,160**

Entity A proposed to sell the disposal group at Rs 19,00,000. It estimates that the costs to sell will be Rs 70,000. This cost consists of professional fee to be paid to external lawyers and accountants. As at 31st March 20X2, there has been no change to the plan to sell the disposal group and entity A still expects to sell it within one year of initial classification. Mr. X, an accountant of Entity A remeasured the following assets/ liabilities in accordance with respective standards as on 31st March 20X2:

Available for sale	**(in Rs.000's)**
Financial assets	410
Deferred tax assets	230
Current assets- Inventory, receivables and cash balances	400
Current liabilities	900
Non- current liabilities- provisions	250

The disposal group has not been trading well and its fair value less costs to sell has fallen to Rs.16,50,000.

Required:

What would be the value of all assets/ liabilities within the disposal group as on the following dates in accordance with Ind AS 105?

(a) 15th September, 20X1 and

(b) 31st March, 20X2

Solution :

(a) As at 15th September, 20X1

The disposal group should be measured at Rs.18,30,000 (19,00,000 – 70,000). The impairment write down of Rs.3,30,000 (Rs.21,60,000 – Rs.18,30,000) should be recorded within profit from continuing operations.

The impairment of Rs.3,30,000 should be allocated to the carrying values of the appropriate non-current assets.

Asset/ (liability)	**Carrying value as at 15 June 2004**	**Impairment**	**Revised carrying value as per IND AS 105**
Attributed goodwill	200	(200)	-
Intangible assets	930	(62)	868
Financial asset measured at fair value through other comprehensive income	360	-	360
Property, plant & equipment	1,020	(68)	952
Deferred tax asset	250	-	250

Current assets – inventory, receivables and cash balances	520	-	520
Current liabilities	(870)	-	(870)
Non-current liabilities – provisions	(250	-	(250)
Total	**2,160**	**(330)**	**1,830**

The impairment loss is allocated first to goodwill and then pro rata to the other assets of the disposal group within Ind AS 105 measurement scope. Following assets are not in the measurement scope of the standard- financial asset measured at other comprehensive income, the deferred tax asset or the current assets. In addition, the impairment allocation can only be made against assets and is not allocated to liabilities.

(b) As on 31st March. 20X2:

All of the assets and liabilities, outside the scope of measurement under IND AS 105, are remeasured in accordance with the relevant standards. The assets that are remeasured in this case under the relevant standards are the Financial asset measured at fair value through other comprehensive income (Ind AS 109), the deferred tax asset (Ind AS 12), the current assets and liabilities (various standards) and the non-current liabilities (Ind AS 37).

Asset/ (liability)	Carrying amount as on 15 September, 20X1	Change in value to 31st March 20X2	Impairment	Revised carrying value as per Ind AS 105
Attributed goodwill	-	-	-	-
Intangible assets	868	-	-29	839
Financial asset measured at fair value through other comprehensive income	360	50	-	410
Property, plant & equipment	952	-	-31	921
Deferred tax asset	250	(20)	-	230
Current assets – inventory, receivables and cash balances	520	(120)	-	400
Current liabilities	(870)	(30)	-	(900)
Non-current liabilities – provisions	(250)	-	-	(250)
Total	**1,830**	**(120)**	**(60)**	**1,650**

Question 2 : Nov 2018 – PAPER

PB Limited purchased a plastic bottle manufacturing plant for Rs.24 lakh on 1st April, 2015. The useful life of the plant is 8 years. On 30th September, 2017, PB Limited temporarily stops using the manufacturing plant because demand has declined. However, the plant is maintained in a workable condition and it will be used in future when demand picks up.

The accountant of PB Limited decided to treat the plant as held for sale until the demand picks up and accordingly measures the plant at lower of carrying amount and fair value less cost to sell.

The accountant has also stopped charging depreciation for rest of the period considering the plant as held for sale. The fair value less cost to sell on 30th September, 2017 and 31st March, 2018 was Rs.13.5 lakh and Rs.12 lakh respectively.
The accountant has made the following working:

Carrying amount on initial classification as held for sale	**Rs.**	**Rs.**
Purchase price of Plant	24,00,000	
Less: Accumulated Depreciation [(Rs.24,00,000/8)x2.5 years]	7,50,000	16,50,000
Fair value less cost to sell as on 31st March, 2017		12,00,000
The value lower of the above two		12,00,000

Balance Sheet extracts as on 31st March, 2018

Particulars	**Rs.**
Assets	
Current Assets	
Other Current Assets	
Assets classified as held for sale	12,00,000

Required:
Analyze whether the above accounting treatment is in compliance with the Ind AS. If not, advise the correct treatment showing necessary workings.

Solution :
As per Ind AS 105 'Non-current Assets Held for Sale and Discontinued Operations', an entity shall classify a non-current asset as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use.
For an Asset to be classified as held for sale it should be
1) Available for immediate sale in present condition and
2) Sale must be highly probable.
The Asset should be available for sale in present condition. The terms that are usual and customary for sale does not disqualify the Asset from being classified as held for sale. Its cannot be classified as held for sale if entity intends to sell it in distant future.
Sale is highly probable if :
1) The appropriate level of management is committed to plan to sell.
2) An Active Programme to trade a buyer is in Place.
3) The Asset is marketed for sale at a price that is reasonable in relation to its current fair value.
4) The sale if expected to be completed within 1 year.
5) Significant charges or withdrawal from plan to sale the Asset are unlikely.
Ind AS 105 also states that entity shall not classify an Asset as held for sale if the Asset is abandoned.
The Accountant of PB has treated the plant as held for which is not correct and not in accordance to Ind AS 105. It should not have stopped charging depreciation.
Instead entity should have impaired the Asset as per Ind AS 36.

Working :

Purchase Price	24,00,000
Accumulated dep. $\left(\frac{24,00,000}{8}\right) \times 3$	9,00,000
Carrying Amount	15,00,000
Recoverable Amount	12,00,000
Impairment Loss	3,00,000

Recoverable Amount is higher of
Value in use = Nil (since it is not in use)
Fair value less cost to sale = 12,00,000

Question 3 : May 2019 – RTP

CK Ltd. prepares the financial statement under Ind AS for the quarter year ended 30th June, 2018. During the 3 months ended 30th June, 2018 following events occurred:
On 1st April, 2018, the Company has decided to sell one of its divisions as a going concern following a recent change in its geographical focus. The proposed sale would involve the buyer acquiring the non-monetary assets (including goodwill) of the division, with the Company collecting any outstanding trade receivables relating to the division and settling any current liabilities.
On 1st April, 2018, the carrying amount of the assets of the division were as follows:

- Purchased Goodwill – Rs.60,000
- Property, Plant & Equipment (average remaining estimated useful life two years) – Rs.20,00,000
- Inventories – Rs.10,00,000

From 1st April, 2018, the Company has started to actively market the division and has received number of serious enquiries. On 1st April, 2018 the directors estimated that they would receive Rs.32,00,000 from the sale of the division. Since 1st April, 2018, market condition has improved and as on 1st August, 2018 the Company received and accepted a firm offer to purchase the division for Rs.33,00,000.
The sale is expected to be completed on 30th September, 2018 and Rs.33,00,000 can be assumed to be a reasonable estimate of the value of the division as on 30th June, 2018. During the period from 1st April to 30th June inventories of the division costing Rs.8,00,000 were sold for Rs.12,00,000. At 30th June, 2018, the total cost of the inventories of the division was Rs.9,00,000. All of these inventories have an estimated net realisable value that is in excess of their cost.
The Company has approached you to suggest how the proposed sale will be reported in the interim financial statements for the quarter ended 30th June, 2018 giving relevant explanations.

Solution :

The decision to offer the division for sale on 1st April, 2018 means that from that date the division has been classified as held for sale. The division available for immediate sale, is being actively marketed at a reasonable price and the sale is expected to be completed within one year.

The consequence of this classification is that the assets of the division will be measured at the lower of their existing carrying amounts and their fair value less cost to sell. Here the division shall be measured at their existing carrying amount ie Rs.30,60,000 since it is less than the fair value less cost to sell Rs.32,00,000.

The increase in expected selling price will not be accounted for since earlier there was no impairment to division held for sale.

The assets of the division need to be presented separately from other assets in the balance sheet. Their major classes should be separately disclosed either on the face of the balance sheet or in the notes.

The Property, Plant and Equipment shall not be depreciated after 1st April, 2018 so its carrying value at 30th June, 2018 will be Rs.20,00,000 only. The inventories of the division will be shown at Rs.9,00,000.

The division will be regarded as discontinued operation for the quarter ended 30th June, 2018. It represents a separate line of business and is held for sale at the year end.

The Statement of Profit and Loss should disclose, as a single amount, the post-tax profit or loss of the division on classification as held for sale.

Further, as per Ind AS 33, EPS will also be disclosed separately for the discontinued operation.

Question 4 : Nov 2019 – PAPER

On June 1, 2018 entity D Limited plans to sell a group of assets and liabilities, which is classified as a disposal group. On July 31, 2018, the Board of Directors approved and committed to the plan to sell the manufacturing unit by entering into a firm purchase commitment with entity G Limited. However, since the manufacturing unit is regulated, the approval from the regulator is needed for sale. The approval from the regulator is customary and highly probable to be received by November 30, 2018 and the sale is expected to be completed by March 31, 2019. Entity D Limited follows December year end. The assets and liabilities attributable to this manufacturing unit are as under :

(Rs. in lakhs)

Particular	**Carrying value as on December 31, 2017**	**Carrying value as on July 31, 2018**
Goodwill	1,000	1,000
Plant and Machinery	2,000	1,800
Building	4,000	3,700
Debtors	1,700	2,100
Inventory	1,400	800
Creditors	(600)	(500)
Loans	(4,000)	(3,700)
Net	**5,500**	**5,200**

The fair value of the manufacturing unit as on December 31, 2017 is Rs.4,000 and as on July 31, 2018 is Rs.3,700. The cost to sell is 200 on both these dates. The disposal group is not sold at the period end i.e., December 31, 2018. The fair value as on December 31, 2018 is lower then the carrying value of the disposal group as on that date.

Required :

(i) Assets whether the manufacturing unit can be classified a held for sale and reasons thereof. If yes, then at which date?

(ii) The measurement of the manufacturing unit as on the date of classification as held for sale.

(iii) The measurement of the manufacturing unit as at the end of the year.

Solution :

1. Assessing whether the manufacturing unit can be classified as held for sale

The manufacturing unit can be classified as held for sale due to the following reasons:

(a) The disposal group is available for immediate sale and in its present condition. The regulatory approval is customary and it is expected to be received in one year. The date at which the disposal group must be classified as held for sale is 31st July, 20X1, i.e., the date at which management becomes committed to the plan.

(b) The sale is highly probable as the appropriate level of management i.e., board of directors in this case have approved the plan.

(c) A firm purchase agreement has been entered with the buyer.

(d) The sale is expected to be complete by 31st March, 20X2, i.e., within one year from the date of classification.

2. Measurement of the manufacturing unit as on the date of classification as held for sale

Following steps need to be followed:

Step 1: Immediately before the initial classification of the asset (or disposal group) as held for sale, the carrying amounts of the asset (or all the assets and liabilities in the group) shall be measured in accordance with applicable Ind AS.

This has been done and the carrying value of the disposal group as on 31st July, 20X1 is determined at Rs.5,600. The difference between the carrying value as on 31st December, 20X0 and 31st July, 20X1 is accounted for as per the relevant Ind AS.

Step 2: An entity shall measure a non-current asset (or disposal group) classified as held for sale at the lower of its carrying amount and fair value less costs to sell.

The fair value less cost to sell of the disposal group as on 31st July, 20X1 is Rs.3,500 (i.e.3,700 – 200). This is lower than the carrying value of Rs.5,200. Thus an impairment loss needs to be recognised and allocated first towards goodwill and thereafter pro-rata between assets of the disposal group which are within the scope of Ind AS 105 based on their carrying value. Thus, the assets will be measured as under:

Particulars	**Carrying value**	**Impairment**	**Carrying value**
			as per Ind AS 105
	31st July, 20X1		**31st July, 20X1**
Goodwill	1,000	(1,000)	-
Plant and Machinery	1,800	(230)	1,570
Building	3,700	(470)	3,230
Debtors	2,100	-	2,100

Inventory	800	-	800
Creditors	(500)	-	(500)
Loans	(3,700)	-	(3,700)
	5,200	(1,700)	3,500

3. Measurement of the manufacturing unit as on the date of classification as at the year end
The measurement as at the year-end shall be on similar lines as done above.
The assets and liabilities in the disposal group not within the scope of this Standard are measured as per the respective Standards.
The fair value less cost to sell of the disposal group as a whole is calculated. This fair value less cost to sell as at the year-end shall be compared with the carrying value as at the date of classification as held for sale. It is provided that the fair value as on the year end is less than the carrying amount as on that date – thus the impairment loss shall be allocated in the same way between the assets of the disposal group falling within the scope of this standard as shown above.

Question 5 : Nov 2021 – RTP

On February 28, 20X1, Entity X is committed to the following plans:

(a) To sell a property after completion of certain renovations to increase its value prior to selling it. The renovations are expected to be completed within a short span of time i.e., 2 months.

(b) To sell a commercial building to a buyer after the occupant vacates the building. The time required for vacating the building is usual and customary for sale of such commercial property. The entity considers the sale to be highly probable.

Can the above-mentioned property and commercial building be classified as non-current assets held for sale at the reporting date i.e. 31st March, 20X1?

Solution :

Ind AS 105 provides guidance on classification of a non-current asset held for sale in paragraph 7 which states that, the asset (or disposal group) must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups) and its sale must be highly probable.

(a) In respect of Entity X's plan to sell property which is being renovated and such renovation is incomplete as at the reporting date. Although, the renovations are expected to be completed within 2 months from the reporting date i.e., March 31, 20X1, the property cannot be classified as held for sale at the reporting date as it is not available for sale immediately in its present condition.

(b) In case of Entity X's plan to sell commercial building, it intends to transfer the commercial building to a buyer after the occupant vacates the building and the time required for vacating such building is usual and customary for sale of such non-current asset. Accordingly, the criterion of the asset being available for immediate sale would be met and hence, the commercial building can be classified as held for sale at the reporting date.

Question 6 : May 2022 – RTP

X Ltd. acquires B Ltd. exclusively with a view to sale and it meets the criteria to be classified as discontinued operation as per Ind AS 105. Further, following information is available about B Ltd.:

Fair value of total assets excluding liabilities on acquisition – Rs. 360

Costs to sell as on acquisition and on reporting date – Rs. 10

Fair value of liabilities on acquisition and reporting date – Rs. 80

Fair value of total assets excluding liabilities on the reporting date – Rs. 340

How discontinued operation pertaining to B Ltd. should be measured in consolidated financial statements of X Ltd. on acquisition date and reporting date?

Solution :

Ind AS 105 defines a disposal group as a group of assets to be disposed of, by sale or otherwise, together as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction. The group includes goodwill acquired in a business combination if the group is a cash-generating unit to which goodwill has been allocated in accordance with the requirements of paragraphs 80–87 of Ind AS 36, Impairment of Assets, or if it is an operation within such a cash- generating unit.

In the given case, B Ltd. is acquired exclusively with a view to sell and meets the criteria to be classified as discontinued operation.

The discontinued operation would be measured in accordance with paragraphs 15 and 16 of Ind AS 105

As per para 15, an entity shall measure a non-current asset (or disposal group) classified as held for sale at the lower of its carrying amount and fair value less costs to sell.

As per para 16, if a newly acquired asset (or disposal group) meets the criteria to be classified as held for sale (see paragraph 11), applying paragraph 15 will result in the asset (or disposal group) being measured on initial recognition at the lower of its carrying amount had it not been so classified (for example, cost) and fair value less costs to sell. Hence, if the asset (or disposal group) is acquired as part of a business combination, it shall be measured at fair value less costs to sell.

Therefore, on acquisition date, in line with paragraph 16, X Ltd. will measure B Ltd. as a disposal group at fair value less costs to sell which will be calculated as Fair value of total assets excluding liabilities on acquisition – Costs to sell = Rs. 360 – Rs. 10 = Rs. 350.

Fair value of liabilities on acquisition = Rs. 80.

At the reporting date, in line with paragraph 15, X Ltd. will remeasure the disposal group at the lower of its cost and fair value less costs to sell which will be calculated as:
Fair value of total assets excluding liabilities on subsequent reporting date – Costs to sell
= Rs. 340 – Rs. 10 = Rs. 330
Fair value of liabilities on reporting date = Rs. 80.
At the reporting date, X Ltd. shall present these assets and liabilities separately from other assets and liabilities in its consolidated financial statements.
In the statement of profit and loss, X Ltd. shall recognise loss on subsequent measurement (of net assets at fair value) of B Ltd. which equals to Rs. 20 (Rs. 270 – Rs. 250).

Thanks ….

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IND AS – 23
BORROWING COST

CHAPTER - 8

Question 1 : May 2018 – RTP

An entity constructs a new head office building commencing on 1st September 20X1, which continues till 31st December 20X1. Directly attributable expenditure at the beginning of the month on this asset are Rs.100,000 in September 20X1 and Rs.250,000 in each of the months of October to December 20X1.

The entity has not taken any specific borrowings to finance the construction of the asset, but has incurred finance costs on its general borrowings during the construction period. During the year, the entity had issued 10% debentures with a face value of Rs.20 lacs and had an overdraft of Rs.500,000, which increased to Rs.750,000 in December 20X1. Interest was paid on the overdraft at 15% until 1 October 20X1, then the rate was increased to 16%.

Calculate the capitalization rate for computation of borrowing cost in accordance with IND AS 23 'Borrowing Costs'.

Solution :

1) Calculation of Capitalisation Rate

$$= \frac{2,79,583}{25,20,833} \times 100 = 11.09\%$$

Loan	Period	Wt	Rate	Interest
20,00,000	12m	2,00,000	10%	2,00,000
5,00,000	9m	3,75,000	15%	56,250
5,00,000	2m	83,333	16%	13,333
7,50,000	1m	62,500	16%	10,000
		25,20,833		2,79,583

2) Amount utilised for Asset

Amount	Period	Wt
1,00,000	4m	33,333
2,50,000	3m	62,500
2,50,000	2m	41,667
2,50,000	1m	20,833
		1,58,333

3) Borrowing cost to be capitalised

= 1,58,333 × 11.09% = 17,559

Question 2 : Nov 2018 – RTP

K Ltd. began construction of a new building at an estimated cost of Rs.7 lakh on 1st April, 2017. To finance construction of the building it obtained a specific loan of Rs.2 lakh from a financial institution at an interest rate of 9% per annum.

The company's other outstanding loans were:

Amount	Rate of Interest per annum
Rs.7,00,000	12%
Rs.9,00,000	11%

The expenditure incurred on the construction was:

April, 2017	Rs.1,50,000
August, 2017	Rs.2,00,000
October, 2017	Rs.3,50,000
January, 2018	Rs.1,00,000

The construction of building was completed by 31st January, 2018. Following the provisions of Ind AS 23 'Borrowing Costs', calculate the amount of interest to be capitalized and pass necessary journal entry for capitalizing the cost and borrowing cost in respect of the building as on 31st January, 2018.

Solution :

(i) Calculation of capitalization rate on borrowings other than specific borrowings

Amount of loan (Rs.)	Rate of interest		Amount of interest (Rs.)
7,00,000	12%	=	84,000
9,00,000	11%	=	99,000
16,00,000		=	1,83,000
Weighted average rate of interest (1,83,000/16,00,000) x 100			11.4375%

(ii) Computation of borrowing cost to be capitalized for specific borrowings and general borrowings based on weighted average accumulated expenses

Date of incurrence of expenditure	Amount spent	Financed through	Calculation	Rs.
1st April, 2017	1,50,000	Specific borrowing	1,50,000 x 9% x 10/12	11,250
1st August, 2017	2,00,000	Specific borrowing	50,000 x 9% x 10/12	3,750
		General borrowing	1,50,000 x 11.4375% x 6/12	8,578.125
1st October, 2017	3,50,000	General borrowing	3,50,000 x 11.4375% x 4/12	13,343.75
1st January, 2018	1,00,000	General borrowing	1,00,000 x 11.4375% x 1/12	953.125
				37,875

Note : Since construction of building started on 1st April, 2017, it is presumed that all the later expenditures on construction of building had been incurred at the beginning of the respective month.

(iii) Total expenses to be capitalized for building

	Rs.
Cost of building Rs.(1,50,000 + 2,00,000 + 3,50,000 + 1,00,000)	8,00,000
Add : Amount of interest to be capitalized	37,875
	8,37,875

(iv) Journal Entry

Date	Particulars	Rs.	Rs.
31.1.2018	Building account Dr. To Bank account To Interest payable (borrowing cost) (Being expenditure incurred on construction of building and borrowing cost thereon capitalized)	8,37,875	 8,00,0000 37,875

Note : In the above journal entry, it is assumed that interest amount will be paid at the year end. Hence, entry for interest payable has been passed on 31.1.2018.

Alternatively, following journal entry may be passed if interest is paid on the date of capitalization:

Date	Particulars	Rs.	Rs.
31.1.2018	Building account Dr. To Bank account (Being expenditure incurred on construction of building and borrowing cost thereon capitalized)	8,37,875	 8,37,875

Question 3 : Nov 2019 – RTP

On 1st April, 20X1, entity A contracted for the construction of a building for Rs.22,00,000. The land under the building is regarded as a separate asset and is not part of the qualifying assets. The building was completed at the end of March, 20X2, and during the period the following were made to the contractor.

Payment date	Amount (Rs.'000)
1st April, 20X1	200
30th June, 20X1	600
31st December, 20X1	1,200
31st March, 20X2	200
Total	**2,200**

Entity A's borrowings at its year end of 31st March, 20X2 were as follows:

a. 10%, 4-year note with simple interest payable annually, which relates specifically to the project; debt outstanding on 31st March, 20X2 amounted to Rs.7,00,000. Interest of Rs.65,000 was incurred on these borrowings during the year, and interest income of Rs. 20,000 was earned on these funds while they were held in anticipation of payments.

b. 12.5% 10-year note with simple interest payable annually; debt outstanding at 1st April, 20X1 amounted to Rs.1,000,000 and remained unchanged during the year; and

c. 10% 10-year note with simple interest payable annually; debt outstanding at 1st April, 20X1 amounted to Rs.1,500,000 and remained unchanged during the year.

What amount of the borrowing costs can be capitalized at year end as per relevant Ind AS?

Solution :

As per Ind AS 23, when an entity borrows funds specifically for the purpose of obtaining a qualifying asset, the entity should determine the amount of borrowing costs eligible for capitalisation as the actual borrowing costs incurred on that borrowing during the period less any investment income on the temporary investment of those borrowings.

The amount of borrowing costs eligible for capitalization, in cases where the funds are borrowed generally, should be determined based on the expenditure incurred in obtaining a qualifying asset. The costs incurred should first be allocated to the specific borrowings.

Analysis of expenditure:

Date	Expenditure (Rs.'000)	Amount allocated in general borrowings (Rs.'000)	Weighted for period outstanding (Rs.'000)	
1st April 20X1	200	0		0
30th June 20X1	600	100*	100 × 9/12 =	75
31st Dec 20X1	1,200	1,200	1,200 × 3/12 =	300
31st March 20X2	200	200	200 × 0/12 =	0
Total	2,200			375

*Specific borrowings of Rs.7,00,000 fully utilized on 1st April & on 30th June to the extent of Rs.5,00,000 hence remaining expenditure of Rs.1,00,000 allocated to general borrowings.

The expenditure rate relating to general borrowings should be the weighted average of the borrowing costs applicable to the entity's borrowings that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset.

Capitalisation rate = $\frac{(10,00,000 \times 12.5\%) + (15,00,000 \times 10\%)}{10,00,000 + 15,00,000}$ = 11%

Borrowing cost to be capitalized:	Amount
	(Rs.)
On specific loan	65,000
On General borrowing (3,75,000 × 11%)	41,250
Total	1,06,250
Less interest income on specific borrowings	(20,000)
Amount eligible for capitalization	86,250
Therefore, the borrowing costs to be capitalized are Rs.86,250.	

Question 4 : Nov 2019 – PAPER

An entity constructs a new office building commencing on 1st September, 2018, which continues till 31st December, 2018 (and is expected to go beyond a year). Directly attributable expenditure at the beginning of the month on this asset are Rs.2 Lakhs in September 2018 and Rs.4 Lakhs in each of the months of October to December 2018.

The entity has not taken any specific borrowings to finance the construction of the building but has incurred finance costs on its general borrowings during the construction period. During the year, the entity had issued 9% debentures with a face value of Rs.30 Lakhs and had an overdraft of Rs.4 Lakhs, which increased to Rs.8 Lakhs in December 2018. Interest was paid on the overdraft at 12% until 1st October, 2018 and then the rate was increased to 15%.

Calculate the Capitalization rate for computation of borrowing cost in accordance with Ind AS 'Borrowing Cost'.

Solution :

1) Calculation of Capitalisation Rate

Loan	Period	Wt	Rate	Interest
30,00,000	12m	30,00,000	9%	2,70,000
4,00,000	9m	3,00,000	12%	36,000
4,00,000	2m	66,667	15%	10,000
8,00,000	1m	66,667	15%	10,000
		34,33,333		3,26,000

$$CR = \frac{3,26,000}{34,33,000} \times 100 = 9.495\%$$

2) Amount utilised for Asset

Amount	Period	Wt
2,00,000	4m	66,667
4,00,000	3m	1,00,000
4,00,000	2m	66,667
4,00,000	1m	33,333
		2,66,667

3) Borrowing cost to be capitalized

= 2,66,667 × 9.495%

= 25,200

Question 5 : May 2021 – RTP

How will you capitalise the interest when qualifying assets are funded by borrowings in the nature of bonds that are issued at discount?

Y Ltd. issued at the start of year 1, 10% (interest paid annually and having maturity period of 4 years) bonds with a face value of Rs. 2,00,000 at a discount of 10% to finance a qualifying asset which is ready for intended use at the end of year 2.
Compute the amount of borrowing costs to be capitalized if the company amortizes discount using Effective Interest Rate method by applying 13.39% p.a. of EIR.

Solution :
As per the Standard, borrowing costs may include interest expense calculated using the effective interest method. Further, capitalisation of borrowing cost should cease where substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete. Thus, only that portion of the amortized discount should be capitalised as part of the cost of a qualifying asset which relates to the period during which acquisition, construction or production of the asset takes place.

Capitalisation of Interest
Hence based on the above explanation the amount of borrowing cost of year 1 & 2 are to be capitalised and the borrowing cost relating to year 3 & 4 should be expensed.

Quantum of Borrowing
The value of the bond to Y Ltd. is the transaction price ie ` 1,80,000 (2,00,000 – 20,000)
Therefore, Y Ltd will recognize the borrowing at ` 1,80,000.

Computation of the amount of Borrowing Cost to be Capitalised
Y Ltd will capitalise the interest (borrowing cost) using the effective interest rate of 13.39% for two years as the qualifying asset is ready for intended use at the end of the year 2, the details of which are as follows:

Year	Opening Borrowing	Interest expense @ 13.39% to be capitalised	Total	Interest paid	Closing Borrowing
	(1)	(2)	(3)	(4)	(5) = (3) - (4)
1	1,80,000	24,102	2,04,102	20,000	1,84,102
2	1,84,102	24,651	2,08,753	20,000	1,88,753
		48,753			

Accordingly, borrowing cost of Rs.48,753 will be capitalized to the cost of qualifying asset.

Question 6 : Nov 2021 – RTP

Nikka Limited has obtained a term loan of Rs. 620 lacs for a complete renovation and modernisation of its Factory on 1st April, 20X1. Plant and Machinery was acquired under the modernisation scheme and installation was completed on 30th April, 20X2. An expenditure of Rs. 510 lacs was incurred on installation of Plant and Machinery, Rs. 54 lacs has been advanced to suppliers for additional assets (acquired on 25th April, 20X1) which were also installed on 30th April, 20X2 and the balance loan of Rs. 56 lacs has been used for working capital purposes. Management of Nikka Limited considers the 12 months period as substantial period of time to get the asset ready for its intended use.

The company has paid total interest of Rs. 68.20 lacs during financial year 20X1-20X2 on the above loan. The accountant seeks your advice how to account for the interest paid in the books of accounts. Will your answer be different, if the whole process of renovation and modernization gets completed by 28th February, 20X2?

Solution :

As per Ind AS 23, Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset form part of the cost of that asset. Other borrowing costs are recognised as an expense.

Where, a qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

Accordingly, the treatment of Interest of Rs. 68.20 lacs occurred during the year 20X1-20X2 would be as follows:

(i) When construction of asset completed on 30th April, 20X2

The treatment for total borrowing cost of Rs. 68.20 lakh will be as follows:

Purpose	**Nature**	**Interest to be capitalised**	**Interest to be charged to profit and loss account**
		Rs. in lakh	**Rs. in lakh**
Modernisation and renovation of plant and machinery	Qualifying asset	[68.20 x (510/620)] = 56.10	
Advance to suppliers for additional assets	Qualifying asset	[68.20 x (54/620)] = 5.94	
Working Capital	Not a qualifying asset		[68.20 x (56/620)] = 6.16
		62.04	**6.16**

(ii) When construction of assets is completed by 28th February, 20X2

When the process of renovation gets completed in less than 12 months, the plant and machinery and the additional assets will not be considered as qualifying assets (until and unless the entity specifically considers that the assets took substantial period of time for completing their construction). Accordingly, the whole of interest will be required to be charged off / expensed off to Profit and loss account.

Question 7 : May 2022 – RTP

X Ltd. commenced the construction of a plant (qualifying asset) on 1st September, 20X1, estimated to cost Rs. 10 crores. For this purpose, X has not raised any specific borrowings, rather it intends to use general borrowings, which have a weighted average cost of 11%. Total borrowing costs incurred during the period, viz., 1st September, 20X1 to 31st March, 20X2 were Rs. 0.5 crore. The other relevant details are as follows:

(Rs. in crore)

Month	Cost of construction Accrued	Cash outflows (paid in advance at the start of each month)
September	1.50	3
October	0.50	1.7
November	1.50	2.5
December	0.50	-
January	1.80	1
February	0.70	-
March	3.00	1.5

Based on the above information, discuss the treatment of borrowing cost as per cash outflow basis and accrual basis and also suggest the appropriate amount of interest that should be capitalised to the cost of the plant in the financial statements for the year ended 31st March, 20X2?

Solution :

Paragraph 14 of Ind AS 23, inter-alia, states that to the extent that an entity borrows funds generally and uses them for the purpose of obtaining a qualifying asset, the entity shall determine the amount of borrowing costs eligible for capitalisation by applying a capitalisation rate to the expenditures on that asset. The capitalisation rate shall be the weighted average of the borrowing costs applicable to all borrowings of the entity that are outstanding during the period. However, an entity shall exclude from this calculation borrowing costs applicable to borrowings made specifically for the purpose of obtaining a qualifying asset until substantially all the activities necessary to prepare that asset for its intended use or sale are complete. The amount of borrowing costs that an entity capitalises during a period shall not exceed the amount of borrowing costs it incurred during that period.

In this context, a question arises whether such expenditure should be based on costs accrued or actual cash outflows. To contrast these two alternatives, presented below is the computation of borrowing costs based on both the alternatives:

Month	Cost of construction Accrued	Average capital expenditure	Cash outflows (paid in advance at the start of each month)	Average capital expenditure
September	1.50	1.50 x 7/12 = 0.875	3.00	3.00 x 7/12 = 1.75
October	0.50	0.50 x 6/12 = 0.25	1.70	1.70 x 6/12 = 0.85
November	1.50	1.50 x 5/12 = 0.625	2.50	2.50 x 5/12 = 1.04
December	0.50	0.50 x 4/12 = 0.17	-	-
January	1.80	1.80 x 3/12 = 0.45	1.00	1 x 3/12 = 0.25
February	0.70	0.70 x 2/12 = 0.12	-	-
March	3.00	3.00 x 1/12 = 0.25	1.50	1.50 x 1/12 = 0.125
	9.50	**2.74**	**9.70**	**4.02**

If the average capital expenditure on the basis of costs accrued is taken, the borrowing costs eligible to be capitalised would be Rs. 2.74 crore x 11% = 0.30 crore. Whereas, if average capital expenditure on the basis of cash flows is taken, the borrowing costs eligible to be capitalised would be Rs. 4.02 crore x 11% = 0.44 crore. Thus, there is a wide variance in the amount of borrowing cost to be capitalised, based on the accrual basis and on actual cash flows basis. This divergence is often experienced during the implementation of large projects, for example, an advance given to a supplier involves an upfront cash outflow while the actual expenditure accrues in later periods (with the receipt of goods and services).

As per paragraph 18 of Ind AS 23, expenditures on a qualifying asset include only those expenditures that have resulted in payments of cash, transfers of other assets or the assumption of interest-bearing liabilities. Expenditures are reduced by any progress payments received and grants received in connection with the asset (see Ind AS 20, Accounting for Government Grants and Disclosure of Government Assistance). The average carrying amount of the asset during a period, including borrowing costs previously capitalised, is normally a reasonable approximation of the expenditures to which the capitalization rate is applied in that period.

Where cash has been paid but the corresponding cost has not yet accrued interest becomes payable on payment of cash. Therefore, the amount so paid should be considered for determining the amount of interest eligible for capitalisation, subject to the fulfillment of other conditions prescribed in paragraph 16 of Ind AS 23. Accordingly, in the present case, interest should be computed on the basis of the cash flows rather than on the basis of costs accrued. Therefore, the amount of interest eligible for capitalisation would be Rs. 0.44 crore.

Another important factor to be noted is that paragraph 14 requires, inter alia, that the amount of borrowing costs that an entity capitalises during a period shall not exceed the amount of borrowing costs it incurred during that period. Thus, the amount of borrowing costs to be capitalised should not exceed the total borrowing costs incurred during the period, that is Rs. 0.5 crore.

Thanks ....

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IND AS – 36
IMPAIRMENT OF ASSETS

CHAPTER - 9

Question 1 : May 2018 – RTP

Himalaya Ltd. which is in a business of manufacturing and export of its product. Sometimes, back in 20X4, the Government put restriction on export of goods exported by Himalaya Ltd. and due to that restriction Himalaya Ltd. impaired its assets. Himalaya Ltd. acquired identifiable assets worth of Rs.4,000 lakhs for Rs.6,000 lakh at the end of the year 20X0. The difference is treated as goodwill. The useful life of identifiable assets is 15 years and depreciated on straight line basis. When Government put the restriction at the end of 20X4, the company recognised the impairment loss by determining the recoverable amount of assets for Rs.2,720 lakh. In 20X6 Government lifted the restriction imposed on the export and due to this favourable change, Himalaya Ltd. re-estimate recoverable amount, which was estimated at Rs.3,420 lakh.

Required:

(i) Calculation and allocation of impairment loss in 20X4.

(ii) Reversal of impairment loss and its allocation as per Ind AS 36 in 20X6

Solution :

1. (i) Calculation and allocation of impairment loss in 20X4

(Amount in Rs.lakhs)

	Asset	Goodwill	Total
20X0	4,000	2,000	6,000
–Dep. (4 yrs.)	1,067	–	1,067
20X4 – Carrying amount	2,933	2,000	4,933
Recoverable Amt.			2,720
Impairment Loss	213	2,000	2,213
Carrying amount after impairment	2,720	–	2,720

Note: As per Ind AS 36 impairment loss should be first charged to goodwill.

(ii) Reversal of impairment at end of 2006

(a) Carrying amount asset before Reversal :

		Asset
	20X4	2,720
	–Dep.(2 yrs.)	495
	Carrying before Reversal	2,225
(b)	Carrying amount before Reversal	2,225
	+ Reversal	175
	Carrying amount after Reversal	2,400

Note : As per Ind AS 36 carrying amount after reversal should be lower of :

(a) Recoverable amount 3,420

(b) Carrying after depreciation without impairment

= 4,000 – Depreciation for 6 yrs. (15 yrs. of life)

= 4,000 – 1,600 = 2,400

Question 2 : Nov 2018 – RTP

M Ltd. has three cash-generating units: A, B and C. Due to adverse changes in the technological environment, M Ltd. conducted impairment tests of each of its cash-generating units. On 31st March, 2018, the carrying amounts of A, B and C are Rs.100 lakhs, Rs.150 lakhs and Rs.200 lakhs respectively.

The operations are conducted from a headquarter. The carrying amount of the headquarter assets is Rs.200 lakhs: a headquarter building of Rs.150 lakhs and a research centre of Rs.50 lakhs. The relative carrying amounts of the cash-generating units are a reasonable indication of the proportion of the head-quarter building devoted to each cash-generating unit. The carrying amount of the research centre cannot be allocated on a reasonable basis to the individual cash-generating units.

Following is the remaining estimated useful life of:

	A	**B**	**C**	**Head quarter assets**
Remaining estimated useful life	10	20	20	20

The headquarter assets are depreciated on a straight-line basis.

The recoverable amount of each cash generating unit is based on its value in use since net selling price for each CGU cannot be calculated. Therefore, Value in use is equal to

	A	**B**	**C**	**M Ltd. as a whole**
Recoverable amount	199	164	271	720*

*The research centre generates additional future cash flows for the enterprise as a whole. Therefore, the sum of the value in use of each individual CGU is less than the value in use of the business as a whole. The additional cash flows are not attributable to the headquarter building.

Solution :

1. Allocation of building to CGU A, B and C.

It should be done on the basis of carrying amount × life.

A = Life (10) × Carrying amount (100) = 1,000

B = Life (20) × Carrying amount (150) = 3,000

C = Life (20) × Carrying amount (200) = 4,000

i.e. 1 : 3 : 4

i.e. $150 \times \frac{1}{8}$ = 18.75 to A

$150 \times \frac{3}{8}$ = 56.25 to B

$150 \times \frac{4}{8}$ = 75 to C

2. Check for impairment loss for CGU after allocation of building.

	A	B	C
Carrying Amount	100	150	200
+Building	18.75	56.25	75
	118.75	206.25	275
Recoverable amount	199	164	271
Impairment loss	–	42.25	4

Impairment loss should be apply to building and CGU in rate of its carrying amount.

i.e. $42.25 \times \frac{150}{206.25}$ = 30.73 to CGU B

$42.25 \times \frac{56.25}{206.25}$ = 11.52 to Building

$4 \times \frac{200}{275}$ = 2.91 to CGU C

$4 \times \frac{75}{275}$ = 1.09 to Building

3. Carrying amount after impairment :

	A	B	C	Total
Carrying amount before	100	150	200	150
– Impairment loss	–	30.73	2.91	12.61
	100	119.27	197.09	137.39

4. Check of impairment of larger CGU (Including A, B, C, Building and Research Centre) :

	A	B	C	Building	Research Centre	Total
Carrying amount	100	119.27	197.09	137.39	50	603.75
Recoverable Amount	–	–	–	–	–	720
Impairment loss						Nil

Question 3 : Nov 2018 – PAPER

A machine was acquired by ABC Ltd. 15 years ago at a cost of Rs.20 crore. Its accumulated depreciation as at 31st March, 2018 was Rs.16.60 crore. Depreciation estimated for the financial year 2018-19 is Rs.1 crore. Estimated Net Selling Price of the machine as on 31st March, 2018 was Rs.1.20 crore, which is expected to decline by 20 per cent by the end of the next financial year. Its value in use has been computed at Rs.1.40 crore as on 1st April, 2018, which is expected to decrease by 30 per cent by the end of the financial year. Assuming that other conditions of relevant Accounting Standard for applicability of the impairment are satisfied:

(i) What should be the carrying amount of this machine as at 31st March, 2019?

(ii) How much will be the amount of write off (impairment loss) for the financial year ended 31st March, 2019?

(iii) If the machine had been revalued ten years ago and the current revaluation reserves against this plant were to be Rs.48 lakh, how would you answer to questions (i) and (ii) above?

(iv) If the value in use was zero and the company was required to incur a cost of Rs.8 lakh to dispose of the plant, what would be your response to questions (i) and (ii) above?

Solution :

As per the requirement of the question, the following solution has been drawn on the basis of AS 28

		Rs.in crore
(i)	Carrying amount of plant (before impairment) as on 31st March, 2019	2.4
	Carrying amount of plant (after impairment) as on 31st March, 2019	0.98
(ii)	Amount of impairment loss for the financial year ended 31st March, 2019 (2.4 Cr.- 0.98 Cr)	1.42
(iii)	If the plant had been revalued ten years ago	
	Debit to revaluation reserve	0.48
	Amount charged to profit and loss (1.42 - 0.48)	0.94
(iv)	If Value in use was zero	
	Value in use (a)	Nil
	Net selling price (b)	-0.08
	Recoverable amount [higher of (a) and (b)]	Nil
	Carrying amount (closing book value)	Nil
	Amount of write off (impairment loss) (Rs.2.4 Cr – Nil)	2.4
	Entire book value of plant will be written off and charged to profit and loss account.	

Working Notes:

(1) Calculation of Closing Book Value, as at 31st March, 2019

	Rs. in crore
Opening book value as on 1.4.2018 (Rs.20 crore -16.60 crore)	3.40
Less: Depreciation for financial year 2018–2019	(1.00)
Closing book value as on 31.3.2019 (before impairment)	2.40

(2) Calculation of Estimated Net Selling Price on 31st March, 2019

	Rs. in crore
Estimated net selling price as on 1.4.2018	1.20
Less: Estimated decrease during the year (20% of Rs.1.20 Cr.)	(0.24)
Estimated net selling price as on 31.3.2019	0.96

(3) Calculation of Estimated Value in Use of Plant on 31st March, 2019

	Rs.in crore
Estimated value in use as on 1.4.2018	1.40
Less: Estimated decrease during the year (30% of Rs.1.40 Cr.)	(0.42)
Estimated value in use as on 31.3.2019	0.98

(4) Recoverable amount as on 31.3.2019 is equal to higher of Net selling price and value in use

	Rs.in crore
Net selling price	0.96
Value in use	0.98
Recoverable amount	0.98
Impairment Loss [Carrying amount – Recoverable amount ie. (2.40 Cr. – 0.98 Cr)]	1.42
Revised carrying amount on 31.3.2019 is equal to Recoverable amount (after impairment)	0.98 Cr.

Question 4 : Nov 2018 – PAPER / Nov 2020 - Paper

XYZ Limited has three cash-generating units - X, Y and Z, the carrying amounts of which as on 31st March, 2018 are as follows:

Cash Generating Units	Carrying Amount (Rs.in lakh)	Remaining useful life in years
X	800	20
Y	1000	10
Z	1200	20

XYZ Limited also has corporate assets having a remaining useful life of 20 years as given below:

Corporate Assets	Carrying amount (Rs.in lakh)	Remarks
AU	800	The carrying amount of AU can be allocated on a reasonable basis to the individual cash generating units.
BU	400	The carrying amount of BU cannot be allocated on a reasonable basis to the individual cash-generating units.

Recoverable amounts as on 31st March, 2018 are as follows:

Cash-generating units	Recoverable amount (Rs.in lakh)
X	1000
Y	1200
Z	1400
XYZ Limited	3900

Calculate the impairment loss if any of XYZ Ltd. Ignore decimals.

Solution :

(i) Allocation of corporate assets to CGU

(Rs. in lakh)

	Particulars	**X**	**Y**	**Z**	**Total**
(a)	Carrying amount	800	1,000	1,200	3,000
(b)	Useful life	20 years	10 years	20 years	
(c)	Weight (CA x Life)	16,000	10,000	24,000	
(d)	Allocation of carrying amount of AU (16 : 10 : 24)	256	160	384	800
(e)	Carrying amount after allocation of AU) (a+f)	1,056	1,160	1,584	3,800

(ii) Calculation of impairment loss

Step 1: Impairment losses for individual cash-generating units and its allocation

(a) Impairment loss of each cash-generating units

(Rs. in lakh)

Particulars	**X**	**Y**	**Z**
Carrying amount (after allocation of AU)	1,056	1,160	1,584
Recoverable amount	1,000	1,200	1,400
Impairment loss	56	Nil	184

(b) Allocation of the impairment loss (after rounding off)

(Rs. in lakh)

Allocation to	**X**		**Z**	
AU	14	(56x256/1,056)	45	(184x384/1,584)
Other assets in cash-generating units	42	(56x800/1056)	139	(184x1,200/ 1,584)
Impairment loss	56		184	

Step 2: Impairment loss for the larger cash-generating unit, i.e., XYZ Ltd. as a whole

Particulars	**X**	**Y**	**Z**	**AU**	**BU**	**XYZ Ltd.**
Carrying amount	800	1,000	1,200	800	400	4,200
Impairment loss (Step I)	(420	-	(139)	(59)*	-	(240)
Carrying amount (after Step I)	758	1,000	1,061	741	400	3,960
Recoverable amount						3,900
Impairment loss for the 'larger' cash-generating unit						60

*Rs.14 lakh + Rs.45 lakh = Rs.59 lakh.

Question 5 : May 2019 – RTP

Elia limited is a manufacturing company which deals in to manufacturing of cold drinks and beverages. It is having various plants across India. There is a Machinery A in the Baroda plant which is used for the purpose of bottling. There is one more machinery which is Machinery B clubbed with Machinery A. Machinery A can individually have an output and also sold independently in the open market. Machinery B cannot be sold in isolation and without clubbing with Machine A it cannot produce output as well. The Company considers this group of assets as a Cash Generating Unit and an Inventory amounting to Rs.2 Lakh and Goodwill amounting to Rs.1.50 Lakhs is included in such CGU.

Machinery A was purchased on 1st April 2013 for Rs.10 Lakhs and residual value is Rs.50 thousands. Machinery B was purchased on 1st April, 2015 for Rs.5 Lakhs with no residual value. The useful life of both Machine A and B is 10 years. The Company expects following cash flows in the next 5 years pertaining to Machinery A. The incremental borrowing rate of the company is 10%.

Year	Cash Flows from Machinery A
1	1,50,000
2	1,00,000
3	1,00,000
4	1,50,000
5	1,00,000 (excluding Residual Value)
Total	**6,00,000**

On 31st March, 2018, the professional valuers have estimated that the current market value of Machinery A is Rs.7 lakhs. The valuation fee was Rs.1 lakh. There is a need to dismantle the machinery before delivering it to the buyer. Dismantling cost is Rs.1.50 lakhs. Specialised packaging cost would be Rs.25 thousand and legal fees would be Rs.75 thousand.

The Inventory has been valued in accordance with Ind AS 2. The recoverable value of CGU is Rs.10 Lakh as on 31st March, 2018. In the next year, the company has done the assessment of recoverability of the CGU and found that the value of such CGU is Rs.11 Lakhs ie on 31st March, 2019. The Recoverable value of Machine A is Rs.4,50,000 and combined Machine A and B is Rs.7,60,000 as on 31st March, 2019.

Required:

a) Compute the impairment loss on CGU and carrying value of each asset after charging impairment loss for the year ending 31st March, 2018 by providing all the relevant working notes to arrive at such calculation.

b) Compute the prospective depreciation for the year 2018-2019 on the above assets.

c) Compute the carrying value of CGU as at 31st March, 2019.

Solution :

(a) Computation of impairment loss and carrying value of each of the asset in CGU after impairment loss

(i) Calculation of carrying value of Machinery A and B before impairment

Machinery A		
Cost	(A)	Rs.10,00,000
Residual Value		Rs.50,000
Useful life		10 years
Useful life already elapsed		5 years
Yearly depreciation	(B)	Rs.95,000
WDV as at 31st March, 2018 [A- (B x 5)]		**Rs.5,25,000**
Machinery B		
Cost	(C)	Rs.5,00,000
Residual Value		-
Useful life		10 years
Useful life already elapsed		3 years
Yearly depreciation	(D)	Rs.50,000
WDV as at 31st March, 2018 [C- (D x 3)]		**Rs.3,50,000**

(ii) Calculation of Value-in-use of Machinery A

Period	Cash Flows (Rs.)	PVF	PV
1	1,50,000	0.91	1,36,350
2	1,00,000	0.83	82,600
3	1,00,000	0.75	75,100
4	1,50,000	0.68	1,02,450
5	1,00,000	0.62	62,100
5	50,000	0.62	31,050
Value in use			**4,89,650**

(iii) Calculation of Fair Value less cost of disposal of Machinery A

	Rs.
Fair Value	7,00,000
Less: Dismantling cost	(1,50,000)
Packaging cost	(25,000)
Legal Fees	(75,000)
Fair value less cost of disposal	**4,50,000**

(iv) Calculation of Impairment loss on Machinery A

	Rs.
Carrying Value	5,25,000

Less: Recoverable Value ie higher of Value-in-use and Fair value less cost of disposal	4,89,650
Impairment Loss	**35,350**

(v) Calculation of Impairment loss of CGU

1. First goodwill will be impaired fully and then the remaining impairment loss of Rs.75,000 will be allocated to Machinery A and B.
2. If we allocate remaining impairment loss to Machinery A and B on pro-rata basis, it would come to Rs.45,000 on Machinery A. However, the impairment loss of Machinery A cannot exceed Rs.35,350. Hence, impairment to CGU will be as follows:

	Carrying value before impairment loss	**Impairment loss**	**Carrying value after impairment loss**
	Rs.	**Rs.**	**Rs.**
Machinery A	5,25,000	35,350	4,89,650
Machinery B	3,50,000	39,650*	3,10,350
Inventory	2,00,000	-	2,00,000
Goodwill	1,50,000	1,50,000	-
Total	**12,25,000**	**2,25,000**	**10,00,000**

* Balancing figure.

(b) Carrying value after adjustment of depreciation

	Rs.
Machinery A [4,89,650 – {(4,89,650 – 50,000)/5}]	4,01,720
Machinery B [3,10,350 – (3,10,350/7)]	2,66,014
Inventory	2,00,000
Goodwill	-
Total	**8,67,734**

(c) Calculation of carrying value of CGU as on 31st March, 2019

The revised value of CGU is Rs.11 Lakh. However, impaired goodwill cannot be reversed. Further, the individual assets cannot be increased by lower of recoverable value or Carrying Value as if the assets were never impaired.

Accordingly, the carrying value as on 31st March, 2019 assuming that the impairment loss had never incurred, will be:

	Carrying Value	**Recoverable Value**	**Final CV as at 31st Mar 2019**
Machinery A	4,30,000	4,50,000	4,30,000
Machinery B	3,00,000	(7,60,000 – 4,50,000) 3,10,000	3,00,000

Inventory	2,00,000	2,00,000	2,00,000
Goodwill	-		
Total	**9,30,000**	**9,60,000**	**9,30,000**

Hence the impairment loss to be reversed will be limited to Rs.62,266 only (Rs.9,30,000 – Rs.8,67,734).

Question 6 : Nov 2019 – RTP

East Ltd. (East) owns a machine used in the manufacture of steering wheels, which are sold directly to major car manufacturers.

- The machine was purchased on 1st April, 20X1 at a cost of Rs.5,00,000 through a vendor financing arrangement on which interest is being charged at the rate of 10 per cent per annum.
- During the year ended 31st March, 20X3, East sold 10,000 steering wheels at a selling price of Rs.190 per wheel.
- The most recent financial budget approved by East's management, covering the period 1st April, 20X3 – 31st March, 20X8, including that the company expects to sell each steering wheel for Rs.200 during 20X3-X4, the price rising in later years in line with a forecast inflation of 3 per cent per annum.
- During the year ended 31st March, 20X4, East expects to sell 10,000 steering wheels. The number is forecast to increase by 5 per cent each year until 31st March, 20X8.
- East estimates that each steering wheel costs Rs.160 to manufacture, which includes Rs.110 variable costs, Rs.30 share of fixed overheads and Rs.20 transport costs.
- Costs are expected to rise by 1 per cent during 20X4-X5, and then by 2 per cent per annum until 31st March, 20X8.
- During 20X5-X6, the machine will be subject to regular maintenance costing Rs.50,000.
- In 20X3-X4, East expects to invest in new technology costing Rs.1,00,000. This technology will reduce the variable costs of manufacturing each steering wheel from Rs.110 to Rs.100 and the share of fixed overheads from Rs.30 to Rs.15 (subject to the availability of technology, which is still under development).
- East is depreciating the machine using the straight line method over the machine's 10 year estimated useful life. The current estimate (based on similar assets that have reached the end of their useful lives) of the disposal proceeds from selling the machine is Rs.80,000 net of disposal costs. East expects to dispose of the machine at the end of March, 20X8.
- East has determined a pre-tax discount rate of 8 per cent, which reflects the market's assessment of the time value of money and the risks associated with this asset.

Assume a tax rate of 30%. What is the value in use of the machine in accordance with Ind AS 36?

Solution :

Calculation of the value in use of the machine owned by East Ltd. (East) includes the projected cash inflow (i.e. sales income) from the continued use of the machine and projected cash outflows that are necessarily incurred to generate those cash inflows (i.e cost of goods sold). Additionally, projected cash inflows include Rs.80,000 from the disposal of the asset in March, 20X8. Cash outflows include routing capital expenditures of Rs.50,000 in 20X5-X6

As per Ind AS 36, estimates of future cash flows shall not include:

- Cash inflows from receivables
- Cash outflows from payables
- Cash inflows or outflows expected to arise from future restructuring to which an entity is not yet committed
- Cash inflows or outflows expected to arise from improving or enhancing the asset's performance
- Cash inflows or outflows from financing activities
- Income tax receipts or payments.

Hence in this case, cash flows do not include financing interest (i.e. 10%), tax (i.e. 30%) and capital expenditures to which East has not yet committed (i.e. Rs.1,00,000). They also do not include any savings in cash outflows from these capital expenditure, as required by Ind AS 36.

The cash flows (inflows and outflows) are presented below in nominal terms. They include an increase of 3% per annum to the forecast price per unit (B), in line with forecast inflation. The cash flows are discounted by applying a discount rate (8%) that is also adjusted for inflation.

Note: Figures are calculated on full scale and then rounded off to the nearest absolute value.

Year ended	20X3-X4	20X4-X5	20X5-20X6	20X6-X7	20X7-X8	Value in use
Quantity (A)	10,000	10,500	11,025	11,576	12,155	
Price per unit(B)	Rs.200	Rs.206	Rs.212	Rs.219	Rs.225	
Estimated cash inflows (C = A x B)	Rs.20,00,000	Rs.21,63,000	Rs.23,37,300	Rs.25,35,144	Rs.27,34,875	
Misc. cash inflow disposal proceeds (D)					Rs.80,000	
Total estimated cash inflows (E=C+D)	Rs.20,00,000	Rs.21,63,000	Rs.23,37,300	Rs.25,35,144	Rs.28,14,875	
Cost per unit (F)	Rs.160	Rs.162	Rs.165	Rs.168	Rs.171	
Estimated cash outflows (G = A x F)	(Rs.16,00,000)	(Rs.17,01,000)	(Rs.18,19,125)	(Rs.19,44,768)	(Rs.20,78,505)	
Misc. cash outflow: maintenance costs (H)			(Rs.50,000)			
Total estimated cash outflows (I = G + H)	(Rs.16,00,000)	(Rs.17,01,000)	(Rs.18,69,125)	(Rs.19,44,768)	(Rs.20,78,505)	
Net cash flows (J = E - I)	Rs.4,00,000	Rs.4,62,000	Rs.4,68,175	Rs.5,90,376	Rs.7,36,370	
Discount factor 8% (K)	0.9259	0.8573	0.7938	0.7350	0.6806	
Discounted future cash flows (L = J x K)	Rs.3,70,360	Rs.3,96,073	Rs.3,71,637	Rs.4,33,926	Rs.5,01,173	Rs.20,73,169

Question 7 : May 2020 – RTP

PQR Ltd. is the company which has performed well in the past but one of its major assets, an item of equipment, suffered a significant and unexpected deterioration in performance. Management expects to use the machine for a further four years after 31st March 20X6, but at a reduced level. The equipment will be scrapped after four years. The financial accountant for PQR Ltd. has produced a set of cash-flow projections for the equipment for the next four years, ranging from optimistic to pessimistic. CFO thought that the projections were too conservative, and he intended to use the highest figures each year. These were as follows :

	Rs. '000
Year ended 31st March 20X7	276
Year ended 31st March 20X8	192
Year ended 31st March 20X9	120
Year ended 31st March 20Y0	114

The above cash inflows should be assumed to occur on the last day of each financial year. The pre-tax discount rate is 9%. The machine could have been sold at 31st March 20X6 for Rs.6,00,000 and related selling expenses in this regard could have been Rs.96,000. The machine had been re valued previously, and at 31st March 20X6 an amount of Rs.36,000 was held in revaluation surplus in respect of the asset. The carrying value of the asset at 31st March 20X6 was Rs.6,60,000. The Indian government has indicated that it may compensate the company for any loss in value of the assets up to its recoverable amount.

Calculate impairment loss, if any and revised depreciation of asset. Also suggest how Impairment loss, if any would be set off and how compensation from government be accounted for?

Solution :

Carrying amount of asset on 31st March 20X6 = Rs.6,60,000

Calculation of Value in Use :

Year ended	Cash flow Rs.	Discount factor @ 9%	Amount Rs.
31st March, 20X7	2,76,000	0.9174	2,53,202
31st March, 20X8	1,92,000	0.8417	1,61,606
31st March, 20X9	1,20,000	0.7722	92,664
31st March, 20Y0	1,14,000	0.7084	80,758
		Total (Value in Use)	5,88,230

Calculation of Recoverable amount :

Particulars	Amount (Rs.)
Value in use	5,88,230
Fair value less costs of disposal (6,00,000 – 96,000)	5,04,000
Recoverable amount (Higher of value in use and fair value less costs of disposal)	5,88,230

Calculation of Impairment loss:

Particulars	Amount (Rs.)
Carrying amount	6,60,000
Less: Recoverable amount	(5,88,230)
Impairment loss	71,770

Calculation of Revised carrying amount:

Particulars	Amount (Rs.)
Carrying amount	6,60,000

Less: Impairment loss	(71,770)
Revised carrying amount	5,88,230

Calculation of Revised Depreciation:
Revised carrying amount – Residual value
Remaining life = (5,88,230 - 0) / 4 = Rs.1,47,058 per annum

Set off of Impairment loss:
The impairment loss of Rs.71,770 must first be set off against any revaluation surplus in relation to the same asset. Therefore, the revaluation surplus of rs.36,000 is eliminated against impairment loss, and the remainder of the impairment loss Rs.35,770 (Rs.71,770 – Rs.36,000) is charged to profit and loss.

Treatment of Government compensation:
Any compensation by government would be accounted for as such when it becomes receivable. At this time, the government has only stated that it may reimburse the company and therefore credit should not be taken for any potential government receipt.

Question 8 : Nov 2020 – RTP

The UK entity with a sterling functional currency has a property located in US, which was acquired at a cost of US$ 1.8 million when the exchange rate was ₤1 = US$ 1.60. The property is carried at cost. At the balance sheet date, the recoverable amount of the property (as a result of an impairment review) amounted to US$ 1.62 million, when the exchange rate ₤1 = US$ 1.80. Compute the amount which is to be reported in Profit & Loss of UK entity as a result of impairment, if any. Ignore depreciation. Also analyse the total impairment loss on account of change in value due to impairment component and exchange component.

Solution :

1)	Cost of Asset (18,00,000 $/1.6)			11,25,000
	– Recoverable Amount (16,20,000/1.8)			9,00,000
	Impairment Loss			2,25,000
2)	Impairment Loss			2,25,000
	(a)	Exchange Component		
		(18,00,000/1.8) =	10,00,000	
		(18,00,000/1.6) =	11,25,000	1,25,000
	(b)	Fall in value		
		(18,00,000/1.8) =	10,00,000	
		(16,20,000/1.8) =	9,00,000	1,00,000

Question 9 : May 2021 – RTP

On 31 March 20X1, Vision Ltd acquired 80% of the equity shares of Mission Ltd for Rs. 190 million. The fair values of the net assets of Mission Ltd that were included in the consolidated statement of financial position of Vision Ltd at 31 March 20X1 were Rs. 200 million. It is the Group's policy to value the non-controlling interest in subsidiaries at the date of acquisition at its proportionate share of the fair value of the subsidiaries' identifiable net assets.

On 31 March 20X4, Vision Ltd carried out its annual review of the goodwill on consolidation of Mission Ltd and found evidence of impairment. No impairment had been evident when the reviews were carried out at 31 March 20X2 and 31 March 20X3. The review involved allocating the assets of Mission Ltd into three cash-generating units and computing the value in use of each unit. The carrying values of the individual units before any impairment adjustments are given below:

	Unit A Rs. in million	**Unit B Rs. in million**	**Unit C Rs. in million**
Intangible assets	30	10	-
Property, Plant and Equipment	80	50	60
Current Assets	60	30	40
Total	170	90	100
Value in use of unit	180	66	104

It was not possible to meaningfully allocate the goodwill on consolidation to the individual cash generating units but all the other net assets of Mission Ltd are allocated in the table shown above. The intangible assets of Mission Ltd have no ascertainable market value but all the current assets have a market value that is at least equal to their carrying value. The value in use of Mission Ltd as a single cash-generating unit on 31 March 20X4 is Rs. 350 million.

Discuss and compute the accounting treatment of impairment of goodwill as per Ind AS 36?

Solution :

The goodwill on consolidation of Mission Ltd that is recognized in the consolidated balance sheet of Vision Ltd is Rs. 30 million (Rs. 190 million – 80% x Rs. 200 million). This can only be reviewed for impairment as part of the cash generating units to which it relates. Since here the goodwill cannot be meaningfully allocated to the units, the impairment review is in two parts.

Units A and C have values in use that are more than their carrying values. However, the value in use of Unit B is less than its carrying amount. This means that the assets of unit B are impaired by Rs. 24 million (Rs. 90 million – Rs. 66 million). This impairment loss will be charged to the statement of profit and loss.

Assets of Unit B will be written down on a pro-rata basis as shown in the table below:

(Rs. in million)

Asset	**Impact on carrying value**		
	Existing	**Impairment**	**Revised**
Intangible assets	10	(4)	6
Property, plant and equipment	50	(20)	30
Current assets	30	Nil*	30

Total	90	(24)	66

* The current assets are not impaired because they are expected to realize at least their carrying value when disposed of.

Following this review, the three units plus the goodwill are reviewed together i.e. treating Mission Limited as single cash generating Unit. The impact of this is shown in the following table, given that the recoverable amount of the business as a whole is Rs. 350 million:

(Rs. in million)

Component	**Impact of impairment review on carrying value**		
	Existing	**Impairment**	**Revised**
Goodwill (see note below)	37.50	(23.50)	14.00
Unit A	170.00	Nil	170.00
Unit B (revised)	66.00	Nil	66.00
Unit C	100.00	Nil	100.00
Total	373.50	(23.50)	350.00

Note: As per Appendix C of Ind AS 36, given that the subsidiary is 80% owned the goodwill must first be grossed up to reflect a notional 100% investment. Therefore, the goodwill will be grossed up to Rs. 37.50 million (Rs. 30 million x 100/80).

The impairment loss of Rs. 23.50 million is all allocated to goodwill, leaving the carrying values of the individual units of the business as shown in the table immediately above.

The table shows that the notional goodwill that relates to a 100% interest is written down by Rs. 23.50 million to Rs. 14.00 million. However, in the consolidated financial statements the goodwill that is recognized is based on an 80% interest so the loss that is actually recognized is Rs. 18.80 million (Rs. 23.50 million x 80%) and the closing consolidated goodwill figure is Rs. 11.20 million (Rs. 14.00 million x 80%) or (Rs. 30 million – Rs. 18.80 million).

Question 10 : July 2021 – Paper

A Limited purchased as asset of Rs.200 lakh on 1st April 2017. It has useful life of 4 years with no residual value. Recoverable amount of the asset is as follows :

As on	Recoverable amount
31st March, 2018	Rs.120 lakh
31st March, 2019	Rs.80 lakh
31st March 2020	Rs.56 lakh

Calculate the amount of impairment loss or its reversal, if any,

– On 31st March, 2018;
– On 31st March, 2019;
– On 31st March, 2020;

Depreciation is provided on SLM basis under the cost method.

Solution :

As on 31st March, 2018

Carrying amount of the asset (opening balance)	Rs. 200 lakh

Depreciation (Rs. 200 lakh / 4 years)	(Rs. 50 lakh)
Carrying amount of the asset (closing balance)	Rs. 150 lakh
Recoverable amount (given)	Rs. 120 lakh
Difference	Rs. 30 lakh

Therefore, an impairment loss of Rs. 30 lakh should be recognised as on 31st March, 2018. Depreciation for subsequent years should be charged on the carrying amount of the asset (after providing for impairment loss), i.e., Rs. 120 lakh.

As on 31st March, 2019

Carrying amount of the asset (opening balance)	Rs. 120 lakh
Depreciation (Rs. 120 lakh / 3 years)	(Rs. 40 lakh)
Carrying amount of the asset (closing balance)	Rs. 80 lakh
Recoverable amount (Given)	Rs. 80 lakh
Difference	NIL

Therefore, no impairment loss should be recognised as on 31st March, 2019.

As on 31st March, 2020

Carrying amount of the asset (opening balance)	Rs. 80 lakh
Depreciation (Rs. 80 lakh / 2 years)	(Rs. 40 lakh)
Carrying amount of the asset (closing balance)	Rs. 40 lakh
Recoverable amount (given)	Rs. 56 lakh
Difference	(Rs. 16 lakh)

Since, the recoverable amount of the asset exceeds the carrying amount of the asset by Rs. 16 lakh, impairment loss recognised earlier should be reversed. However, reversal of an impairment loss should not exceed the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognised for the asset in prior years. Carrying amount as on 31st March, 2020 had no impairment loss being recognised would have been Rs. 50 lakh [ie. Rs. 200 lakh – (200 lakh / 4 x 3)]. Therefore, the reversal of an impairment loss of Rs. 10 lakh (Rs. 50 lakh - Rs. 40 lakh) should be done as on 31st March, 2020.

Thanks ....

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IND AS – 116 LEASES

CHAPTER - 10

Question 1 : Nov 2020 – RTP

Entity X (lessee) entered into a lease agreement ('lease agreement') with Entity Y (lessor) to lease an entire floor of a shopping mall for a period of 9 years. The annual lease rent of Rs. 70,000 is payable at year end. To carry out its operations smoothly, Entity X simultaneously entered into another agreement ('facilities agreement') with Entity Y for using certain other facilities owned by Entity Y such as passenger lifts, DG sets, power supply infrastructure, parking space etc., which are specifically mentioned in the agreement, for annual service charges amounting to Rs. 1,00,000. As per the agreement, the ownership of the facilities shall remain with Entity Y. Lessee's incremental borrowing rate is 10%.

The facilities agreement clearly specifies that it shall be co-existent and coterminous with 'lease agreement'. The facility agreement shall stand terminated automatically on termination or expiry of 'lease agreement'.

Entity X has assessed that the stand-alone price of 'lease agreement' is Rs.1,20,000 per year and stand-alone price of the 'facilities agreement' is Rs.80,000 per year. Entity X has not elected to apply the practical expedient in paragraph 15 of Ind AS 116 of not to separate non-lease component (s) from lease component(s) and accordingly it separates non-lease components from lease components.

How will Entity X account for lease liability as at the commencement date?

Solution :

1) As per IND AS 116, the Entity X identifies that contract contains lease of premises and non-lease component of facilities availed. Since Entity X has not availed practically expedient as provided, it will separate lease and non-lease component.

2) As per IND AS 116, the total consideration of 1,70,000 (1,00,000 + 70,000) should be allocated to lease and non-lease in ratio of their stand along price as follows :

Building = $1{,}70{,}000 \times \dfrac{1{,}20{,}000}{1{,}20{,}000 + 80{,}000}$ = 1,02,000

Facilities = $1{,}70{,}000 \times \dfrac{80{,}000}{1{,}20{,}000 + 80{,}000}$ = 68,000

3) Leases should recognise ROV Asset and Lease liability at commencement date.
Incremental borrowing cost = 10%
$\therefore$ PV of LR = 1,02,000 + PVIFA (10%, 9)
= 5,87,420

4) Non lease component of Rs.68,000 should be changed to P/L at end of every year.

Question 2 : Nov 2020 – Paper

Venus Ltd. (Seller-lessee) sells a building to Mars Ltd. (Buyer-lessor) for cash of Rs. 28,00,000. Immediately before the transaction, the building is carried at a cost of Rs. 13,00,000. At the same time, Seller- lessee enters into a contract with Buyer-lessor for the right to use the building for 20 years, with an annual payment of Rs. 2,00,000 payable at the end of each year.
The terms and conditions of the transaction are such that the transfer of the building by Seller-lessee satisfies the requirements for determining when a performance obligation is satisfied in accordance with Ind AS 115 "Revenue from Contracts with Customers".
The fair value of the building at the date of sale is Rs. 25,00,000. Initial direct costs, if any, are to be ignored. The interest rate implicit in the lease is 12% p.a., which is readily determinable by Seller-lessee. Present Value (PV) of annual payments (20 payments of Rs. 2,00,000 each discounted @ 12%) is Rs. 14,94,000.
Buyer-lessor classifies the lease of the building as an operating lease. How should the said transaction be accounted by Venus Ltd.?

Solution :

Considering facts of the case, Venus Ltd. (seller-lessee) and Mars Ltd. (buyer-lessor) account for the transaction as a sale and leaseback.
Firstly, since the consideration for the sale of the building is not at fair value, Seller-lessee and Buyer - lessor make adjustments to measure the sale proceeds at fair value. Thus, the amount of the excess sale price of Rs. 3,00,000 (as calculated below) is recognised as additional financing provided by Buyer-lessor to Seller-lessee.

Sale Price:	28,00,000
Less: Fair Value (at the date of sale):	(25,00,000)
Additional financing provided by Buyer-lessor to Seller-lessee	3,00,000

The present value of the annual payments is Rs. 14,94,000 (as given in the question).
Out of this Rs. 14,94,000, Rs. 3,00,000 relates to the additional financing (as calculated above) and balance Rs. 11,94,000 relates to the lease.

Accounting by Venus Ltd. (seller-lessee):

At the commencement date, Seller-lessee measures the ROU asset arising from the leaseback of the building at the proportion of the previous carrying amount of the building that relates to the right-of-use retained by Seller-lessee, calculated as follows:

Carrying Amount	(A)	13,00,000
Fair Value (at the date of sale)	(B)	25,00,000
Discounted lease payments for the 20 year ROU asset	(C)	11,94,000
ROU Asset	[(A / B) x C]	6,20,880

Seller-lessee recognises only the amount of the gain that relates to the rights transferred to Buyer-lessor, calculated as follows:

Fair Value (at the date of sale)	(A)	25,00,000

Carrying Amount	(B)	13,00,000
Discounted lease payments for the 20-year ROU asset	(C)	11,94,000
Gain on sale of building	(D) = (A - B)	12,00,000
Relating to the right to use the building retained by Seller-lessee	(E)=[(D/A)xC]	5,73,120
Relating to the rights transferred to Buyer-lessor	(D - E)	6,26,880

At the commencement date, Seller-lessee accounts for the transaction, as follows:

Bank / Cash A/c	Dr.	28,00,000	
ROU Asset A/c	Dr.	6,20,880	
To Building			13,00,000
To Financial Liability			14,94,000
To Gain on rights transferred			6,26,880

Question 3 : Jan 2021 – Paper

Coups Limited availed a machine on lease from Ferrari Limited. The terms and conditions of the Lease are as under:

Lease period is 3 years, machine costing Rs.8,00,000.

- Machine has expected useful life of 5 years.
- Machine reverts back to Ferrari Limited on termination of lease.
- The unguaranteed residual value is estimated at Rs.50,000 at the end of 3rd year.
- 3 equal annual installments are made at the end of each year.
- Implicit Interest Rate (IRR) = 10%.
- Present value of Rs.1 due at the end of 3rd year at 10% rate of interest is 0.7513.
- Present value of annuity of Rs.1 due at the end of 3rd year at 10% IRR is 2.4868.

You are required to ascertain whether it is a Finance Lease or Operating Lease and also calculate Unearned Finance Income with the relevant context to relevant Ind AS.

Solution :

It is assumed that the fair value of the machine on lease is equivalent to the cost of the machine.

(i) A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership of an underlying asset. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership of an underlying asset.

(ii) Computation of annual lease payment to the lessor

	Rs.
Cost of equipment / fair value	8,00,000
Unguaranteed residual value	50,000
Present value of residual value after third year @ 10% (50,000 x 0.7513)	37,565
Fair value to be recovered from lease payments (8,00,000 – 37,565)	7,62,435
Present value of annuity for three years is 2.4868	
Annual lease payment = 7,62,435 / 2.4868	3,06,593

The present value of lease payment i.e., Rs.7,62,435 is more than 95% of the fair market value i.e., Rs.8,00,000. The present value of minimum lease payments substantially covers the initial fair value of the leased asset and lease term (i.e. 3 years) covers the major part of the life of asset (i.e. 5 years). Therefore, it constitutes a finance lease.

(iii) Computation of Unearned Finance Income

	Rs.
Total lease payments (Rs.3,06,593 x 3)	9,19,779
Add: Unguaranteed residual value	50,000
Gross investment in the lease	9,69,779
Less: Present value of investment (lease payments and residual value) (37,565 + 7,62,435)	(8,00,000)
Unearned finance income	1,69,779

Question 4 : May 2021 – RTP

Entity X is an Indian entity whose functional currency is Indian Rupee. It has taken a plant on lease from Entity Y for 5 years to use in its manufacturing process for which it has to pay annual rentals in arrears of USD 10,000 every year. On the commencement date, exchange rate was USD = Rs. 68. The average rate for Year 1 was Rs. 69 and at the end of year 1, the exchange rate was Rs. 70. The incremental borrowing rate of Entity X on commencement of the lease for a USD borrowing was 5% p.a.

How will entity X measure the right of use (ROU) asset and lease liability initially and at the end of Year 1?

Solution :

On initial measurement, Entity X will measure the lease liability and ROU asset as under:

Year	**Lease Payments (USD)**	**Present Value factor @ 5%**	**Present Value of Lease Payment**	**Conversion rate (spot rate)**	**INR value**
1	10,000	0.952	9,520	68	6,47,360
2	10,000	0.907	9,070	68	6,16,760
3	10,000	0.864	8,640	68	5,87,520
4	10,000	0.823	8,230	68	5,59,640
5	10,000	0.784	7,840	68	5,33,120
Total			**43,300**		**29,44,400**

As per Ind AS 21, The Effects of Changes in Foreign Exchange Rates, monetary assets and liabilities are restated at each reporting date at the closing rate and the difference due to foreign exchange movement is recognised in profit and loss whereas non-monetary assets and liabilities carried measured in terms of historical cost in foreign currency are not restated.

Accordingly, the ROU asset in the given case being a non-monetary asset measured in terms of historical cost in foreign currency will not be restated but the lease liability being a monetary liability will be restated at each reporting date with the resultant difference being taken to profit and loss.

At the end of Year 1, the lease liability will be measured in terms of USD as under:
Lease Liability:

Year	Initial Value (USD) (a)	Lease Payment (b)	Interest @ 5% (c) = (a x 5%)	Closing Value (USD) (d = a + c - b)
1	43,300	10,000	2,165	35,465

Interest at the rate of 5% will be accounted for in profit and loss at average rate of Rs. 69 (i.e., USD 2,165 x 69) = Rs. 1,49,385.

Particulars		Dr. (Rs.)	Cr. (Rs.)
Interest Expense	Dr.	1,49,385	
To Lease liability			1,49,385

Lease payment would be accounted for at the reporting date exchange rate, i.e. Rs. 70 at the end of year 1

Particulars		Dr. (Rs.)	Cr. (Rs.)
Lease liability	Dr.	7,00,000	
To Cash			7,00,000

As per the guidance above under Ind AS 21, the lease liability will be restated using the reporting date exchange rate i.e., Rs. 70 at the end of Year 1. Accordingly, the lease liability will be measured at Rs. 24,82,550 (35,465 x Rs. 70) with the corresponding impact due to exchange rate movement of Rs. 88,765 (24,82,550 – (29,44,400 + 1,49,385 – 700,000) taken to profit and loss.
At the end of year 1, the ROU asset will be measured as under:

Year	Opening Balance (Rs.)	Depreciation (Rs.)	Closing Balance (Rs.)
1	29,44,400	5,88,880	23,55,520

Question 5 : July 2021 – Paper

Ted entered into a lease contract with lessor to lease 2,000 sqm of retail space for 5 years. The rentals are payable monthly in advance. The lease commenced on 1st April 2019. In the year 2020, as a direct consequence of Covid 19 pandemic, Ted has negotiated with the lessor which may results in the following situations.

- Lessor agrees a rent concession under which the monthly rent will be reduced by 30% per month for the 12 months commencing 1st October, 2020.
- Ted is granted a rent concession by the lessor whereby the lease payments for the period October 2020 to December 2020 are deferred. Three months are added to the end of the lease term at same monthly rent.
- Lessor offers to reduce monthly rent by 50% for the months October 2020 to March 2021 on the condition that its space is reduced from 2,000 sq m to 1,500 sq m.

Analyse the given situations in the light of Ind AS 116 and comment on whether rent concession/deferral is eligible for practical expedient?

Solution :

Applicability of practical expedient:

The practical expedient applies only to rent concessions occurring as a direct consequence of the covid-19 pandemic.

As a practical expedient, a lessee may elect not to assess a rent concession as a lease modification only if **all** of the following conditions are met:

(a) the change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change;

(b) any reduction in lease payments affects only payments originally due on or before the 30th June, 2021; and

(c) there is no substantive change to other terms and conditions of the contract

Analysis:

Based on above guidance, answer to the given situations with the lessor would be as follows:

- Lessor agrees a rent concession under which the monthly rent will be reduced by 30% per month for the 12 months commencing 1st October 2020:
  The rent deferral does not satisfy the criteria to apply the practical expedient because out of the listed eligibility criteria given in Ind AS 116, rent concession reduces lease payments starting from October, 2020 and reduction will continue till September, 2021 which is beyond 30th June 2021. Therefore, Ted is not permitted to apply the practical expedient.
- Ted is granted a rent concession by the lessor whereby the lease payments for the period October 2020 to December 2020 are deferred. Three months are added to the end of the lease term at same monthly rent:
  (a) condition is met since revised consideration in the lease is substantially the same as the original
  (b) condition is met since the rent concession only reduces lease payments originally due in 2020 – i.e. before 30th June 2021.
  (c) condition is met since the lessee assesses that three-month extension at the end of the lease term is with substantially the same lease payments. Hence, it would not constitute a substantive change.

  Since, the rent concession is a direct consequence of COVID-19 and all three conditions are met, rent concession is eligible for application of practical expedient in this case.
- Lessor offers to reduce monthly rent by 50% for the months October 2020 to March 2021 on the condition that its space is reduced from 2,000 sqm to 1,500 sqm:
  The rent concession does not satisfy the criteria to apply the practical expedient because out of the listed eligibility criteria given in Ind AS 116, there is a substantive change to the terms and conditions of the lease as there is a change in the scope of lease by reducing the space from 2,000 sqm to 1,500 sqm. Therefore, Ted is not permitted to apply the practical expedient.

Question 6 : Nov 2021 – RTP

The Company has entered into a lease agreement for its retail store as on 1st April, 20X1 for a period of 10 years. A lease rental of Rs. 56,000 per annum is payable in arrears. The Company recognized a lease liability of Rs. 3,51,613 at inception using an incremental borrowing rate of 9.5% p.a. as at 1st April 20X1. As per the terms of lease agreement, the lease rental shall be adjusted every 2 years to give effect of inflation. Inflation cost index as notified by the Income tax department shall be used to derive the lease payments. Inflation cost index was 280 for financial year 20X1-20X2 and 301 for financial year 20X3-20X4. The current incremental borrowing rate is 8% p.a.

Show the Journal entry at the beginning of year 3, to account for change in lease.

Solution :

As per para 27 (b) of Ind AS 116, variable lease payments that depend on an index or a rate, are initially measured using the index or rate as at the commencement date.

At the beginning of the third year, Lessee remeasures the lease liability at the present value of eight payments of Rs. 60,200 discounted at an original discount rate of 9.5% per annum as per para 43 of Ind AS 116.

Year	Revised lease rental	Discount factor @ 9.5%	Present value
3	[(56,000 / 280) x 301] = 60,200	0.913	54,963
4	60,200	0.834	50,207
5	60,200	0.762	45,872
6	60,200	0.696	41,899
7	60,200	0.635	38,277
8	60,200	0.58	34,916
9	60,200	0.53	31,906
10	60,200	0.484	29,137
			3,27,127

Table showing amortised cost of lease liability

Year	Opening balance	Interest @ 9.5%	Rental paid	Closing balance
1	3,51,613	33,403	56,000	3,29,016
2	3,29,016	31,257	56,000	3,04,273

Difference of Rs. 22,854 (3,27,127 – 3,04,273) will increase the lease liability with corresponding increase in ROU Asset as per para 39 of Ind AS 116.

Journal entry at the beginning of year 3 would be:

Right-of-use asset	Dr.	Rs. 22,854	
To Lease liability			Rs. 22,854

Question 7 : May 2022 – RTP

Case I

Scenario 1: The 'last mile' is a dedicated cable that connects Entity Y's network with the end customer's device. The use of this cable is at the discretion of the customer. Entity Y decides the location of end points and has right to replace the lines (dedicated cable), however it is not practical to replace the lines, since replacement would require additional costs to be incurred without any corresponding benefit. Whether the arrangement would be within the scope of Ind AS 116?

Scenario 2: If it is practical for the Entity Y to replace the lines and Entity Y would benefit from this replacement, would the answer be different?

Case II

Customer X enters into a 10-year contract with a utility company, Entity Y, for the right to use three specified, physically distinct fibers within a larger cable connecting Mumbai to Delhi. Customer makes the decisions about the use of the fibers by connecting each end of the fibers to its electronic equipment. Entity Y owns extra fibers but can substitute those for Customer's fibers only for reasons of repairs, maintenance or malfunction. The useful life of the fiber is 15 years. Whether this arrangement is covered under Ind AS 116?

Case III

Customer X enters into a 10-year contract with Entity Y for the right to use a specified amount of capacity within a cable connecting Mumbai to Delhi. The specified amount is equivalent to Customer X having the use of the full capacity of three fiber strands within the cable (the cable contains multiple fibers with similar capacities). Entity Y makes decisions about the transmission of data (i.e., Entity Y lights the fibers, makes decisions about which fibers are used to transmit Customer's traffic). The useful life of the fiber is 15 years. Whether this arrangement is covered under Ind AS 116?

Solution :

Paragraph 9, B9, B13 and B14 of Ind AS 116 state the following:

"9 At inception of a contract, an entity shall assess whether the contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration."

"B9 To assess whether a contract conveys the right to control the use of an identified asset for a period of time, an entity shall assess whether, throughout the period of use, the customer has both of the following:

(a) the right to obtain substantially all of the economic benefits from use of the identified asset; and

(b) the right to direct the use of the identified asset."

"B13 An asset is typically identified by being explicitly specified in a contract. However, an asset can also be identified by being implicitly specified at the time that the asset is made available for use by the customer."

"B14 Even if an asset is specified, a customer does not have the right to use an identified asset if the supplier has the substantive right to substitute the asset throughout the period of use. A supplier's right to substitute an asset is substantive only if both of the following conditions exist:

(a) the supplier has the practical ability to substitute alternative assets throughout the period of use (for example, the customer cannot prevent the supplier from substituting the asset and alternative assets are readily available to the supplier or could be sourced by the supplier within a reasonable period of time); and

(b) the supplier would benefit economically from the exercise of its right to substitute the asset (i.e., the economic benefits associated with substituting the asset are expected to exceed the costs associated with substituting the asset)."

Paragraph B20 of Ind AS 116 which provides guidance regarding identified asset in case of portion of assets states that a capacity portion of an asset is an identified asset if it is physically distinct (for example, a floor of a building). A capacity or other portion of an asset that is not physically distinct (for example, a capacity portion of a fibre optic cable) is not an identified asset, unless it represents substantially all of the capacity of the asset and thereby provides the customer with the right to obtain substantially all of the economic benefits from use of the asset.

Paragraph B21 of Ind AS 116, inter alia, states that to control the use of an identified asset, a customer is required to have the right to obtain substantially all of the economic benefits from use of the asset throughout the period of use (for example, by having exclusive use of the asset throughout that period). A customer can obtain economic benefits from use of an asset directly or indirectly in many ways, such as by using, holding or subleasing the asset.

Further, paragraph B24 of Ind AS 116 provides that a customer has the right to direct the use of an identified asset throughout the period of use if the customer has the right to direct how and for what purpose the asset is used throughout the period of use.

Paragraph B25 of Ind AS 116 states that a customer has the right to direct how and for what purpose the asset is used if, within the scope of its right of use defined in the contract, it can change how and for what purpose the asset is used throughout the period of use. In making this assessment, an entity considers the decision-making rights that are most relevant to changing how and for what purpose the asset is used throughout the period of use. Decision-making rights are relevant when they affect the economic benefits to be derived from use. The decision-making rights that are most relevant are likely to be different for different contracts, depending on the nature of the asset and the terms and conditions of the contract.

Case I

Scenario 1:

(i) As per paragraph B13 of Ind AS 116, 'Last mile' which is a dedicated cable is an identified asset since it is physically distinct.

(ii) There are no substantive substitution rights with Entity Y, as it does not have the practical ability to substitute alternative assets throughout the period of use.

Thus, this arrangement is within the scope of Ind AS 116.

Scenario 2:

If Entity Y has the practical ability to replace the lines and it would benefit from such replacement, Entity Y has substantive substitution rights. In such case, this arrangement for the 'last mile cable' will not be within the scope of Ind AS 116.

Case II

The fibers are specified in the contract and are physically distinct. Hence, in accordance with paragraph B13 and B20, the said three fibers are identified asset.

Paragraph B18, inter alia, states that the supplier's right or obligation to substitute the asset for repairs and maintenance, if the asset is not operating properly or if a technical upgrade becomes available does not preclude the customer from having the right to use an identified asset.

Further, paragraph B27 provides that although rights such as those to operate or maintain an asset are often essential to the efficient use of an asset, they are not rights to direct how and for what purpose the asset is used and can actually be dependent on the decisions about how and for what purpose the asset is used.

In accordance with the above, as Entity Y can substitute these three distinct fibers only for reasons of repairs, maintenance or malfunction, it does not preclude them from being an identified asset.

Further, the Customer X has right to control the use of the identified fibers for 10 year since it has–

(a) the right to obtain substantially all of the economic benefits from use of the identified fibers throughout the period of use, i.e., 10 years; and

(b) the right to direct the use of the fibers as it makes the decisions about the use of the fibers, i.e., it has right to direct how and for what purpose the fibers are used throughout the period of use.

Hence, this arrangement is within the scope of Ind AS 116.

Case III

Paragraph B20 specifically provides that a capacity or other portion of an asset that is not physically distinct (for example, a capacity portion of a fiber optic cable) is not an identified asset, unless it represents substantially all of the capacity of the asset and thereby provides the customer with the right to obtain substantially all of the economic benefits from use of the asset.

In the given case, the capacity portion that will be provided to Customer X is not physically distinct from the remaining capacity of the cable and does not represent substantially all of the capacity of the cable, thus, it is not an identified asset. Further, Entity Y makes all decisions about the transmission of data, (i.e., supplier lights the fibers, makes decisions about which fibers are used to transmit customer's traffic).

Thus, the contract does not contain a lease and is therefore not within the scope of Ind AS 116.

Thanks ....

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IND AS – 41 AGRICULTURE

CHAPTER - 11

Question 1 : Nov 2018 – RTP

As at 31st March, 2017, a plantation consists of 100 Pinus Radiata trees that were planted 10 years earlier. The tree takes 30 years to mature, and will ultimately be processed into building material for houses or furniture. The enterprise's weighted average cost of capital is 6% p.a.

Only mature trees have established fair values by reference to a quoted price in an active market. The fair value (inclusive of current transport costs to get 100 logs to market) for a mature tree of the same grade as in the plantation is:

As at 31st March, 2017: 171

As at 31st March, 2018: 165

Assume that there would be immaterial cash flow between now and point of harvest.

The present value factor of Rs.1 @ 6% for

19th year = 0.331

20th year = 0.312

State the value of such plantation as on 31st March, 2017 and 2018 and the gain or loss to be recognised as per Ind AS.

Solution :

As at 31st March, 2017, the mature plantation would have been valued at 17,100 (171 x 100).

As at 31st March, 2018, the mature plantation would have been valued at 16,500 (165 x 100).

Assuming immaterial cash flow between now and the point of harvest, the fair value (and therefore the amount reported as an asset on the statement of financial position) of the plantation is estimated as follows:

As at 31st March, 2017: 17,100 x 0.312 = 5,335.20.

As at 31st March, 2018: 16,500 x 0.331 = 5,461.50.

Gain or loss

The difference in fair value of the plantation between the two year end dates is 126.30 (5,461.50 – 5,335.20), which will be reported as a gain in the statement or profit or loss (regardless of the fact that it has not yet been realised).

Question 2 : Nov 2020 – RTP

Entity A purchased cattle at an auction on 30th June 2019

Purchase price at 30th June 2019	Rs.1,00,000
Costs of transporting the cattle back to the entity's farm	Rs.1,000
Sales price of the cattle at 31st March, 2020	Rs.1,10,000

The company would have to incur similar transportation costs if it were to sell the cattle at auction, in addition to an auctioneer's fee of 2% of sales price. The auctioneer charges 2% of the selling price, from both, the buyer as well as the seller.
Calculate the amount at which cattle is to be recognised in books on initial recognition and at year end 31st March, 2020.

Solution :

1) As per IND AS 41, Biological Assets should be measured at fair value less cost to sale. According, cattle should be recognised at

Purchase price	1,00,000
– Cost of transportation	1,000
– Auctioneer's commission (2%)	2,000
	97,000

2) Since the amount paid is 1,03,000, i.e. (1,00,000 + 1,000 + 2,000) the difference should be recorded as recognition loss.

3) Subsequent measurement at 31/3/2020

Sale value	1,10,000
– Transport cost	1,000
– Auctioneer Commission (2%)	2,200
	1,06,800

Question 3 : Jan 2021 – Paper

On 1st November 2019, Crattle Agro Limited purchased 100 goats of special breed from a market for Rs.10,00,000 with a transaction cost of 2%. Goats fair value decreased from Rs.10,00,000 to Rs.9,00,000 as on 31st March 2020. Determine the fair value on the date of purchase and as on financial year ended 31st March 2020. Also pass relevant journal entries on 1st November 2019 and 31st March 2020.

Solution :

The fair value less cost to sell of goats on the date of purchase i.e. on 1st November, 2019, would be Rs.9,80,000 (10,00,000-20,000). Expense of Rs. 20,000 would be recognised in profit and loss.

On date of Purchase

Biological Asset	Dr.	9,80,000	
Expense on initial recognition	Dr.	20,000	
To Bank			10,00,000
(Being biological asset purchased)			

On 31st March, 2020 goats would be measured at Rs. 8,82,000 as Biological Asset (9,00,000-18,000) and loss of Rs. 98,000 (9,80,000 - 8,82,000) would be recognised in profit or loss.

At the end of reporting period

Loss – Change in fair value	Dr.	98,000	
To Biological Asset			98,000

(Being change in fair value recognised at the end of reporting period)
Note: It is assumed that the transaction cost is borne by the seller.

Question 4 : May 2021 – RTP

Analyse whether the following activities fall within the scope of Ind AS 41 with proper reasoning:

- Managing animal-related recreational activities like Zoo
- Fishing in the ocean
- Fish farming
- Development of living organisms such as cells, bacteria and viruses
- Growing of plants to be used in the production of drugs
- Purchase of 25 dogs for security purpose of the company's premises.

Solution :

Activity	Whether in the scope of Ind AS 41?	Remarks
Managing animal-related recreational activities like Zoo	No	Since the primary purpose is to show the animals to public for recreational purposes, there is no management of biological transformation but simply control of the number of animals. Hence it will not fall in the purview of considered in the definition of agricultural activity.
Fishing in the ocean	No	Fishing in ocean is harvesting biological assets from unmanaged sources. There is no management of biological transformation since fish grow naturally in the ocean. Hence, it will not fall in the scope of the definition of agricultural activity.
Fish farming	Yes	Managing the growth of fish and then harvest for sale is agricultural activity within the scope of Ind AS 41 since there is management of biological transformation of biological assets for sale or additional biological assets.
Development of living organisms such as cells, bacteria viruses	Analysis required	The development of living organisms for research purposes does not qualify as agricultural activity, as those organisms are not being developed for sale, or for conversion into agricultural produce or into additional biological assets. Hence, development of such organisms for the said

		purposes does not fall under the scope of Ind AS 41. However, if the organisms are being developed for sale or use in dairy products, the activity will be considered as agricultural activity under the scope of Ind AS 41.
Growing of plants to be used in the production of drugs	Yes	If an entity grows plants for using it in production of drugs, the activity will be agricultural activity. Hence it will come under the scope of Ind AS 41.
Purchase of 25 dogs for security purposes of the company's premises	No	Ind AS 41 is applied to account for the biological assets when they relate to agricultural activity. Guard dogs for security purposes do not qualify as agricultural activity, since they are not being kept for sale, or for conversion into agricultural produce or into additional biological assets. Hence, they are outside the scope of Ind AS 41.

Question 5 : July 2021 – Paper

Sewa Dairy Limited prepared financial statements to 31st March each year. On 1st April 2020 the Company carried out the following transactions :

- Purchased a land for Rs.60 lakhs
- Purchased 200 dairy cows (Average age at 1st April 2020 – 2 years) for Rs.20 lakhs. Received a non – refundable grant of Rs.10 lakhs towards the acquisition of the cows.

During the year ending 31st March 2021n the company on its dairy cows incurred Rs.8.50 lakhs to maintain their condition 9food and protection) and Rs.4.60 lakhs as breeding fee to a local farmer. On 1st October 2020, 120 calves were born. There were no other changes in the number of animals during the year ended 31st March 2021. Sewa Dairy Limited had 3,200 litres of unsold milk in inventory as on 31st March 2021. The milk was sold on 1st and 2nd April 2021 at market prices.

The information regarding fair values is as follows :

Items	**Fair values less cost to sell (All values in Rs.)**		
	1st April 2020	**1st Oct. 2020**	**31st March 2021**
Land	60 Lakhs	70 Lakhs	80 Lakhs
New born calves (per calf)	2,000	2,300	2,500
6 months old calves (per calf)	2,200	2,500	2,800
2 years old cow (per cow)	10,000	10,250	10,500
3 years old cow (per cow)	10,500	10,800	11,000
Milk per litre	25	27	30

Prepare extract from the Balance Sheet (assuming land under cost method) and Statement of Profit and Loss that would be reflected in the financial statements of Sewa dairy Limited for the year ended 31st March, 2021. Discuss the relevant Ind AS in support of your workings.

Solution :

Extract from the Statement of Profit and Loss of Sewa Diary Limited
for the period ended on 31st March, 2021

		WN	Amount
Income			
Change in fair value of purchased dairy cow		WN 2	2,00,000
Government Grant		WN 3	10,00,000
Change in the fair value of newly born calves		WN 4	3,36,000
Fair Value of Milk		WN 5	96,000
Total Income	**(A)**		**16,32,000**
Expenses			
Maintenance Costs		WN 2	8,50,000
Breeding Fee		WN 2	4,60,000
Total Expense	**(B)**		(13,10,000)
Net Income	**(A-B)**		3,22,000

Extracts from Balance Sheet of Sewa Diary Limited
As at 31st March, 2021

	WN		Amount
Property, Plant and Equipment:			
Land	WN 1		60,00,000
Biological assets other than bearer plants:			
Dairy Cow	WN 2	22,00,000	
Calves	WN 4	3,36,000	25,36,000
Inventory:			
Milk	WN 5		96,000

Working Notes:

1. **Land:** The purchase of the land is not covered by Ind AS 41. The relevant standard which would apply to this transaction is Ind AS 16. Under this standard, the land would initially be recorded at cost and depreciated over its useful economic life, which is usually considered to be infinite. Hence, no depreciation would be appropriate. Under Cost Model, no recognition would be made for post-acquisition changes in the value of land.
2. **Dairy Cows:** Under the 'fair value model' laid down in Ind AS 41 the mature cows would be recognised in the Balance Sheet at 31st March, 2021 at the fair value of 200 x Rs. 11,000 = Rs. 22,00,000.
   Increase in price change 200 x (10,500 - 10,000) = 1,00,000
   Increase in physical change 200 x (11,000 – 10,500) = 1,00,000
   The total difference between the fair value of matured herd and its initial cost (Rs. 22,00,000 – Rs. 20,00,000 = a gain of Rs. 2,00,000) would be recognised in the profit and

loss along with the maintenance cost and breeding fee of Rs. 8,50,000 and Rs. 4,60,000 respectively.

3. **Grant:** Grant relating to agricultural activity is not subject to the normal requirement of Ind AS 20. Under Ind AS 41 such grants are credited to income as soon as they are unconditionally receivable rather than being recognised over the useful economic life of the herd. Therefore, Rs. 10,00,000 would be credited to income of the company.
4. **Calves:** They are a biological asset and the fair value model is applied. The breeding fee is charged to income and an asset of 120 x Rs. 2,800 = Rs. 3,36,000 recognised in the Balance sheet and credited to Profit and loss.
5. **Milk:** This is agricultural produce and initially recognised on the same basis as biological assets. Thus, the milk would be valued at 3,200 x Rs. 30 = Rs. 96,000. This is regarded as 'cost' for the future application of Ind AS 2 to the unsold milk.

Thanks ....

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IND AS – 21 THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATE

CHAPTER - 12

Question 1 : May 2018 – RTP

On 30th January, 20X1, A Ltd. purchased a machinery for $5,000 from USA supplier on credit basis. A's Ltd. functional currency is the Rupee. The exchange rate on the date of transaction is 1$= Rs.60. The fair value of the machinery determined on 31st March, 20X1 is $ 5,500. The exchange rate on 31st March, 20X1 is 1$= Rs.65. The payment to overseas supplier done on 31st March 20X2 and the exchange rate on 31st March 20X2 is 1$= Rs.67. The fair value of the machinery remain unchanged for the year ended on 31st March 20X2. Prepare the Journal entries for the year ended on 31st March 20X1 and year 20X2 according to Ind AS 21.

Solution :

Journal Entries

Purchase of Machinery on credit basis on 30th January 20X1:

		Rs.	Rs.
Machinery A/c (5,000 x $ 60)	Dr.	3,00,000	
To Creditors			3,00,000
(Initial transaction will be recorded at exchange rate on the date of transaction)			

Exchange difference arising on translating monetary item on 31st March 20X1:

		Rs.	Rs.
Machinery A/c [(5,500 x $ 65) – (5,000 x $ 60)]	Dr.	57,500	
To Profit & loss a/c (Exchange Profit & Loss)			57,500
Profit & Loss A/c [(5,000 x $ 65) – (5,000 x $ 60)]	Dr.	25,000	
To Creditors			20,000

Exchange difference arising on translating monetary item and settlement of creditors on 31st March 20X2:

		Rs.	Rs.
Creditors A/c (5,000 x $65)	Dr.	3,25,000	
Profit & loss A/c [(5,000 x ($ 67 -$ 65)]	Dr.	10,000	
To Bank A/c			3,35,000

Machinery A/c [(5,500*($ 67-$ 65)) To Profit & loss A/c	Dr.	11,000	 11,000

Question 2 : Nov 2018 – RTP

On 1st January, 2018, P Ltd. purchased a machine for $ 2 lakhs. The functional currency of P Ltd. is Rupees. At that date the exchange rate was $1= Rs.68. P Ltd. is not required to pay for this purchase until 30th June, 2018. Rupees strengthened against the $ in the three months following purchase and by 31st March, 2018 the exchange rate was $1 = Rs.65. CFO of P Ltd. feels that these exchange fluctuations wouldn't affect the financial statements because P Ltd. has an asset and a liability denominated in rupees. Which was initially the same amount. He also feels that P Ltd. depreciates this machine over four years so the future year-end amounts won't be the same.
Examine the impact of this transaction on the financial statements of P Ltd. for the year ended 31st March, 2018 as per Ind AS.

Solution :

As per Ind AS 21

01/01/2018	Asset A/c To Creditor A/c ($2,00,000 × 68)	Dr.	1,36,00,000	 1,36,00,000
31/03/2018	Asset – Non Monetary Item – Carried at Cost Creditor – Monetary Item Creditor A/c To FC gain (P/L) ($2,00,000 × (68 – 65)	 Dr.	 6,00,000	 6,00,000
31/03/2018	Depreciation A/c To Asset (1,36,00,000 × $\frac{1}{4} \times \frac{3}{12}$)	Dr.	8,50,000	 8,50,000

The closing Balance of PPE on 31/03/2018 1,27,50,000.

Question 3 : May 2019 – RTP

Supplier, A Ltd., enters into a contract with a customer, B Ltd., on 1st January, 2018 to deliver goods in exchange for total consideration of USD 50 million and receives an upfront payment of USD 20 million on this date. The functional currency of the supplier is INR. The goods are delivered and revenue is recognised on 31st March, 2018. USD 30 million is received on 1st April, 2018 in full and final settlement of the purchase consideration.
State the date of transaction for advance consideration and recognition of revenue. Also state the amount of revenue in INR to be recognized on the date of recognition of revenue. The exchange rates on 1st January, 2018 and 31st March, 2018 are Rs.72 per USD and Rs.75 per USD respectively.

Solution :

01/01/2018	Bank A/c To Advance from Customer (20 × 72) Note : Revenue will be recognised on 31/3/2018 as goods will be delivered on 31/3/2018	Dr.	1,440	1,440
31/03/2018	Advance from Customer (20 × 72) Customer A/c (30 × 75) To Sales A/c Note : balance 30 USD will be booked at exchange rate existing as 31/3/2018.	Dr. Dr.	1,440 2,250	3,690
01/04/2018	Bank A/c To Customer A/c	Dr.	2,250	2,250

Question 4 : Nov 2019 – RTP

Global Limited, an Indian company acquired on 30th September, 20X1 70% of the share capital of Mark Limited, an entity registered as company in Germany. The functional currency of Global Limited is Rupees and its financial year end is 31st March, 20X2.

(i) The fair value of the net assets of Mark Limited was 23 million EURO and the purchase consideration paid is 17.5 million EURO on 30th September, 20X1.
The exchange rates as at 30th September, 20X1 was Rs.82 / EURO and at 31st March, 20X2 was Rs.84 / EURO.
What is the value at which the goodwill has to be recognised in the financial statements of Global Limited as on 31st March, 20X2?

(ii) Mark Limited sold goods costing 2.4 million EURO to Global Limited for 4.2 million EURO during the year ended 31st March, 20X2. The exchange rate on the date of purchase by Global Limited was Rs.83 / EURO and on 31st March, 20X2 was Rs.84 / EURO. The entire goods purchased from Mark Limited are unsold as on 31st March, 20X2. Determine the unrealised profit to be eliminated in the preparation of consolidated financial statements.

Solution :

(i) Ind AS 21 requires that goodwill arose on business combination shall be expressed in the functional currency of the foreign operation and shall be translated at the closing rate. In this case the amount of goodwill will be as follows:

Net identifiable asset	Dr.	23 million	
Goodwill(bal. fig.)	Dr.	1.4 million	
To Bank			17.5 million
To NCI (23 x 30%)			6.9 million

Thus, goodwill on reporting date would be 1.4 million EURO × Rs.84
= Rs.117.6 million

(ii)

Particulars	EURO in million
Sale price of Inventory	4.20
Unrealised Profit [a]	1.80

Exchange rate as on date of purchase of Inventory [b] Rs.83 / Euro

Unrealized profit to be eliminated [a x b] Rs.149.40 million

As per Ind AS 21 "income and expenses for each statement of profit and loss presented (i.e. including comparatives) shall be translated at exchange rates at the dates of the transactions".

In the given case, purchase of inventory is an expense item shown in the statement profit and loss account. Hence, the exchange rate on the date of purchase of inventory is taken for calculation of unrealized profit which is to be eliminated on the event of consolidation.

Question 5 : Nov 2019 – PAPER

What is the functional currency of an entity?

What are the primary and secondary factors that influence determination of functional currency?

Solution :

- An entity measures its assets, liabilities, equity, income and expenses in its functional currency.
- All transactions in currencies other than the functional currency are foreign currency transactions.

  Ind AS 21 requires each entity to determine its functional currency.
- In determining its functional currency, an entity emphasises the currency that determines the pricing of the transactions that it undertakes, rather than focusing on the currency in which those transactions are denominated.
- The following are the factors that may be considered in determining an appropriate functional currency:
  (a) the currency that mainly influences sales prices for goods and services; this often will be the currency in which sales prices are denominated and settled;
  (b) the currency of the country whose competitive forces and regulations mainly determine the sales prices of its goods and services; and
  (c) the currency that mainly influences labour, material and other costs of providing goods and services; often this will be the currency in which these costs are denominated and settled.
- Other factors that may provide supporting evidence to determine an entity's functional currency are:
  (a) the currency in which funds from financing activities i.e., issuing debt and equity instruments) are generated;
  (b) the currency in which receipts from operating activities are usually retained.

Question 6 : May 2020 – RTP

On 1st April, 20X1, Makers Ltd. raised a long term loan from foreign investors. The investors subscribed for 6 million Foreign Currency (FCY) loan notes at par. It incurred incremental issue costs of FCY 2,00,000. Interest of FCY 6,00,000 is payable annually on 31st March, starting from 31st March, 20X2. The loan is repayable in FCY on 31st March, 20X7 at a premium and the effective annual interest rate implicit in the loan is 12%. The appropriate measurement basis for this loan is amortised cost. Relevant exchange rates are as follows:

– 1st April, 20X1 - FCY 1 = Rs.2.50.
– 31st March, 20X2 – FCY 1 = Rs.2.75.
– Average rate for the year ended 31st Match, 20X2 – FCY 1 = Rs.2.42. The functional currency of the group is Indian Rupee.

What would be the appropriate accounting treatment for the foreign currency loan in the books of Makers Ltd. for the FY 20X1-20X2? Calculate the initial measurement amount for the loan, finance cost for the year, closing balance and exchange gain / loss.

Solution :

Initial carrying amount of loan in books

Loan amount received	=	60,00,000 FCY
Less: Incremental issue costs	=	2,00,000 FCY
		58,00,000 FCY

Ind AS 21, "The Effect of Changes in Foreign Exchange Rates" states that foreign currency transactions are initially recorded at the rate of exchange in force when the transaction was first recognized.

Loan to be converted in INR = 58,00,000 FCY x Rs.2.50/FCY
= Rs.1,45,00,000

Therefore, the loan would initially be recorded at Rs.1,45,00,000.

Calculation of amortized cost of loan (in FCY) at the year end:

Period	Opening Financial Liability (FCY)	Interest @ 12% (FCY)	Cash Flow (FCY)	Closing Financial Liability (FCY)
	A	B	C	A + B – C
20X1-20X2	58,00,000	6,96,000	6,00,000	58,96,000

The finance cost in FCY is 6,96,000

The finance cost would be recorded at an average rate for the period since it accrues over a period of time.

Hence, the finance cost for FY 20X1-20X2 in INR is Rs.16,84,320 (6,96,000 FCY x Rs.2.42 / FCY)

The actual payment of interest would be recorded at 6,00,000 x 2.75 = INR 16,50,000

The loan balance is a monetary item so it is translated at the rate of exchange at the reporting date.

So the closing loan balance in INR is 58,96,000 FCY x INR 2.75 / FCY = Rs.1,62,14,000

The exchange differences that are created by this treatment are recognized in profit and loss.

In this case, the exchange difference is

Rs.[1,62,14,000 – (1,45,00,000 + 16,84,320 – 16,50,000)] = Rs.16,79,680.
This exchange difference is taken to profit and loss.

Question 7 : Nov 2020 – RTP

An Indian entity, whose functional currency is rupees, purchases USD dominated bond at its fair value of USD 1,000. The bond carries stated interest @ 4.7% p.a. on its face value. The said interest is received at the year end. The bond has maturity period of 5 years and is redeemable at its face value of USD 1,250. The fair value of the bond at the end of year 1 is USD 1,060. The exchange rate on the date of transaction and at the end of year 1 are USD 1 = Rs.40 and USD 1 = Rs.45, respectively. The weighted average exchange rate for the year is 1 USD = Rs.42.
The entity has determined that it is holding the bond as part of an investment portfolio whose objective is met both by holding the asset to collect contractual cash flows and selling the asset. The purchased USD bond is to be classified under the FVTOCI category.
The bond results in effective interest rate (EIR) of 10% p.a.
Calculate gain or loss to be recognised in Profit & Loss and Other Comprehensive Income for year 1. Also pass journal entry to recognise gain or loss on above. (Round off the figures to nearest rupees)

Solution :

Indian Co., functional current = Rs.

Exchange Rate =	Date of purchase	Rs./$ 40
	Year end	Rs./$ 45
	Average	Rs./$ 42

Investment in debt – Classified at OCI (Object Collect / Sell)

1) Cost of Bond = 1,000 × 40 = Rs.40,000

Investment A/c	Dr.	40,000	
To Bank			40,000

2) Interest Accrued = 1,000 × 10% × 42 = 4,200

Investment A/c	Dr.	4,200	
To Interest A/c			4,200

3) Interest Received = 1,250 × 4.7% × 45 = 2,643.75

Bank A/c	Dr.	2,643.75	
To Investment			2,643.75

4) Amortised Cost in Rs. = 40,000 + 4,200 – 2,643.75 = 41,556.25
Amortised Cost in $ = 1,000 + 100 – 58.75 = 1,41.25
= 1,041.25 × 45 = 46,856.25

Diff. recognised in P/L = 46,856.25 – 41,556.25 = 5,300

Investment A/c	Dr.	5,300	
To P/L			5,300

5. Fair Value at End

= $1,060 × 45 = 47,700

Diff. = 47,700 – 46,856.25 = 843.75

Should be recognised through OCI

Investment (Bonds) A/c	Dr.	843.75	
To OCI A/c			843.75

Question 8 : May 2021 – RTP

Monsoon Limited acquired, on 30 September, 20X2, 70% of the share capital of Mark Limited, an entity registered as company in Germany. The functional currency of Monsoon Limited is Indian Rupee and its financial year ends on 31 March, 20X3.

The fair value of the net assets of Mark Limited was 23 million EURO and the purchase consideration paid is 17.5 million EURO on 30 September, 20X2.

The exchange rates as on 30 September, 20X2 was Rs. 82 per EURO and at 31 March, 20X3 was Rs. 84 per EURO.

On acquisition of Mark limited, what is the value at which the goodwill / capital reserve has to be recognized in the financial statements of Monsoon Limited as on 31 March 20X3?

Solution :

Para 47 of Ind AS 21 requires that goodwill arose on business combination shall be expressed in the functional currency of the foreign operation and shall be translated at the closing rate in accordance with paragraphs 39 and 42.

In this case, the amount of goodwill will be as follows:

Net identifiable asset	Dr.	Rs. 23 million	
Goodwill (bal. fig.)	Dr.	Rs. 1.4 million	
To Bank (Purchase consideration)			Rs. 17.5 million
To NCI (23 x 30%)			Rs. 6.9 million

Thus, goodwill on reporting date in the books of Monsoon Limited would be

= 1.4 million EURO x Rs. 84 = Rs. 117.6 million.

Question 9 : July 2021 – Paper

SB Limited is engaged in the business of producing extracts from the natural plants for pharmaceuticals and Ayurvedic companies. It has a wholly owned subsidiary, UB Limited which is engaged in the business of pharmaceuticals. UB Limited purchases the pharmaceuticals extracts from its parent company. The demand of UB Limited is very high and hence to caster its shortfall,

UB Limited also purchases the pharmaceutical extracts from other companies. Purchases are made at the competitive prices.
SB Limited sold pharmaceuticals extracts to UB Limited for Euro 10 lakhs on 1st February, 2021. The cost of these extracts was Rs.770 lakhs in the books of SB Limited at the time of sale. At the year-end i.e. 31st March, 2021, all these pharmaceutical extracts were lying as closing stock and payable with UB Limited.
Euro is the functional current of UB Limited while Indian Rupee is the functional currency of SB Limited.
Following additional information is available :
Exchange rate on 1st February, 2021 1 Euro = Rs.85
Exchange rate on 31st March, 2021 1 Euro = Rs.88
Provide the accounting treatment of the above in the books of SB Limited and UB Limited. Also show its impact on consolidated financial statements. Support your answer by Journal entries, wherever necessary. Assume NRV to be higher than the cost.

Solution :
Accounting treatment in the books of SB Ltd (Functional Currency INR)
SB Ltd will recognize sales of Rs. 850 lakh (10 lacs Euro x Rs. 85)
Profit on sale of inventory = 850 lakh – 770 lakh = Rs. 80 lakh.
On balance sheet date receivable from UB Ltd. will be translated at closing rate i.e. 1 Euro = Rs. 88. Therefore, unrealised forex gain will be recorded in standalone profit and loss of Rs. 30 lakh [i.e. (Rs. 88 - Rs. 85) x 10 lakh Euro].

Journal Entries

Date		**(Rs. in lakh)**	**(Rs. in lakh)**
1.2.2021	UB Ltd. A/c Dr. To Sales (Being revenue recorded on initial recognition)	850	850
31.3.2021	UB Ltd. A/c Dr. To Foreign exchange difference (unrealised) (Being foreign exchange difference recorded at year end)	30	30

Accounting treatment in the books of UB Ltd (Functional currency EURO)

Date		**in Euros**	**in Euros**
1.2.2021	Purchase account Dr. To SB limited (Being purchased recorded at the date of transaction)	10 lakh	10 lakh

UB Ltd will recognize inventory on 1st February, 2021 of Euro 10 lakh which will also be its closing stock at year end

Accounting treatment in the consolidated financial statements
Receivable and payable in respect of abovementioned sale / purchase between SB Ltd and UB Ltd will get eliminated
The closing stock of UB Ltd will be recorded at lower of cost or NRV.
Since the question ask to assume that NRV is higher than cost, inventory will be measured at cost only. Therefore, no write off is required.
The amount of closing stock of Rs. 850 lakh include two components–

- Cost of inventory for Rs. 770 lakh ; and
- Profit element of Rs. 80 lakh; and

At the time of consolidation, the second element amounting to Rs. 80 lakh will be eliminated from the closing stock.

	(Rs. in lakh)	(Rs. in lakh)
Consolidated P&L A/c Dr.	80	
To Inventory		80
(Being profit element of intragroup transaction eliminated)		

Thanks ....

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IND AS – 7
CASH FLOW STATEMENT

CHAPTER - 13

Question 1 : May 2018 – RTP

Company A acquires 70% of the equity stake in Company B on July 20, 20X1. The consideration paid for this transaction is as below:

(a) Cash consideration of Rs.15,00,000

(b) 200,000 equity shares having face of Rs.10 and fair value of Rs.15 per share.

On the date of acquisition, Company B has cash and cash equivalent balance of Rs.2,50,000 in its books of account.

On October 10, 20X2, Company A further acquires 10% stake in Company B for cash consideration of Rs.8,00,000.

Advise how the above transactions will be disclosed/presented in the statement of cash flows as per Ind AS 7.

Solution :

1) As per Ind AS 7, the aggregate cash flows arising from obtaining control of subsidiary shall be presented separately and classified as investing activities.

2) As per Ind AS 7, the aggregate amount of the cash paid or received as consideration for obtaining subsidiaries is reported in the statement of cash flows net of cash and cash equivalents acquired or disposed of as part of such transactions, events or changes in circumstances.

   Further, investing and financing transactions that do not require the use of cash or cash equivalents shall be excluded from a statement of cash flows. Such transactions shall be disclosed elsewhere in the financial statements in a way that provides all the relevant information about these investing and financing activities.

3) As per Ind AS 7, cash flows arising from changes in ownership interests in a subsidiary that do not result in a loss of control shall be classified as cash flows from financing activities, unless the subsidiary is held by an investment entity, as defined in Ind AS 110, and is required to be measured at fair value through profit or loss.

4) Considering the above, for the financial year ended March 31, 20X2 total consideration of Rs.15,00,000 less Rs.2,50,000 will be shown under investing activities as "Acquisition of the subsidiary (net of cash acquired)".

5) There will not be any impact of issuance of equity shares as consideration in the cash flow statement however a proper disclosure shall be given elsewhere in the financial statements in a way that provides all the relevant information about the issuance of equity shares for non-cash consideration.

6) Further, in the statement of cash flows for the year ended March 31, 20X3, cash consideration paid for the acquisition of additional 10% stake in Company B will be shown under financing activities.

Question 2 : May 2019 – RTP

Z Ltd. has no foreign currency cash flow for the year 2017. It holds some deposit in a bank in the USA. The balances as on 31.12.2017 and 31.12.2018 were US$ 100,000 and US$ 102,000 respectively. The exchange rate on December 31, 2017 was US$1 = Rs.45. The same on 31.12.2018 was US$1 = Rs.50. The increase in the balance was on account of interest credited on 31.12.2018. Thus, the deposit was reported at Rs.45,00,000 in the balance sheet as on December 31, 2017. It was reported at Rs.51,00,000 in the balance sheet as on 31.12.2018. How these transactions should be presented in cash flow for the year ended 31.12.2018 as per Ind AS 7?

Solution :

The profit and loss account was credited by Rs.1,00,000 (US$ 2000 × Rs.50) towards interest income. It was credited by the exchange difference of US$ 100,000 × (Rs.50 – Rs.45) that is, Rs.500,000. In preparing the cash flow statement, Rs.500,000, the exchange difference, should be deducted from the 'net profit before taxes, and extraordinary item'. However, in order to reconcile the opening balance of the cash and cash equivalents with its closing balance, the exchange difference Rs.500,000, should be added to the opening balance in note to cash flow statement.

Cash flows arising from transactions in a foreign currency shall be recorded in Z Ltd.'s functional currency by applying to the foreign currency amount the exchange rate between the functional currency and the foreign currency at the date of the cash flow.

Question 3 : Nov 2019 – RTP

Following is the balance sheet of Kuber Limited for the year ended 31st March, 20X2

(Rs.in lacs)

	20X2	**20X1**
ASSETS		
Non-current Assets		
Property, plant and equipment	13,000	12,500
Intangible assets	50	30
Other financial assets	145	170
Deferred tax asset (net)	855	750
Other non-current assets	800	770
Total non-current assets	**14,850**	**14,220**
Current assets		
Financial assets		

Investments	2,300	2,500
Cash and cash equivalents	220	460
Other current assets	195	85
Total current assets	**2,715**	**3,045**
Total Assets		
EQUITY AND LIABILITIES		
Equity		
Equity share capital	300	300
Other equity	12,000	8,000
Total equity	**12,300**	**8,300**
Liabilities		
Non-current liabilities		
Long-term borrowings	2,000	5,000
Other non-current liabilities	2,740	3,615
Total non-current liabilities	**4,740**	**8,615**
Current liabilities		
Financial liabilities		
Trade payables	150	90
Bank Overdraft	75	60
Other current liabilities	300	200
Total current liabilities	**525**	**350**
Total liabilities	**5,265**	**8,965**
Total Equity and Liabilities	**17,565**	**17,265**

Additional Information :

(1) Profit after tax for the year ended 31st March, 20X2- Rs.4,450 lacs

(2) Interim Dividend paid during the year – Rs.450 lacs

(3) Depreciation and amortisation charged in the statement of profit and loss during the current year are as under

(a) Property, Plant and Equipment – Rs.500 lacs

(b) Intangible Assets – Rs.20 lacs

(4) During the year ended 31st March, 20X2 two machineries were sold for Rs.10 lacs. The carrying amount of these machineries as on 31st March, 20X2 is Rs.60 lacs.

(5) Income taxes paid during the year Rs.105 lacs

Using the above information of Kuber Limited, construct a statement of cash flows under indirect method. Other non-current / current assets and liabilities are related to operations of Kuber Ltd. and do not contain any element of financing and investing activities.

Solution :

Statement of Cash Flows

		Rs. in lacs
Cash flows from Operating Activities		
Net Profit after Tax	4,450	
Add: Tax Paid	105	
	4,555	
Add: Depreciation & Amortisation (500 + 20)	520	
Less: Gain on Sale of Machine (70-60)	(10)	
Less: Increase in Deferred Tax Asset (855-750)	(105)	
	4,960	
Change in operating assets and liabilities		
Add: Decrease in financial asset (170 - 145)	25	
Less: Increase in other non-current asset (800 - 770)	(30)	
Less: Increase in other current asset (195 - 85)	(110)	
Less: Decrease in other non-current liabilities (3,615 – 2,740)	(875)	
Add: Increase in other current liabilities (300 - 200)	100	
Add: Increase in trade payables (150-90)	60	
	4,130	
Less: Income Tax	(105)	
Cash generated from Operating Activities		**4,025**
Cash flows from Investing Activities		
Sale of Machinery	70	
Purchase of Machinery [13,000-(12,500 – 500-60)]	(1,060)	
Purchase of Intangible Asset [50-(30-20)]	(40)	
Sale of Financial asset - Investment (2,500 – 2,300)	200	
Cash outflow from Investing Activities		**(830)**
Cash flows from Financing Activities		
Dividend Paid	(450)	
Long term borrowings paid (5,000 – 2,000)	(3,000)	
Cash outflow from Financing Activities		**(3,450)**
Net Cash outflow from all the activities		**(255)**
Opening cash and cash equivalents (460 – 60)		**400**
Closing cash and cash equivalents (220 – 75)		**145**

Question 4 : May 2020 – RTP / Nov 2020 – Paper

Entity A acquired a subsidiary, Entity B, during the year. Summarised information from the Consolidated Statement of Profit and Loss and Balance Sheet is provided, together with some supplementary information.

Consolidated Statement of Profit and Loss	Amount (Rs.)
Revenue	3,80,000
Cost of sales	(2,20,000)
Gross profit	1,60,000
Depreciation	(30,000)
Other operating expenses	(56,000)
Interest cost	(4,000)
Profit before taxation	**70,000**
Taxation	(15,000)
Profit after taxation	**55,000**

Consolidated balance sheet	20X2	20X1
Assets	**Amount (Rs.)**	**Amount (Rs.)**
Cash and cash equivalents	8,000	5,000
Trade receivables	54,000	50,000
Inventories	30,000	35,000
Property, plant and equipment	1,60,000	80,000
Goodwill	18,000	—
Total assets	**2,70,000**	**1,70,000**
Liabilities		
Trade payables	68,000	60,000
Income tax payable	12,000	11,000
Long term debt	1,00,000	64,000
Total liabilities	**1,80,000**	**1,35,000**
Shareholders' equity	**90,000**	**35,000**
Total liabilities and shareholders'	**2,70,000**	**1,70,000**

Other information :

All of the shares of entity B were acquired for Rs.74,000 in cash. The fair values of assets acquired and liabilities assumed were:

Particulars	Amount (Rs.)
Inventories	4,000
Trade receivables	8,000
Cash	2,000
Property, plant and equipment	1,10,000
Trade payables	(32,000)
Long term debt	(36,000)
Goodwill	18,000
Cash consideration paid	**74,000**

Prepare the Consolidated Statement of Cash Flows for the year 20X2, as per Ind AS 7.

Solution :

This information will be incorporated into the Consolidated Statement of Cash Flows as follows:

Statement of Cash Flows for the year ended 20X2 (extract)

	Amount (Rs.)	Amount (Rs.)
Cash flows from operating activities		
Profit before taxation	70,000	
Adjustments for non-cash items:		
Depreciation	30,000	
Decrease in inventories (W.N. 1)	9,000	
Decrease in trade receivables (W.N. 2)	4,000	
Decrease in trade payables (W.N. 3)	(24,000)	
Interest paid to be included in financing activities	4,000	
Taxation (11,000 + 15,000 – 12,000)	(14,000)	
Net cash generated from operating activities		79,000
Cash flows from investing activities		
Cash paid to acquire subsidiary (74,000 – 2,000)	(72,000)	
Net cash outflow from investing activities		(72,000)
Cash flows from financing activities		
Interest paid	(4,000)	
Net cash outflow from financing activities		(4,000)
Increase in cash and cash equivalents during the year		**3,000**
Cash and cash equivalents at the beginning of the year		**5,000**
Cash and cash equivalents at the end of the year		**8,000**

Working Notes:

1. Calculation of change in inventory during the year

	Rs.
Total inventories of the Group at the end of the year	30,000
Inventories acquired during the year from subsidiary	(4,000)
	26,000
Opening inventories	35,000
Decrease in inventories	9,000

2. Calculation of change in Trade Receivables during the year

	Rs.
Total trade receivables of the Group at the end of the year	54,000
Trade receivables acquired during the year from subsidiary	(8,000)
	46,000
Opening trade receivables	50,000
Decrease in trade receivables	4,000

3. Calculation of change in Trade Payables during the year

	Rs.
Trade payables at the end of the year	68,000

Trade payables of the subsidiary assumed during the year	(32,000)
	36,000
Opening trade payables	60,000
Decrease in trade payables	24,000

Question 5 : Nov 2020 – RTP

During the financial year 2019-2020, Akola Limited have paid various taxes & reproduced the below mentioned records for your perusal:

- Capital gain tax of Rs.20 crore on sale of office premises at a sale consideration of Rs.100 crore.
- Income Tax of Rs.3 crore on Business profits amounting Rs.30 crore (assume entire business profit as cash profit).
- Dividend Distribution Tax of Rs.2 crore on payment of dividend amounting Rs.20 crore to its shareholders.
- Income tax Refund of Rs.1.5 crore (Refund on taxes paid in earlier periods for business profits).

You need to determine the net cash flow from operating activities, investing activities and financing activities of Akola Limited as per relevant Ind AS.

Solution :

1)

Particulars	Amount (Rs. Cr.)	Activity
Sale Consideration	100	Investing Activity
Capital gain tax	(20)	Investing Activity
Business Profit (Cash Profit)	30	Operating Activity
Tax on Business Profit (30%)	(3)	Operating Activity
Dividend Payment	(20)	Financing Activity
Dividend distribution tax	(2)	Financing Activity
Income Tax Refund	1.5	Operating Activity

2) Net Calculations

Operating Activity	28.5
Investing Activity	80
Financing Activity	(22)
Net Cash or Equivalent generated	86.5

Question 6 : Jan 2021 – Paper

Z Ltd. (India) has an overseas branch in USA. It has a bank account having balance of USD 7,000 as on 1st April 2019. During the financial year 2019-2020, Z Ltd. Acquired computers for its USA office for USD 280 which was paid on same date. There is no other transaction reported in USA or India.

Exchange rates between INR and USD during the financial year 2019-2020 were:

Date	**USD 1 to INR**
1st April 2019	70.00
30th November 2019	71.00 (Date of purchase of computer)
31st March 2020	71.50
Average for 2019-2020	70.50

Please prepare the extract of Cash Flow Statement for the year ended 31st March 2020 as per the relevant Ind AS and also show the foreign exchange profitability from these transactions for the financial year 2019-2020?

Solution :

In the books of Z Ltd.

Statement of Cash Flows for the year ended 31st March 2020

	Rs.	**Rs.**
Cash flows from operating activities		
Net Profit (Refer Working Note)	10,360	
Adjustments for non-cash items:		
Foreign Exchange Gain	(10,360)	
Net cash outflow from operating activities		0
Cash flows from investing activities		
Acquisition of Property, Plant and Equipment	(19,880)	
Net cash outflow from Investing activities		(19,880)
Cash flows from financing activities		0
Net change in cash and cash equivalents		(19,880)
Cash and cash equivalents at the beginning of the year i.e. 1st April 2019		4,90,000
Foreign Exchange difference		10,360
Cash and cash equivalents at the end of the year i.e. 31st March 2020		4,80,480

Working Note:

Computation of Foreign Exchange Gain

Bank Account USD	**Date**	**USD**	**Exchange Rate**	**Rs.**
Opening balance	1.4.2019	7,000	70.00	4,90,000
Less: Purchase of Computer	30.11.2019	280	71.00	19,880
Closing balance calculated		6,720		4,70,120
Closing balance (at year end spot rate)	31.3.2020	6,720	71.50	4,80,480
Foreign Exchange Gain credited to Profit and Loss account				10,360

Question 7 : May 2021 – RTP

From the following data, identify the nature of activities as per Ind AS 7.

S.no	Nature of transaction
1	Cash paid to employees
2	Cash paid for development of property costs
3	Borrowings repaid
4	Cash paid to suppliers
5	Loan to Director
6	Bonus shares issued
7	Dividends paid
8	Cash received from trade receivables
9	Proceeds from sale of PPE
10	Depreciation of PPE
11	Advance received from customers
12	Purchased goodwill
13	Payment of promissory notes

Solution :

S.no	Nature of transaction	Activity as per Ind AS 7
1	Cash paid to employees	Operating activity
2	Cash paid for development of property costs	Investing activity
3	Borrowings repaid	Financing activity
4	Cash paid to suppliers	Operating activity
5	Loan to Director	Investing activity
6	Bonus shares issued	Non-cash item
7	Dividends paid	Financing activity
8	Cash received from trade receivables	Operating activity
9	Proceeds from sale of PPE	Investing activity
10	Depreciation of PPE	Non-cash item
11	Advance received from customers	Operating activity
12	Purchased goodwill	Investing activity
13	Payment of promissory notes	Financing activity

Question 8 : Nov 2021 – RTP

From the following data of Galaxy Ltd., prepare statement of cash flows showing cash generated from Operating Activities using direct method as per Ind AS 7:

	31.3.20X2 (Rs.)	31.3.20X1 (Rs.)
Current Assets:		
Inventory	1,20,000	1,65,000

Trade receivables	2,05,000	1,88,000
Cash & cash equivalents	35,000	20,500
Current Liabilities:		
Trade payable	1,95,000	2,15,000
Provision for tax	48,000	65,000

Summary of Statement of Profit and Loss		Rs.
Sales	85,50,000	
Less: Cost of sales	(56,00,000)	29,50,000
Other Income		
Interest income	20,000	
Fire insurance claim received	1,10,000	1,30,000
		30,80,000
Depreciation	(24,000)	
Administrative and selling expenses	(15,40,000)	
Interest expenses	(36,000)	
Foreign exchange loss	(18,000)	(16,18,000)
Net Profit before tax and extraordinary income		14,62,000
Income Tax		(95,000)
Net Profit		13,67,000

Additional information:

(i) Trade receivables and Trade payables include amounts relating to credit sale and credit purchase only.

(ii) Foreign exchange loss represents increment in liability of a long-term borrowing due to exchange rate fluctuation between acquisition date and balance sheet date.

Solution :

Statement Cash Flows from operating activities
of Galaxy Ltd. for the year ended 31 March 20X2 (Direct Method)

Particulars	**Rs.**	**Rs.**
Operating Activities:		
Cash received from Trade receivables (W.N. 3)		85,33,000
Less: Cash paid to Suppliers (W.N.2)	55,75,000	
Payment for Administration and Selling expenses	15,40,000	
Payment for Income Tax (W.N.4)	1,12,000	(72,27,000)
		13,06,000
Adjustment for exceptional items (fire insurance claim)		1,10,000
Net cash generated from operating activities		14,16,000

Working Notes:

1. Calculation of total purchases

Cost of Sales = Opening stock + Purchases – Closing Stock
Rs. 56,00,000 = Rs. 1,65,000 + Purchases – Rs. 1,20,000
Purchases = Rs. 55,55,000

2. Calculation of cash paid to Suppliers

Trade Payables

	Rs.		Rs.
To Bank A/c (balancing figure)	55,75,000	By Balance b/d	2,15,000
To Balance c/d	1,95,000	By Purchases (W.N. 1)	55,55,000
	57,70,000		**57,70,000**

3. Calculation of cash received from Customers

Trade Receivables

	Rs.		**Rs.**
To Balance b/d	1,88,000	By Bank A/c (balancing figure)	85,33,000
To Sales	85,50,000	By Balance c/d	2,05,000
	87,38,000		**87,38,000**

4. Calculation of tax paid during the year in cash

Provision for tax

	Rs.		**Rs.**
To Bank A/c (balancing figure)	1,12,000	By Balance b/d	65,000
To Balance c/d	48,000	By Profit and Loss A/c	95,000
	1,60,000		**1,60,000**

Thanks ....

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IND AS – 108
OPERATING SEGMENTS

CHAPTER - 14

Question 1 : May 2018 – PAPER

Seeds Ltd. is operating in oil industry. Its business segments comprise crushing and refining. Certain information for financial year 2017-18 is given below:

(Rs.in lakh)

Segments	External Sale	Tax	Other Operating Income	Result	Assets	Liabilities
Crushing	1,00,000	2,500	20,000	5,000	25,000	15,000
Refining	35,000	1,500	7,500	2,000	15,000	5,000

Additional Information: (Rs.in lakh)

- Unallocated revenue net of expenses is Rs.1,500.
- Interest and bank charges is Rs.1,000
- Income-tax expense is Rs.1,000 (current tax Rs.975 and deferred tax Rs.25)
- Investments Rs.5,000 and unallocated assets Rs.5,000
- Unallocated liabilities, Reserves & Surplus and Share capital are Rs.10,000; Rs.15,000 and Rs.5,000 respectively.
- Depreciation amounts for crushing and refining are Rs.500 and Rs.150 respectively.
- Capital expenditure for crushing and refining are Rs.2,500 and Rs.1,000 respectively.
- Revenue from outside India is Rs.15,000 and segment assets outside India Rs.5,000.

Based on the above information, how Seeds Ltd. would disclose information about reportable segment revenue, profit or loss, assets and liabilities for financial year 2017-18?

Solution :

(1) Segment revenues, results and other information

(Rs.in lakh)

	Revenue	**Coating**	**Others**	**Total**
1	**External sales (gross)**	1,00,000	35,000	1,35,000
	Tax	(2,500)	(1,500)	(4,000)
	External sales (net)	97,500	33,500	1,31,000
	Other operating income	20,000	7,500	27,500
	Total Revenue	1,17,500	41,000	1,58,500
2	**Results**			
	Segment results	5,000	2,000	7,000
	Unallocated income (net of unallocated expenses)			1,500

	Profit from operation before interest, taxation and exceptional items			8,500
	Interest and bank charges			(1,000)
	Profit before exceptional items			7,500
	Exceptional items			Nil
	Profit before taxation			7,500
	Less: Income Taxes			
	Current taxes			(975)
	Deferred taxes			(25)
	Profit after taxation			6,500
3	**Other Information**			
(a)	**Assets**			
	Segment Assets	25,000	15,000	40,000
	Investments			5,000
	Unallocated assets			5,000
	Total Assets			50,000
(b)	**Liabilities/Shareholder's funds**			
	Segment liabilities	15,000	5,000	20,000
	Unallocated liabilities			10,000
	Share capital			5,000
	Reserves and surplus			15,000
	Total liabilities / shareholder's funds			50,000
(c)	**Others**			
	Capital Expenditure	2,500	1,000	3,500
	Depreciation	500	150	650

(2) Geographical Information

			(Rs.in lakh)
	India	**Outside India**	**Total**
Revenue	1,43,500	15,000	1,58,500
Segment assets	35,000	5,000	40,000
Capital expenditure	3,500	-	3,500

Note: Segment revenue, results, assets and liabilities include the respective amounts identifiable to each of the segments.

Question 2 : May 2019 – RTP

An entity uses the weighted average cost formula to assign costs to inventories and cost of goods sold for financial reporting purposes, but the reports provided to the chief operating decision maker use the First-In, First-Out (FIFO) method for evaluating the performance of segment operations. Which cost formula should be used for Ind AS 108 disclosure purposes?

Solution :

The entity should use First-In, First-Out (FIFO) method for its Ind AS 108 disclosures, even though it uses the weighted average cost formula for measuring inventories for inclusion in its financial statements. Where chief operating decision maker uses only one measure of segment asset, same measure should be used to report segment information. Accordingly, in the given case, the method used in preparing the financial information for the chief operating decision maker should be used for reporting under Ind AS 108.

However, reconciliation between the segment results and results as per financial statements needs to be given by the entity in its segment report.

Question 3 : May 2020 – RTP

ABC Limited has 5 operating segments namely A, B, C, D and E. The profit/ loss of respective segments for the year ended March 31, 20X1 are as follows :

Segment	Profit/(Loss) (Rs.in crore)
A	780
B	1,500
C	(2,300)
D	(4,500)
E	6,000
Total	**1,480**

Based on the quantitative thresholds, which of the above segments A to E would be considered as reportable segments for the year ending March 31, 20X1?

Solution :

With regard to quantitative thresholds to determine reportable segment relevant in context of instant case, of Ind AS 108 may be noted which provides as follows:

"The absolute amount of its reported profit or loss is 10 per cent or more of the greater, in absolute amount, of (i) the combined reported profit of all operating segments that did not report a loss and (ii) the combined reported loss of all operating segments that reported a loss."

In compliance with Ind AS 108, the segment profit/loss of respective segment will be compared with the greater of the following:

(i) All segments in profit, i.e., A, B and E – Total profit Rs.8,280 crores.

(ii) All segments in loss, i.e., C and D – Total loss Rs.6,800 crores.

Greater of the above – Rs.8,280 crores.

Based on the above, reportable segments will be determined as follows:

Segment	Profit/(Loss) (Rs.in crore)	As absolute % of Rs.8,280 crore	Reportable segment
A	780	9%	No
B	1,500	18%	Yes
C	(2,300)	28%	Yes
D	(4,500)	54%	Yes

E	6,000	72%	Yes

Hence B, C, D, E are reportable segments.

Question 4 : Nov 2020 – Paper

John Limited has identified four segments for which revenue data is given as per below:

	External Sale (Rs.)	Internal Sale (Rs.)	Total (Rs.)
Segment A	4,00,000	Nil	4,00,000
Segment B	80,000	Nil	80,000
Segment C	90,000	20,000	1,10,000
Segment D	70,000	6,20,000	6,90,000
Total sales	6,40,000	6,40,000	12,80,000

The following additional information is available with respect to John Limited:
Segment C is a high growing business and management expects that this segment to make a significant contribution to external revenue in coming years.
Discuss, which of the segments would be reportable under the threshold criteria identified in Ind AS 108 and why?

Solution :

Threshold amount of 10% of total revenue is Rs. 1,28,000 (Rs. 12,80,000 × 10%).
Segment A exceeds the quantitative threshold (Rs. 4,00,000 > Rs. 1,28,000) and hence is a reportable segment.
Segment D exceeds the quantitative threshold (Rs. 6,90,000 > Rs. 1,28,000) and hence is a reportable segment.
Segment B & C do not meet the quantitative threshold amount and may not be classified as reportable segment.
However, the total external revenue generated by these two segments A & D represent only 73.44% (Rs. 4,70,000 / 6,40,000 x 100) of the entity's total external revenue. If the total external revenue reported by operating segments constitutes less than 75% of the entity's total external revenue, additional operating segments should be identified as reportable segments until at least 75% of the revenue is included in reportable segments.
In case of John Limited, it is given that Segment C is a high growing business and management expects this segment to make a significant contribution to external revenue in coming years. In accordance with the requirement of Ind AS 108, John Limited may designate segment C as a reportable segment, making the total external revenue attributable to reportable segments be 87.5% (Rs. 5,60,000/ 6,40,000 x 100) of total entity's external revenue.
In this situation, Segments A, C and D will be reportable segments and Segment B will be shown as other segment.

Alternatively, Segment B may be considered as a reportable segment instead of Segment C, based on the choice of John Ltd. 's management, if it meets the definition of operating segment. If Segment B is considered as reportable segment, external revenue reported will be Rs. 4,00,000 + Rs. 80,000 + Rs. 70,000 = Rs. 5,50,000

% of Total External Revenue = Rs. 5,50,000 / Rs. 6,40,000 = 85.94%
Segments A, B and D will be reportable segments and Segment C will be shown as other segment.

Question 5 : Jan 2021 – Paper

Heavy Goods Ltd. has 6 operating segments namely L-Q (below). The total revenues (internal and external), profits or losses and assets are set out below: (In Rs.)

Segment	Inter Segment Sales	External Sales	Profit / loss	Total assets
L	4,200	12,300	3,000	37,500
M	3,500	7,750	1,500	23,250
N	1,000	3,500	-1,500	15,750
0	0	5,250	-750	10,500
P	500	5,500	900	10,500
Q	1,200	1,050	600	5,250
	10,400	35,350	3,750	1,02,750

Heavy Goods Ltd. needs to determine how many reportable segments it has. You are required to advice Heavy Goods Ltd. as per the criteria defined in Ind AS 108.

Solution :

As per paragraph 13 of Ind AS 108, an entity shall report separately information about an operating segment that meets any of the following quantitative thresholds:

(a) Its reported revenue, including both sales to external customers and inter –segment sales or transfers, is 10 per cent or more of the combined revenue, internal and external, of all operating segments.
Combined total sales of all the segment = Rs.10,400 + Rs.35,350 = Rs.45,750.
10% thresholds = 45,750 x 10% = 4,575.

(b) The absolute amount of its reported profit or loss is 10 per cent or more of the greater, in absolute amount, of
  (i) the combined reported profit of all operating segments that did not report a loss and
  (ii) the combined reported loss of all operating segments that reported a loss.
In the given situation, combined reported profit = Rs.6,000 and combined reported loss (Rs.2,250). Hence, for 10% thresholds Rs.6,000 will be considered.
10% thresholds = Rs.6,000 x 10% = Rs.600

(c) Its assets are 10 per cent or more of the combined assets of all operating segments.
Combined total assets of all the segment = Rs.1,02,750
10% thresholds = Rs.1,02,750 x 10% = 10,275

Accordingly, quantitative thresholds are calculated below:

Segments	L	M	N	O	P	Q	Reportable segments

% segment sales to total sales	36.66%	24.59%	9.84%	11.48%	13.11%	4.92%	L, M,O,P
% segment profit to total profits	50%	25%	25%	12.50%	15%	10%	L,M,N,O,P,Q
% segment assets to total assets	36.50%	22.63%	15.33%	10.22%	10.22%	5.11%	L,M,N,O,P

Segments L, M, O and P clearly satisfy the revenue and assets tests and they are separate reportable segments.

Segments N does not satisfy the revenue test, but it does satisfy the asset test and it is a reportable segment.

Segment Q does not satisfy the revenue or the assets test but is does satisfy the profits test. Therefore, Segment Q is also a reportable segment.

Hence, **all segments** i.e; L, M, N, O, P and Q are reportable segments.

Question 6 : July 2021 – Paper

U Limited is operating in paint industry. Is business segments comprise paints (wall pains, lead paints, zinc paints, aluminium paints etc.), and other (consisting of primer, varnish, thinner and related products). Certain information for financial Year 2020-2021 is given below :

Segments	External Revenue (Inc. GST)	GST	Other operating income	Result	Assets	Liabilities
Paints	10,000	250	2000	500	2500	1500
Other	3,500	150	750	200	1500	500

Additional Information :

(i) Unallocated income (Net of expenses) is Rs.1,50,00,000.

(ii) Interest and bank charges is Rs.1,00,00,000.

(iii) Income tax expenses is Rs.1,00,00,000 9Current tax

(iv) Unallocated investments are Rs.5,00,00,000 and other assets are rs.5,00,00,000.

(v) Unallocated Liabilities, Reserve and surplus and share capital are Rs.10,00,00,000, Rs.15,00,00,000 and Rs.500,00,000 respectively.

(vi) Depreciation amounts for paints and other are Rs.50,00,000 and Rs.15,00,000 respectively.

(vii) Capital expenditure for paints and others are Rs.2,50,00,000 and rs.1,00,00,000 respectively.

(viii) Revenue from outside India is Rs.31,00,000 and segment assets outside India is Rs.5,00,00,000

Based on the above information, how U Limited would disclose information about reportable segment revenue, profit or loss, assets and liabilities and others for financial year 2020-2021. Ignore corresponding figures for the previous year.

Solution :

Segment information

(A) Information about operating segment

(1) the company's operating segments comprise:

Paints: consisting of wall paints, lead paints, zinc paints, aluminum paints etc.

Others: consisting of primer, varnish, thinner and related products.

(2) Segment revenues, results and other information:

(Rs. in lakh)

	Revenue	**Paints**	**Others**	**Total**
1.	External Revenue (gross)	10,000	3,500	13,500
	GST	(250)	(150)	(400)
	Total Revenue (net)	9,750	3,350	13,100
	Other operating Income	2,000	750	2,750
	Total Revenue	11,750	4,100	15,850
2.	Results			
	Segment results	500	200	700
	Unallocated income (net of unallocated expenses)			150
	Profit from operation before interest, taxation and exceptional items			850
	Interest and bank charges			(100)
	Profit before exceptional items			750
	Exceptional items			Nil
	Profit before taxation			750
	Income Taxes			
	-Current taxes			(97.5)
	-Deferred taxes			(2.5)
	Profit after taxation			650
3.	Other Information			
(a)	Assets			
	Segment Assets	2,500	1,500	4,000
	Investments			500
	Unallocated assets			500
	Total Assets			5,000
(b)	Liabilities/Shareholder's funds			
	Segment liabilities	1,500	500	2,000
	Unallocated liabilities			1,000
	Share capital			500
	Reserves and surplus			1,500
	Total liabilities / shareholder's funds			5,000
(c)	Others			

	Capital Expenditure	(250)	(100)	
	Depreciation	(50)	(15)	

Geographical Information				(Rs. in lakh)
		India	Outside India	Total
	Revenue	12,750	3,100	15,850
	Segment assets	4,500	500	5,000
	Capital expenditure (250 + 100)	350		350

Question 7 : May 2022 – RTP

XYZ Ltd. has eight segments namely A, B, C, D, E, F, G and H. The information regarding respective segments for the year ended 31st March, 20X1 is as follows:

Segments	**A**	**B**	**C**	**D**	**E**	**F**	**G**	**H**
External sales	0	255	15	10	15	50	25	35
Inter-segment sales	100	60	30	5	—	—	—	—
Total	**100**	**315**	**45**	**15**	**15**	**50**	**25**	**35**
Segment result Profit/(Loss)	**5**	**(90)**	**15**	**(5)**	**8**	**(5)**	**5**	**7**
Segment assets	**15**	**47**	**5**	**11**	**3**	**5**	**5**	**9**

Identify which of the above segments out of A to H would be considered as reportable segments of XYZ Ltd. for the year ending 31st March, 20X1?

Solution :

An entity has eight segments and the relevant information is as follows:

Criterial 1: Segment revenue is 10% or more of total external + intersegment sales

Segments	**A**	**B**	**C**	**D**	**E**	**F**	**G**	**H**	**Total**
Total sales	100	315	45	15	15	50	25	35	600
% to total sales	16.7	52.5	7.5	2.5	2.5	8.3	4.2	5.8	
Reportable segments	**A**	**B**	-	-	-	-	-	-	

Criteria 2: 10% or more of segment result

Consider segment profit and loss separately in absolute terms

Segments	**A**	**B**	**C**	**D**	**E**	**F**	**G**	**H**	**Total**
Profit	5	-	15	-	8	-	5	7	40
Segments loss	-	90	-	5	-	5	-	-	100

Since segment loss is greater, we select 100 as evaluating the segment percentage

Segments	**A**	**B**	**C**	**D**	**E**	**F**	**G**	**H**	**Total**
% to segment loss	5	90	15	5	8	5	5	7	
Reportable segments	-	**B**	**C**	-	-	-	-	-	

Criteria 2: 10% or more of segment assets

Segments	A	B	C	D	E	F	G	H	Total
Assets	15	47	5	11	3	5	5	9	100
%	15	47	5	11	3	5	5	9	100
Reportable segments	A	B	-	D	-	-	-	-	

Based on the above 3 criteria, the Reportable Segments are A, B, C & D

However, 75% test for external sales should also be checked.

Reportable Segments	A	B	C	D	TOTAL
External sales	0	255	15	10	280
Total entity's sales (external)					**405**
% of reportable segments external sales to entity's sales					**69.14%**
Required percentage					**75%**

Hence, in the above scenario, additional operating segments need to be identified as reportable segments, till the 75% test is satisfied, even if those segments do not satisfy the quantitative threshold limits.

Thanks ....

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IND AS – 34 INTERIL FINANCIAL REPORTING

CHAPTER - 15

Question 1 : Nov 2018 – PAPER

Navya Limited manufacturer of ceramic tiles has shown a net profit of Rs.15,00,000 for the first quarter of 2018-2019. Following adjustments were made while computing the net profit:

(i) Bad debts of Rs.1,64,000 incurred during the quarter. 75% of the bad debts have been deferred for the next three quarters (25% for each quarter).

(ii) Sales promotion expenses of Rs.5,00,000 incurred in the first quarter and 90% expenses deferred to the next three quarters (30% for each quarter) on the basis that the sales in these quarters will be high in comparison to first quarter.

(iii) Additional depreciation of Rs.3,50,000 resulting from the change in the method of depreciation has been taken into consideration.

(iv) Extra-ordinary loss of Rs.1,36,000 incurred during the quarter has been fully recognized in this quarter.

Discuss the treatment required under Ind AS 34 and ascertain the correct net profit to be shown in the Interim Financial report of first quarter to be presented to the Board of Directors.

Solution :

As per Ind AS 34, Interim Financial Reporting, the quarterly net profit should be adjusted and restated as follows:

(i) Bad debts of Rs.1,64,000 have been incurred during current quarter. Out of this, the company has deferred 75% i.e. Rs.1,23,000 to the next 3 quarters. This treatment is not correct as the expenses incurred during an interim reporting period should be recognised in the same period unless conditions mentioned in Ind AS 34 are fulfilled. Accordingly, Rs.1,23,000 should be deducted from the net profit of the current quarter Rs.15,00,000.

(ii) Deferment of sales promotion expenses of Rs.4,50,000 is not correct. It should be charged in the quarter in which the expenses have been incurred. Hence, it should be charged in the first quarter only.

(iii) Recognising additional depreciation of Rs.3,50,000 in the same quarter is correct and is in tune with Ind AS 34.

(iv) The treatment of extra-ordinary loss of Rs.1,36,000 being recognised in the same quarter is correct.

Accordingly,

Net Profit	Rs.15,00,000
Bad Debts	Rs.1,23,000
Sales Promotion Expenses	Rs.4,50,000

Rs.9,27,000

Question 2 : Nov 2019 – RTP

An entity reports quarterly, earns Rs.1,50,000 pre-tax profit in the first quarter but expects to incur losses of Rs.50,000 in each of the three remaining quarters. The entity operates in a jurisdiction in which its estimated average annual income tax rate is 30%.

The management believes that since the entity has zero income for the year, its income-tax expense for the year will be zero. State whether the management's views are correct. If not, then calculate the tax expense for each quarter as well as for the year as per Ind AS 34.

Solution :

As per Ind AS 34 'Interim Financial Reporting', income tax expense is recognised in each interim period based on the best estimate of the weighted average annual income tax rate expected for the full financial year.

Accordingly, the management's contention that since the net income for the year will be zero no income tax expense shall be charged quarterly in the interim financial report, is not correct.

The following table shows the correct income tax expense to be reported each quarter in accordance with Ind AS 34:

Period	**Pre-tax earnings (in Rs.)**	**Effective tax rate**	**Tax expense (in Rs.)**
First Quarter	1,50,000	30%	45,000
Second Quarter	(50,000)	30%	(15,000)
Third Quarter	(50,000)	30%	(15,000)
Fourth Quarter	(50,000)	30%	(15,000)
Annual	**0**		**0**

Question 3 : Nov 2020 – RTP

An entity's accounting year ends is 31st December, but its tax year end is 31st March. The entity publishes an interim financial report for each quarter of the year ended 31st December, 2019. The entity's profit before tax is steady at `10,000 each quarter, and the estimated effective tax rate is 25% for the year ended 31st March, 2019 and 30% for the year ended 31st March, 2020. How the related tax charge would be calculated for the year 2019 and its quarters.

Solution :

Since Entity's accounting year differs from tax years, more than one tax rate might be applied during the accounting year.

Effective tax rate for 18 - 19 = 25%

for 19 – 20 = 30%

	Q1 Ending 31/3/19	**Q2 Ending 30/6/19**	**Q3 Ending 30/9/19**	**Q4 Ending 31/12/19**
PBT	10,000	10,000	10,000	10,000

Effective tax rate	25%	30%	30%	30%
Tax	(2,500)	(3,000)	(3,000)	(3,000)
PAT	7,500	7,000	7,000	7,000

Question 4 : July 2021 – Paper

Heavy Limited has a plant with normal capacity to produce 90,000 units of a product per annum and expected fixed production overhead for the year is Rs.18,00,000. There are no quarterly/seasonal variations. Hence, normal expected production of each quarter is uniform. The actual production of the year is 87,000 units. The production details of each quarter are as under :

Quarter I : 20,000 units
Quarter II : 24,000 units
Quarter III : 23,500 units
Quarter IV : 19,500 units

Calculate the allocation of fixed production overhead for all the four quarters. Will the quarterly results affect annual result?

Give your answer as per Ind AS 34 read with Ind AS 2.

Solution :

Since it is considered that there is no quarterly / seasonal variation, then normal expected production for each quarter is 22,500 units (90,000 units / 4 quarters) and fixed production overheads for the quarter are Rs. 4,50,000 (Rs. 18,00,000 / 4 quarters).

Fixed production overhead to be allocated per unit of production in every quarter will be Rs. 20 per unit.

(Fixed overheads / Normal production i.e. Rs. 4,50,000 / 22,500 units

Particulars	**Quarters**			
	I	**II**	**III**	**IV**
Actual fixed production overheads on year to date basis (Rs.)	4,50,000	9,00,000	13,50,000	18,00,000
Actual production (Units)	20,000	24,000	23,500	19,500
Actual production year to date basis (Units)	20,000	44,000	67,500	87,000
Fixed overheads to be absorbed on year to date basis (Rs.)	4,00,000	8,80,000	13,50,000	17,40,000
Under recovery year to date (Rs.)	**50,000**	**20,000**	**NIL**	**60,000**

Quarter I:

Unallocated fixed production overheads Rs. 50,000 (i.e. Rs. 4,50,000 – Rs. 4,00,000) to be charged as expense as per Ind AS 2 and consequently as per Ind AS 34.

Quarter II:

Since production increased in second quarter by 1,500 units (24,000 – 22,500) i.e. more than the normal expected production, hence Rs. 30,000 (1,500 units x Rs. 20 per unit) will be reversed by way of a credit to the statement of profit and loss of the 2nd quarter and debit to cost of production / inventory cost.

Quarter III:

Earlier, Rs. 50,000 was not allocated to production / inventory cost in the 1st quarter. Out of it, Rs. 30,000 was reversed in the 2nd quarter. To allocate entire Rs. 13,50,000 till third quarter to the production, as per Ind AS 34, remaining Rs. 20,000 (Rs. 50,000 – Rs. 30,000) will be reversed by way of a credit to the statement of profit and loss of the 3rd quarter and debit to the cost of production / inventory cost.

Quarter IV:

Unallocated fixed production overheads Rs. 60,000 {i.e. Rs. 4,50,000 – (Rs. 20 x 19,500)} in the 4th quarter will be expensed off as per the principles of Ind AS 2 and Ind AS 34 by way of a charge to the statement of profit and loss.

For the year:

The cumulative result of all the quarters would also result in unallocated overheads of Rs. 60,000, thus, meeting the requirements of Ind AS 34 that the quarterly results should not affect the measurement of the annual result.

Question 5 : Nov 2021 – RTP

While preparing interim financial statements for the half-year ended 30 September 20X2, an entity discovers a material error (an improper expense accrual) in the interim financial statements for the period ended 30 September 20X1 and the annual financial statements for the year ended 31 March 20X2. The entity does not intend to restate the comparative amounts for the prior period presented in the interim financial statements as it believes it would be sufficient to correct the error by restating the comparatives in the annual financial statements for the year ended 31 March 20X3. Is this acceptable? Discuss in accordance with relevant Ind AS.

Solution :

Paragraph 42 of Ind AS 8, inter alia, states that an entity shall correct material prior period errors retrospectively in the first set of financial statements approved for issue after their discovery by restating the comparative amounts for the prior period(s) presented in which the error occurred.

Paragraph 28 of Ind AS 34 requires an entity to apply the same accounting policies in its interim financial statements as are applied in its annual financial statements (except for accounting policy changes made after the date of the most recent annual financial statements that are to be reflected in the next annual financial statements).

Paragraph 15B of Ind AS 34 cites ‘corrections of prior period errors’ as an example of events or transactions which need to be explained in an entity’s interim financial report if they are significant to an understanding of the changes in financial position and performance of the entity since the end of the last annual reporting period.

Paragraph 25 of Ind AS 34, Interim Financial Statements, states as follows:

“While judgement is always required in assessing materiality, this Standard bases the recognition and disclosure decision on data for the interim period by itself for reasons of understandability of the interim figures. Thus, for example, unusual items, changes in accounting policies or estimates, and errors are recognised and disclosed on the basis of materiality in relation to interim period data to avoid misleading inferences that might result from non-disclosure. The overriding goal is to ensure that an interim financial report includes all information that is relevant to understanding an entity's financial position and performance during the interim period."

In view of the above, the entity is required to correct the error and restate the comparative amounts in interim financial statements for the half-year ended 30 September 20X2.

Thanks ....

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IND AS – 8 ACCOUNTING POLICIES, CHANGES IN ACCOUNTING ESTIMATES & ERRORS

CHAPTER - 16

Question 1 : May 2019 – RTP

ABC Ltd. changed its method adopted for inventory valuation in the year 2018-2019. Prior to the change, inventory was valued using the first in first out method (FIFO). However, it was felt that in order to match current practice and to make the financial statements more relevant and reliable, a weighted average valuation model would be more appropriate.

The effect of the change in the method of valuation of inventory was as follows:

- 31st March, 2017 - Increase of Rs.10 million
- 31st March, 2018 - Increase of Rs.15 million
- 31st March, 2019 - Increase of Rs.20 million

Profit or loss under the FIFO valuation model are as follows:

	2018-2019	**2017-2018**
Revenue	324	296
Cost of goods	(173)	(164)
Gross profit	**151**	**132**
Expenses	(83)	(74)
Profit	**68**	**58**

Retained earnings at 31st March, 2017 were Rs.423 million

Present the change in accounting policy in the profit or loss and produce an extract of the statement of changes in equity in accordance with Ind AS 8.

Solution :

Profit or loss under weighted average valuation method is as follows :

	2018-2019	**2017-2018 (Restated)**
Revenue	324	296
Cost of goods	(168)	(159)
Gross profit	**156**	**137**
Expenses	(83)	(74)
Profit	**73**	**63**

Statement of changes in Equity (extract)

	Retained earnings	Retained earnings (Original)
At 1st April, 2017	423	423
Change in inventory valuation policy	10	-
At 1st April, 2017 (Restated)	**433**	**-**
Profit for the year 2017-2018	63	58
At 31st March, 2018	**496**	**481**
Profit for the 2018-2019	73	68
At 31st March, 2019	**569**	**549**

Question 2 : Nov 2019 – RTP

During 20X4-X5, Cheery Limited discovered that some products that had been sold during 20X3-X4 were incorrectly included in inventory at 31st March, 20X4 at Rs.6,500.

Cheery Limited's accounting records for 20X4-X5 show sales of Rs.104,000, cost of goods sold of Rs.86,500 including Rs.6,500 for the error in opening inventory), and income taxes of Rs.5,250.

In 20X3-X4, Cheery Limited reported:

	Rs.
Sales	73,500
Cost of goods sold	(53,500)
Profit before income taxes	20,000
Income taxes	(6,000)
Profit	14,000
Basic and diluted EPS	2.8

The 20X3-X4 opening retained earnings was Rs.20,000 and closing retained earnings was Rs.34,000. Cheery Limited's income tax rate was 30% for 20X4-X5 and 20X3-X4. It had no other income or expenses.

Cheery Limited had Rs.50,000 (5,000 shares of Rs.10 each) of share capital throughout, and no other components of equity except for retained earnings.

State how the above will be treated /accounted in Cheery Limited's Statement of profit and loss, statement of changes in equity and in notes wherever required for current period and earlier period(s) as per relevant Ind AS.

Solution :

Cheery Limited

Extract from the Statement of profit and loss

		(Restated)
	20X4-X5	**20X3-X4**
	Rs.	**Rs.**
Sales	1,04,000	73,500
Cost of goods sold	(80,000)	(60,000)
Profit before income taxes	**24,000**	**13,500**

Income taxes	(7,200)	(4,050)
Profit	**16,800**	**9,450**
Basic and diluted EPS	3.36	1.89

Cheery Limited
Statement of Changes in Equity

	Share capital	Retained earnings	Total
Balance at 31st March, 20X3	50,000	20,000	70,000
Profit for the year ended 31st March, 20X4 as restated	______	9,450	9,450
Balance at 31st March, 20X4	**50,000**	**29,450**	**79,450**
Profit for the year ended 31st March, 20X5	______	16,800	16,800
Balance at 31st March, 20X5	**50,000**	**46,250**	**96,250**

Extract from the Notes

Some products that had been sold in 20X3-X4 were incorrectly included in inventory at 31st March, 20X4 at Rs.6,500. The financial statements of 20X3-X4 have been restated to correct this error. The effect of the restatement on those financial statements is summarized below:

	Effect on 20X3-X4
(Increase) in cost of goods sold	(6,500)
Decrease in income tax expenses	1,950
(Decrease) in profit	(4,550)
(Decrease) in basic and diluted EPS	(0.91)
(Decrease) in inventory	(6,500)
Decrease in income tax payable	1,950
(Decrease) in equity	(4,550)

There is no effect on the balance sheet at the beginning of the preceding period i.e. 1st April, 20X3.

Question 3 : May 2020 – RTP

While preparing the financial statements for the year ended 31st March, 20X3, Alpha Limited has observed two issues in the previous year Ind AS financial statements (i.e. 31st March, 20X2) which are as follows:

Issue 1:

The company had presented certain material liabilities as non-current in its financial statements for periods as on 31st March, 20X2. While preparing annual financial statements for the year ended 31st March, 20X3, management discovers that these liabilities should have been classified as current. The management intends to restate the comparative amounts for the prior period presented (i.e., as at 31st March, 20X2).

Issue 2:

The company had charged off certain expenses as finance costs in the year ended 31st March, 20X2. While preparing annual financial statements for the year ended 31st March, 20X3, it was discovered that these expenses should have been classified as other expenses instead of finance costs. The error occurred because the management inadvertently misinterpreted certain facts. The entity intends to restate the comparative amounts for the prior period presented in which the error occurred (i.e., year ended 31st March, 20X2).

What is your analysis and recommendation in respect of the issues noted with the previously presented set of financial statements for the year ended 31st March, 20X2?

Solution :

As per Ind AS 8 'Accounting Policies, Changes in Accounting Estimates and Errors', errors can arise in respect of the recognition, measurement, presentation or disclosure of elements of financial statements. Financial statements do not comply with Ind AS if they contain either material errors or immaterial errors made intentionally to achieve a particular presentation of an entity's financial position, financial performance or cash flows. Potential current period errors discovered in that period are corrected before the financial statements are approved for issue. However, material errors are sometimes not discovered until a subsequent period, and these prior period errors are corrected in the comparative information presented in the financial statements for that subsequent period.

Accordingly, the stated issues in question are to dealt as under:

Issue 1

In accordance with para 41, the reclassification of liabilities from non-current to current would be considered as correction of an error under Ind AS 8. Accordingly, in the financial statements for the year ended March 31, 20X3, the comparative amounts as at 31 March 20X2 would be restated to reflect the correct classification.

Ind AS 1 requires an entity to present a third balance sheet as at the beginning of the preceding period in addition to the minimum comparative financial statements, if, inter alia, it makes a retrospective restatement of items in its financial statements and the restatement has a material effect on the information in the balance sheet at the beginning of the preceding period. Accordingly, the entity should present a third balance sheet as at the beginning of the preceding period, i.e., as at 1 April 20X1 in addition to the comparatives for the financial year 20X1-20X2.

Issue 2

In accordance with para 41, the reclassification of expenses from finance costs to other expenses would be considered as correction of an error under Ind AS 8. Accordingly, in the financial statements for the year ended 31 March, 20X3, the comparative amounts for the year ended 31 March 20X2 would be restated to reflect the correct classification.

Ind AS 1 requires an entity to present a third balance sheet as at the beginning of the preceding period in addition to the minimum comparative financial statements if, inter alia, it makes a retrospective restatement of items in its financial statements and the restatement has a material effect on the information in the balance sheet at the beginning of the preceding period.

In the given case, the retrospective restatement of relevant items in statement of profit and loss has no effect on the information in the balance sheet at the beginning of the preceding period (1 April 20X1). Therefore, the entity is not required to present a third balance sheet.

Question 4 : May 2021 – RTP

In 20X3-20X4, after the entity's 31 March 20X3 annual financial statements were approved for issue, a latent defect in the composition of a new product manufactured by the entity was discovered (that is, a defect that could not be discovered by reasonable or customary inspection). As a result of the latent defect the entity incurred Rs.100,000 in unanticipated costs for fulfilling its warranty obligation in respect of sales made before 31 March 20X3. An additional Rs.20,000 was incurred to rectify the latent defect in products sold during 20X3-20X4 before the defect was detected and the production process rectified, Rs.5,000 of which relates to items of inventory at 31 March 20X3. The defective inventory was reported at cost Rs. 15,000 in the 20X2-20X3 financial statements when its selling price less costs to complete and sell was estimated at Rs.18,000. The accounting estimates made in preparing the 31 March 20X3 financial statements were appropriately made using all reliable information that the entity could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Analyse the above situation in accordance with relevant Ind AS.

Solution :

Ind AS 8 is applied in selecting and applying accounting policies, and accounting for changes in accounting policies, changes in accounting estimates and corrections of prior period errors.

A change in accounting estimate is an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset. This change in accounting estimate is an outcome of the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors.

Further, the effect of change in an accounting estimate, shall be recognised prospectively by including it in profit or loss in: (a) the period of the change, if the change affects that period only; or (b) the period of the change and future periods, if the change affects both.

Prior period errors are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:

(a) was available when financial statements for those periods were approved for issue; and

(b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.

On the basis of above provisions, the given situation would be dealt as follows:

The defect was neither known nor reasonably possible to detect at 31 March 20X3 or before the financial statements were approved for issue, so understatement of the warranty provision Rs. 1,00,000 and overstatement of inventory Rs. 2,000 (Note 1) in the 31 March 20X3 financial statements are not a prior period errors.

The effects of the latent defect that relate to the entity's financial position at 31 March 20X3 are changes in accounting estimates.

In preparing its financial statements for 31 March 20X3, the entity made the warranty provision and inventory valuation appropriately using all reliable information that the entity could reasonably be expected to have obtained and had taken into account the same in the preparation and presentation of those financial statements.

Consequently, the additional costs are expensed in calculating profit or loss for 20X3-20X4.

Working Note:

Inventory is measured at the lower of cost (ie Rs. 15,000) and fair value less costs to complete and sell (ie Rs. 18,000 originally estimated minus Rs. 5,000 costs to rectify latent defect) = Rs. 13,000.

Thanks ….

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IND AS – 37 PROVISIONS, CONTINGENT LIABILITIES & CONTINGENET ASSETS

CHAPTER - 17

Question 1 : Nov 2018 – RTP

U Ltd. is a large conglomerate with a number of subsidiaries. It is preparing consolidated financial statements as on 31st March 2018 as per the notified Ind AS. The financial statements are due to be authorised for issue on 15th May 2018. It is seeking your assistance for some transactions that have taken place in some of its subsidiaries during the year.

1) G Ltd. is a wholly owned subsidiary of U Ltd. engaged in management consultancy services. On 31st January 2018, the board of directors of U Ltd. decided to discontinue the business of G Ltd. from 30th April 2018. They made a public announcement of their decision on 15th February 2018.
2) G Ltd. does not have many assets or liabilities and it is estimated that the outstanding trade receivables and payables would be settled by 31st May 2018. U Ltd. would collect any amounts still owed by G Ltd's customers after 31st May 2018. They have offered the employees of G Ltd. termination payments or alternative employment opportunities.
3) Following are some of the details relating to G Ltd.:
   - On the date of public announcement, it is estimated by G Ltd. that it would have to pay 540 lakhs as termination payments to employees and the costs for relocation of employees who would remain with the Group would be Rs.60 lakhs. The actual termination payments totalling to Rs.520 lakhs were made in full on 15th May 2018. As per latest estimates made on 15th May 2018, the total relocation cost is Rs.63 lakhs.
   - G Ltd. had taken a property on operating lease, which was expiring on 31st March 2022. The present value of the future lease rentals (using an appropriate discount rate) is Rs.430 lakhs. On 15th May 2018, G Ltd. made a payment to the lessor of Rs.410 lakhs in return for early termination of the lease.
4) The loss after tax of G Ltd. for the year ended 31st March 2018 was Rs.400 lakhs. G Ltd. made further operating losses totalling Rs.60 lakhs till 30th April 2018.

How should U Ltd. present the decision to discontinue the business of G Ltd. in its consolidated statement of comprehensive income as per Ind AS?

What are the provisions that the Company is required to make as per Ind AS 37?

Solution :

A discontinued operation is one that is discontinued in the period or classified as held for sale at the year end. The operations of G Ltd were discontinued on 30th April 2018 and therefore, would be treated as discontinued operation for the year ending 31st March 2019. It does not meet the criteria for held for sale since the company is terminating its business and does not hold these for sale.

Accordingly, the results of G Ltd will be included on a line-by-line basis in the consolidated statement of comprehensive income as part of the profit from continuing operations of U Ltd for the year ending 31st March 2018.

As per para Ind AS 37 'Provisions, Contingent Liabilities and Contingent Assets', restructuring includes sale or termination of a line of business. A constructive obligation to restructure arises when:

(a) an entity has a detailed formal plan for the restructuring

(b) has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

The Board of directors of U Ltd have decided to terminate the operations of G Ltd. from 30th April 2018. They have made a formal announcement on 15th February 2018, thus creating a valid expectation that the termination will be implemented. This creates a constructive obligation on the company and requires provisions for restructuring.

A restructuring provision includes only the direct expenditures arising from the restructuring that are necessarily entailed by the restructuring and are not associated with the ongoing activities of the entity.

The termination payments fulfil the above condition. As per Ind AS 10 'Events after Reporting Date', events that provide additional evidence of conditions existing at the reporting date should be reflected in the financial statements. Therefore, the company should make a provision for Rs. 520 lakhs in this respect.

The relocation costs relate to the future conduct of the business and are not liabilities for restructuring at the end of the reporting period. Hence, these would be recognised on the same basis as if they arose independently of a restructuring.

The operating lease would be regarded as an onerous contract. A provision would be made at the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it. Hence, a provision shall be made for Rs. 410 lakhs.

Further operating losses relate to future events and do not form a part of the closure provision.

Therefore, the total provision required = Rs.520 lakhs + Rs.410 lakhs = Rs.930 lakhs

Question 2 : Nov 2018 – PAPER

Sun Limited has entered into a binding agreement with Moon Limited to buy a custom-made machine for Rs.4,00,000. At the end of 2017-18, before delivery of the machine, Sun Limited had to change its method of production. The new method will not require the machine ordered which is to be scrapped after delivery. The expected scrap value is nil. Given that the asset is yet to be delivered, should any liability be recognized for the potential loss? If so, give reasons for the same, the amount of liability as well as the accounting entry.

Solution :

As per Ind AS 37, Executory contracts are contracts under which

❖ neither party has performed any of its obligations; or

❖ both parties have partially performed their obligations to an equal extent.

The contract entered by Sun Ltd. is an executory contract, since the delivery has not yet taken place.

Ind AS 37 is applied to executory contracts only if they are onerous.

Ind AS 37 defines an onerous contract as a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

As per the facts given in the question, Sun Ltd. will not require the machine ordered. However, since it is a binding agreement, the entity cannot exit / cancel the agreement. Further, Sun Ltd. has to scrap the machine after delivery at nil scrap value.

These circumstances do indicate that the agreement/contract is an onerous contract. Therefore, a provision should be made for the onerous element of Rs.4,00,000 ie the full cost of the machine.

		Rs.	**Rs.**
Onerous Contract Provision Expense A/c	Dr.	4,00,000	
To Provision for Onerous Contract Liability A/c			4,00,000
(Being asset to be received due to binding agreement recognized)			
Profit and Loss Account (Loss due to onerous contract)	Dr.	4,00,000	
To Onerous Contract Provision Expense A/c			4,00,000
(Being loss due to onerous contract recognized and asset derecognsied)			

Question 3 : Nov 2019 – RTP

(a) A manufacturer gives warranties at the time of sale to purchasers of its product. Under the terms of the contract for sale, the manufacturer undertakes to remedy, by repair or replacement, manufacturing defects that become apparent within three years from the date of sale. As this is the first year that the warranty has been available, there is no data from the firm to indicate whether there will be claim under the warranties. However, industry research suggests that it is likely that such claims will be forthcoming.

Should the manufacturer recognize a provision in accordance with the requirements of Ind AS 37. Why or why not?

(b) Assume that the firm has not been operating its warranty for five years, and reliable data exists to suggest the following:

- If minor defects occur in all products sold, repair costs of Rs.20,00,000 would result.
- If major defects are detected in all products, costs of Rs.50,00,000 would result.

- The manufacturer's past experience and future expectations indicate that each year 80% of the goods sold will have no defects. 15% of the goods sold will have minor defects, and 5% of the goods sold will have major defects.

Calculate the expected value of the cost of repairs in accordance with the requirements of Ind AS 37, if any. Ignore both income tax and the effect of discounting.

Solution :

(a) For a provision to be recognized, Para 14 of Ind AS 37 requires that:

a) an entity has a present obligation (legal or constructive) as a result of a past event;

b) it is probable that an outflow of resources embodying economic benefits will required to settle the obligation, and

c) a reliable estimate can be made of the amount of the obligation.

Here, the manufacturer has a present legal obligation. The obligation event is the sale of the product with a warranty.

Ind AS 37 outlines that the future sacrifice of economic benefits is probable when it is more likely than less likely that the future sacrifice of economic benefits will required. The probability that settlement will be required will be determined by considering the class of obligation (warranties) as a whole. In accordance with para 24 of Ind AS 37, it is more likely than less likely that a future sacrifice of economic benefits will be required to settle the class of obligations as a whole.

If a reliable estimate can be made the provision can be measured reliably. Past data can provide reliable measures, even if the data is not firm specific but rather industry based. Ind AS 37 notes that only in extremely rare cases, a reliable measure of a provision cannot be obtained. Difficulty in estimating the amount of a provision under conditions of significant uncertainty does not justify non-recognition of the provision.

Here, the manufacturer should recognize a provision based on the best estimate of the consideration required to settle the present obligation as at the reporting date.

(b) The expected value of cost of repairs in accordance with Ind AS 37 is:

(80% × nil) + (15% × Rs.20,00,000) + (5% × Rs.50,00,000) = 3,00,000 + 2,50,000 = 5,50,000

Question 4 : May 2020 – RTP

Entity XYZ entered into a contract to supply 1000 television sets for Rs.2 million. An increase in the cost of inputs has resulted into an increase in the cost of sales to Rs.2.5 million. The penalty for non- performance of the contract is expected to be Rs.0.25 million. Is the contract onerous and how much provision in this regard is required?

Solution :

IND AS 37 "Provisions, Contingent Liabilities and Contingent Assets" defines an onerous contingent as.

A contract in which cost of meeting obligation under contract exceeds the economic benefit expected to be received.

In the above case since the cost of sales have exceeded contract price the contract is onerous.

If the contract is completed the cost will exceed by 0.5 i.e. 2.5 – 2. Also entity XYZ can pay penalty for non performance of Rs.0.25 million
∴ Entity XYZ should provide for Rs.0.25 million.

Question 5 : Nov 2020 – Paper

Sophia Ltd. has fabricated special equipment (Inverter panel) during the financial year 2018-2019 as per drawing and design supplied by the customer. However, due to a liquidity crunch, the customer has requested the company for postponement in delivery schedule and requested the company to withhold the delivery of finished products and discontinue the production of balance items.
As a result of the above, the details of customer balance and the goods held by the company as work-in-progress and finished goods as on 31 March 2020 are as follows:

Inverter panel (WIP)	Rs.255 lakhs
Inverter panel (Finished goods)	Rs.165 lakhs
Sundry Debtor (Inverter panel)	Rs.195 lakhs

The petition for winding up against the customer has been filed during the financial year 2019-2020 by Sophia Ltd.
You are required to Comment with explanation on provision to be made for Rs. 615 lakh included in Sundry Debtors, Finished goods and Work-in-Progress in the financial statement for the Financial year 2019-2020.

Solution :

Sophia Ltd. is a manufacturer of inverter panel. As per Ind AS 2 'Inventories', inventories are assets (a) held for sale in the ordinary course of business; (b) in the process of production for such sale; or (c) in the form of materials or supplies to be consumed in the production process or in the rendering of services. Therefore, inverter panel held in its stock will be considered as its inventory. Further, as per the standard, inventory at the end of the year is to be valued at lower of cost or NRV.
As the customer has postponed the delivery schedule due to liquidity crunch the entire cost incurred for inverter panel which were to be supplied has been shown in Inventory. The inverter panel are in the possession of the Company which can be sold in the market. Hence company should value such inventory as per principle laid down in Ind AS 2 i.e. lower of Cost or NRV. Though, the goods were produced as per specifications of the buyer the Company should determine the NRV of these goods in the market and value the goods accordingly. Change in value of such inverter panel should be provided for in the books.
In the absence of the NRV of WIP and Finished product given in the question, assuming that cost is lower, the company shall value its inventory as per Ind AS 2 at Rs. 420 lakhs [i.e inverter panel (WIP) Rs. 255 lakhs + inverter panel (finished products) Rs. 165 lakhs].

Alternatively, if it is assumed that there is no buyer for such fabricated inverter panel, then the NRV will be Nil. In such a case, full value of finished goods and WIP will be provided for in the books.

As regards balance of Sundry Debtors, since the Company has filed a petition for winding up against the customer in 2019-2020, it is probable that amount is not recoverable from the party. Hence, the provision for doubtful debts for Rs. 195 lakhs shall be made in the books against the amount of debtors.

Question 6 : May 2021 – RTP

A manufacturer gives warranties to the purchasers of its goods. Under the terms of the warranty, the manufacturer undertakes to make good, by repair or replacement, manufacturing defects that become apparent within three years from the date of sale to the purchasers.

On 30 April 20X1, a manufacturing defect was detected in the goods manufactured by the entity between 1 March 20X1 and 30 April 20X1.

At 31 March 20X1 (the entity's reporting date), the entity held approximately one week's sales in inventories.

The entity's financial statements for the year ended 31 March 20X1 have not yet been finalised.

Three separate categories of goods require separate consideration:

Category 1—defective goods sold on or before 31 March 20X1

Category 2—defective goods held on 31 March 20X1

Category 3—defective goods manufactured in 20X1-20X2

State the accounting treatment of the above categories in accordance with relevant Ind AS.

Solution :

Category 1—defective goods sold on or before 31 March 20X1

If customer has the option to purchase warranty separately, the warranty is a distinct service because the entity promises to provide the service to the customer in addition to the product that has the functionality described in the contract. In that case, entity shall account for the promised warranty as a performance obligation and allocate a portion of the transaction price to that performance obligation.

If a customer does not have the option to purchase a warranty separately, an entity shall account for the warranty in accordance with Ind AS 37, Provisions, Contingent Liabilities and Contingent Assets, unless it provides the customer with a service in addition to the assurance that the product complies with agreed-upon specifications. If that is the case, then, the promised service is a performance obligation. Entity shall allocate the transaction price to the product and the service.

If an entity promises both an assurance-type warranty and a service-type warranty but cannot reasonably account for them separately, the entity shall account for both of the warranties together as a single performance obligation.

A law that requires an entity to pay compensation if its products cause harm or damage does not give rise to a performance obligation. The entity shall account for such obligations in accordance with Ind AS 37.

Category 2—defective goods held on 31 March 20X1

At 31 March 20X1, the entity did not have a present obligation to make good the unsold defective goods that it held in inventories. Accordingly, at 31 March 20X1 the entity should not recognise a provision in respect of the defective inventories.

For this category, the detection of the manufacturing defect in April 20X1 is an adjusting event after the end of the reporting period as per Ind AS 10, Events after the End of the Reporting Period. It provides evidence of a manufacturing defect in inventories held at 31 March 20X1.

Category 3—defective goods manufactured in 20X1-20X2

At 31 March 20X1 the entity did not have a present obligation to make good any defective goods that it might manufacture in the future. Accordingly, at 31 March 20X1 the entity should not recognise a provision in respect of the defective goods manufactured in 20X1-20X2.

For this category, the detection of the manufacturing defect in April 20X1 is a non-adjusting event after the end of the reporting period as per Ind AS 10, Events After the End of the Reporting Period.

Question 7 : May 2022 – RTP

XYZ Ltd. offers a six-month warranty on its small to medium sized equipment, which can be put to use by the customer with no installation support. The warranty comes with the equipment and the customer cannot purchase it separately. This equipment is typically sold at a gross margin of 40%. XYZ Ltd. has made a provision of Rs. 30,000 during the year ended 31st March, 20X2, which is approximately 1% of its gross margin on the sale of these equipment. Based on past experience, it is expected that 1% of equipment sold have been returned as faulty within the warranty period. Faulty equipment returned to XYZ Ltd. during the warranty period are scrapped and the sale value is fully refunded to the customer.

Assuming that sales occurred evenly during the year, how should XYZ Ltd. evaluate whether any additional warranty provision is required on equipment sold in the past as at 31st March, 20X2? Had the warranty period been 2 years instead of six months, what additional criteria would XYZ Ltd. need to consider?

Solution :

Calculation of additional warranty provisions:

Warranty claim covers 1% of gross margin, whereas customers are refunded the full selling price. As the goods are scrapped it is assumed XYZ Ltd has no potential for re-imbursement from its supplier regarding the faulty goods.

A calculation of warranty provision is set out below:

1% of annual gross margin is Rs. 30,000 therefore 100% of annual gross margin must be Rs. 30,00,000. Since gross margin is 40%, sales should be Rs. 75,00,000. As provide in the question that the sales are evenly spread during the year and given the six month warranty, half of the sales occurred in the second half of the year is still covered within the warranty period as follows.

	% age	Annual sales	Product under warranty at 31st March, 20X2	Percentage expected to be returned	Warranty provision
		Rs.	Rs.	Rs.	Rs.
Gross margin	40%	30,00,000			
Selling price	100%	75,00,000	37,50,000	1%	37,500

The warranty provision should therefore be increased by Rs. 7,500 (Rs. 37,500 – Rs. 30,000). As the provision is expected to be used in the next 6 months no discounting is required.

If the warranty period is 2 years:

Since the outstanding period of warranties is 6 months (i.e. less than a year), no discounting is required. However, if a longer warranty period is to be given, the entity will have to take into account the effect of the time value of money. The amount of provision shall be the present value of the expenditures expected to be required to settle the warranty obligation. (Refer Para 45 of Ind AS 37)

The discount rate shall be a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The discount rate shall not reflect risks for which future cash flow estimates have been adjusted. (Refer Para 47 of Ind AS 37)

	% age	**Annual sales**	**Product under warranty at 31st March, 20X2**	**Percentage expected to be returned**	**Warranty provision**
		Rs.	**Rs.**	**Rs.**	**Rs.**
Gross margin	40%	30,00,000			
Selling price	100%	75,00,000	75,00,000	1%	75,000

The warranty provision should therefore be increased by Rs. 45,000 (Rs. 75,000 – Rs. 30,000). Further discounting of provision would be required.

Thanks ....

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IND AS – 103
BUSINESS COMBINATION

CHAPTER - 18

Question 1 : May 2018 – RTP

On 1 April 20X1, Alpha Ltd. acquires 80 percent of the equity interest of Beta Pvt. Ltd. in exchange for cash of Rs 300. Due to legal compulsion, Beta Pvt. Ltd. had to dispose of their investments by a specified date. Therefore, they did not have sufficient time to market Beta Pvt. Ltd. to multiple potential buyers. The management of Alpha Ltd. initially measures the separately recognizable identifiable assets acquired and the liabilities assumed as of the acquisition date in accordance with the requirement of Ind AS 103. The identifiable assets are measured at Rs 500 and the liabilities assumed are measured at Rs 100. Alpha Ltd. engages on independent consultant, who determined that the fair value of 20 per cent non-controlling interest in Beta Pvt. Ltd. is Rs 84.
Alpha Ltd. reviewed the procedures it used to identify and measure the assets acquired and liabilities assumed and to measure the fair value of both the non controlling interest in Beta Pvt. Ltd. and the consideration transferred. After the review, it decided that the procedures and resulting measures were appropriate.
Calculate the gain or loss on acquisition of Beta Pvt. Ltd. and also show the journal entries for accounting of its acquisition. Also calculate the value of the non-controlling interest in Beta Pvt. Ltd. on the basis of proportionate interest method, if alternatively applied?

Solution :

1. Calculation of goodwill / gain on bargain purchase :

Consideration paid	300	
+ NCI at fair value	84	
	384	
– FV of net asset (500 – 100)		400
Gain from bargain purchase		16

2. Journal Entry :

		Dr.	Cr.
Assets A/c	Dr.	500	
To Liability			100
To Bank			300
To NCI			84
To Gain on bargain purchase (CR)			16

Question 2 : May 2018 – PAPER

Notorola Limited has two divisions A and B. Division A has been making constant profits while Division B has been invariably suffering losses.

On 31st March 2018, the division-wise draft extract of the Balance Sheet was as follows:

(Rs.in crore)

	A	B	Total
Fixed Assets Cost	500	1000	1500
Depreciation	(450)	(800)	(1250)
Net Fixed Assets (A)	50	200	250
Current Assets	400	1000	1400
Less: Current Liabilities	(50)	(800)	(850)
Net Current Assets (B)	350	200	550
Total (A) + (B)	**400**	**400**	**800**
Financed by :			
Loan Funds	-	600	60
Capital : Equity Rs.10 each	50	-	50
Surplus	350	-200	150
Total	**400**	**400**	**800**

Division B along with its assets and liabilities was sold for Rs.50 crore to Senovo Limited a new company, who allotted 2 crore equity shares of Rs.10 each at a premium of Rs.15 per share to the members of Notorola Limited in full settlement of the consideration, in proportion to their shareholding in the company. One of the members of the Notorola Limited was holding 52% shares of the company.

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

(i) Pass journal entries in the books of Notorola Limited.

(ii) Prepare the Balance Sheet of Notorola Limited after the entries in (i).

(iii) Prepare the Balance Sheet of Senovo Limited.

Balance Sheet prepared for (ii) and (iii) above should comply with the relevant Ind AS and Schedule III of the Companies Act, 2013. Provide Notes to Accounts, for 'Other Equity' in case of (ii) and 'Share Capital' in case of (iii), only.

Solution :

(i) Journal of Notorola Ltd.

(Rs. In crore)

		Dr.	Cr.
Loan Funds	Dr.	600	
Current Liabilities	Dr.	800	
Provision for Depreciation	Dr.	800	
To Fixed Assets			1,000
To Current Assets			1,000
To Capital Reserve			200

(Being division B along with its assets and liabilities sold to Senovo Ltd. for Rs.50 crore)		

(ii) **Notorola Ltd.**

Balance Sheet after demerger

(Rs.in crore)

ASSETS	**Note No.**	**Amount**
Non-current assets		
Property, Plant and Equipment		50
Current assets		400
		450
EQUITY AND LIABILITIES		
Equity		
Equity share capital (of face value of Rs.10 each)	1	50
Other equity	2	350
Liabilities		
Current liabilities		
Current liabilities		50
		450

Notes to Accounts

		Rs. in crore
1	**Equity Share Capital**	
	5 crore equity shares of face value of Rs.10 each	50
	Consequent to transfer of Division B to newly incorporated company Senovo Ltd., the members of the company have been allotted 2 crore equity shares of Rs.10 each at a premium of Rs.15 per share of Senovo Ltd., in full settlement of the consideration in proportion to their shareholding in the company	
2	**Other Equity**	
	Surplus (350 - 200)	150
	Add: Capital Reserve on reconstruction	200
		350

(iii) **Balance Sheet of Senovo Ltd.**

(Rs.in crore)

	Note No.	**Amount**
ASSETS		
Non-current assets		
Property, Plant and Equipment		200
Current assets		1,000
		1,200

EQUITY AND LIABILITIES		
Equity	1	20
Equity share capital (of face value of INR 10 each)	2	(220)
Other equity		
Liabilities		
Non-current liabilities		
Financial liabilities		
Borrowings		600
Current liabilities		
Current liabilities		800
		1,200

Notes to Accounts

		(Rs. In crore)
1.	**Share Capital** Issued and Paid-up capital 2 crore Equity shares of Rs.10 each fully paid up (All the above shares have been allotted to the members of Notorola Ltd. on takeover of Division B from Notorola Ltd. as fully paid-up pursuant to contract without payment being received in cash)	20
2.	**Other Equity (800 + 600 + 20) – (1,000 + 200)**	220

Question 3 : Nov 2018 – RTP

ABC Ltd. prepares consolidated financial statements upto 31st March each year. On 1st July 2017, ABC Ltd. acquired 75% of the equity shares of JKL Ltd. and gained control of JKL Ltd. the issued shares of JKL Ltd. is 1,20,00,000 equity shares. Details of the purchase consideration are as follows:

– On 1st July, 2017, ABC Ltd. issued two shares for every three shares acquired in JKL Ltd. On 1st July, 2017, the market value of an equity share in ABC Ltd. was Rs.6.50 and the market value of an equity share in JKL Ltd. was Rs.6.

– On 30th June, 2018, ABC Ltd. will make a cash payment of Rs.71,50,000 to the former shareholders of JKL Ltd. who sold their shares to ABC Ltd. on 1st July, 2017. On 1st July, 2017, ABC Ltd. would have to pay interest at an annual rate of 10% on borrowings.

– On 30th June, 2019, ABC Ltd. may make a cash payment of Rs.3,00,00,000 to the former shareholders of JKL Ltd. who sold their shares to ABC Ltd. on 1st July, 2017. This payment is contingent upon the revenues of ABC Ltd. growing by 15% over the two-year period from 1st July, 2017 to 30th June, 2019. On 1st July, 2017, the fair value of this contingent consideration was Rs.2,50,00,000. On 31st March, 2018, the fair value of the contingent consideration was Rs.2,20,00,000.

On 1st July, 2017, the carrying values of the identifiable net assets of JKL Ltd. in the books of that company was Rs.6,00,00,000. On 1st July, 2017, the fair values of these net assets was Rs.7,00,00,000. The rate of deferred tax to apply to temporary differences is 20%.

During the nine months ended on 31st March, 2018, JKL Ltd. had a poorer than expected operating performance. Therefore, on 31st March, 2018 it was necessary for ABC Ltd. to recognise an impairment of the goodwill arising on acquisition of JKL Ltd., amounting to 10% of its total computed value.
Compute the impairment of goodwill in the consolidated financial statements of ABC Ltd. under both the methods permitted by Ind AS 103 for the initial computation of the non-controlling interest in JKL Ltd. at the acquisition date.

Solution :

Computation of goodwill impairment

	NCI at fair value	NCI at of net assets
	Rs. in '000	**Rs. in '000**
Cost of investment		
Share exchange (12,000 x 75% x 2/3 x Rs.6.50)	39,000	39,000
Deferred consideration (7,150 / 1.10)	6,500	6,500
Contingent consideration	25,000	25,000
Non-controlling interest at date of acquisition:		
Fair value – 3000 x Rs.6	18,000	
% of net assets – 68,000 (Refer W.N.) x 25%	–	17,000
Net assets on the acquisition date (Refer W.N.)	(68,000)	(68,000)
Goodwill on acquisition	20,500	19,500
Impairment @ 10%	2,050	1,950

Working Note:

Net assets on the acquisition date	Rs. '000
Fair value at acquisition date	70,000
Deferred tax on fair value adjustments [20% x (70,000 – 60,000)]	(2,000)
	68,000

Question 4 : Nov 2018 – RTP

Smart Technologies Inc. is a Company incorporated in India in 1998 having business in the field of development and installation of softwares, trading of computer peripherals and other IT related equipment and provision of cloud computing services along with other services incidental thereto. It is one of the leading brands in India.
After witnessing immense popularity and support in its niche market, Smart Technologies further grew by bringing its subsidiaries namely:

Company Name	Principle Activity
Cloudustries India Private Limited	Provision of cloud computing services.
Micro Fly India Private Limited	Trading of computer peripherals like mouse, keyboard, printer etc.

Smart Technologies started preparing its financial statements based on Ind AS from 1st April, 2015 on voluntary basis. The Microfly India Pvt. Ltd. is planning to merge the business of Cloudstries India Pvt. Ltd. with its own for which it presented before the members in the meeting the below extract of latest audited Balance Sheet of Cloudustries (prepared on the basis of Ind AS) for the year ended 31st March, 2017:

Balance Sheet as at March 31, 2017 **(Rs. in Crores)**

Assets	
Non-current assets	
Property, plant and Equipment	15.00
	15.00
Current Assets	
(a) Financial assets	
Trade Receivables	10.00
Cash and cash equivalents	10.00
Other current assets	8.00
	28.00
Total	**43.00**
Equity and Liabilities	
Equity	
Equity Share Capital	45.00
Other Equity	
Reserves and Surplus (Accumulated Losses)*	(24.80)
	20.20
Liabilities	
Non-current Liabilities	
Financial liabilities	
Borrowings	2.80
Current Liabilities	20.00
	22.80
Total	**43.00**

*The Tax Loss carried forward of the company is Rs.27.20 crores

On September 5, 2017, the merger got approved by the Directors. The purchase consideration payable by MicroFly to Cloudustries was fixed at Rs.18.00 crores payable in cash and that MicroFly take over all the assets and liabilities of Cloudustries.

Present the statement showing the calculation of assets/liabilities taken over as per Ind AS. Also mention the accounting of difference between consideration and assets/liabilities taken over.

Solution :

Before the merger, Cloudustries and MicroFly are the subsidiary of Smart Technologies Inc. As the control is not transitory, the proposed merger will fall under the category of Business combination of entities under common control, it will be accounted as per Appendix C of Ind AS 103 "Business Combination" and Pooling of Interest Method would be applied.

Statement showing the calculation of assets/liabilities taken over and treatment of difference between consideration and assets/liabilities taken over:

(a) Net asset taken over: **(Rs.in crore)**

Assets taken over:	
Property, Plant and Equipment	15.00
Cash and cash equivalents	10.00
Other current assets	8.00
Trade Receivables	10.00
Total - A	**43.00**
Less: Liabilities taken over:	
Borrowings	2.80
Current Liabilities	20.00
Total - B	**22.80**
Net Asset taken over (A-B)	**20.20**

(b) Treatment of difference between consideration and assets/liabilities taken over:

(Rs.in crore)

Net Asset taken over - A	20.20
Less: Purchase Consideration - B	18.00
Difference (A – B)	**1.80**

The difference between consideration and assets/liabilities taken over of Rs.1.80 crore shall be transferred to capital reserve.

Question 5 : Nov 2018 – PAPER

Moon Ltd. acquires 75% of Star Limited on 1st April, 2017 for consideration transferred rs.60 lakh. Moon Limited intends to recognize the Non-Controlling Interest (NCI) at proportionate share of fair value of identifiable assets. With the assistance of a suitably qualified valuation professional, Moon Limited measures the identifiable net assets of Star Limited at Rs.90 lakh. Moon Limited performs a review and determines that the business combination did not include any transactions that should be accounted for separately from the business combination.

State whether the procedures followed by Moon Limited and the resulting measurements are appropriate or not. Also calculate the bargain purchase gain in the process.

Solution :

The amount of Star Ltd.'s identifiable net assets exceeds the fair value of the consideration transferred plus the fair value of the NCI in Star Ltd.'s, resulting in an initial indication of a gain on a bargain purchase. Accordingly, Moon Ltd. reviews the procedures it used to identify and measure the identifiable net assets acquired, to measure the fair value of both the NCI and the consideration transferred, and to identify transactions that were not part of the business combination.

Following that review, Moon Ltd. can conclude that the procedures followed and the resulting measurements were appropriate.

	Rs.
Identifiable net assets	90,00,000
Less: Consideration transferred	(60,00,000)
NCI (90,00,000 × 25%)	(22,50,000)
Gain on bargain purchase	7,50,000

Question 6 : May 2019 – RTP

How should contingent consideration payable in relation to a business combination be accounted for on initial recognition and at the subsequent measurement as per Ind AS in the following cases:

(i) On 1 April 2016, A Ltd. acquires 100% interest in B Ltd. As per the terms of agreement the purchase consideration is payable in the following 2 tranches:

a. an immediate issuance of 10 lakhs shares of A Ltd. having face value of INR 10 per share;

b. a further issuance of 2 lakhs shares after one year if the profit before interest and tax of B Ltd. for the first year following acquisition exceeds INR 1 crore.

i. The fair value of the shares of A Ltd. on the date of acquisition is INR 20 per share. Further, the management has estimated that on the date of acquisition, the fair value of contingent consideration is Rs.25 lakhs.

ii. During the year ended 31 March 2017, the profit before interest and tax of B Ltd. exceeded Rs.1 crore. As on 31 March 2017, the fair value of shares of A Ltd. is Rs.25 per share.

(ii) Continuing with the fact pattern in (a) above except for:

c. The number of shares to be issued after one year is not fixed.

d. Rather, A Ltd. agreed to issue variable number of shares having a fair value equal to Rs.40 lakhs after one year, if the profit before interest and tax for the first year following acquisition exceeds Rs.1 crore. A Ltd. issued shares with Rs.40 lakhs after a year.

Solution :

(i) In the given case the amount of purchase consideration to be recognized **<u>on initial recognition</u>** shall be as follows:

Fair value of shares issued (10,00,000 x Rs.20)	Rs.2,00,00,000
Fair value of contingent consideration	Rs.25,00,000
Total purchase consideration	Rs.2,25,00,000

<u>Subsequent measurement of contingent consideration payable for business combination</u>

In general, an equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Ind AS 32 describes an equity instrument as one that meets both of the following conditions:

(a) There is no contractual obligation to deliver cash or another financial asset to another party, or to exchange financial assets or financial liabilities with another party under potentially unfavorable conditions (for the issuer of the instrument).

(b) If the instrument will or may be settled in the issuer's own equity instruments, then it is:

(i) a non-derivative that comprises an obligation for the issuer to deliver a fixed number of its own equity instruments; or

(ii) a derivative that will be settled only by the issuer exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

In the given case, given that the acquirer has an obligation to issue fixed number of shares on fulfilment of the contingency, the contingent consideration will be classified as equity as per the requirements of Ind AS 32.

As per paragraph 58 of Ind AS 103, contingent consideration classified as equity should not be re-measured and its subsequent settlement should be accounted for within equity.

Here, the obligation to pay contingent consideration amounting to Rs.25,00,000 is recognized as a part of equity and therefore not re-measured subsequently or on issuance of shares.

(ii) The amount of purchase consideration to be recognized **<u>on initial recognition</u>** is shall be as follows:

Fair value shares issued (10,00,000 × Rs.20)	Rs.2,00,00,000
Fair value of contingent consideration	Rs.25,00,000
Total purchase consideration	Rs.2,25,00,000

<u>Subsequent measurement of contingent consideration payable for business combination</u>

The contingent consideration will be classified as liability as per Ind AS 32.

As per paragraph 58 of Ind AS 103, contingent consideration not classified as equity should be measured at fair value at each reporting date and changes in fair value should be recognized in profit or loss.

As at 31 March 2017, (being the date of settlement of contingent consideration), the liability would be measured at its fair value and the resulting loss of Rs.15,00,000 (Rs.40,00,000 – Rs.25,00,000) should be recognized in the profit or loss for the period. A Ltd. would recognize issuance of 160,000 (Rs.40,00,000/25) shares at a premium of Rs.15 per share.

Question 7 : Nov 2019 – RTP

H Ltd. acquired equity shares of S Ltd., a listed company, in two tranches as mentioned in the below table:

Date	Equity stake purchased	Remarks
1st November, 20X6	15%	The shares were purchased based on the quoted price on the stock exchange on the relevant dates.
1st January, 20X7	45%	

Both the above-mentioned companies have Rupees as their functional currency. Consequently, H Ltd. acquired control over S Ltd. on 1st January, 20X7. Following is the Balance Sheet of S Ltd. as on that date:

	(Rs.in crore)	(Rs.in crore)
ASSETS:		
Non-current assets		
(a) Property, plant and equipment	40.0	90.0
(b) Intangible assets	20.0	30.0
(c) Financial assets		
- Investments	100.0	350.0
Current assets		
(a) Inventories		
(b) Financial assets	20.0	20.0
- Trade receivables		
- Cash held in functional	20.0	20.0
Currency	4.0	4.5
(c) Other current assets		
Non-current asset held for sale	4.0	4.5
TOTAL ASSETS	208	
EQUITY AND LIABILITIES:		
Equity		
(a) Share capital (face value Rs.100)	12.0	50.4
(b) Other equity	141.0	Not applicable
Non-current liabilities		
(a) Financial liabilities		
- Borrowings	20.0	20.0
Current liabilities		
(a) Financial liabilities		
- Trade payables	28.0	28.0
(b) Provision for warranties	3.0	3.0
(c) Current tax liabilities	4.0	4.0
TOTAL EQUITY AND LIABILITIES	208.0	

Other information :

Property, plant and equipment in the above Balance Sheet include leasehold motor vehicles having carrying value of Rs.1 crore and fair value of Rs.1.2 crore. The date of inception of the lease was 1st April, 20X0. On the inception of the lease, S Ltd. had correctly classified the lease as a finance lease. However, if facts and circumstances as on 1st April, 20X7 are considered, the lease would be classified as an operating lease.

Following is the statement of contingent liabilities of S Ltd. as on 1st January, 20X7:

Particulars	Fair value (Rs. in crore)	Remarks
Law suit filed by a customer for a claim of Rs.2 crore	0.5	It is not probable that an outflow of resources embodying economic benefits will be

		required to settle the claim. Any amount which would be paid in respect of law suit will be tax deductible.
Income tax demand of Rs.7 crore raised by tax authorities; S Ltd. has challenged the demand in the court.	2.0	It is not probable that an outflow of resources embodying economic benefits will be required to settle the claim.

In relation to the above-mentioned contingent liabilities, S Ltd. has given an indemnification undertaking to H Ltd. up to a maximum of Rs.1 crore.

Rs.1 crore represents the acquisition date fair value of the indemnification undertaking.

Any amount which would be received in respect of the above undertaking shall not be taxable.

The tax bases of the assets and liabilities of S Ltd. is equal to their respective carrying values being recognised in its Balance Sheet.

Carrying value of non-current asset held for sale of Rs.4 crore represents its fair value less cost to sell in accordance with the relevant Ind AS.

In consideration of the additional stake purchased by H Ltd. on 1st January, 20X7, it has issued to the selling shareholders of S Ltd. 1 equity share of H Ltd. for every 2 shares held in S Ltd. Fair value of equity shares of H Ltd. as on 1st January, 20X7 is Rs.10,000 per share.

On 1st January, 20X7, H Ltd. has paid Rs.50 crore in cash to the selling shareholders of S Ltd. Additionally, on 31st March, 20X9, H Ltd. will pay Rs.30 crore to the selling shareholders of S Ltd. if return on equity of S Ltd. for the year ended 31st March, 20X9 is more than 25% per annum. H Ltd. has estimated the fair value of this obligation as on 1st January, 20X7 and 31st March, 20X7 as Rs.22 crore and Rs.23 crore respectively. The change in fair value of the obligation is attributable to the change in facts and circumstances after the acquisition date.

Quoted price of equity shares of S Ltd. as on various dates is as follows:

As on November, 20X6 Rs.350 per share
As on 1st January, 20X7 Rs.395 per share
As on 31st March, 20X7 Rs.420 per share

On 31st May, 20X7, H Ltd. learned that certain customer relationships existing as on 1st January, 20X7, which met the recognition criteria of an intangible asset as on that date, were not considered during the accounting of business combination for the year ended 31st March, 20X7. The fair value of such customer relationships as on 1st January, 20X7 was Rs.3.5 crore (assume that there are no temporary differences associated with customer relations; consequently, there is no impact of income taxes on customer relations).

On 31st May, 20X7 itself, H Ltd. further learned that due to additional customer relationships being developed during the period 1st January, 20X7 to 31st March, 20X7, the fair value of such customer relationships has increased to Rs.4 crore as on 31st March, 20X7.

On 31st December, 20X7, H Ltd. has established that it has obtained all the information necessary for the accounting of the business combination and that more information is not obtainable.

H Ltd. and S Ltd. are not related parties and follow Ind AS for financial reporting. Income tax rate applicable is 30%.

You are required to provide your detailed responses to the following, along with reasoning and computation notes:

(a) What should be the goodwill or bargain purchase gain to be recognised by H Ltd. in its financial statements for the year ended 31st March, 20X7. For this purpose, measure non-controlling interest using proportionate share of the fair value of the identifiable net assets of S Ltd.

(b) Will the amount of non-controlling interest, goodwill, or bargain purchase gain so recognised in (a) above change subsequent to 31st March, 20X7? If yes, provide relevant journal entries.

(c) What should be the accounting treatment of the contingent consideration as on 31st March, 20X7?

Solution :

(i) As an only exception to the principle of classification or designation of assets as they exist at the acquisition date is that for lease contract and insurance contracts classification which will be based on the basis of the conditions existing at inception and not on acquisition date.

Therefore, H Ltd. would be required to retain the original lease classification of the lease arrangements and thereby recognise the lease arrangements as finance lease.

(ii) The requirements in Ind AS 37 'Provisions, Contingent Liabilities and Contingent Assets', do not apply in determining which contingent liabilities to recognise as of the acquisition date as per Ind AS 103 'Business Combination'. Instead, the acquirer shall recognise as of the acquisition date a contingent liability assumed in a business combination if it is a present obligation that arises from past events and its fair value can be measured reliably. Therefore, contrary to Ind AS 37, the acquirer recognises a contingent liability assumed in a business combination at the acquisition date even if it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation. Hence H Ltd. will recognize contingent liability of Rs.2.5 cr.

Since S Ltd. has indemnified for Rs.1 cr., H Ltd. shall recognise an indemnification asset at the same time for Rs.1 cr.

As per the information given in the question, this indemnified asset is not taxable. Hence, its tax base will be equal to its carrying amount. No deferred tax will arise on it.

(iii) As per Ind AS 103, non-current assets held for sale should be measured at fair value less cost to sell in accordance with Ind AS 105 'Non-current Assets Held for Sale and Discontinued Operations'. Therefore, its carrying value as per balance sheet has been considered in the calculation of net assets.

(iv) Any equity interest in S Ltd. held by H Ltd. immediately before obtaining control over S Ltd. is adjusted to acquisition-date fair value. Any resulting gain or loss is recognised in the profit or loss of H Ltd.

Calculation of purchase consideration as per Ind AS 103

Rs. in lakh

Investment in S Ltd.			
On 1st Nov. 20X6	15%	[(12/100) × 395 × 15%]	7.11

On 1st Jan. 20X7	45%		
Own equity given		10,000 × 12% × 45% × ½	270
Cash			50
Contingent consideration			22
			349.11

(v) Calculation of deferred tax on assets and liabilities acquired as part of the business combination, including current tax and goodwill.

Item	**Rs. in crore**				
	Book value	**Fair value**	**Tax base**	**Taxable (deductible) temporary difference**	**Deferred tax assets (liability) @ 30%**
Property, plant and equipment	40	90	40	50	(15)
Intangible assets	20	30	20	10	(3)
Investments	100	350	100	250	(75)
Inventories	20	20	20	-	-
Trade receivables	20	20	20	-	-
Cash held in functional currency	4	4	4	-	-
Non-current asset held for sale	4	4	4	-	-
Indemnified asset	-	1	1	-	-
Borrowings	20	20	20	-	-
Trade payables	28	28	28	-	-
Provision for warranties	3	3	3	-	-
Current tax liabilities	4	4	4	-	-
Contingent liability		0.5	-	(0.5)	0.15
Deferred tax Liability					(92.85)

(vi) Calculation of identifiable net assets acquired

	Rs.in crore	**Rs.in crore**
Property, plant and equipment	90	519
Intangible assets	30	-150.35
Investments	350	368.65
Inventories	20	
Trade receivables	20	
Cash held in functional currency	4	
Non-current asset held for sale	4	

Indemnified asset	1	
Total asset		519
Less: Borrowings	20	
Trade payables	28	
Provision for warranties	3	
Current tax liabilities	4	
Contingent liability (2 + 0.5)	2.50	
Deferred tax liability (W.N.2)	92.85	(150.35)
Net identifiable assets		368.65

(a) Calculation of NCI by proportionate share of net assets

Net identifiable assets of S Ltd. on 1.1.20X7 (Refer W.N.3) = 372.85 crore

NCI on 1.1.20X7 = 368.65 crore × 40% = 147.46 crore

Calculation of Goodwill as per Ind AS 103

Goodwill on 1.1.20X7 = Purchase consideration + NCI – Net assets

= 349.11 + 147.46 – 368.65

= 127.92 crore

(b) As per para 45 of Ind AS 103 'Business Combination', if the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the acquirer shall report in its financial statements provisional amounts for the items for which the accounting is incomplete.

During the measurement period, the acquirer shall retrospectively adjust the provisional amounts recognised at the acquisition date to reflect new information obtained about facts and circumstances that existed as of the acquisition date and, if known, would have affected the measurement of the amounts recognised as of that date.

During the measurement period, the acquirer shall also recognise additional assets or liabilities if new information is obtained about facts and circumstances that existed as of the acquisition date and, if known, would have resulted in the recognition of those assets and liabilities as of that date.

The measurement period ends as soon as the acquirer receives the information it was seeking about facts and circumstances that existed as of the acquisition date or learns that more information is not obtainable. However, the measurement period shall not exceed one year from the acquisition date.

Further, as per para 46 of Ind AS 103, the measurement period is the period after the acquisition date during which the acquirer may adjust the provisional amounts recognised for a business combination. The measurement period provides the acquirer with a reasonable time to obtain the information necessary to identify and measure the following as of the acquisition date in accordance with the requirements of this Ind AS:

(a) the identifiable assets acquired, liabilities assumed and any non-controlling interest in the acquiree;

(b) …..
(c) ……; and
(d) the resulting goodwill or gain on a bargain purchase.

Para 48 states that the acquirer recognises an increase (decrease) in the provisional amount recognised for an identifiable asset (liability) by means of a decrease (increase) in goodwill.

Para 49 states that during the measurement period, the acquirer shall recognise adjustments to the provisional amounts as if the accounting for the business combination had been completed at the acquisition date.

Para 50 states that after the measurement period ends, the acquirer shall revise the accounting for a business combination only to correct an error in accordance with Ind AS 8 'Accounting Policies, Changes in Accounting Estimates and Errors'.

On 31st December, 20X7, H Ltd. has established that it has obtained all the information necessary for the accounting of the business combination and the more information is not obtainable. Therefore, the measurement period for acquisition of S Ltd. ends on 31st December, 20X7.

On 31st May, 20X7 (i.e. within the measurement period), H Ltd. learned that certain customer relationships existing as on 1st January, 20X7 which met the recognition criteria of an intangible asset as on that date were not considered during the accounting of business combination for the year ended 31st March, 20X7. Therefore, H Ltd. shall account for the acquisition date fair value of customer relations existing on 1st January, 20X7 as an identifiable intangible asset. The corresponding adjustment shall be made in the amount of goodwill.

Accordingly, the amount of goodwill will be changed due to identification of new asset from retrospective date for changes in fair value of assets and liabilities earlier recognised on provisional amount (subject to meeting the condition above for measurement period). NCI changes would impact the consolidated retained earnings (parent's share). Also NCI will be increased or decreased based on the profit during the post-acquisition period.

Journal entry

Customer relationship	Dr.	3.5 crore	
To NCI			1.4 crore
To Goodwill			2.1 crore

However, the increase in the value of customer relations after the acquisition date shall not be accounted by H Ltd., as the customer relations developed after 1st January, 20X7 represents internally generated intangible assets which are not eligible for recognition on the balance sheet.

(c) Since the contingent considerations payable by H Ltd is not classified as equity and is within the scope of Ind AS 109 'Financial Instruments', the changes in the fair value shall be recognised in profit or loss. Change in Fair value of contingent consideration (23-22) Rs.1 crore will be recognized in the Statement of Profit and Loss.

Question 8 : Nov 2019 – PAPER

The Balance sheet of David Ltd. and Parker ltd as on 31st march, 2019 is given below :

(Rs. in lakhs)

Assets	David Ltd.	Parker Ltd.
Non-Current Assets :		
Property, plant and equipment	400	600
Investment	300	200
Current assets :		
Inventories	300	100
Financial Assets		
Traders receivables	400	200
Cash and cash equivalent	150	200
Others	300	300
Total	**1,850**	**1,600**
Equity and Liabilities		
Equity		
Share capital-Equity shares of Rs.100 each for Parker Ltd & Rs.10 each for David Limited	500	400
Other Equity	700	275
Non-Current liabilities :		
Long term borrowings	200	300
Long term provisions	100	80
Deferred Tax	20	55
Current Liabilities :		
Short term borrowings	130	170
Trade payables	200	320
Total	**1,820**	**1,600**

Other information :

(i) David Ltd. acquired 70% shares of Parker Ltd. on 1st April, 2019 by issuing its own shares in the ratio of 1 share of David Ltd. for every 2 shares of Parker Ltd. The fair value of the shares of David Ltd. was Rs.50 per share.

(ii) The fair value exercise resulted in the following :

(1) Fair value of property, plant and equipment (PPE) on 1st April, 2019 was Rs.450 lakhs.

(2) David Ltd. agreed to pay an additional payment as consideration that is higher of Rs.30 lakh and 25% of any excess profits in the first year after acquisition, over its profits in the preceding 12 months made by Parker Ltd. This additional amount will be due after 3 years. Parker Ltd. has earned Rs.20 lakh profit in the preceding year and expects to earn another Rs.10 Lakh.

(3) In addition to above, David Ltd. also has agreed to pay one of the founder shareholder-Director a payment of Rs.25 lakhs provided he says with the Company for two years after the acquisition.

(4) Parker Ltd. had certain equity settled share-based payment award (original award) which got replaced by the new awards issued by David Ltd. As per the original term the vesting period was 4 years and as of the acquisition date the employees of Parker Ltd. have already served 2 years of service. As per the replaced awards, the vesting period has been reduced to one year (one year from the acquisition date). The fair value of the award on the acquisition date was as follows

Original award – Rs.6 lakhs

Replacement award – Rs.9 lakhs

(5) Parker Ltd. had a lawsuit pending with a customer who had made a claim of Rs.35 lakhs. Management reliably estimated the fair value of the liability to be Rs.10 lakhs

(6) The applicable tax rate for both entities is 40%.

You are required to prepare opening consolidated balance sheet of David Ltd. as on 1st April, 2019 along with workings. Assume discount rate of 8%.

Solution :

1) Calculation of purchase consideration

(a) Issue of shares

1 share for 2 shares held

No. of share of Parker	4 lakh
% Acquisition	70%
No. of share acquired	2.8 lakh
No. of share to be issued	1.4 lakh
Issue price	50
Consideration	70 lakhs

(b) Contingent consideration = $\frac{30}{(1.08)^3}$ = 23.81 lakhs

(c) Replacement Award

Step1 : Fair value of original award = 6 lakh

Step 2 : Fair value replacement award = 9 lakh

Step 3 : Pre combination obligation = $\frac{6}{4} \times 2$ = 3 lakh

Step 4 : Post combination cost = 9 – 3 = 6 lakh

Note : Pre combination obligation = 3 lakh is paid off

Post combination cost = 6 lakh

Total : PC = A + B + C = 70 + 23.8 + 3 = 96.81 lakhs

2) Calculation of goodwill / gain from Bargain purchase

(a) Calculation of Net Assets

Assets	: Property, Plant & Equipment	450
	Investments	200
	Inventories	100

	Trade Receivable	200	
	Cash & Cash Equivalent	200	
	Other CA	300	1,450
Liabilities	: Long term Borrowings	300	
	Long term Provisions	80	
	Deferred tax	55	
	Short term Borrowings	170	
	Trade Payables	320	
	Contingent liability	10	935
			515
DTA	: Assets = 600 – 450 = 150		
	Liability = 10 – Nil = 10		
	$160 \times 40\%$		64
Net Assets			579

(b)

Consideration paid	96.81
+ NCI (AT Prop. Share) ($579 \times 30\%$)	173.7
	270.51
– Fair Value of Net Assets	579
Capital Reserve	308.49

Note : Amount payable to Director Should be booked as on Expense

3) Consolidated balance sheet of David Ltd.

Assets

1)	Non Current Assets	
	Property, Plant & Equipment	850
	Investments	500
2)	Current Assets	
	Inventory	400
	FA	
	Trade Receivable	600
	Cash & Cash Equivalent	350
	Other CA	600
		3,300
	Equity & Liability	
1)	Equity	
	Share Capital	514
	Other Equity (700 + 308.49 + 56 3)	1067.49
	Non Controlling Interest	173.70
2)	Non Current Liability	
	Long term Borrowing	500
	Long term provisions (100 + 80 + 23.81)	203.81
	Deffered tax (20 + 55.64)	11

3)	Current Liability	
	Financial liability	
	Short term Borrowings	300
	Trade payable	520
	Provisions for Law suit damage	10
		3300

Question 9 : Nov 2020 – RTP

Veera Limited and Zeera Limited are both in the business of manufacturing and selling of Lubricant. Veera Limited and Zeera Limited shareholders agree to join forces to benefit from lower delivery and distribution costs. The business combination is carried out by setting up a new entity called Meera Limited that issues 100 shares to Veera Limited's shareholders and 50 shares to Zeera Limited's shareholders in exchange for the transfer of the shares in those entities. The number of shares reflects the relative fair values of the entities before the combination. Also respective company's shareholders gets the voting rights in Meera Limited based on their respective shareholding.

Determine the acquirer by applying the principles of Ind AS 103 'Business Combinations'.

Solution :

As per IND AS 103 acquirer is

– Usually which issues equity
– Entity which gets longer voting rights
– Entity which has control over management
– Entity which is larger in size etc.

Based on information given in question entity Veera Ltd. is issued 100 shares of total of 150 shares i.e. 100/150 = 66.67% which represents total voting right and ∴ Entity Veera is acquirer.

Question 10 : Nov 2020 – Paper

P Limited and S Limited are in business of manufacturing garments. P Limited holds 30% of equity shares of S Limited for last several years. P Limited obtains control of S Limited when it acquires further 65% stake of S Limited's shares, thereby resulting in a total holding of 95% on 31 December 2019. The acquisition had the following features:

(i) P Limited transfers cash of Rs. 50,00,000 and issues 90,000 shares on 31 December 2019. The market price of P Limited's shares on the date of issue was Rs. 10 per share. The equity shares issued as per this transaction will comprise 5% of the post-acquisition capital of P Limited.

(ii) P Limited agrees to pay additional consideration of Rs. 4,00,000, if the cumulative profits of S Limited exceeds Rs. 40,00,000 over the next two years. At the acquisition date, it is not considered probable that extra consideration will be paid. The fair value of contingent consideration is determined to be Rs. 2,00,000 at the acquisition date.

(iii) P Limited spent acquisition-related costs of Rs. 2,00,000.

(iv) The fair value of the NCI is determined to be Rs. 5,00,000 at the acquisition date based on market price. P Limited decided to measure non-controlling interest at fair value for this transaction.

(v) P Limited has owned 30% of the shares in S Limited for several years. At 31 December 20.19, the investment is included in P Limited's consolidated balance sheet at Rs. 8,00,000. The fair value of previous holdings accounted for using the equity method is arrived at Rs. 18,00,000.

The fair value of S Limited's net identifiable assets at 31 December 2019 is Rs. 45,00,000, determined in accordance with Ind AS 103.

Analyze the transaction and determine the accounting under acquisition method for the business combination by P Limited.

Solution :

Identify the acquirer

In this case, P Limited has paid cash consideration to shareholders of S Limited. Further, the shares issued to S Limited pursuant to the acquisition do not transfer control of P Limited to erstwhile shareholders of S Limited. Therefore, P Limited is the acquirer and S Limited is the acquiree.

Determine acquisition date

As the control over the business of S Limited is transferred to P Limited on 31 December 2019, that date is considered as the acquisition date.

Determine the purchase consideration

The purchase consideration in this case will comprise of the following:

Cash consideration	Rs. 50,00,000
Equity shares issued (90,000 x 10 i.e., at fair value)	Rs. 9,00,000
Contingent consideration (at fair value)	Rs. 2,00,000
Fair value of previously held interest	Rs. 18,00,000
Total purchase consideration	Rs. 79,00,000

Acquisition cost incurred by and on behalf of P Limited for acquisition of S Limited should be recognised in the Statement of Profit and Loss. As such, an amount of Rs. 2,00,000 should be recognised in the Statement of Profit and Loss.

Fair value of identifiable assets and liabilities

The fair value of identifiable net assets (as given in the question) Rs. 45,00,000.

Non-Controlling Interest

The management has decided to recognise NCI at its fair value, which is given in the question as Rs. 5,00,000.

Re-measure previously held interests in case business combination is achieved in stages

In this case, the control has been acquired in stages i.e., before acquisition to control, P Limited exercised significant influence over S Limited. As such, the previously held interest should be measured at fair value and the difference between the fair value and the carrying amount as at the acquisition date should be recognised in the Statement of Profit and Loss. As such, an amount of Rs. 10,00,000 (i.e. 18,00,000 – 8,00,000) will be recognised in the Statement of Profit and Loss.

Determination of goodwill or gain on bargain purchase

Goodwill should be calculated as follows: **(Rs.)**

Total consideration	79,00,000
Recognised amount of any non-controlling interest	5,00,000
Less: Fair value of net identifiable assets	(45,00,000)
Goodwill	39,00,000

Question 11 : Jan 2021 – Paper

On 1st April 2017, Kara Ltd. granted an award of 150 share options to each of its 1,000 employees, on condition of continuous employment with Kara Ltd. for three years and the benefits will then be settled in cash of an equivalent amount of share price. Fair value of each option on the grant date was Rs. 129.

Towards the end of 31st March 2018, Kara Ltd.'s share price dropped; so on 1st April 2018 management chose to reduce the exercise price of the options.

At the date of the re-pricing, the fair value of each of the original share options granted was Rs. 50 and the fair value of each re-priced option was Rs. 80. Thus, the incremental fair value of each modified option was Rs. 30.

At the date of the award, management estimated that 10% of employees would leave the entity before the end of three years (i.e., 900 awards would vest). During financial year 2018-2019, it became apparent that fewer employees than expected were leaving, so management revised its estimate of the number of leavers to only 5% (i.e. 950 awards would vest). At the end of 31st March 2020, awards to 930 employees actually vested.

Determine the expense for each year and pass appropriate journal entries as per the relevant Ind AS.

Solution :

Note: The first para of the question states that "benefits will then be settled in cash of an equivalent amount of share price." This implies that the award is cash settled share-based payment. However, the second and third para talks about repricing of the option which arises in case of equity settled share-based payment.

Hence, two alternative solutions have been provided based on the information taking certain assumptions.

1st Alternative based on the assumption that the award is cash settled share-based payment.

In such a situation, the services received against share-based payment plan to be settled in cash are measured at fair value of the liability and the liability continues to be remeasured at every reporting date until it is actually paid off.

There is a vesting condition attached to the share-based payment plans i.e. to remain in service for next 3 years. The recognition of such share-based payment plans should be done by recognizing fair value of the liability at the time of services received and not at the date of grant. The liability so recognized will be fair valued at each reporting date and difference in fair value will be charged to profit or loss for the period.

Calculation of expenses:

<u>For the year ended 31st March 2018</u>

= Rs.50 x 150 awards x 900 employees x (1 year /3 years of service)
= Rs.22,50,000

For the year ended 31st March 2019

Note: It is assumed that the fair value of Rs.80 each of repriced option continues at the end of the remaining reporting period ie 31st March, 2019 and 31st March, 2020
= [Rs.80 x 150 awards x 950 employees x (2 year / 3 years of service)] - Rs.22,50,000
= Rs.7,60,00,000 – Rs.22,50,000 = Rs.53,50,000

For the year ended 31st March 2020

= [Rs.80 x 150 awards x 930 employees] - Rs.22,50,000 - Rs.53,50,000
= Rs.1,11,60,000 – Rs.22,50,000 - Rs.53,50,000= Rs.35,60,000

Journal Entries

31st March, 2018			
Employee benefits expenses To Share based payment liability (Fair value of the liability recognized)	Dr.	22,50,000	22,50,000
31st March, 2019			
Employee benefits expenses To Share based payment liability (Fair value of the liability re-measured)	Dr.	53,50,000	53,50,000
31st March, 2020			
Employee benefits expenses To Share based payment liability (Fair value of the liability recognized)	Dr.	35,60,000	35,60,000
Share based payment liability To Bank (Being liability for awards settled in cash)	Dr.	1,11,60,000	1,11,60,000

2nd Alternative based on fair value at the grant date (ignoring the fact that the award has to be settled in cash).

Calculation of expenses:

For the year ended 31st March 2018

= [Rs.129 x 150 awards x 900 employees x (1 year /3 years of service)]
= Rs.58,05,000

For the year ended 31st March 2019

Ind AS 102 requires the entity to recognise the effects of repricing that increase the total fair value of the share-based payment arrangement or are otherwise beneficial to the employee.

If the repricing increases the fair value of the equity instruments granted standard requires the entity to include the incremental fair value granted (ie the difference between the fair value of the repriced equity instrument and that of the original equity instrument, both estimated as at the date of the modification) in the measurement of the amount recognised for services received as consideration for the equity instruments granted.

If the repricing occurs during the vesting period, the incremental fair value granted is included in the measurement of the amount recognised for services received over the period from the repricing date until the date when the repriced equity instruments vest, in addition to the amount based on the grant date fair value of the original equity instruments, which is recognised over the remainder of the original vesting period. Accordingly, the amounts recognised are as follows:

Year ended	Calculation	Compensation expense for period Rs.	Cumulative compensation expense Rs.
31-Mar-18	[Rs.129 x 150 awards x 900 employees x (1 year /3 years of service)]	58,05,000	58,05,000
31-Mar-19	[Rs.129 x 150 awards x 950 employees x (2 year /3 years of service)] + (80-50) x 150 awards x 950 employees x (1 year / 2 years of service) - 58,05,000	85,87,500	1,43,92,500
31-Mar-20	[(Rs.129 + 30) x 150 awards x 930 employees] - 1,43,92,500	77,88,000	2,21,80,500

Journal Entries

31st March, 2018			
Employee benefits expenses To Outstanding Share based payment option (Fair value of the liability recognized)	Dr.	58,05,000	58,05,000
31st March, 2019			
Employee benefits expenses To Outstanding Share based payment option (Fair value of the liability re-measured)	Dr.	85,87,500	85,87,500
31st March, 2020			
Employee benefits expenses To Outstanding Share based payment option (Fair value of the liability recognized)	Dr.	77,88,000	77,88,000
Outstanding Share based payment option To Equity share capital (Being award settled)	Dr.	2,21,80,500	2,21,80,500

Question 12 : May 2021 – RTP

Bima Ltd. acquired 65% of shares on 1 June, 20X1 in Nafa Ltd. which is engaged in production of components of machinery. Nafa Ltd. has 1,00,000 equity shares of Rs. 10 each. The quoted market price of shares of Nafa Ltd. was Rs. 12 on the date of acquisition. The fair value of Nafa Ltd.'s identifiable net assets as on 1 June, 20X1 was Rs. 80,00,000.

Bima Ltd. wired Rs. 50,00,000 in cash and issued 50,000 equity shares as purchase consideration on the date of acquisition. The quoted market price of shares of Bima Ltd. on the date of issue was Rs. 25 per share.

Bima Ltd. also agrees to pay additional consideration of Rs. 15,00,000, if the cumulative profit earned by Nafa Ltd. exceeds Rs. 1 crore over the next three years. On the date of acquisition, Nafa Ltd. assessed and determined that it is considered probable that the extra consideration will be paid. The fair value of this consideration on the date of acquisition is Rs. 9,80,000. Nafa Ltd. incurred Rs. 1,50,000 in relation to the acquisition. It measures Non-controlling interest at fair value.

How will the acquisition of Nafa Ltd. be accounted by Bima Ltd., under Ind AS 103? Prepare detailed workings and pass the necessary journal entry.

Solution :

Computation of Goodwill / Capital reserve on consolidation as per Ind AS 103

Particulars	**Rs.**
Cost of investment:	
Share exchange (50,000 x 25)	12,50,000
Cash consideration	50,00,000
Contingent consideration	9,80,000
Consideration transferred at date of acquisition [A]	72,30,000
Fair value of non-controlling interest at date of acquisition [B] (1,00,000 x 35% x 12)	4,20,000
Total [C] = [A] + [B]	76,50,000
Net assets acquired at date of acquisition [D]	(80,00,000)
Capital Reserve [D] – [C]	3,50,000

In a business combination, acquisition-related costs (including stamp duty) are expensed in the period in which such costs are incurred and are not included as part of the consideration transferred. Therefore, Rs.1,50,000 incurred by Nafa Ltd. in relation to acquisition, will be ignored by Bima Ltd.

Journal entry at the date of acquisition by Bima Limited as per Ind AS 103:

		Rs.	**Rs.**
Identifiable net assets	Dr.	80,00,000	
To Equity share capital (50,000 x 10)			5,00,000
To Securities Premium (50,000 x 15)			7,50,000
To Cash			50,00,000
To Provision for contingent consideration to Nafa Ltd.			9,80,000
To Non-controlling Interest			4,20,000
To Capital Reserve			3,50,000

Question 13 : July 2021 – Paper

As part of its business expansion strategy, UG Limited is in process of setting up a health care intermediates business. The process is at very initial stage. Towards this, UG Limited acquired on 1st April 2020, 100% ordinary shares of AG Limited. AG Limited manufactures health care intermediates. The purchase consideration of AG Limited was b way of a share exchange valued at Rs.1,750 lakhs. The fair value of AG Limited's net assets was Rs.750 lakhs, but this fair value does not include :

- A patent owned by AG Limited manufactures health care intermediate drug that has a remaining life of 10 years. A consultant has estimated the value of this patent at Rs.500 lakhs. However, the outcome of clinical trials for the same is awaited. If the trials are successful, the value of the drug would fetch estimated Rs.750 lakhs.
- AG Limited has developed and patented a new vaccine which has been approved for clinical use. The cot of developing the vaccine was Rs.600 lakhs. Based on an early assessment of its sales success; its market value has been estimated at Rs.1,000 lakhs by a valuer.

  UG Limited has requested you to suggest the accounting treatment of the above transaction under applicable Ind As.

Solution :

Recognition Principle as per Ind AS:

As per para 13 of Ind AS 103 'Business Combinations', the acquirer's application of the recognition principle and conditions may result in recognising some assets and liabilities that the acquiree had not previously recognised as assets and liabilities in its financial statements. This may be the case when the asset is developed by the entity internally and charged the related costs to expense.

Accounting Treatment:

Based on the above, the company can recognise following Intangible assets while determining Goodwill / Bargain Purchase for the transaction:

(i) **Patent owned by AG Limited:** The patent owned will be recognised at fair value by UG Limited even though it was not recognised by AG Limited in its financial statements. The patent will be amortised over the remaining useful life of the asset i.e. 10 years. Since the company is awaiting the outcome of the trials, the value of the patent cannot be estimated at Rs. 750 lakh and the extra Rs. 250 lakh should only be disclosed as a Contingent Asset and not recognised.

(ii) **Patent internally developed by AG Limited:** As per para 18 of Ind AS 103 'Business Combinations', the acquirer shall measure the identifiable assets acquired and the liabilities assumed at their acquisition date fair values. Since the patent developed has been approved for clinical use, it is an identifiable asset, hence the same will be measured at fair value i.e. Rs. 1,000 lakh on the acquisition date.

Hence the revised working would be as follows:

	Rs.
Fair value of net assets of AG Limited	750 lakh

Add: Patent (500 lakh + 1,000 lakh)	1,500 lakh
	2,250 lakh
Purchase consideration	(1,750 lakh)
Gain on bargain purchase	500 lakh

Question 14 : Nov 2021 – RTP

Company X is engaged in the business of exploration & development of Oil & Gas Blocks.

Company X currently holds participating interest (PI) in below mentioned producing Block as follows :

Block Name	Company X	Company Y	Company Z	Total
AWM/01	30%	60%	10%	100%

For the above Block, Company X, Y & Z has entered into unincorporated Joint Venture.

Company Y is the Operator of the Block AWM/01. Company X & Company Z are the Joint Operators. Company Y incurs all the expenditure on behalf of Joint Venture and raise cash call to Company X & Company Z at each month end in respect of their share of expenditure incurred in Joint Venture. All the manpower and requisite facilities / machineries owned by the Joint venture and thereby owned by all the Joint Operators.

For past few months, due to liquidity issues, Company Z defaulted in payment of cash calls to operators. Therefore, company Y (Operator) has issued notice to company Z for withdrawal of their participating right from on 01.04.20X1. However, company Z has filed the appeal with arbitrator on 30.04.20X1.

Financial performance of company Z has not been improved in subsequent months and therefore company Z has decided to withdraw participating interest rights from Block AWM/01 and entered into sale agreement with Company X & Company Y. As per the terms of the agreement, dated 31.5.20X1, Company X will receive 33.33% share & Company Y will receive 66.67% share of PI rights owned by Company Z.

Company X is required to pay Rs.1 Lacs against 33.33% share of PI rights owned by Company Z.

After signing of sale agreement, Operator (company Y) approach government of India for modification in PSC (Production Sharing Contract) i.e. removal of Company Z from PSC of AWM/01 and government has approved this transaction on 30.6.20X1. Government approval for the modification in PSC is essential given the industry in which the joint-operators operate.

Balance sheet of Company X & Company Z are as follows:

Particulars	**Company X**		**Company Z**	
	31.5.20X1 Rs.	**30.6.20X1 Rs.**	**31.5.20X1 Rs.**	**30.6.20X1 Rs.**
Assets				
Non-Current Assets				
Property, Plant & Equipment	5,00,000	10,00,000	1,50,000	3,00,000
Right of Use Asset	1,00,000	2,00,000	10,000	20,000
Development CWIP	50,000	1,00,000	50,000	1,00,000
Financial Assets				

Loan receivable	25,000	50,000	25,000	50,000
Total Non-Current Assets	**6,75,000**	**13,50,000**	**2,35,000**	**4,70,000**
Current assets				
Inventories	1,00,000	2,00,000	15,000	30,000
Financial Assets				
Trade receivables	1,50,000	3,00,000	50,000	1,00,000
Cash and cash equivalents	2,00,000	4,00,000	1,00,000	2,00,000
Other Current Assets	2,25,000	50,000	25,000	50,000
Total Current Assets	**6,75,000**	**9,50,000**	**1,90,000**	**3,80,000**
Total Assets	**13,50,000**	**23,00,000**	**4,25,000**	**8,50,000**
Equity and Liabilities				
Equity				
Equity share capital	3,00,000	3,00,000	1,00,000	1,00,000
Other equity	2,00,000	3,00,000	75,000	2,50,000
Total Equity	**5,00,000**	**6,00,000**	**1,75,000**	**3,50,000**
Liabilities				
Non-Current Liabilities				
Provisions	4,00,000	8,00,000	1,00,000	2,00,000
Other Liabilities	1,50,000	3,00,000	50,000	1,00,000
Total Non-Current Liabilities	**5,50,000**	**11,00,000**	**1,50,000**	**3,00,000**
Current Liabilities				
Financial Liabilities				
Trade Payables	3,00,000	6,00,000	1,00,000	2,00,000
Total Current Liabilities	**3,00,000**	**6,00,000**	**1,00,000**	**2,00,000**
Total Liabilities	**13,50,000**	**23,00,000**	**4,25,000**	**8,50,000**

Additional Information:

1. Fair Value of PPE & Development CWIP owned by Company Z as per Market participant approach is Rs. 5,00,000 & Rs. 2,00,000 respectively.
2. Fair Value of all the other assets and liabilities acquired are assumed to be at their carrying values (except cash & cash equivalents). Cash and cash equivalents of Company Z are not to be acquired by Company X as per the terms of agreement.
3. Tax rate is assumed to be 30%.
4. As per Ind AS 28, all the joint operators are joint ventures whereby each parties that have joint control of the arrangement have rights to the net assets of the arrangement and therefore every operator records their share of assets and liabilities in their books.

You need to determine the following:

1. Whether the above acquisition falls under business or asset acquisition as defined under business combination standard Ind AS 103?
2. Determine the acquisition date in the above transaction.
3. Prepare Journal entries for the above-mentioned transaction.

4. Draft the Balance Sheet for Company X based on your analysis in Part 1 above as at acquisition date.

Solution :

(1) Ind AS 103 defines business as an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing goods or services to customers, generating investment income (such as dividends or interest) or generating other income from ordinary activities.

For a transaction to meet the definition of a business combination (and for the acquisition method of accounting to apply), the entity must gain control of an integrated set of assets and activities that is more than a collection of assets or a combination of assets and liabilities.

To be capable of being conducted and managed for the purpose identified in the definition of a business, an integrated set of activities and assets requires two essential elements—inputs and processes applied to those inputs.

Therefore, an integrated set of activities and assets must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output.

In the aforesaid transaction, Company X acquired share of participating rights owned by Company Z for the producing Block (AWM/01). The output exist in this transaction (Considering AWM/01) is a producing block. Also all the manpower and requisite facilities / machineries are owned by Joint venture and thereby all the Joint

Operators. Hence, acquiring participating rights tantamount to acquire inputs (Expertise Manpower & Machinery) and it is critical to the ability to continue producing outputs. Thus, the said acquisition will fall under the Business Acquisition and hence standard Ind AS 103 is to be applied for the same.

(2) As per paragraph 8 of Ind AS 103, acquisition date is the date on which the acquirer obtains control of the acquiree. Further, paragraph 9 of Ind AS 103 clarifies that the date on which the acquirer obtains control of the acquiree is generally the date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree—the closing date. However, the acquirer might obtain control on a date that is either earlier or later than the closing date.

An acquirer shall consider all pertinent facts and circumstances in identifying the acquisition date. Since government of India (GOI) approval is a substantive approval for Company X to acquire control of Company Z's operations, the date of acquisition cannot be earlier than the date on which approval is obtained from GOI. This is pertinent given that the approval from GOI is considered to be a substantive process and accordingly, the acquisition is considered to be completed only on receipt of such approval. Hence acquisition date in the above scenario is 30.6.20X1.

(3) **Journal entry for acquisition**

Particulars		Amount (Rs.)	Amount (Rs.)
Property Plant & Equipment	Dr.	1,66,650	

Right-of-use Asset	Dr.	6,666	
Development CWIP	Dr.	66,660	
Financial Assets - Loan Receivables	Dr.	16,665	
Inventories	Dr.	9,999	
Trade Receivables	Dr.	33,330	
Other Current Assets	Dr.	16,665	
To Provisions			66,660
To Other Liabilities			33,330
To Trade Payables			66,660
To Deferred Tax Liability			29,997
To Cash & Cash Equivalent (Purchase consideration)			1,00,000
To Gain on bargain purchase (Other Comprehensive Income)			19,988
(Being assets acquired and liabilities assumed from Company Z recorded at fair value along gain on bargain purchase)			

(4) **Balance Sheet of Company X as at 30.6.20X1**

(Pre & Post Acquisition of PI rights pertaining to Company Z)

Particulars	**Pre-Acquisition**	**Adjustments**	**Post-Acquisition**
	30.6.20X1		**30.6.20X1**
Assets			
Non - Current Assets			
Property Plant & Equipment	10,00,000	1,66,650	11,66,650
Right of Use Asset	2,00,000	6,666	2,06,666
Development CWIP	1,00,000	66,660	1,66,660
Financial Assets			
Loan receivable	50,000	16,665	66,665
Total Non-Current Assets	**13,50,000**		**16,06,641**
Current assets			
Inventories	2,00,000	9,999	2,09,999
Financial Assets			
Trade receivables	3,00,000	33,330	3,33,330
Cash and cash equivalents	4,00,000	(1,00,000)	3,00,000
Other Current Assets	50,000	16,665	66,665
Total Current Assets	**9,50,000**		**9,09,994**
Total Assets	**23,00,000**		**25,16,635**
Equity and Liabilities			
Equity			
Equity share capital	3,00,000	-	3,00,000
Other equity	3,00,000	-	3,00,000
Capital Reserve (OCI)	-	19,988	19,988

Total Equity	**6,00,000**		**6,19,988**
Liabilities			
Non-Current Liabilities			
Provisions	8,00,000	66,660	8,66,660
Other Liabilities	3,00,000	33,330	3,33,330
Deferred Tax Liability	-	29,997	29,997
Total Non-Current Liabilities	**11,00,000**		**12,29,987**
Current Liabilities			
Financial liabilities			
Trade Payables	6,00,000	66,660	6,66,660
Total Current Liabilities	**6,00,000**		**6,66,660**
Total Equity and Liabilities	**23,00,000**		**25,16,635**

Working Notes :

1. Determination of Company Z's balance acquired by Company X on 30.6.20X1 (Acquisition Date)

Particulars	**As per Company Z Books 30.6.20X1**	**Carrying Value 33.33% Share**	**Acquisition Date Value**	**Remarks**
	Rs.	**Rs.**	**Rs.**	
Assets				
Non-Current Assets				
Property Plant & Equipment	3,00,000	99,990	1,66,650	Note 1
Right of Use Asset	20,000	6,666	6,666	
Development CWIP	1,00,000	33,330	66,660	Note 1
Financial Assets				
Loan receivable	50,000	16,665	16,665	
Total Non-Current Assets	**4,70,000**	**1,56,651**	**2,56,641**	
Current assets				
Inventories	30,000	9,999	9,999	
Financial Assets				
Trade receivables	1,00,000	33,330	33,330	
Cash and cash equivalents	2,00,000	66,660	66,660	
Other Current Assets	50,000	16,665	16,665	
Total Current Assets	**3,80,000**	**1,26,654**	**1,26,654**	
Liabilities				
Non-Current Liabilities				
Provisions	2,00,000	66,660	66,660	
Other Liabilities	1,00,000	33,330	33,330	
Total Non-Current Liabilities	**3,00,000**	**99,990**	**99,990**	
Current Liabilities				
Financial liabilities				
Trade Payables	2,00,000	66,660	66,660	

Total Current Liabilities	**2,00,000**	**66,660**	**66,660**	

Note 1: Fair Value of PPE:

Fair Value of PPE in Company Z Books	Rs. 5,00,000
33.33% Share acquired by Company X	Rs. 1,66,650

Note 2: Fair Value of Development CWIP:

Fair Value of PPE in Company Z Books	Rs. 2,00,000
33.33% Share acquired by Company X	Rs. 66,660

2. Computation Goodwill/Bargain Purchase Gain

Particulars	**As at 30.6.20X1 (Rs.)**
Total Non - Current Assets	2,56,641
Total Current Assets (Except Cash & Cash Equivalent of Rs. 66,660) (1,26,654 – 66,660)	59,994
Total Non-Current Liabilities	(99,990)
Total Current Liabilities	(66,660)
Total Deferred Tax Liability (Refer Working note 3)	(29,997)
Net Assets Acquired	**1,19,988**
Less: Consideration Paid	(1,00,000)
Gain on Bargain Purchase (To be transferred to OCI)	**19,988**

*In extremely rare circumstances, an acquirer will make a bargain purchase in a business combination in which the value of net assets acquired in a business combination exceeds the purchase consideration. The acquirer shall recognise the resulting gain in other comprehensive income on the acquisition date and accumulate the same in equity as capital reserve, if the reason for bargain purchase gain is clear and evidence exist. If there does not exist clear evidence of the underlying reasons for classifying the business combination as a bargain purchase, then the gain shall be recognised directly in equity as capital reserve. Since in above scenario it is clearly evident that due to liquidity issues, Company Z has to withdraw their participating right from AWM/01. The said bargain purchase gain should be transferred to other comprehensive income on the acquisition date.

3. Computation of Deferred Tax Liability arising on Business Combination

Particulars	**Acquisition Date Value (Rs.)**
Total Non - Current Assets	2,56,641
Total Current Assets (Except Cash & Cash Equivalent of Rs. 66,660)	59,994

Total Non-Current Liabilities	-99,990
Total Current Liabilities	-66,660
Net Assets Acquired at Fair Value	1,49,985
Book value of Net Assets Acquired	49,995
Temporary Difference	99,990
DTL @ 30% on Temporary Difference	29,997

Note: As per Ind AS 103, in case an entity acquires another entity step by step through series of purchase then the acquisition date will be the date on which the acquirer obtains control. Till the time the control is obtained the investment will be accounted as per the requirements of other Ind AS 109, if the investments are covered under that standard or as per Ind AS 28, if the investments are in Associates or Joint Ventures.

If a business combination is achieved in stages, the acquirer shall remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognise the resulting gain or loss, if any, in profit or loss or other comprehensive income, as appropriate.

Since in the above transaction, company X does not hold any prior interest in Company Z & company holds only 30% PI rights in Block AWM/01 through unincorporated joint venture, this is not a case of step acquisition.

Question 15 : May 2022 – RTP

Entity A acquires entity B. Entity A agrees with the former shareholders of entity B to pay Rs. 900, with an additional payment of Rs. 500 if the subsequent earnings of entity B reach a specified target in three years. The former shareholders also become employees. On the acquisition date, the fair value of the net assets of entity B amount to Rs. 850, and the fair value of additional payment is estimated at Rs. 200. At the acquisition date, the outflow of additional payment is not probable.

Over the next three years, the cumulative earnings of entity B (before considering the effects of the additional payments) amount to Rs. 1,050. At the end of year three, entity A pays Rs. 500 as the conditions were met.

State the impact on the financial position and results of classifying the payments as remuneration and contingent consideration.

Solution :

The impact on the financial position and results of classifying the payments as remuneration and contingent consideration is tabulated as follows:

	Additional Payment is classified as	
	Remuneration	**Contingent consideration**
Consideration	900	900
Fair value of additional payment	0	200
Total consideration	**900**	**1,100**

Fair value of net assets	(850)	(850
Goodwill at acquisition date	**50**	**250**
Subsequent changes in additional payment	0	0
Total Goodwill	**50**	**250**
Cumulative earnings (before considering additional payment)	1,050	1,050
Impact of additional payment	(500)	(300)
Reported results across three years	**550**	**750**

Thanks ….

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IND AS – 110 CONSOLIDATION OF FINANCIAL STATEMENTS

CHAPTER - 19

Question 1 : May 2018 – PAPER

Hold Limited acquired 100% ordinary shares of Rs.100 each of Sub Limited on 1st October, 2017. On 31st March, 2018 the summarized Balance Sheets of the two companies were as given below:

	Particulars	Hold Limited (Rs.)	Sub Limited (Rs.)
I.	**Assets**		
	(1) Non-current Assets		
	(i) Property, Plant & Equipment		
	(a) Land & Building	30,00,000	36,00,000
	(b) Plant & machinery	48,00,000	27,00,000
	(ii) Investment in Sub Limited	68,00,000	
	(2) Current Assets		
	(i) Inventory	24,00,000	7,28,000
	(ii) Financial Assets		
	(a) Trade Receivables	11,96,000	8,00,000
	(b) Cash & Cash Equivalents	2,90,000	1,60,000
	Total	**1,84,86,000**	**79,8,000**
II.	**Equity and Liabilities**		
	(1) Equity		
	(i) Equity Share Capital (Shares of Rs.100 each fully paid)	1,00,00,000	40,00,000
	(ii) Other Equity		
	(a) Other Reserves	48,00,000	20,00,000
	(b) Retained Earnings	11,44,000	16,40,000
	(2) Current Liabilities		
	Financial Liabilities		
	(a) Bank Overdraft	16,00,000	-
	(b) Trade Payable	9,42,000	3,48,000
		1,84,86,000	**79,88,000**

The retained earnings of Sub Limited showed a credit balance of Rs.6,00,000 on 1st April, 2017 out of which a dividend of 10% was paid on 1st November 2017. Hold Limited has credited the dividend received to retained earnings account. There was no fresh addition to other reserves in case of both companies during the current financial year. There was no opening balance in the retained earnings in the books of Hold Limited.

Following are the changes in fair value as per respective Ind AS from the book value as on 1st October, 2017 in the books of Sub Limited which is to be considered while consolidating the Balance Sheets.

(i) Fair value of Plant and Machinery was Rs.40,00,000. (Rate of depreciation on Plant and Machinery is 10% p.a.)

(ii) Land and Building appreciated by Rs.20,00,000.

(iii) Inventories increased by Rs.3,00,000.

(iv) Trade payable increased by Rs.2,00,000.

Prepare Consolidated Balance Sheet as on 31st March, 2018. The Balance Sheet should comply with the relevant Ind AS and Schedule III of the Companies Act, 2013.

Solution :

Consolidated Balance Sheet of Hold Ltd. and its subsidiary, Sub Ltd.
As on 31st March, 2018

Particulars	**Rs.**
Assets	
(1) Non-current assets	
Property, Plant & Equipment	1,72,00,000
Goodwill	
(2) Current Assets	
Inventories	34,28,000
Financial Assets	
Trade Receivables	19,96,000
Cash & Cash equivalents	4,50,000
Total	**2,30,74,000**
Equity and Liabilities	
Equity	
Share Capital	1,00,00,000
Other Equity	99,84,000
Liability	
(1) Non Current Liabilities	
(2) Current Liabilities	
Financial Liabilities	
Short term borrowings	16,00,000
Trade Payables	14,90,000
Total	**2,30,74,000**

Working Notes :

1. Calculation of goodwill

	Rs.
Consideration Paid	68,00,000
Fair value of Net Assets (40,00,000 + 4,00,000 + 61,70,000)	1,05,70,000
Goodwill gain from bargain purchase	37,70,000

2. Statement for changes in equity

	Sh.Cap	**Other Equity**	**Total**
OP.	1,00,00,000	59,44,000	1,59,44,000
-Div.	-	(4,00,000)	(2,00,000)
+ Gain	-	37,70,000	37,70,000
+ Reserves of Subsidiary	-	6,70,000	6,70,000
	1,00,00,000	**99,84,000**	**1,99,84,000**

3. Reserves of Subsidiary

Res. 20,00,000 Pre RF 16,40,000

1/4 6,00,000 14,40,000

–Div. 4,00,000

Pre. 2,00,000 7,20,000 7,20,000

Pre Post

Pre	29,20,000	Post	7,20,000
+ Plant	11,50,000	-Dep.	50,000
+ L & B	20,00,000		6,70,000
+ Inventory	3,00,000		
– TP	(2,00,000)		
	61,70,000		

4. PPE

L &B	Hold	30,00,000
	Sub. (36,00,000 + 20,00,000)	56,00,000
P & M	Hold	48,00,000
	Sub. (27,00,000 + 11,50,000 – 50,000)	38,00,000
		1,72,00,000

	CP	**RP**
1/4/17	30,00,000	
–Dep.	1,50,000	
30/9/17	28,50,000	40,00,000
–Dep.	1,50,000	2,00,000

31/3/18	27,00,000	38,00,000

5. **Inventory**

Hold	24,00,000
Sub. (7,28,000 + 3,00,000)	10,28,000
	34,28,000

6. **Trade Payable**

Hold	9,42,000
Sub. (3,48,000 + 2,00,000)	5,48,000
	14,90,000

Question 2 : May 2018 – PAPER

XYZ Limited acquired 70% of equity shares of TUV Limited on 1st April, 2010 at cost of Rs.20,00,000 when TUV Limited had an equity share capital of Rs.20,00,000 and reserve and surplus of Rs.1,60,000. In the four consecutive years, TUV Limited, fared badly and suffered losses of Rs.5,00,000, Rs.8,00,000, Rs.10,00,000 and Rs.2,40,000 respectively. Thereafter in 2014-15, TUV Limited, experienced turnaround and registered an annual profit of Rs.1,00,000. In the next two years i.e. 2015-16 and 2016-17, TUV Limited recorded annual profits of Rs.2,00,000 and Rs.3,00,000 respectively. Calculate the Non controlling interests and cost of control at the end of each year for the purpose of consolidation, as per Ind AS 110 "Consolidated Financial Statements".

Solution :

1) **Date of Acquisition 1/4/2010**
Acquirer – XYZ Ltd.
Acquiree – TUV Ltd.
% Acquired = 705
NCI = 30%

2) **Calculation of cost of control on 1/1/2010**

Consideration paid (70%)	20,00,000	
+ NCI (At Proportional share) (30%)		6,48,000
	26,48,000	
– FV of NA (20,00,000 + 1,60,000) (100%)		21,60,000
Goodwill	4,88,000	

3) **NCI and Cost of Control at end of each year as per Ind AS 110.**

Details	P/L	NCI	Holding	Goodwill
01/04/2010	-	6,48,000	-	4,88,000
2010-11	(5,00,000)	(1,50,000)	(3,50,000)	-
31/3/2011	-	4,98,000	-	4,88,000
2011-12	(8,00,000)	(2,40,000)	(5,60,000)	-

31/3/2012	-	2,58,000	-	4,88,000
2012-13	(10,00,000)	(3,00,000)	(7,00,000)	-
31/3/2013	-	(42,000)	-	4,88,000
2013-14	(2,40,000)	(72,000)	(1,68,000)	-
3/3/2014	-	(1,14,000)	-	4,88,000
2014-15	1,00,000	30,000	70,000	-
31/3/2015	-	(84,000)	-	4,88,000
2015-16	2,00,000	60,000	1,40,000	-
31/3/2016	-	(24,000)	-	4,88,000
2016-17	3,00,000	90,000	2,10,000	-
31/3/2017	-	66,000	-	4,88,000

Note :

1) P/L in subsequent yrs after acquisition does not have any impact on goodwill. Goodwill should be checked for impairment every year.
2) As per Ind AS 21 loss of subsidiary should be born by holding and minority interest will not be shown negative.

Question 3 : Nov 2018 – RTP

Sumati Ltd. acquired 100% (50,00,000) equity shares of Rs.10 each in Sheetal Ltd. on 1st April, 2014. Sheetal Ltd. was incorporated on 1st April, 2014.

Sumati Ltd. acquired 80% (24,00,000) equity shares in Dharam Ltd. for Rs.600 lakh on 1st April, 2014 when Dharam Ltd. had share capital of Rs.300 lakh and Reserves and Surplus of Rs.300 lakh. The company amortizes goodwill on consolidation on a SLM basis over a period of 5 years. A full year's amortization is considered if the goodwill exists for more than 6 months.

On 1st April, 2017, Sumati Ltd. sold 12,00,000 equity shares of Dharam Ltd. for cash consideration of Rs.360 lakh with recognition of profit arising out of this sale.

The net assets of Dharam Ltd. on 31st March, 2017 were Rs.700 lakh. The amount of Reserves and Surplus was Rs.880 lakh, Rs.720 lakh and Rs.480 lakh respectively of Sumati Ltd., Sheetal Ltd. and Dharam Ltd. on 31st March, 2017.

The Balance Sheet extracts of the companies as on 31st March, 2018 were as follows:

(Rs.in lakh)

	Sumati Ltd.	**Sheetal Ltd.**	**Dharam Ltd.**
Share Capital (Rs.10 each)	1000	500	300
Reserves and Surplus	1240	910	640
Current Liabilities	460	490	560
	2700	**1900**	**1500**
Fixed Assets	640	420	380
50,00,000 equity shares in Sheetal Ltd.	500		
12,00,000 equity shares in Dharam Ltd.	300		
Current Assets	1260	1480	1120
	2700	**1900**	**1500**

You are required to prepare for Sumati Ltd. Group Balance Sheet as on 31st March, 2018 following Ind AS 110 and Ind AS 111. Notes to Accounts and working notes should form part of your answer.

Solution :

Consolidated Balance Sheet as on 31.3.2018

Particulars	**Note No.**	**(Rs. in lakh)**
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1,000
(b) Reserves and Surplus	2	2,206
(2) Current Liabilities	3	950
Total		**4,156**
II. Assets		
(1) Non-current assets		
Fixed Assets	4	1,060
Non-current investment (Investment in Associate Dharam Ltd.)	5	356
(2) Current assets	6	2,740
Total		**4,156**

Notes to Accounts

		Rs. In lakhs	
1	Share Capital		
	100 lakh Equity shares of Rs.10 each fully paid up		1,000
2	Consolidated Reserves and Surplus as on 31.3.2018		
	Balance of Reserves and surplus of Sumati Ltd. as on 31.3.2018	1,240	
	Add: Post-acquisition reserves and surplus of Sheetal Ltd. (subsidiary)	910	
	Profit accumulated over the years on investment of Sumati Ltd. (304-300)	4	
	Post-acquisition reserves and surplus of Dharam Ltd. (640-480) x 40%	64	
	Less: Goodwill amortised for the period (24/2)	12	2,206
3	Current Liabilities		
	Sumati Ltd.	460	
	Sheetal Ltd.	490	950
4	Fixed Assets		
	Sumati Ltd.	640	
	Sheetal Ltd.	420	1,060
5	Non-current investment (Investment in Associate Dharam Ltd.)		
	Carrying amount of Investment in Associate. [W.N.2]	304	

	(Identified goodwill included in the above Rs. 24 lakh) [W.N.3]		
	Add: Increase in reserves and surplus during the year (640-480) x 40%	64	
	Less: Goodwill written off in the fourth year (Rs. 24 lakh x ½)	(12)	356
6	Current assets		
	Sumati Ltd.	1,260	
	Sheetal Ltd.	1,480	2,740

Working Notes:

1. Cost of Control on acquisition of shares in Dharam Ltd. and amortization of goodwill

	Rs. In lakhs
Investment by Sumati Ltd.	600
Less: Share capital (300 x 80%)	(240)
Capital profit (pre-acquisition) (300 x 80%)	(240)
Goodwill	120
Less: Amortization for 3 years [(120/5) x3]	(72)
Carrying value of goodwill after 3 years	48

2. Ascertainment of carrying value of investment in Dharam Ltd. disposed off and retained

	Rs. In lakh
Net Assets of Dharam Ltd. on the date of disposal	700
Less: Minority's interest in Dharam Ltd. on the date of disposal (700 x 20%)	(140)
Share of Sumati Ltd. in Net Assets	560
Add: Carrying value of Goodwill (Refer W.N.1)	48
Total value of investment in Dharam Ltd. as on 1.4.2017	608
Less: Carrying Value of investment disposed off [Rs.608 lakh x (12 lakh /24 lakh)]	(304)
Carrying Value of investment retained by Sumati Ltd.	304

3. Goodwill arising on the Carrying Value of Unsold Portion of the Investment

	Rs. In lakh
Carrying value of retained 40% holdings in Dharam Ltd. as on 1st April, 2017	304
Less: Share in value of equity of Dharam Ltd., as at date of investment when its subsidiary relationship is transformed to an associate (700 x 40%)	(280)
Goodwill arising on such investment under Equity method as per AS 23	(24)

Question 4 : Nov 2018 – PAPER

Prepare the Consolidated Balance Sheet as on 31st March, 2018 of a group of companies comprising Usha Limited, Nisha Limited and Sandhya Limited. Their summarized balance sheets on that date are given below:

Amounts Rs.in lakh

	Usha Ltd.	Nisha Ltd.	Sandhya Ltd.
Equity and Liabilities			
Shareholder's Equity			
Share capital (Rs.10 per share)	300	200	160
Reserves	90	50	40
Retained earnings	80	25	30
Current Liabilities			
Trade Payables	235	115	90
Bills Payable			
Usha Ltd.	-	35	-
Sandhya Ltd.	15	-	-
	720	**425**	**320**
Assets			
Non-Current Assets			
Tangible assets	160	180	150
Investment:			
16 lakh shares in Nisha Ltd.	170	-	-
12 lakh shares in Sandhya Ltd.	-	140	-
Current Assets			
Cash in hand and at Bank	114	20	20
Bills Receivable	36	-	15
Trade Receivables	130	50	110
Inventories	110	35	25
	720	**425**	**320**

The following additional information is available:

(i) Usha Ltd. holds 80% shares in Nisha Ltd. and Nisha Ltd. holds 75% shares in Sandhya Ltd. Their holdings were acquired on 30th September, 2017.

(ii) The business activities of all the companies are not seasonal in nature and therefore, it can be assumed that profits are earned evenly throughout the year.

(iii) On 1st April, 2017, the following balances stood in the books of Nisha Limited and Sandhya Limited.

Rs.in lakh

	Nisha Ltd.	Sandhya Ltd.
Reserves	40	30
Retained Earnings	10	15

(iv) Rs.5 Lakh included in the inventory figure of Nisha Limited, is inventory which has been purchased from Sandhya Limited at cost plus 25%.

(v) The parent company has adopted an accounting policy to measure Non-controlling interest at fair value (quoted market price) applying Ind AS 103. Assume market prices of Nisha Limited and Sandhya Limited are the same as respective face values.

(vi) The capital profit preferably is to be adjusted against cost of control.

Note: Analysis of profits and notes to accounts must be a part of your answer.

Solution :

1) Usha in Nisha = 80%

Nisha in Sandhya = 75% NCI = 25%

Usha in Sandhya = 80 × 75% = 60% NCI = 40%

2) Consolidated Balance Sheet as on 31/3/2018.

Particulars	**Rs.**
Assets	
1) **NCA**	
PPE	490
Goodwill	
2) **CA**	
Inventory (170 – 1)	169
FA	
Trade Receivable (290 + 1)	291
Cash and Cash Equivalent	154
Total	**1,104**
Equity and Liabilities	
Equity	
Share Capital	300
Other Equity	280.9
NCI	83.1
Liabilities	
1) NCC	–
2) CL	
FL – Trade payable	440
Total	**1,104**

Working Notes :

1) Calculation of goodwill

	Nisha	**Sandhya**
Consideration paid	170	112
+ NCI		
Nisha (200 × 20%)	40	64
Sandjya (160 × 40%)	210	176
Fair value of Net Assets		
Nisha (200 + 62.5)	262.5	–
Sandhya (160 + 57.5)		217.5
Goodwill / Capital Reserve	52.5	41.5
Total	**94**	

2) State for Charge in Equity

Detail	Share Capital	Other Equity	Total	NCI	NCI	Total
OP.	300	170	470	40	64	574
+ Capital Reserve	–	94	94	–	–	94
+ Reserve in Nisha	–	10	10	2.5	–	12.5
+ Reserve in Sandhya	–	6.9	6.9	–	4.6	11.5
– NCI	–	–	–	(28)	–	(28)
	300	280.9		14.5	68.6	

3) Reserves of subsidiary

Nisha Ltd. Reserves 50

Pre 40 10

Pre 5 5 Post

Retained Earnings 25

Pre 10 15

Pre 7.5 7.5 Post

Total Pre 62.5 Post 12.5

↓

W.N.1

10 Holding 2.5 NCI

Sandhya Ltd. Reserves 40

Pre 30 10

Pre 5 5 Post

Retained Earnings 30

Pre 15 15

Pre 7.5 7.5 Post

Total Pre 57.5 Post 12.5

↓ – Inventory (1)

W.N.1 11.5

10 2.5

Holding NCI

Question 5 : May 2019 – RTP

Angel Ltd. has adopted Ind AS with a transition date of 1st April, 2017. Prior to Ind AS adoption, it followed Accounting Standards notified under Companies (Accounting Standards) Rules, 2006 (hereinafter referred to as "IGAAP").

It has made investments in equity shares of Pharma Ltd., a listed company engaged in the business of pharmaceuticals. The shareholding pattern of Pharma Ltd. is given below:

Shareholders (refer Note 1)	Percentage shareholding as on 1st April, 2017
Angel Ltd.	21%
Little Angel Ltd. (refer Note 2)	24%
Wealth Master Mutual Fund (refer Note 3)	3%
Individual public shareholders (refer Note 4)	52%

Notes:

(1) None of the shareholders have entered into any shareholders' agreement.

(2) Little Angel Ltd. is a subsidiary of Angel Ltd. (under Ind AS) in which Angel Ltd. holds 51% voting power.

(3) Wealth Master Mutual Fund is not related party of either Little Angel Ltd. or Pharma Ltd.

(4) Individual public shareholders represent 17,455 individuals. None of the individual shareholders hold more than 1% of voting power in Pharma Ltd.

All commercial decisions of Pharma Ltd. are taken by its directors who are appointed by a simple majority vote of the shareholders in the annual general meetings ("AGM"). The following table shows the voting pattern of past AGMs of Pharma Ltd.:

Shareholders	AGM for the financial year		
	2013-14	2014-15	2015-16
Angel Ltd.	Attended and voted in favour of all the resolutions	Attended and voted in favour of all the resolutions	Attended and voted in favour of all the resolutions
Little Angel Ltd.	Attended and voted as per directions of Angel Ltd.	Attended and voted as per directions of Angel Ltd	Attended and voted as per directions of Angel Ltd
Wealth Master Mutual Fund	Attended and voted in favour of all the resolutions except for the reappointment of the retiring directors	Attended and voted in favour of all the resolutions except for the reappointment of the retiring directors	Attended and voted in favour of all the resolutions except for the reappointment of the retiring directors
Individuals	7% of the individual shareholders attended the AGM. All the individual shareholders voted in favour of all the resolutions, except that 50% of the individual Shareholders voted against the resolution to appoint the retiring directors.	8% of the individual shareholders attended the AGM. All the individual shareholders voted in favour of all the resolutions, except that 50% of the individual Shareholders voted against the resolution to appoint the retiring directors.	6% of the individual shareholders attended the AGM. All the individual shareholders voted in favour of all the resolutions, except that 50% of the individual Shareholders voted against the resolution to appoint the retiring directors.

Pharma Ltd. has obtained substantial long term borrowings from a bank. The loan is payable in 20 years from 1st April, 2017. As per the terms of the borrowing, following actions by Pharma Ltd. will require prior approval of the bank :

- Payment of dividends to the shareholders in cash or kind;
- Buyback of its own equity shares;
- Issue of bonus equity shares;
- Amalgamation of Pharma Ltd. with any other entity; and
- Obtaining additional loans from any entity.

Recently, the Board of Directors of Pharma Ltd. proposed a dividend of Rs. 5 per share. However, when the CFO of Pharma Ltd. approached the bank for obtaining their approval, the bank rejected the proposal citing concerns over the short-term cash liquidity of Pharma Ltd. Having learned about the developments, the Directors of Angel Ltd. along with the Directors of Little Angel Ltd. approached the bank with a request to re-consider its decision. The Directors of Angel Ltd. and Little Angel Ltd. urged the bank to approve a reduced dividend of at least Rs. 2 per share. However, the bank categorically refused to approve any payout of dividend.

Under IGAAP, Angel Ltd. has classified Pharma Ltd. as its associate. As the CFO of Angel Ltd., you are required to comment on the correct classification of Pharma Ltd. on transition to Ind AS.

Solution :

To determine whether Pharma Limited can be continued to be classified as an associate on transition to Ind AS, we will have to determine whether Angel Limited controls Pharma Limited as defined under Ind AS 110.

An investor controls an investee if and only if the investor has all the following:

(a) Power over investee

(b) Exposure, or rights, to variable returns from its involvement with the investee

(c) Ability to use power over the investee to affect the amount of the investor's returns.

Since Angel Ltd. does not have majority voting rights in Pharma Ltd. we will have to determine whether the existing voting rights of Angel Ltd. are sufficient to provide it power over Pharma Ltd.

Analysis of each of the three elements of the definition of control:

Elements / conditions	**Analysis**
Power over investee	Angel Limited along with its subsidiary Little Angel Limited (hereinafter referred to as "the Angel group") does not have majority voting rights in Pharma Limited. Therefore, in order to determine whether Angel group have power over Pharma Limited. we will need to analyse whether Angel group, by virtue of its non-majority voting power, have practical ability to unilaterally direct the relevant activities of Pharma Limited. In other words, we will need to analyse whether Angel group has **de facto power** over Pharma Limited. Following is the analysis of de facto power of Angel over Pharma Limited: - The public shareholding of Pharma Limited (that is, 52% represents thousands of shareholders none individually holding material shareholding, - The actual participation of Individual public shareholders in the general meetings is minimal (that is, in the range of 6% to 8%). - Even the public shareholders who attend the meeting do not consult with each other to vote. - Therefore, as per guidance of Ind AS 110, the public shareholders will not be able to outvote Angel group (who is the largest shareholder group) in any general meeting. Based on the above-mentioned analysis, we can conclude that Angel group has de facto power over Pharma Limited.

Exposure, or rights, to variable returns from its involvement with the investee	Angel group has exposure to variable returns from its involvement with Pharma Limited by virtue of its equity stake.
Ability to use power over the investee to affect the amount of the investor's returns	Angel group has ability to use its power (in the capacity of a principal and not an agent) to affect the amount of returns from Pharma Limited because it is in the position to appoint directors of Pharma Limited who would take all the decisions regarding relevant activities of Pharma Limited. Here, it is worthwhile to evaluate whether certain rights held by the bank would prevent Angel Limited's ability to use the power over Pharma Limited to affect its returns. It is to be noted that, all the rights held by the bank in relation to Pharma Limited are protective in nature as they do not relate to the relevant activities (that is, activities that significantly affect he Pharma Limited's returns) of Pharma Limited. As per Ind AS 110, protective rights are the rights designed to protect the interest of the party holding those rights without giving that party power over the entity to which those rights relate. Therefore, the protective rights held by the bank should not be considered while evaluating whether or not Angel Group has control over Pharma Limited.
Conclusion : Since all the three elements of definition of control is present, it can be concluded that Angel Limited has control over Pharma Limited.	

Since it has been established that Angel Limited has control over Pharma Limited, upon transition to Ind AS, Angel Limited shall classify Pharma Limited as its subsidiary.

Question 6 : Nov 2019 – RTP

What will be the accounting treatment of dividend distribution tax in the consolidated financial statements in case of partly-owned subsidiary in the following scenarios:

Scenario 1: H Limited (holding company) holds 12,000 equity shares in S Limited (Subsidiary of H Limited) with 60% holding. Accordingly, S Limited is a partly-owned subsidiary of H Limited. During the year 20X1, S Limited paid a dividend @ Rs.10 per share and DDT @ 20% on it.

Should the share of H Limited in DDT paid by S Limited amounting to Rs.24,000 (60% x Rs.40,000) be charged as expense in the consolidated profit and loss of H Limited?

Scenario 2 (A): Extending the situation given in scenario 1, H Limited also pays dividend of Rs.300,000 to its shareholders and DDT liability @ 20% thereon amounts to Rs.60,000. As per the tax laws, DDT paid by S Ltd. of Rs.24,000 is allowed as set off against the DDT liability of H Ltd., resulting in H Ltd. paying Rs.36,000 (Rs.60,000 – Rs.24,000) as DDT to tax authorities.

Scenario 2(B)
If in (A) above, H Limited pays dividend amounting to Rs.100,000 with DDT liability @ 20% amounting to Rs.20,000.

Scenario (3):
Will the answer be different for the treatment of dividend distribution tax paid by associate in the consolidated financial statement of investor, if as per tax laws the DDT paid by associate is not allowed set-off against the DDT liability of the investor?

Solution :

Scenario 1: Since H Limited is holding 12,000 shares it has received Rs.1,20,000 as dividend from S Limited. In the consolidated financial statements of H Ltd., dividend income earned by H Ltd. and dividend recorded by S Ltd. in its equity will both get eliminated as a result of consolidation adjustments. Dividend paid by S Ltd. to the 40% non-controlling interest (NCI) shareholders will be recorded in the Statement of Changes in Equity as reduction of NCI balance (as shares are classified as equity as per Ind AS 32).

DDT of Rs.40,000 paid to tax authorities has two components- One Rs.24,000 (related to H Limited's shareholding and other Rs.16,000 (40,000 × 40%) belong to non controlling interest (NCI) shareholders of S Limited). DDT of Rs.16,000 (pertaining to non-controlling interest (NCI) shareholders) will be recorded in the Statement of Changes in Equity along with dividend. DDT of Rs.24,000 paid outside the consolidated Group shall be charged as tax expense in the consolidated statement of profit and loss of H Ltd.

In accordance with the above, in the given case, CFS of H limited will be as under:

Transactions	H Ltd.	S Ltd.	Consol Adjustments	CFS H Ltd.
Dividend Income (P&L)	1,20,000	-	(1,20,000)	-
Dividend (in Statement of Changes in Equity by way of reduction of NCI)	-	(2,00,000)	1,20,000	(80,000)
DDT (in Statement of Changes in Equity by way of reduction of NCI)	-	(40,000)	24,000	(16,000)
DDT (in Statement of P&L)	-	-	(24,000)	(24,000)

Scenario 2 (A) : If DDT paid by the subsidiary S Ltd. is allowed as a set off against the DDT liability of its parent H Ltd. (as per the tax laws), then the amount of such DDT should be recognised in the consolidated statement of changes in equity of parent H Ltd.

In the given case, share of H Limited in DDT paid by S Limited is Rs.24,000 and entire Rs.24,000 was utilised by H Limited while paying dividend to its own shareholders.

Accordingly, DDT of Rs.76,000 (Rs.40,000 of DDT paid by S Ltd. (of which Rs.16,000 is attributable to NCI) and Rs.36,000 of DDT paid by H Ltd.) should be recognised in the consolidated statement of changes in equity of parent H Ltd. No amount will be charged to consolidated statement of profit and loss. The basis for such accounting would be that due to Parent H Ltd's transaction of distributing dividend to its shareholders (a transaction recorded in Parent H Ltd's equity) and the related DDT set-off, this DDT paid by the subsidiary is effectively a tax on distribution of dividend to the shareholders of the parent company.

In accordance with the above, in the given case, CFS of H limited will be as under:

Transactions	H Ltd.	S Ltd.	Consol Adjustments	CFS H Ltd.
Dividend Income (P&L)	1,20,000	-	(1,20,000)	-
Dividend (in Statement of Changes in Equity)	(3,00,000)	(2,00,000)	1,20,000	(3,80,000)*
DDT (in Statement of Changes in Equity)	(36,000)	(40,000)	-	(76,000)*

*Dividend of Rs.80,000 and DDT of Rs.16,000 will be reflected as reduction from non-controlling interest.

Scenario 2(B): In the given case, share of H Limited in DDT paid by S Limited is Rs.24,000 out of which only Rs.20,000 was utilised by H Limited while paying dividend by its own. Therefore, balance Rs.4,000 should be charged in the consolidated statement of profit and loss.

In accordance with the above, in the given case, CFS of H limited will be as under:

Transactions	H Ltd.	S Ltd.	Consol Adjustments	CFS H Ltd.
Dividend Income (P&L)	1,20,000	-	(1,20,000)	-
Dividend (in Statement of Changes in Equity)	(1,00,000)	(2,00,000)	1,20,000	(1,80,000)*
DDT (in Statement of Changes in Equity)	-	(40,000)	4,000	(36,000)*
DDT (in Statement of P&L)	-	-	(4,000)	(4,000)

*Dividend of Rs.80,000 and DDT of Rs.16,000 will be reflected as reduction from non- controlling interest.

Scenario (3): Considering that as per tax laws, DDT paid by associate is not allowed set off against the DDT liability of the investor, the investor's share of DDT would be accounted by the investor company by crediting its investment account in the associate and recording a corresponding debit adjustment towards its share of profit or loss of the associate.

Question 7 : May 2020 – RTP

Gamma Limited, a parent company, is engaged in manufacturing and retail activities. The group holds investments in different entities as follows:

- Gamma Limited holds 100% Investment in G Limited and D Limited;
- G Limited and D Limited hold 60% and 40% in GD Limited respectively;
- Delta Limited is a 100% subsidiary of GD Limited

Firstly, Gamma Limited wants you to suggest whether GD Limited can avail the exemption from the preparation and presentation of consolidated financial statements as per applicable Ind AS?

Secondly, if all other facts remain the same as above except that G Limited and D Limited are both owned by an Individual (say, Mr. X) instead of Gamma Limited, then explain whether GD Limited can avail the exemption from the preparation and presentation of consolidated financial statements.

Solution :

As per paragraph 4(a) of Ind AS 110, an entity that is a parent shall present consolidated financial statements. This Ind AS applies to all entities, except as follows:

A parent need not present consolidated financial statements if it meets all the following conditions:

(i) it is a wholly-owned subsidiary or is a partially-owned subsidiary of another entity and all its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting consolidated financial statements;

(ii) its debt or equity instruments are not traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets);

(iii) it did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; and

(iv) its ultimate or any intermediate parent produces financial statements that are available for public use and comply with Ind ASs, in which subsidiaries are consolidated or are measured at fair value through profit or loss in accordance with this Ind AS.

In accordance with the above, it may be noted that as per paragraph 4(a)(i) above, a parent need not present consolidated financial statements if it is a:

— wholly-owned subsidiary; or

— is a partially-owned subsidiary of another entity and all its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting consolidated financial statements.

Although GD Limited is a partly-owned subsidiary of G Limited, it is the wholly-owned subsidiary of Gamma Limited (and therefore satisfies the condition 4(a)(i) of Ind AS 110 without regard to the relationship with its immediate owners, i.e. G Limited and D Limited). Thus, GD Limited being the wholly owned subsidiary fulfils the conditions as mentioned under paragraph 4(a)(i) and is not required to inform its other owner D Limited of its intention not to prepare the consolidated financial statements.

Thus, in accordance with the above, GD Limited may take the exemption given under paragraph 4(a) of Ind AS 110 from presentation of consolidated financial statements.

In Alternative Scenario, where both G Limited and D Limited are owned by an individual Mr. X, then GD Limited is ultimately wholly in control of Mr. X (i.e., an individual) and hence it cannot be considered as a wholly owned subsidiary of an entity.

This is because Ind AS 110 makes use of the term ‘entity’ and the word 'entity’ includes a company as well as any other form of entity. Since, Mr. X is an ‘individual’ and not an ‘entity’, therefore, GD Limited cannot be considered as wholly owned subsidiary of an entity.

Therefore, in the given case, GD Limited is a partially-owned subsidiary of another entity. Accordingly, in order to avail the exemption under paragraph 4(a), its other owner, D Limited should be informed about and do not object to GD Limited not presenting consolidated financial statements. Further, for the purpose of consolidation of G Limited and D Limited, GD Limited will be required to provide relevant financial information as per Ind AS.

Question 8 : Nov 2020 – Paper

Parent Limited, prepares consolidated financial statements of the group on 31 March every year. During the year ended 31 March 2020, the following events affected the tax position of the group:

(i) S Limited, a wholly owned subsidiary of Parent Limited, incurred a loss of Rs. 20,00,000 which is adjustable from future taxable profits of the company for tax purposes. S Limited is unable to utilize this loss against previous tax liabilities. Income Tax Act does not allow S Limited to transfer the tax loss to other group companies. However, it allows S Limited to carry forward the loss and utilize it against company's future taxable profits. The directors of Parent Limited estimate that S Limited will not make any taxable profits in the foreseeable future.

(ii) On 1 April 2019, Parent Limited borrowed Rs. 50,00,000. The cost incurred by Parent Limited for arranging the borrowing was Rs. 1,00,000 on the said date and this expenditure is qualified for deduction under the Income Tax Act for the accounting year 2019-2020. The loan was given for a three-year period. As per agreement, no principal or interest was payable on the loan during the tenure of loan but the amount repayable on 31 March 2022 will be by way of a bullet payment of Rs. 65,21,900. As per Parent Limited, this equates to an effective annual interest rate of 10% on loan. As per the Income-tax Act, a further expense of Rs. 15,21,900 will be claimable from taxable income till the loan is repaid on 31 March 2022.

The rate of corporate income tax to be assumed @ 20%.

Explain and show how each of these events would affect the deferred tax assets/liabilities in the consolidated balance sheet of Parent Limited as at 31 March 2020 as per applicable Ind AS.

You are also required to examine whether the effective rate of interest arrived at by Parent Limited for the loan of Rs. 50,00,000 is in accordance with applicable Ind AS or not?

Solution :

(i) The tax loss creates a potential deferred tax asset for the group since its carrying value is nil and its tax base is Rs. 20,00,000.

However, no deferred tax asset can be recognised because there is no prospect of being able to reduce tax liabilities in the foreseeable future as no taxable profits are anticipated.

(ii) The carrying value of the loan at 31 March 2020 is Rs. 53,90,000 (Rs. 50,00,000 – Rs. 1,00,000 + (Rs. 49,00,000 x 10%)).

The tax base of the loan is Rs. 50,00,000.

This creates a deductible temporary difference of Rs. 3,90,000 (Rs. 53,90,000 – Rs. 50,00,000) and a potential deferred tax asset of Rs. 78,000 (Rs. 3,90,000 x 20%).

If there are prospects of availability of taxable profits in future, deferred tax asset can be recognised.

Amortisation Table for verification of effective rate of interest

Year	Opening balance (Rs.) (A)	Interest @ 10% (Rs.) (B)	Closing balance (Rs.) (A) + (B)
1	(50,00,000 – 1,00,000) 49,00,000	4,90,000	53,90,000

2	53,90,000	5,39,000	59,29,000
3	59,29,000	5,92,900	65,21,900

Since the closing balance calculated as per the above table on the basis of 10% matches with the bullet payment of Rs. 65,21,900, it assures that 10% rate of interest taken as effective rate of interest is correct and is in accordance with Ind AS 109. It considers the impact of cost of borrowing adjusted from the loan amount at initial recognition.

Question 9 : Jan 2021 – Paper

On 1st April 2017, A Limited acquired 80% of the share capital of S Limited. On acquisition date the share capital and reserves of S Ltd. stood at Rs.5,00,000 and Rs.1,25,000 respectively. A Limited paid initial cash consideration of Rs.10,00,000. Additionally, A Limited issued 2,00,000 equity shares with a nominal value of Rs.1 per share at current market value of Rs.1.80 per share.

It was also agreed that A Limited would pay a further sum of Rs.5,00,000 after three years.

A Limited's cost of capital is 10%. The appropriate discount factor for Rs.1 @ 10% receivable at the end of

1st year: 0.91

2nd year: 0.83

3rd year: 0.75

The shares and deferred consideration have not yet been recorded by A limited.

Below are the Balance Sheet of A Limited and S Limited as at 31st March, 2019:

	A Limited (Rs.000)	**S Limited (Rs.000)**
Non-current assets:		
Property, plant & equipment	5,500	1,500
Investment in S Limited at cost	1,000	
Current assets:		
Inventory	550	100
Receivables	400	200
Cash	200	50
	7,650	1,850
Equity:		
Share capital	2,000	500
Retained earnings	1,400	300
	3,400	800
Non-current liabilities	3,000	400
Current liabilities	1,250	650
	7,650	1,850

Further information :

(i) On the date of acquisition the fair values of S Limited's plant exceeded its book value by Rs.2,00,000. The plant had a remaining useful life of five years at this date;

(ii) The consolidated goodwill has been impaired by Rs.2,58,000; and

(iii) The A Limited Group, values the non-controlling interest using the fair value method. At the date of acquisition, the fair value of the 20% non-controlling interest was Rs.3,80,000.

You are required to prepare Consolidated Balance Sheet of A Limited as at 31st March, 2019. (Notes to Account on Consolidated Balance Sheet is not required).

Solution :

Consolidated Balance Sheet of A Ltd. and its subsidiary, S Ltd. as at 31st March, 2019

	Particulars	Rs. in 000s
I.	**Assets**	
	(1) Non-current assets	
	(i) Property Plant & Equipment (W.N.4)	7,120.00
	(ii) Intangible asset – Goodwill (W.N.3)	1,032.00
	(2) Current Assets	
	(i) Inventories (550 + 100)	650.00
	(ii) Financial Assets	
	(a) Trade Receivables (400 + 200)	600.00
	(b) Cash & Cash equivalents (200 + 50)	250.00
	Total Assets	**9,652.00**
II.	**Equity and Liabilities**	
	(1) Equity	
	(i) Equity Share Capital (2,000 + 200)	2,200.00
	(ii) Other Equity	
	(a) Retained Earnings (W.N.6)	1,190.85
	(b) Securities Premium	160.00
	(2) Non-Controlling Interest (W.N.5)	347.40
	(3) Non-Current Liabilities (3,000 + 400)	3,400.00
	(4) Current Liabilities (W.N.8)	2,353.75
	Total Equity & Liabilities	**9,652.00**

Notes:

1. Since the question required not to prepare Notes to Account, the column of Note to Accounts had not been drawn.
2. It is assumed that shares were issued during the year 2018-2019 and entries are yet to be made.

Working Notes:

1. Calculation of purchase consideration at the acquisition date i.e. 1st April, 2017

	Rs. in 000s
Payment made by A Ltd. to S Ltd.	
Cash	1,000.00
Equity shares (2,00,000 shares x Rs.1.80)	360.00
Present value of deferred consideration (Rs.5,00,000 x 0.75)	375.00

Total consideration	1,735.00

2. Calculation of net assets i.e. net worth at the acquisition date i.e. 1st April, 2017

	Rs. in 000s
Share capital of S Ltd.	500.00
Reserves of S Ltd.	125.00
Fair value increase on Property, Plant and Equipment	200.00
Net worth on acquisition date	825.00

3. Calculation of Goodwill at the acquisition date i.e. 1st April, 2017 and 31st March, 2019

	Rs. in 000s
Purchase consideration (W.N.1)	1,735.00
Non-controlling interest at fair value (as given in the question)	380.00
	2,115.00
Less: Net worth (W.N.2)	(825.00)
Goodwill as on 1st April 2017	1,290.00
Less: Impairment (as given in the question)	258.00
Goodwill as on 31st March 2019	1,032.00

4. Calculation of Property, Plant and Equipment as on 31st March 2019

			Rs. in 000s
A Ltd.			5,500.00
S Ltd.		1,500.00	
Add: Net fair value gain not recorded yet	200.00		
Less: Depreciation [(200/5) x 2]	(80.00)	120.00	1620.00
			7120.00

5. Calculation of Post-acquisition gain (after adjustment of impairment on goodwill) and value of NCI as on 31st March 2019

		Rs. in 000s NCI (20%)	Rs. in 000s A Ltd. (80%)
Acquisition date balance		380.00	Nil
Closing balance of Retained Earnings	300.00		
Less: Pre-acquisition balance	(125.00)		
Post-acquisition gain	175.00		
Less: Additional Depreciation on PPE [(200/5) x 2]	(80.00)		
Share in post-acquisition gain	95.00	19.00	76.00
Less: Impairment on goodwill	258.00	(51.60)	(206.40)

	347.40	(130.40)

6. Consolidated Retained Earnings as on 31st March 2019

	Rs. in 000s
A Ltd.	1,400.00
Add: Share of post-acquisition loss of S Ltd. (W.N.5)	(130.40)
Less: Finance cost on deferred consideration (37.5 + 41.25) (W.N.7)	(78.75)
Retained Earnings as on 31st March 2019	1,190.85

7. Calculation of value of deferred consideration as on 31st March 2019

	Rs. in 000s
Value of deferred consideration as on 1st April 2017 (W.N.1)	375.00
Add: Finance cost for the year 2017-2018 (375 x 10%)	37.50
	412.50
Add: Finance cost for the year 2018-2019 (412.50 x 10%)	41.25
Deferred consideration as on 31st March 2019	453.75

8. Calculation of current Liability as on 31st March 2019

	Rs. in 000s
A Ltd.	1,250.00
S Ltd.	650.00
Deferred consideration as on 31st March 2019 (W.N.7)	453.75
Current Liability as on 31st March 2019	2,353.75

Question 10 : July 2021 – Paper

Given below are the balance sheets of a group of companies com prising LX, MX Limited and NX Limited as on 31st march 2021 :

Rs. In lakhs

Particulars	LX Limited	MX Limited	NX Limited
Assets			
Non-current Assets			
Property, Plant and Equipment Investment	1,500	1,600	1,400
17.0 lakh shares in MX Limited	2,620	–	–
9.6 lakh shares in NX Limited	–	1,350	–
Current Assets			
Inventories	1,230	730	1,180
Financial Assets			
Trade Receivables	1,415	270	620
Bills Receivables	650	60	-
Cash in hand and at Bank	1,085	90	150
	8,500	**4,100**	**3,350**

Equity and Liabilities			
Shareholders' Equity			
Share Capital (Rs.100 per share)	3,400	2,000	1,600
Other Equity			
– Reserve	1,150	810	580
– Retained	1,030	600	310
Current Liabilities			
Financial Liabilities			
Trade Payables	2,920	690	805
Bills Payable	–	–	–
MX Limited	–	–	55
	8,500	**4,100**	**3,350**

LX Limited holds 85% shares in MX Limited, which were acquired on 1st April 2020 and MX Limited holds 60% shares in NX Limited, which were acquired on 30th September 2020. The following balance stood in the books of MX Limited and NX Limited as on 1st April 2020 :

Particulars	MX Limited Rs. In Lakhs	NX Limited Rs. In Lakhs
Reserves	760	520
Retained earnings	480	150

The business activities of NX Limited are not seasonal in nature.

The parent company has adopted an accounting policy to measure non-controlling interest at first value applying IND AS 103. The fair value is to be determined at quoted market price. The given market price of MX Limited is Rs.120 per share and NX Limited is Rs.125, per share.

Prepare the consolidated Balance Sheet as on 31st March 2021 of the group of companies LX Limited, Mx Limited and NX Limited.

Solution :

Consolidated Balance Sheet of the Group as at 31st March, 2021

Particulars	Note No.	Rs. in lakh
ASSETS		
Non-current assets		
Property, plant and equipment	1	4,500.00
Current assets		
(a) Inventories	2	3,140.00
(b) Financial assets		
Trade receivables	3	2,305.00
Bills receivables	4	655
Cash and cash equivalents	5	1,325.00
Total assets		**11,925.00**
EQUITY & LIABILITIES		
Equity attributable to owners of parent		

Share Capital		3,400.00
Other Equity	6	2,893.10
Non-controlling interests (W.N.4)		1,216.90
LIABILITIES		
Non-current liabilities		Nil
Current liabilities		
(a) Financial Liabilities		
Trade payables	7	4,415.00
Total equity and liabilities		**11,925.00**

Notes to Accounts **(Rs. in lakh)**

1	**Property Plant & Equipment**		
	LX Ltd.	1,500	
	MX Ltd.	1,600	
	NX Ltd.	1,400	4,500
2	**Inventories**		
	LX Ltd.	1,230	
	MX Ltd.	730	
	NX Ltd.	1,180	3,140
3	**Trade Receivables**		
	LX Ltd.	1,415	
	MX Ltd.	270	
	NX Ltd.	620	2,305
4	**Bills Receivables**		
	LX Ltd.	650	
	MX Ltd. (60-55)	5	655
5	**Cash & Cash equivalents**		
	LX Ltd.	1,085	
	MX Ltd.	90	
	NX Ltd.	150	1,325
6	**Other Equity**		
	Reserve (W.N.5)	1,207.80	
	Retained earnings (W.N.5)	1,172.80	
	Capital Reserve (W.N.3)	512.50	2,893.10
7	**Trade Payables**		
	LX Ltd.	2,920	
	MX Ltd.	690	
	NX Ltd.	805	4,415

Working Notes:

1. Analysis of Reserves and Surplus **(Rs. in lakh)**

	MX Ltd.		NX Ltd.
Reserves as on 1.4.2020	760		520
Increase during the year 2020-2021 (580 - 520)		60	
Increase for the half year till 30.9.2020	____		30
Balance on acquisition date (A)	760		550
Total balance as on 31.3.2021	810		580
Post-acquisition balance	50		30
Retained Earnings as on 1.4.2020	480		150
Increase during the year 2020-2021 (310 - 150)		160	
Increase for the half year till 30.9.2020	____		80
Balance on acquisition date (B)	480		230
Total balance as on 31.3.2021	600		310
Post-acquisition balance	120		80
Total balance on the acquisition date (A+B)	1,240		780

2. Calculation of Effective Interest of LX Ltd. in NX Ltd.

Acquisition by LX Ltd. in MX Ltd.	= 85%
Acquisition by MX Ltd. in NX Ltd.	= 60%
Acquisition by Group in NX Ltd. (85% x 60%)	= 51%
Non-controlling Interest	= 49%

3. Calculation of Goodwill / Capital Reserve on the acquisition

	MX Ltd.	NX Ltd.
Investment or consideration	2,620.00	(1,350 x 85%) 1,147.50
Add: NCI at Fair value		
[(2,000 / 100) x 120 x 15%]	360.00	
[(1,600 / 100) x 125 x 49%]	-	980.00
	2,980.00	2,127.50
Less: Identifiable net assets (Share Capital + Increase in the Reserves and Surplus till acquisition date)	(2,000+760+480) (3,240.00)	(1,600+550+230) (2,380.00)
Capital Reserve	260.00	252.50
Total Capital Reserve (260 + 252.50)	512.50	

4. Calculation of Non-controlling Interest

	MX Ltd.	NX Ltd.
At Fair Value (See Note 3)	360.00	980.00
Add: Post Acquisition Reserves (W.N.1)	(50 x 15%) 7.50	(30 x 49%) 14.70
Add: Post Acquisition Retained Earnings (W.N.1)	(120 x 15%) 18.00	(80 x 49%) 39.20
Less: NCI share of investment in NX Ltd.	(1,350 x 15%) (202.50)*	-
	183.00	1,033.90
Total (183.00 + 1,033.90)		1,216.90

***Note:** The non-controlling interest in MX Ltd. will take its proportion in NX Ltd. Therefore, they have to bear their proportion in the investment by MX Ltd. (in NX Ltd.) also.

5. Calculation of Consolidated Other Equity

	Reserves	Retained Earnings
LX Ltd.	1,150.00	1,030.00
Add: Share in MX Ltd.	(50 x 85%) 42.50	(120 x 85%) 102.00
Add: Share in NX Ltd.	(30 x 51%) 15.30	(80 x 51%) 40.80
	1,207.80	1,172.80

Question 11 : Nov 2021 – RTP

PP Ltd., a non-investment entity, is the parent of Praja Ltd. within the meaning of Ind AS 110 'Consolidated Financial Statements'. The investment in Praja Ltd. was carried in the separate financial statements of PP Ltd. at fair value with changes in fair value recognised in the other comprehensive income. On 1st April, 20X2, PP Ltd. qualifies as one that is an investment entity. Carrying amount of the investment on 1st April, 20X2 was Rs. 8,00,000. The fair value of its investment in Praja Ltd was Rs. 10,00,000 on that date. PP Ltd had recognised in OCI an amount of Rs. 1,00,000 as a previous fair value increase related to the investment in Praja Ltd.

How would PP Ltd account for the investment in Praja Ltd on the date of change of its classification/status as an investment entity, in its separate financial statements?

Solution :

(i) As per paragraph 11B(b) of Ind AS 27, on the date of change, ie, 1st April, 20X2, PP Ltd (the parent) becoming an investment entity, its investment in Praja Ltd (the subsidiary) shall be at fair value through profit and loss in accordance with Ind AS 109. Accordingly, the new carrying amount will be Rs. 10,00,000.

(ii) The difference between the new carrying amount and the carrying amount of the investment on the date of change will be recognised in the profit and loss. Hence, PP Ltd will recognise an amount of Rs. 2,00,000 (Rs. 10,00,000 – Rs. 8,00,000) in profit and loss as gain.

(iii) Any fair value adjustments previously recognised in OCI in respect of subsidiary ie Praja Ltd. shall be treated as if the investment entity had disposed off the subsidiary at the date of change in status as per para 11B(b) of Ind AS 27.

Further, as per para B5.7.1 of Ind AS 109, amounts presented in other comprehensive income shall not be subsequently transferred to profit or loss. However, the entity may transfer the cumulative gain or loss within equity.

Therefore, the company shall not reclassify the fair value gains or losses to profit or loss on change in classification from FVTOCI to FVTPL. However, the company may transfer the fair value gains or losses from one component to the other within equity.

Moreover, Paragraph 11A(e) of Ind AS 107, requires disclosure of any transfers of the cumulative gain or loss within equity during the period and the reason for such transfers. Accordingly, PP Ltd. shall provide the disclosures if it transfers the cumulative gain or loss from one component to the other within equity.

Particulars	**Rs.**
Carrying amount of investment in Praja Ltd [as per (i) above]	10,00,000
Amounts recognised in profit and loss relating to investment in Praja Ltd [as per (ii) above]	2,00,000

Question 12 : Nov 2021 – RTP

Solar Limited has an 80% interest in its subsidiary, Mars Limited. Solar Limited holds a direct interest of 25% in Venus Limited. Mars Limited also holds a 30% interest in Venus Limited. The decisions concerning relevant activities of Venus Limited require a simple majority of votes. How should Solar Limited account for its investment in Venus Limited in its consolidated financial statements?

Solution :

In the present case, Solar Limited controls Mars Limited (since it holds 80% of its voting rights). Consequently, it also controls the voting rights associated with 30% equity interest held by Mars Limited in Venus Limited. Solar Limited also has 25% direct equity interest and related voting power in Venus Limited. Thus, Solar Limited controls 55% (30% + 25%) voting power of Venus Limited. As the decisions concerning relevant activities of Venus Limited require a simple majority of votes. Solar Limited controls Venus Limited and should therefore consolidate it in accordance with Ind AS 110.

Although, Solar Limited controls Venus Limited, its entitlement to the subsidiary's economic benefits is determined on the basis of its actual ownership interest. For the purposes of the consolidated financial statements, Solar Limited's share in Venus Limited is determined as 49% [25% + (80% × 30%)]. As a result, 51% of profit or loss, other comprehensive income and net assets of Venus Limited shall be attributed to the non-controlling interests in the consolidated financial statements (this comprises 6% attributable to holders of non-controlling interests in Mars Limited [reflecting 20% interest of non-controlling shareholders of Mars Limited in 30% of Venus Limited] and 45% to holders of non-controlling interests in Venus Limited).

Thanks ....

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IND AS – 32, 107, 109 FINANCIAL INSTREMENTS

CHAPTER - 20

Question 1 : May 2018 – RTP

On 1st April, 20X4, Shelter Ltd. issued 5,000, 8% convertible debentures with a face value of Rs.100 each maturing on 31st March, 20X9. The debentures are convertible into equity shares of Shelter Ltd. at a conversion price of Rs.105 per share. Interest is payable annually in cash. At the date of issue, Shelter Ltd. could have issued non-convertible debt with a 5 year term bearing a coupon interest rate of 12%. On 1st April, 20X7, the convertible debentures have a fair value of Rs.5,25,000. Shelter Ltd. makes a tender offer to debenture holders to repurchase the debentures for Rs.5,25,000, which the holders accepted. At the date of repurchase, Shelter Ltd. could have issued non-convertible debt with a 2 year term bearing a coupon interest rate of 9%. Show accounting entries in the books of Shelter Ltd. for recording of equity and liability component:

(i) At the time of initial recognition and

(ii) At the time of repurchase of the convertible debentures.

The following present values of Rs. 1 at 8%, 9% & 12% are supplied to you:

Interest Rate	Year 1	Year 2	Year 3	Year 4	Year 5
8%	0.926	0.857	0.794	0.735	0.681
9%	0.917	0.842	0.772	0.708	0.65
10%	0.893	0.797	0.712	0.636	0.567

Solution :

(i) At the time of initial recognition

	Rs.
Liability component	
Present value of 5 yearly interest payments of Rs.40,000, discounted at 12% annuity (40,000 x 3.605)	1,44,200
Present value of Rs.5,00,000 due at the end of 5 years, discounted at 12%, compounded yearly (5,00,000 x 0.567)	2,83,500
	4,27,700
Equity component	
(Rs.5,00,000 – Rs.4,27,700)	72,300
Total proceeds	5,00,000

Note:

1) Since rs.105 is the conversion price of debentures into equity shares and not the redemption price, the liability component is calculated @ Rs.100 each only.

Journal Entry

		Rs.	Rs.
Bank	Dr.	5,00,000	
To 8% Debentures (Liability component)			4,27,700
To 8% Debentures (Equity component)			72,300
(Being Debentures are initially recorded a fair value)			

2) Conversion is assumed at option of investor.

(ii) At the time of repurchase of convertible debentures

The repurchase price is allocated as follows:

	Carrying Value @ 12%	Fair Value @ 9%	Difference
	Rs.	Rs.	Rs.
Liability component			
Present value of 2 remaining yearly interest payments of Rs.40,000, discounted at 12% and 9%, respectively	67,600	70,360	
Present value of Rs.5,00,000 due in 2 years, discounted at 12% and 9%, compounded yearly, respectively	3,98,500	4,21,000	
Liability component	4,66,100	4,91,360	(25,260)
Equity component			
(5,25,000 - 4,91,360)	72,300	33,640*	38,660
Total	**5,38,400**	**5,25,000**	**13,400**

*(5,25,000 – 4,91,360) = 33,640

Journal Entries

		Rs.	Rs.
8% Debentures (Liability component)	Dr.	4,66,100	
Profit and loss A/c (Debt settlement expense)	Dr.	25,260	
To Bank A/c			4,91,360
(Being the repurchase of the liability component recognised)			
8% Debentures (Equity component)	Dr.	72,300	
To Bank A/c		33,640	
To Reserves and Surplus A/c			38,660
(Being the cash paid for the equity component recognised)			

Question 2 : May 2018 – PAPER

S Limited issued redeemable preference shares to its Holding Company -H Limited. The terms of the instrument have been summarized below. Analyse the given situation, applying the guidance in Ind AS 109 'Financial Instruments', and account for this in the books of H Limited.

Nature	**Non-cumulative redeemable preference shares**
Repayment	Redeemable after 3 years
Date of Allotment	1st April 2015
Date of Repayment	31st March 2018
Total Period	3 Years
Value of Preference Shares issued	5,00,00,000
Dividend Rate	0.0001% Per Annum
Market rate of interest	12% Per Annum
Present value factor	0.7118

Solution :

Applying Ind AS 109 a financial asset shall be recorded a fair value upon initial recognition.
According fair value of investment in S Ltd. shall be.
50,00,000 × 0.7118 = 3,55,90,000
Note : Divided is ignored as the amount is small making it insignificant.
∴ Balance 5,00,000 = 3,55,90,000 = 1,44,10,000 shall be treated as equity

1.4.2015	Preference shares (FA)	3,55,90,000	
	Investment (Equity)	1,44,10,000	
	To Bank		5,00,00,000

Subsequently preference shares shall be carried over at amortised cost.

Year	Opening Balance	Interest (12%)	CF	C/O.
1	3,55,90,000	42,70,800	-	3,98,60,800
2	3,98,60,800	47,83,296	-	4,46,44,096
3	4,46,44,096	53,55,904	5,00,00,000	-

31.3.16	Preference shares (FA)	42,70,800	
	To Interest		42,70,800
31.3.17	Preference shares (FA)	47,83,296	
	To Interest		47,83,296
31.3.18	Preference shares (FA)	53,55,904	
	To Interest		53,55,904
31.3.18	Bank	5,00,00,000	
	To Preference shares		5,00,00,000

Question 3 : May 2018 – PAPER

On 1st January 2017, Expo Limited agreed to purchase USD ($) 40,000 from E&I Bank in future on 31st December 2017 for a rate equal to Rs. 65 per USD. Expo Limited did not pay any amount upon entering into the contract. Expo Limited is a listed company in India and prepares its financial statements on a quarterly basis.
Using the definition of derivative included in Ind AS 109 and following the principles of recognition and measurement as laid down in Ind AS 109, you are required to record the entries for each quarter ended till the date of actual purchases of USD.
For the purpose of accounting, use the following information representing marked to market fair value of forward contracts at each reporting date:

As at 31st March, 2017	Rs.(50,000)
As at 30th June, 2017	Rs.(30,000)
As at 30th September, 2017	Rs.24,000
Spot rate of USD on 31st December, 2017	Rs.62 per USD

Solution :

1) Assessment of the arrangement using the definition of derivative included under Ind AS 109.

Derivative is a financial instrument or other contract within the scope of this Standard with all three of the following **characteristics**:

(a) its value changes in response to the change in foreign exchange rate (emphasis laid)

(b) it requires no initial net investment or an initial net investment is smaller than would be required for other types of contracts with similar response to changes in market factors.

(c) it is settled at a future date.

Upon evaluation of contract in question, on the basis of the definition of derivative, it is noted that the contract meets the definition of a derivative as follows:

(a) the value of the contract to purchase USD at a fixed price changes in response to changes in foreign exchange rate.

(b) the initial amount paid to enter into the contract is zero. A contract which would give the holder a similar response to foreign exchange rate changes would have required an investment of USD 40,000 on inception.

(c) the contract is settled in future

The derivative is a forward exchange contract.

As per Ind AS 109, derivatives are measured at fair value upon initial recognition and are subsequently measured at fair value through profit and loss.

2) Accounting in each Quarter

(i)	1.1.2017	No Entry	Fair Value is Nil		
(ii)	31.3.2017	Loss (P & L)		50,000	
		To FC (FL)			50,000
(iii)	30.6.2017	FC (FL)		20,000	

		To gain (P & L)		20,000
(iv)	30.9.2017	FC (FL)	30,000	
		FC (FA)	24,000	
		To gain (P & L)		54,000
(v)	31.12.2017	Bank (USD) (40,000 × 62)	24,80,000	
		Loss (P & L)	1,44,000	
		To FC(FA)		24,000
		To Bank (40,000 × 65)		26,00,000

Question 4 : Nov 2018 – PAPER

On 1st April 2017, A Ltd. lent Rs.2 crores to a supplier in order to assist them with their expansion plans. The arrangement of the loan cost the company Rs. 10 lakhs. The company has agreed not to charge interest on this loan to help the supplier's short-term cash flow but expected the supplier to repay Rs.2.40 crores on 31st March 2019. As calculated by the finance team of the company, the effective annual rate of interest on this loan is 6.9% On 28th February 2018, the company received the information that poor economic climate has caused the supplier significant problems and in order to help them, the company agreed to reduce the amount repayable by them on 31st March 2019 to Rs.2.20 crores. Suggest the accounting entries as per applicable Ind AS.

Solution :

The loan to the supplier would be regarded as a financial asset. The relevant accounting standard Ind AS 109 provides that financial assets are normally measured at fair value.

If the financial asset in which the only expected future cash inflows are the receipts of principal and interest and the investor intends to collect these inflows rather than dispose of the asset to a third party, then Ind AS 109 allows the asset to be measured at amortised cost using the effective interest method.

If this method is adopted, the costs of issuing the loan are included in its initial carrying value rather than being taken to profit or loss as an immediate expense. This makes the initial carrying value Rs.2,10,00,000.

Under the effective interest method, part of the finance income is recognised in the current period rather than all in the following period when repayment is due. The income recognised in the current period is Rs.14,49,000 (Rs.2,10,00,000 x 6.9%)

In the absence of information regarding the financial difficulties of the supplier the financial asset at 31st March, 2018 would have been measured at Rs.2,24,49,000 (Rs.2,10,00,000 + 14,49,000).

The information regarding financial difficulty of the supplier is objective evidence that the financial asset suffered impairment at 31st March 2018.

The asset is re-measured at the present value of the revised estimated future cash inflows, using the original effective interest rate. Under the revised estimates the closing carrying amount of the asset would be Rs.2,05,79,981 (Rs.2,20,00,000 / 1.069). The reduction in carrying value of

Rs.18,69,019 (Rs.2,24,49,000 – 2,05,79,981) would be charged to profit or loss in the current period as an impairment of a financial asset.
Therefore, the net charge to profit or loss in respect of the current period would be Rs.4,20,019 (18,69,019 – 14,49,000).

Question 5 : Nov 2018 – PAPER

NAV Limited granted a loan of Rs.120 lakh to OLD Limited for 5 years @ 10% p.a. which is Treasury bond yield of equivalent maturity. But the incremental borrowing rate of OLD Limited is 12%. In this case, the loan is granted to OLD Limited at below market rate of interest. Ind AS 109 requires that a financial asset or financial liability is to be measured at fair value at the initial recognition. Should the transaction price be treated as fair value? If not, find out the fair value. What is the accounting treatment of the difference between the transaction price and the fair value on initial recognition in the book of NAV Ltd.?
Present value factors at 12%:

Year	1	2	3	4	5
PVF	0.892	0.797	0.712	0.636	0.567

Solution :

Since the loan is granted to OLD Ltd at 10% i.e below market rate of 12%. It will be considered as loan given at off market terms. Hence the Fair value of the transaction will be lower from its transaction price & not the transaction price.

Calculation of fair value

Year	Future cash flow (in lakh)	Discounting factor @ 12%	Present value (in lakh)
1	12	0.892	10.704
2	12	0.797	9.564
3	12	0.712	8.544
4	12	0.636	7.632
5	120+12=132	0.567	74.844
			111.288

The fair value of the transaction be Rs.111.288 lakh.
Since fair value is based on level 1 input or valuation technique that uses only data from observable markets, difference between fair value and transaction price will be recognized in Profit and Loss as fair value loss i.e Rs.120 lakh– Rs.111.288 lakh= Rs.8.712 lakh.

Question 6 : Nov 2018 – PAPER

Veer Limited issues convertible bonds of Rs.75,00,000 on 1st April, 2018. The bonds have a life of five years and a face value of Rs.20 each, and they offer interest payable at the end of each financial year at a rate of 4.5 per cent annum. The bonds are issued at their face value and each bond can be converted into one ordinary share in Veer Ltd at any time in the next five years. Companies of a similar risk profile have recently issued debt at 6 per cent per annum with similar terms but without the option for conversion.
You are required to:

(i) Provide the appropriate accounting entries for initial recognition as per the relevant Ind AS in the books of the company.
(ii) Calculate the stream of interest expenses across the five years of the life of the bonds.
(iii) Provide the accounting entries if the holders of the bonds elect to convert the bonds to ordinary shares at the end of the fourth year.

Solution :

Present value of bonds at the market rate of debt

Present value of principal to be received in 5 years discounted at 6% (75,00,000 x 0.747)	=	56,02,500
Present value of interest stream discounted at 6% for 5 years (3,37,500 x4.212)	=	14,21,550
Total present value	=	70,24,050
Equity component	=	4,75,950
Total face value of convertible bonds	=	75,00,000

(i) **Journal Entries**

		Dr. (Rs.)	Cr. (Rs.)
1st April, 2018	Dr.	75,00,000	
Cash			70,24,050
To Convertible bonds (liability)			4,75,950
To Convertible bonds (equity component)			
(Being entry to record the convertible bonds and the recognition of the liability and equity components)			
31st March, 2019			
Interest expense	Dr.	4,21,443	
To Cash			3,37,500
To Convertible bonds (liability)			83,943
(Being entry to record the interest expense)			

(ii) The stream of interest expense is summarised below, where interest for a given year is calculated by multiplying the present value of the liability at the beginning of the period by the market rate of interest, this is being 6 per cent.

Date	Payment	Interest expense at 6% (e of previous year x 6%)	Increase in bond liability (c-b)	Total bond liability (e of previous year +d)
(a)	(b)	(c)	(d)	(e)
1st April, 2018				70,24,050
31st March, 2019	3,37,500	4,21,443	83,943	71,07,993
31st March, 2020	3,37,500	4,26,480	88,980	71,96,973
31st March, 2021	3,37,500	4,31,818	94,318	72,91,291

31st March, 2022	3,37,500	4,37,477	99,977	73,91,268
31st March, 2023	3,37,500	4,46,232*	1,08,732	75,00,000

* Difference is due to rounding off.

(iii) If the holders of the bond elect to convert the bonds to ordinary shares at the end of the fourth year (after receiving their interest payments), the entries in the fourth year would be:

		Dr.(Rs.)	Cr.(Rs.)
<u>31st March, 2022</u>			
Interest expense A/c	Dr.	4,37,477	
To Cash A/c			3,37,500
To Convertible bonds (liability) A/c			99,977
(Being entry to record interest expense for the period)			
<u>31st March, 2022</u>	-		
Convertible bonds (liability) A/c	Dr.	73,91,268	
Convertible bonds (equity component) A/c	Dr.	4,75,950	
To Ordinary share capital A/c			78,67,218
(Being entry to record the conversion of bonds into ordinary shares of Veer Limited).			

Question 7 : Nov 2018 – PAPER

Growth Limited on 1st April, 2015 issued 50,000, 7% convertible debentures of face value of Rs.100 per debenture at par. The debentures are redeemable at a premium of 10% on 31st March, 2020 or these may be converted into ordinary shares at the option of the holder. The interest rate for equivalent debentures without conversion rights would have been 10%. The date of transition to Ind AS is 1st April, 2017.

Suggest how Growth Limited should account for this compound financial instrument on the date of transition. Also discuss Ind AS on 'Financial Instrument' presentation in the above context.

The present value of Rs.1 receivable at the end of each year based on discount rates of 7% and 10% can be taken as:

End of Year	1	2	3	4	5
7%	0.94	0.87	0.82	0.76	0.71
10%	0.91	0.83	0.75	0.68	0.62

Solution :

Since the liability is outstanding on the date of Ind AS transition, Growth Ltd. is required to split the convertible debentures into debt and equity portion on the date of transition. Accordingly, first the liability component will be measured discounting the contractually determined stream of future cash flows (interest and principal) to present value by using the discount rate of 10% p.a. (being the market interest rate for similar debentures with no conversion option).

Calculation of Equity & Liability component on initial recognition

	Rs.
Present Interest payments for 5 years on debentures by applying annuity factor [(50,000 × 7% × 100) × 3.79]	13,26,500
PV of principal repayment (including premium) (50,000 × 110 × 0.62)	34,10,000
Total liability component	47,36,500
Total equity component (Balancing figure)	2,63,500
Total proceeds from issue of Debentures	50,00,000

Thus, on the date of transition, the amount of Rs.50,00,000 being the amount of debentures will split as under:

Debt	Rs.47,36,500
Equity	Rs.2,63,500

Question 8 : May 2019 – RTP

KK Ltd. has granted an interest free loan of Rs.10,00,000 to its wholly owned Indian Subsidiary YK Ltd. There is no transaction cost attached to the said loan. The Company has not finalised any terms and conditions including the applicable interest rates on such loans. The Board of Directors of the Company are evaluating various options and has requested your firm to provide your views under Ind AS in following situations:

(i) The Loan given by KK Ltd. to its wholly owned subsidiary YK Ltd. is interest free and such loan is repayable on demand.

(ii) The said Loan is interest free and will be repayable after 3 years from the date of granting such loan. The current market rate of interest for similar loan is 10%. Considering the same, the fair value of the loan at initial recognition is Rs.8,10,150.

(iii) The said loan is interest free and will be repaid as and when the YK Ltd. has funds to repay the Loan amount.

Based on the same, KK Ltd. has requested you to suggest the accounting treatment of the above loan in the stand-alone financial statements of KK Ltd. and YK Ltd. and also in the consolidated financial statements of the group. Consider interest for only one year for the above loan.

Further the Company is also planning to grant interest free loan from YK Ltd. to KK Ltd. in the subsequent period. What will be the accounting treatment of the same under applicable Ind AS?

Solution :

Scenario (i)

Since the loan is repayable on demand, it has fair value equal to cash consideration given. KK Ltd. and YK Ltd. should recognize financial asset and liability, respectively, at the amount of loan given (assuming that loan is repayable within a year). Upon, repayment, both the entities should reverse the entries that were made at the origination.

Journal entries in the books of KK Ltd.

At origination Loan to YK Ltd. A/c To Bank A/c On repayment	 Dr.	 Rs.10,00,000	 Rs.10,00,000

Bank A/c	Dr.	Rs.10,00,000	
To Loan to YK Ltd. A/c			Rs.10,00,000

Journal entries in the books of YK Ltd.

At origination			
Bank A/c	Dr.	Rs.10,00,000	
To Loan from KK Ltd.			Rs.10,00,000
On repayment			
Loan from KK Ltd. A/c	Dr.	Rs.10,00,000	
To Bank A/c			Rs.10,00,000

In the consolidated financial statements, there will be no entry in this regard since loan receivable and loan payable will get set off.

Scenario (ii)

Applying the guidance in Ind AS 109, a 'financial asset' shall be recorded at its fair value upon initial recognition. Fair value is normally the transaction price. However, sometimes certain type of instruments may be exchanged at off market terms (ie, different from market terms for a similar instrument if exchanged between market participants).

If a long-term loan or receivable that carries no interest while similar instruments if exchanged between market participants carry interest, then fair value for such loan receivable will be lower from its transaction price owing to the loss of interest that the holder bears. In such cases where part of the consideration given or received is for something other than the financial instrument, an entity shall measure the fair value of the financial instrument. The difference in fair value and transaction cost will treated as investment in Subsidiary YK Ltd.

Both KK Ltd. and YK Ltd. should recognise financial asset and liability, respectively, at fair value on initial recognition, i.e., the present value of Rs.10,00,000 payable at the end of 3 years using discounting factor of 10%. Since the question mentions fair value of the loan at initial recognition as Rs.8,10,150, the same has been considered. The difference between the loan amount and its fair value is treated as an equity contribution to the subsidiary. This represents a further investment by the parent in the subsidiary.

Journal entries in the books of KK Ltd. (for one year)

At origination			
Loan to YK Ltd. A/c	Dr.	Rs.8,10,150	
Investment in YK Ltd. A/c	Dr.	Rs.1,89,850	
To Bank A/c			Rs.10,00,000
During period to repayment – to recognise interest			

Year 1 – Charging of Interest

At origination			
Loan to YK Ltd. A/c	Dr.	Rs.81,015	
To Interest income A/c			Rs.81,015

Transferring of interest to Profit and Loss

Interest income A/c	Dr.	Rs.81,015	
To Profit and Loss A/c			Rs.81,015
On repayment			
Bank A/c	Dr.	Rs.10,00,000	
To Loan to YK Ltd. A/c			Rs.10,00,000

Note- Interest needs to be recognised in statement of profit and loss. The same cannot be adjusted against capital contribution recognised at origination.

Journal entries in the books of YK Ltd. (for one year)

At origination			
Bank A/c	Dr.	Rs.10,00,000	
To Loan from KK Ltd. A/c			Rs.8,10,150
To Equity Contribution in KK Ltd. A/c			Rs.1,89,850
During period to repayment – to recognise interest			
Year 1			
Interest expense A/c	Dr.	Rs.81,015	
To Loan from KK Ltd. A/c			Rs.81,015
On repayment			
Loan from KK Ltd. A/c	Dr.	Rs.10,00,000	
To Bank A/c			Rs.10,00,000

In the consolidated financial statements, there will be no entry in this regard since loan and interest income/expense will get set off.

Scenario (iii)

Generally, a loan which is repayable when funds are available, cannot be stated as loan repayable on demand. Rather the entity needs to estimate the repayment date and determine its measurement accordingly by applying the concept prescribed in Scenario (ii).

In the consolidated financial statements, there will be no entry in this regard since loan and interest income/expense will get set off.

In case the subsidiary YK Ltd. is planning to grant interest free loan to KK Ltd., then the difference between the fair value of the loan on initial recognition and its nominal value should be treated as dividend distribution by YK Ltd. and dividend income by the parent KK Ltd.

Question 9 : Nov 2019 – RTP

An entity purchases a debt instrument with a fair value of Rs.1,000 on 15th March, 20X1 and measures the debt instrument at fair value through other comprehensive income. The instrument has an interest rate of 5% over the contractual term of 10 years, and has a 5% effective interest rate. At initial recognition, the entity determines that the asset is not a purchased or original credit-impaired asset.

On 31st March 20X1 (the reporting date), the fair value of the debt instrument has decreased to Rs.950 as a result of changes in market interest rates. The entity determines that there has not been a significant increase in credit risk since initial recognition and that ECL should be measured at an amount equal to 12 month ECL, which amounts to Rs.30.

On 1st April 20X1, the entity decides to sell the debt instrument for Rs.950, which is its fair value at that date.

Pass journal entries for recognition, impairment and sale of debt instruments as per Ind AS 109. Entries relating to interest income are not to be provided.

Solution :

On initial recognition

		Debit (Rs.)	Credit (Rs.)
Financial asset-FVOCI	Dr.	1,000	
To Cash			1,000

On Impairment of debt instrument

		Debit (Rs.)	Credit (Rs.)
Impairment expense (P & L)	Dr.	30	
Other comprehensive income	Dr.	20	
To Financial asset-FVOCI			50

The cumulative loss in other comprehensive income at the reporting date was Rs.20. That amount consists of the total fair value change of Rs.50 (that is, Rs.1,000 – Rs.950) offset by the change in the accumulated impairment amount representing 12-month ECL, that was recognized (Rs.30).

On Sale of debt instrument

	Debit (Rs.)	Credit (Rs.)
Cash	950	
To Financial asset – FVOCI		950
Loss on sale (P & L)	20	
To Other compressive income		20

Question 10 : Nov 2019 – PAPER

Vedika Ltd. issued 80,000 8% convertible debentures @ Rs.100 each on 1st April, 2015. The debentures are due for redemption on 31st March, 2019 at a premium of 20%, convertible into equity shares to the extent of 50% and balance to be settled in cash to the debenture holders. The interest rate on equivalent debenture without conversion right was 12%. The conversion to equity qualifies as fixed for fixed.

You are required to separate the debt and equity component at the time of use and show the accounting entries in Vedika Ltd.'s books at initial recognition only. The following present values of Rupee 1 at 8% and 12% are provided for a period of 5 years.

Interest Rate	Year 1	Year 2	Year 3	Year 4	Year 5
8%	0.923	0.853	0.789	0.731	0.677
12%	0.887	0.788	0.701	0.625	0.557

Solution :

In the books of Vedika Ltd.

Convertible debentures issued by Vedika are compound financial instrument. As per Ind AS 109, entity should separate debt from equity and account accordingly.

Debt – FL

Year	CF		PV @ 12%
31/3/16	6,40,000	Int. @ 8%	5,67,680
31/3/17	6,40,000	Int. @ 8%	5,04,320
31/3/18	6,40,000	Int. @ 8%	4,48,640
31/3/19	6,40,000	Int. @ 8%	4,00,000
	40,00,000	50% Principal	25,00,000
	8,00,000	POR 20%	5,00,000
			49,20,640

Equity = TL – FL

= 80,00,000 – 49,20,640 = 30,79,360

Bank A/c	Dr.	80,00,000	
To Debt (FL)			49,20,640
To Equity			30,79,360

Question 11 : Nov 2019 – PAPER

Make necessary journal entries for accounting of the security deposit made by Admire Ltd., whose details are described below. Assume market interest rate for a deposit for similar period to be 12% per annum.

Particulars	**Details**
Date of Security Deposit (Starting Date)	1-Apr-2014
Date of Security Deposit (Finishing Date)	31-Mar-2019
Description	Lease
Total Lease Period	5 years
Discount rate	12.00%
Security deposit (A)	20,00,000
Present value factor at the 5^{th} year	0.567427

Solution :

1) As per IND AS 109, security deposit is an interest free deposit redeemable at end of lease term for Rs.20,00,000. Hence business model is to collect contractual cash flow and shall be accounted for at amortised cost.

2) Deposit should initially be recorded at fair value i.e. $\frac{20,00,000}{(1.12)^5}$ = 11,34,854

Security deposit (FA) 11,34,854

Prepaid lease Exp. (P/L)	8,65,146	
To Bank		20,00,000

3) Deposit should be subsequently carried over at amortised cost

Year	OP	Interest (12%)	Closing
1	11,34,854	1,36,183	12,71,037
2	12,71,037	1,52,524	14,23,561
3	14,23,561	1,70,827	15,94,388
4	15,94,388	1,91,327	17,85,7158
5	17,85,715	2,14,685	20,00,000

Question 12 : May 2020 – RTP

XYZ issued RS.4,80,000 4% redeemable preference shares on 1st April 20X5 at par. Interest is paid annually in arrears, the first payment of interest amounting RS.19,200 was made on 31st March 20X6 and it is debited directly to retained earnings by accountant. The preference shares are redeemable for a cash amount of Rs.7,20,000 on 31st March 20X8. The effective rate of interest on the redeemable preference shares is 18% per annum. The proceeds of the issue have been recorded within equity by accountant as this reflects the legal nature of the shares. Board of directors intends to issue new equity shares over the next two years to build up cash resources to redeem the preference shares.

Mukesh, Accounts manager of XYZ has been told to review the accounting of aforesaid issue. CFO has asked from Mukesh the closing balance of preference shares at the year end. If you were Mukesh, then how much balance you would have shown to CFO on analysis of the stated issue. Prepare necessary adjusting journal entry in the books of account, if required.

Solution :

The preference shares provide the holder with the right to receive a predetermined amount of annual dividend out of profits of the company, together with a fixed amount on redemption.

Whilst the legal form is equity, the shares are in substance debt. The fixed level of dividend is interest and the redemption amount is equivalent to the repayment of a loan.

Under Ind AS 32 'Financial Instruments: Presentation' these instruments should be classified as financial liabilities because there is a contractual obligation to deliver cash. The preference shares should be accounted for at amortised cost using the effective interest rate of 18%.

Year	1 April, 20X5 Rs.	Interest @18% Rs.	Paid at 4% Rs.	31 March, 20X6 Rs.
20X5 - 20X6	4,80,000	86,400	(19,200)	5,47,200

Accordingly, the closing balance of Preference shares at year end i.e. 31st March, 20X6 would be Rs.5,47,200.

Accountant has inadvertently debited interest of Rs.19,200 in the profit and loss. However, the interest of Rs.86,400 should have been debited to profit and loss as finance charge.

Similarly, amount of Rs.5,47,200 should be included in borrowings (non-current liabilities) and consequently, Equity should be reduced by Rs.480,000 proceeds of issue and Rs.67,200 (86,400 – 19,200) i.e. total by 5,47,200.

Necessary adjusting journal entry to rectify the books of accounts will be:

		Rs.	Rs.
Preference share capital (equity) (Balance sheet)	Dr.	4,80,000	
Finance costs (Profit and loss)	Dr.	86,400	
To Equity – Retained earnings (Balance sheet)			19,200
To Preference shares (Long-term Borrowings) (Balance sheet)			5,47,200

Question 13 : Nov 2020 – Paper

On 1 April 2020, Star Limited has advanced a housing loan of Rs.15 lakhs to one of its employee at an interest rate of 6% per annum which is repayable in 5 equal annual installments along with interest at each year end. Employee is not required to give any specific performance against this benefit. The market rate of similar loan for housing finance by banks is 10% per annum.

The accountant of the company has recognized the staff loan in the balance sheet equivalent to the amount of housing loan disbursed i.e. Rs.15 lakhs. The interest income for the year is recognized at the contracted rate in the Statement of Profit and Loss by the company i.e. Rs.90,000 (6% of Rs.15 lakhs).

Analyze whether the above accounting treatment made by the accountant is in compliance with the relevant Ind AS. If not, advise the correct treatment of housing loan, interest and other expenses in the financial statements of Star Limited for the year 2020-2021 along with workings and applicable Ind AS.

You are required to explain how the housing loan should be reflected in the Ind AS compliant Balance Sheet of Star Limited on 31 March 2021.

Solution :

The accounting treatment made by the accountant is not in compliance with Ind AS 109 'Financial Instruments'. As per Ind AS 109, at initial recognition, an entity shall measure a financial asset or financial liability at its fair value. The fair value of a financial instrument at initial recognition is normally the transaction price i.e. the fair value of the consideration given or received.

After initial recognition, an entity shall measure a financial asset either at amortised cost or at fair value through profit and loss or fair value through other comprehensive income.

Here, the loan given to employee is not at market rate. Hence, the fair value of the loan will not be equal to its initial loan proceeds. As per Ind AS 109, a financial instrument is initially measured and recorded in the books at its fair value. Further, interest income to be recognised in the Statement of Profit and Loss will be the finance income recognised at effective rate of interest i.e. @ 10% and not the rate of interest charged by the company i.e. @ 6%.

The correct accounting treatment as per Ind AS 109 will be as under:

For measuring the fair value or present value of the loan at initial recognition, market rate of interest of similar loan is considered (level 1 observable input) ie @ 10%, to discount the cash outflows.

The fair value of the loan shall be as follows:

Date	Outstanding loan	Principal	Interest income @ 6%	Total inflow	Discount factor @ 10%	PV
31-Mar-21	15,00,000	3,00,000	90,000	3,90,000	0.909	3,54,510
31-Mar-22	12,00,000	3,00,000	72,000	3,72,000	0.826	3,07,272
31-Mar-23	9,00,000	3,00,000	54,000	3,54,000	0.751	2,65,854
31-Mar-24	6,00,000	3,00,000	36,000	3,36,000	0.683	2,29,488
31-Mar-25	3,00,000	3,00,000	18,000	3,18,000	0.621	1,97,478
Fair value of the loan						13,54,602

As per Ind AS 19, employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees or for termination of employment. Difference of loan proceeds and present value of the loan (fair value) will be treated as prepaid employee cost irrespective of the fact that employee is not required to give any specific performance against this benefit. This is because employee is required to be in service of the company to continue availing the benefits of concessional rate of interest on housing loan. Practically, once the employee leaves the organisation, they have to repay the outstanding loan because the company provides the loan at concessional rate of interest only to its employees.

Hence, it is an employee benefit given by the company to its employees. This deemed employee cost of Rs. 1,45,398 (15,00,000 – 13,54,602) will be deferred and amortised over the period of loan on straight line basis.

Calculation of amortised cost of loan to employees

Financial year ending on 31 March	Amortised cost (opening balance)	Interest to be recognised @ 10%	Repayment (including interest)	Amortised cost (closing balance)
2021	13,54,602	1,35,460	3,90,000	11,00,062
2022	11,00,062	1,10,006	3,72,000	8,38,068
2023	8,38,068	83,807	3,54,000	5,67,875
2024	5,67,875	56,788	3,36,000	2,88,663
2025	2,88,663	29,337*	3,18,000	-

* 2,88,663 x 10% = Rs. 28,866. Difference of Rs. 471 (29,337 – 28,866) is due to approximation in computation.

Journal Entries to be recorded at every period end:

1. On 1 April 2020

Particulars		Dr. Amount (Rs.)	Cr. Amount (Rs.)
Loan to employee A/c	Dr.	13,54,602	
Prepaid employee cost A/c	Dr.	1,45,398	
To Bank A/c			15,00,000
(Being loan asset recorded at initial fair value)			

2. On 31 March 2021

Particulars		**Dr. Amount (Rs.)**	**Cr. Amount (Rs.)**
Bank A/c	Dr.	3,90,000	
To Finance income A/c (profit and loss) @10%			1,35,460
To Loan to employee A/c			2,54,540
(Being first instalment of repayment of loan accounted for using the amortised cost and effective interest rate @ 10%)			
Employee benefit cost (profit and loss) A/c	Dr.	29,080	
To Prepaid employee cost A/c (1,45,398/5)			29,080
(Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)			

The Following housing loan balances should appear in the financial statements:

Extracts of Balance sheet of Star Ltd. as at 31 March 2021

Non-current asset	
Financial asset	
Loan to employee (11,00,062 – 3,72,000 + 1,10,006)	8,38,068
Other non-current asset	
Prepaid employee cost	87,238
Current asset	
Financial asset	
Loan to employee (3,72,000-1,10,006)	2,61,994
Other current asset	
Prepaid employee cost	29,080

Deferred tax on temporary differences arising on the above-mentioned account balances (appearing in the balance sheet) should be recognised. However, in the absence of any tax rate in the question no deferred tax has been recognised.

Question 14 : Nov 2020 – Paper

On 1 April 2019, 8% convertible loan with a nominal value of Rs. 12,00,000 was issued at par by Cargo Ltd. It is redeemable on 31 March 2023 also at par. Alternatively, it may be converted into equity shares on the basis of 100 new shares for each Rs. 200 worth of loan.

An equivalent loan without the conversion option would have carried interest at 10%. Interest of Rs. 96,000 has already been paid and included as a finance cost.

Present Value (PV) rates are as follows:

Year End	@ 8%	@ 10%
1	0.93	0.91
2	0.86	0.83
3	0.79	0.75
4	0.73	0.68

How will the Company present the above loan notes in the financial statements for the year ended 31 March 2020?

Solution :

There are both 'equity' and 'debt' features in the instrument. An obligation to pay cash i.e. interest at 8% per annum and a redemption amount will be treated as 'financial liability' while option to convert the loan into equity shares is the equity element in the instrument. Therefore, convertible loan is a compound financial instrument.

Calculation of debt and equity component and amount to be recognised in the books:

S. No	Year	Interest amount @ 8%	Discounting factor @ 10%	Amount
Year 1	2020	96,000	0.91	87,360
Year 2	2021	96,000	0.83	79,680
Year 3	2022	96,000	0.75	72,000
Year 4	2023	12,96,000*	0.68	8,81,280
Amount to be recognised as a liability				11,20,320
Initial proceeds				(12,00,000)
Amount to be recognised as equity				79,680

* In year 4, the loan note will be redeemed; therefore, the cash outflow would be Rs. 12,96,000 (Rs. 12,00,000 + Rs. 96,000).

Presentation in the Financial Statements:

In Statement of Profit and Loss for the year ended on 31 March 2020

Finance cost to be recognised in the Statement of Profit and Loss (11,20,320 x 10%)	Rs. 1,12,032
Less: Already charged to the income statement	(Rs. 96,000)
Additional finance charge required to be recognised in the Statement of Profit and Loss	Rs. 16,032

In Balance Sheet as at 31 March 2020

Equity and Liabilities	
Equity	
Other Equity (8% convertible loan)	79,680
Non-current liability	
Financial liability [8% convertible loan – [(11,20,320 + 1,12,032 – 96,000)]	11,36,352

Question 15 : Jan 2021 – Paper

Lovely Limited has a policy of providing subsidized loans to its employees for the purpose of buying 2 Wheelers and 4 Wheelers vehicle. Simran who is a Sales Executive, took a loan for a Four-wheeler vehicle from the Company. The following were the terms of the loan:

- Principal Amount : Rs.9,00,000
- Interest: 5% p.a. for the First Rs.3,00,000 and 8% p.a. for the remaining amount.
- Loan disbursed date: 1st April 2017
- Loan Tenure: 3 Years
- Pre-Payment : Full or Partial payment at the option of the employee.
- Simran shall remain in service till the term of the loan ends.
- The Principal amount should be recovered in 3 equal installments at the end of each year and will be first applied to 8% interest bearing principal.
- The accrued interest shall be paid on annual basis.

The market rate of a comparable loan available to Simran is 12% per annum.
Following table shows the expected contractual cash flows from the loan given to Simran.

(In Rs.)

		Inflows			
Date	**Outflows**	**Principal**	**Interest Income 8%**	**Interest Income 5%**	**Principal Outstanding**
01.04.2017	(9,00,000)				9,00,000
31.03.2018		3,00,000	48,000	15,000	6,00,000
31.03.2019		3,00,000	24,000	15,000	3,00,000
31.03.2020		3,00,000	-	15,000	-

Simran pre-pays Rs.1,00,000 on 31st March, 2019.
Following table shows the actual cash flows from the loan, considering the prepayment on 31st March 2019.

(In Rs.)

		Inflows			
Date	**Outflows**	**Principal**	**Interest Income 8%**	**Interest Income 5%**	**Principal Outstanding**
01.04.2017	(9,00,000)				9,00,000
31.03.2018		3,00,000	48,000	15,000	6,00,000
31.03.2019		4,00,000	24,000	15,000	2,00,000
31.03.2020		2,00,000	-	10,000	-

You are required to pass journal entries in the books of Lovely Limited considering the requirements of Ind AS 109.

Solution :

As per requirement of Ind AS 109, a financial instrument is initially measured and recorded at its fair value. Therefore, considering the market rate of interest of similar loan available to Simran is 12%, the fair value of the contractual cash flows shall be as follows:

Amount in Rs.

	Inflows					
Date	**Principal**	**Interest income 8%**	**Interest income 5%**	**Total inflow**	**Discount factor @ 12%**	**PV**
31.03.2018	3,00,000	48,000	15,000	3,63,000	0.893	3,24,159
31.03.2019	3,00,000	24,000	15,000	3,39,000	0.797	2,70,183
31.03.2020	3,00,000	-	15,000	3,15,000	0.712	2,24,280
Total (fair value)						8,18,622

Benefit to Simran, to be considered as part of employee cost for Lovely Ltd. Rs.81,378 (9,00,000 – 8,18,622).

The deemed employee cost is to be amortised over the period of loan i.e. the minimum period that Simran must remain in service.

The amortization schedule of the Rs.8,18,622 loan is shown in the following table:

Amount in Rs.

Date	**Opening outstanding Loan**	**Total cash inflows (principal repayment + interest)**	**Interest @ 12%**	**Closing outstanding Loan**
01.04.2017	8,18,622			8,18,622
31.03.2018	8,18,622	3,63,000	98,235	5,53,857
31.03.2019	5,53,857	3,39,000	66,463	2,81,320
31.03.2020	2,81,320	3,15,000	33,680*	Nil

* Difference is due to approximation of discounting factor and interest amount.

Journal Entries to be recorded at every period end:

a. 1 April 2017 –

Particulars		**Dr. (Rs.)**	**Cr. (Rs.)**
Loan to employee A/c	Dr.	8,18,622	
Pre-paid employee cost A/c	Dr.	81,378	
To Bank A/c			9,00,000
(Being loan asset recorded at initial fair value)			

b. 31 March 2018 –

Particulars		**Dr. (Rs.)**	**Cr. (Rs.)**
Bank A/c	Dr.	3,63,000	
To Interest income A/c			98,235
To Loan to employee A/c			2,64,765

(Being first instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)			
Employee benefit A/c To Pre-paid employee cost A/c (Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost on straight line basis)	Dr.	27,126	 27,126

c. On 31 March 2019, due to pre-payment of a part of loan by Simran, the carrying value of the loan shall be re-computed by discounting the future remaining cash flows by the original effective interest rate.

There shall be two sets of accounting entries on 31 March 2019, first the realisation of the contractual cash flow as shown below and then the accounting for the prepayment of Rs.1,00,000 included in (d) below:

31 March 2019 –

Particulars		**Dr. (Rs.)**	**Cr. (Rs.)**
Bank A/c To Interest income A/c To Loan to employee A/c (Being second instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)	Dr.	3,39,000	 66,463 2,72,537
Employee benefit (profit and loss) A/c To Pre-paid employee cost A/c (Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)	Dr.	27,126	 27,126

Computation of new carrying value of loan to employee:

	Inflows				
Date	**Principal**	**Interest income 8%**	**Interest income 5%**	**Discount factor @12%**	**PV**
31.03.2020	2,00,000	-	10,000	0.893	1,87,530
Total (revised carrying value)					1,87,530
Less: Current carrying value					2,81,320)
Adjustment required					93,790

The difference between the amount of pre-payment and adjustment to loan shall be considered a gain, though will be recorded as an adjustment to pre-paid employee cost, which shall be amortised over the remaining tenure of the loan.

d. 31 March 2019 prepayment–

Particulars		Dr. (Rs.)	Cr. (Rs.)
Bank A/c	Dr.	1,00,000	
To Pre-paid employee cost A/c			6,210
To Loan to employee A/c			93,790
(Being gain to Lovely Limited recorded as an adjustment to pre-paid employee cost)			

The amortisation schedule of the new carrying amount of loan shall be as follows:

Date	Loan outstanding	Total cash inflows (principal repayment + interest)	Interest @ 12%
31.03.2019	1,87,530		
31.03.2020	-	2,10,000	22,470

Amortisation of employee benefit cost shall be as follows:

Date	Opening Balance	Amortised to P & L	Adjustment	Closing balance
01.04.2017	81,378	27,126		81,378
31.03.2018	81,378	27,126		54,252
31.03.2019	54,252	20,916	6,210	20,916
31.03.2020	20,916			Nil

e. 31 March 2020 –

Particulars		Dr. (Rs.)	Cr. (Rs.)
Bank A/c	Dr.	2,10,000	
To Interest income (profit and loss) @ 12% A/c			22,470
To Loan to employee A/c			1,87,530
(Being last instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)			
Employee benefit (profit and loss) A/c	Dr.	20,916	
To Pre-paid employee cost A/c			20,916
(Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)			

Question 16 : Jan 2021 – Paper

Jewels Ltd. entered into a transaction to purchase 1,000 gms of platinum on 15th January, 2020. The transaction provides for a price payable which is equal to market value of 1,000 gms of platinum on 15th April 2020 and shall be settled by issue of such number of equity shares as is required to settle the aforementioned transaction, at a price of Rs.100 per share on 15th April

2020. Whether this is to be classified as liability or equity as on 31st March 2020 as per Ind AS 109?
You are required to explain with reasons.

Solution :
There is a contract for purchase of 1,000 gms of platinum whose consideration varies in response to changing value of platinum. Analysing this contract as a derivative with all three of the following characteristics:
(a) Value of contract changes in response to change in market value of platinum;
(b) There is no initial net investment
(c) It will be settled at a future date, i.e. 15th April 2020.
Since the above criteria are met, this is a derivative contract.
Now, a derivative contract that is settled in own equity other than exchange of fixed amount of cash for fixed number of shares is classified as 'liability'. In this case, since the contract results in issue of variable number of shares based on transacti on price to be determined in future, hence, this shall be classified as 'derivative financial liability' as per Ind AS 109.

Question 17 : May 2021 – RTP
On 1 April 20X1, Sun Limited guarantees a Rs.10,00,000 loan of Subsidiary – Moon Limited, which Bank STDK has provided to Moon Limited for three years at 8%.
Interest payments are made at the end of each year and the principal is repaid at the end of the loan term.
If Sun Limited had not issued a guarantee, Bank STDK would have charged Moon Limited an interest rate of 11%. Sun Limited does not charge Moon Limited for providing the guarantee.
On 31 March 20X2, there is 1% probability that Moon Limited may default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited.
On 31 March 20X3, there is 3% probability that Moon Limited may default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited.
Provide the accounting treatment of financial guarantee as per Ind AS 109 in the books of Sun Ltd., on initial recognition and in subsequent periods till 31 March 20X3.

Solution :
1 April 20X1
A financial guarantee contract is initially recognised at fair value. The fair value of the guarantee will be the present value of the difference between the net contractual cash flows required under the loan, and the net contractual cash flows that would have been required without the guarantee.

Particulars	Year 1 (Rs.)	Year 2 (Rs.)	Year 3 (Rs.)	Total (Rs.)
Cash flows based on interest rate of 11% (A)	1,10,000	1,10,000	1,10,000	3,30,000
Cash flows based on interest rate of 8% (B)	80,000	80,000	80,000	2,40,000

Interest rate differential (A-B)	30,000	30,000	30,000	90,000
Discount factor @ 11%	0.901	0.812	0.731	
Interest rate differential discounted at 11%	27,030	24,360	21,930	73,320
Fair value of financial guarantee contract (at inception)				**73,320**

Journal Entry

Particulars	**Debit (Rs.)**	**Credit (Rs.)**
Investment in subsidiary Dr. To Financial guarantee (liability) (Being financial guarantee initially recorded)	73,320	 73,320

31 March 20X2

Subsequently at the end of the reporting period, financial guarantee is measured at the higher of:

- the amount of loss allowance; and
- the amount initially recognised less cumulative amortization, where appropriate.

At 31 March 20X2, there is 1% probability that Moon Limited may default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited. The 12-month expected credit losses are therefore Rs.10,000 (Rs.10,00,000 x 1%).

The initial amount recognised less amortisation is Rs.51,385 (Rs.73,320 + Rs.8,065 (interest accrued based on EIR)) – Rs.30,000 (benefit of the guarantee in year 1) Refer table below. The unwound amount is recognised as income in the books of Sun Limited, being the benefit derived by Moon Limited not defaulting on the loan during the period.

Year	**Opening balance Rs.**	**EIR @ 11%**	**Benefits provided Rs.**	**Closing balance Rs.**
1	73,320	8,065	(30,000)	51,385
2	51,385	5,652	(30,000)	27,037
3	27,037	2,963*	(30,000)	-

* Difference is due to approximation

The carrying amount of the financial guarantee liability after amortisation is therefore Rs. 51,385, which is higher than the 12-month expected credit losses of Rs. 10,000. The liability is therefore adjusted to Rs. 51,385 (the higher of the two amounts) as follows:

Particulars	**Debit (Rs.)**	**Credit (Rs.)**
Financial guarantee (liability) Dr. To Profit or loss	21,935	 21,935

(Being financial guarantee subsequently adjusted)		

31 March 20X3

At 31 March 20X3, there is 3% probability that Moon Limited will default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited. The 12-month expected credit losses are therefore Rs. 30,000 (Rs. 10,00,000 x 3%).

The initial amount recognised less accumulated amortisation is Rs. 27,037, which is lower than the 12-month expected credit losses (Rs. 30,000). The liability is therefore adjusted to Rs. 30,000 (the higher of the two amounts) as follows:

Particulars	**Debit (Rs.)**	**Credit (Rs.)**
Financial guarantee (liability) Dr.	21,385*	
To Profit or loss (Note)		21,385
(Being financial guarantee subsequently adjusted)		

* The carrying amount at the end of 31 March 20X2 = Rs. 51,385 less 12-month expected credit losses of Rs. 30,000.

Question 18 : July 2021 – Paper

Softech Limited has a policy of providing subsidized loans to its employees for the purpose of buying or construction of residential houses. Mrs.B is Senior Manager in the Company. The Company granted a loan to her on the following terms :

- Principal amount : Rs.25 lakhs
- Interest rate : 4% for the first Rs.10 lakhs and 7% for the next Rs.15 lakhs.
- Loan disbursed on : 1st January, 2019
- Tenure : 5 years
- Pre payment : Full or partial pre-payment at the option of the employee.
- The principal amount of loan shall be recovered in 5 equal instalments and will be first applied to 7% interest bearing principal
- The accrued interest shall be paid on an annual basis.
- Mrs.B must remain in service till the term of the loan ends.
- The market rate of comparable loan available to Mrs.B, is 12% per annum.
- Give your calculations by adopting the present value factor as :

31.12.2019	31.12.2020	31.12.2021	31.12.2022	31.12.2023
0.8929	0.792	0.7118	0.6355	0.5674

Following table shows the contractually expected cash flows from the loan given to Mrs.B.

(Amount in Rs.)

Date	**Outflows**	**Inflows**			**Principal outstanding**
		Principal	**Interest income (7%)**	**Interest income (4%)**	

1st January 2019	(25,00,000)				25,00,000
31st December, 2019		5,00,000	1,05,000	40,000	20,00,000
31st December, 2020		5,00,000	70,000	40,000	15,00,000
31st December, 2021		5,00,000	35,000	40,000	10,00,000
31st December, 2022		5,00,000	–	40,000	5,00,000
31st December, 2023		5,00,000	–	20,000	–

Mrs.B pre-pays Rs.5,00,000 on 31st December 2020, reducing the outstanding principal as on date to Rs.10,00,000.

Following table shows the actual cash flows from the loan given to Mrs.B, considering the pre-payment event on 31st December, 2020 :

(Amount in Rs.)

Date	Outflows	Inflows			Principal outstanding
		Principal	Interest income (7%)	Interest income (4%)	
1st January 2019	(25,00,000)				25,00,000
31st December, 2019		5,00,000	1,05,000	40,000	20,00,000
31st December, 2020		10,00,000	70,000	40,000	10,00,000
31st December, 2021		5,00,000	–	40,000	5,00,000
31st December, 2022		5,00,000	–	20,000	–
31st December, 2023		–	–	–	–

Record the journal entries (up to 31st December, 2020) in the books of Softech Limited considering the requirements of Ind AS 109.

Solution :

As per Ind AS 109, a financial instrument is initially measured and recorded at its fair value. Therefore, considering the market rate of interest of similar loan available to Mrs. B is 12%, the fair value of the contractual cash flows shall be as follows:

Date	Inflows			Discount factor @12%	PV
	Principal	Interest income @ 7%	Interest income @ 4%		
31st December 2019	5,00,000	1,05,000	40000	0.8929	5,75,921

31st December 2020	5,00,000	70000	40000	0.7972	4,86,292
31st December 2021	5,00,000	35000	40000	0.7118	4,09,285
31st December 2022	5,00,000	-	40000	0.6355	3,43,170
31st December 2023	5,00,000	-	20000	0.5674	2,95,048
Total (fair value)					21,09,716

Benefit to Mrs. B, to be considered a part of employee cost for Softech Limited Rs. 3,90,284 (Rs. 25,00,000 – Rs. 21,09,716).

The deemed employee cost is to be amortised over the period of loan i.e. the minimum period that Mrs. B must remain in service.

The amortization schedule of Rs. 21,09,716 loan is shown in the following table:

Date	**Opening outstanding loan**	**Total cash inflows (principal repayment + interest**	**Interest @ 12%**	**Closing outstanding loan**
1st January 2019	21,09,716	-	-	21,09,716
31st December 2019	21,09,716	6,45,000	2,53,166	17,17,882
31st December 2020	17,17,882	6,10,000	2,06,146	13,14,028
31st December 2021	13,14,028	5,75,000	1,57,683	8,96,711
31st December 2022	8,96,711	5,40,000	1,07,605	4,64,316
31st December 2023	4,64,316	5,20,000	55,684*	-

* Difference of Rs. 34 (55,718 – 55,684) is due to approximation.

Journal Entries in the books of Softech Limited

a. 1st January 2019

Particulars		**Dr. (Rs.)**	**Cr. (Rs.)**
Loan to Mrs. B A/c	Dr.	21,09,716	
Pre-paid employee cost A/c	Dr.	3,90,284	
To Bank A/c			25,00,000
(Being loan asset recorded at initial fair value)			

b. 31st December 2019

Particulars		**Dr. (Rs.)**	**Cr. (Rs.)**
Bank A/c	Dr.	6,45,000	
To Interest income (profit and loss) @ 12% A/c			2,53,166
To Loan to Mrs. B A/c			3,91,834
(Being first instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)			
Employee benefit (profit and loss) A/c	Dr.	78,057	

To Pre-paid employee cost A/c (Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)		78,057

On 31st December 2020, due to pre-payment of a part of loan by Mrs. B, the carrying value of the loan shall be re-computed by discounting the future remaining cash flows by the original effective interest rate.

There shall be two sets of accounting entries on 31st December 2020, first the realisation of the contractual cash flow as shown in (c) below and then the accounting for the pre-payment of Rs. 5,00,000 included in (d) below:

c. 31st December 2020

Particulars	Dr. (Rs.)	Cr. (Rs.)
Bank A/c Dr. To Interest income (profit and loss) @ 12% A/c To Loan to Mrs. B A/c (Being second instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)	6,10,000	 2,06,146 4,03,854
Employee benefit (profit and loss) A/c Dr. To Pre-paid employee cost A/c (Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)	78,057	 78,057

Computation of new carrying value of loan to Mrs. B:

	Inflows				
Date	**Principal**	**Interest income 7%**	**Interest income 4%**	**Discount factor @ 12%**	**PV**
31st December 2021	5,00,000	-	40,000	0.8929	4,82,166
31st December 2022	5,00,000	-	20,000	0.7972	4,14,544
Total (revised carrying value)					8,96,710
Less: Current carrying value					(13,14,028)
Adjustment required					4,17,318

The difference between the amount of pre-payment and adjustment to loan shall be considered a gain, though will be recorded as an adjustment to pre-paid employee cost, which shall be amortised over the remaining tenure of the loan.

d. 31st December 2020 prepayment

Particulars	Dr. (Rs.)	Cr. (Rs.)
Bank A/c Dr.	5,00,000	

To Pre-paid employee cost A/c		82,682
To Loan to Mrs. B A/c		4,17,318
(Being gain to Softech Limited recorded as an adjustment to pre-paid employee cost)		

Amortisation of employee benefit cost shall be as follows:

Date	Opening Balance	Amortised to P&L	Adjustment	Closing Balance
1st January 2019	3,90,284			3,90,284
31st December 2019	3,90,284	78,057		3,12,227
31st December 2020	3,12,227	78,057	82,682	1,51,488

Question 19 : July 2021 – Paper

On 1st October, 2017 Axe Limited issues preference shares to B Limited for a consideration of Rs.18 lakhs. The holder has an option to convert these preference shares to a fixed number of equity instruments of the issuer any time up to period of 4 years. If the holder does not exercise the option, the preference shares are redeemable at the end of 4 years. The preference shares carry a fixed coupon of 5.5% per annum and is payable every year. The prevailing market rate for similar preference shares without the conversion feature is 8% per annum.

Axe Limited has an early redemption option to prepay the instrument at Rs.20 lakhs and on 30th September, 2020, it exercised that option. The interest rate has changed on that date.

At that time, Axe Limited could have issued a 1 year 9that is maturity 30th September, 2021) non-convertible instrument at 6%.

Calculate the value of liability and equity components at the date of initial recognition. Also give amortization schedule.

(Limit discounting factor to 3 decimal places for calculation purpose.)

Solution :

The values of the liability and equity components are calculated as follows:

Present value of principal payable at the end of 4 years (Rs. 18,00,000 discounted at 8% for 4 years i.e. Rs. 18,00,000 x 0.735)	Rs. 13,23,000
Present value of interest payable in arrears for 4 years (Rs. 99,000 (Rs. 18,00,000 x 5.5%) discounted at 8% for each of 4 years (i.e. Rs. 99,000 x 3.312))	Rs. 3,27,888
Total financial liability	Rs. 16,50,888
Consideration amount	(Rs. 18,00,000)
Residual – equity component	Rs. 1,49,112

Therefore, equity component = fair value of compound instrument, say, Rs. 18,00,000 less financial liability component i.e. Rs. 16,50,888 = Rs. 1,49,112.

The amortisation schedule of the instrument is set out below:

Dates	Cash flows	Finance cost at effective interest rate	Liability
1st October 2017	18,00,000	-	16,50,888
30th September 2018	(99,000)	1,32,071	16,83,959
30th September 2019	(99,000)	1,34,717	17,19,676
30th September 2020	(99,000)	1,37,574	17,58,250
30th September 2021	(18,99,000)	1,40,750*	-

***Note:** The difference in amount of finance cost is due to approximation of discounting factor to 3 decimal places

Question 20 : Nov 2021 – RTP

On 1st April, 20X1, PS Limited issued 6,000, 9% convertible debentures with a face value of Rs. 100 each maturing on 31st March, 20X6. The debentures are convertible into equity shares of PS Limited at a conversion price of Rs. 105 per share. Interest is payable annually in cash. At the date of issue, non-convertible debt could have been issued by the company at coupon rate of 13%. On 1st April, 20X4, the convertible debentures have a fair value of Rs. 6,30,000. PS Limited makes a tender offer to debenture-holders to repurchase the debentures for Rs. 6,30,000 which the debenture holders accepted. At the date of repurchase, PS Limited could have issued non-convertible debt with a 2 year term bearing coupon interest @ 10%.

Show accounting entries in the books of PS Limited for recording of equity and liability component:

(i) At the time of initial recognition

(ii) At the time of repurchase of the convertible debentures

Solution :

(i) At the time of initial recognition

	Rs.
Liability component	
Present value of 5 yearly interest payments of Rs. 54,000, discounted at 13% annuity (54,000 x 3.517)	1,89,918
Present value of Rs. 6,00,000 due at the end of 5 years, discounted at 13%, compounded yearly (6,00,000 x 0.543)	3,25,800
	5,15,718
Equity component	
(Rs. 6,00,000 – Rs. 5,15,718)	84,282
Total proceeds	6,00,000

Note: Since Rs. 105 is the conversion price of debentures into equity shares and not the redemption price, the liability component is calculated @ Rs. 100 each only.

Journal Entry

		Rs.	Rs.
Bank	Dr.	6,00,000	
To 9% Debentures (Liability component)			5,15,718

To 9% Debentures (Equity component) (Being debentures initially recorded at fair value)			84,282

(ii) At the time of repurchase of convertible debentures

The repurchase price is allocated as follows:

	Carrying Value @ 13% Rs.	**Fair Value @ 10% Rs.**	**Difference Rs.**
Liability component			
Present value of 2 remaining yearly interest payments of Rs. 54,000, discounted at 13% and 10%, respectively	90,072	93,690	
Present value of Rs. 6,00,000 due in 2 years, discounted at 13% and 10%, compounded yearly, respectively	4,69,800	4,95,600	
Liability component	5,59,872	5,89,290	-29,418
Equity component	84,282*	40,710**	43,572
Total	6,44,154	6,30,000	14,154

*See Note (i)

**6,30,000 – 5,89,290 = 40,710

Journal Entries

		Rs.	**Rs.**
9% Debentures (Liability component)	Dr.	5,59,872	
Profit and loss A/c (Debt settlement expense)	Dr.	29,418	
To Bank A/c			
(Being the repurchase of the liability component recognised)			
9% Debentures (Equity component)	Dr.	84,282	
To Bank A/c			40,710
To Retained Earnings A/c			43,572
(Being the cash paid for the equity component recognised)			

Question 21 : May 2022 – RTP

On 1st April, 2X01, Entity X issued a 10% convertible debenture with a face value of Rs. 1,000 maturing on 31st March, 2X11. The debenture is convertible into ordinary shares of Entity X at a conversion price of Rs. 50 per share. Interest is payable yearly in cash. On 1st April, 2X02, to induce the holder to convert the convertible debenture promptly, Entity X reduces the conversion price to Rs. 40 if the debenture is converted before 1st June, 2X02 (ie, within 60 days). The market price of Entity X's ordinary shares on the date the terms are amended is Rs. 80 per share. How will the revised terms be accounted?

Solution :

The fair value of the incremental consideration paid by Entity X is calculated as follows:

Number of ordinary shares to be issued to debenture holders under amended terms			
Particulars			
Face value			Rs. 1,000
New conversion price		Rs. 40 per share	
Number of ordinary shares to be issued to debenture holders under amended terms	1,000 / Rs. 40		25 Shares
Number of ordinary shares to be issued to debenture holders under original terms			
Face value			Rs. 1,000
Original conversion price		Rs. 50 per share	
Number of ordinary shares to be issued to debenture holders under original terms	1,000 / Rs. 50		20 Shares
Number of additional shares to be issued to debenture holders under amended terms			5 Shares
Value of additional shares upon conversion (to be recognised as loss in P&L)			
5 shares x Rs. 80 per share			Rs. 400

Question 22 : May 2022 – RTP

ABC Ltd. issues 4% 1,00,000 OCPS at a face value of Rs. 100 per share on 1st April, 20X1 and these are redeemable after 5 years, ie, on 31st March, 20X6. Dividend is non-cumulative. Each preference shares entitles the holders to 10 equity shares and the preference shares are optionally convertible by the holder at any time until maturity.

How will the preference shares be classified at initial recognition assuming that a comparable instrument carries a market interest rate of 7%? Provide journal entries for year 1. Will this classification be changed subsequently in case there is likelihood that OCPS will be encashed at the end of the maturity period?

Solution :

The OCPS is redeemable at the end of the 5th year. Hence, the preference share contains a liability component. Further the dividend payable on the preference shares is non-cumulative. The holder may also be able to convert the preference shares at his option any time until maturity.

Paragraph AG 37 of Ind AS 32, *Financial Instruments: Presentation* states that non-cumulative dividends paid at the discretion of the issuer entity is part of equity element.

Paragraph 29 of Ind AS 32, *Financial Instruments: Presentation*, requires separate recognition of components of a financial instrument that (a) creates a financial liability of the entity; and (b) grants an option to the holder of the instrument to convert it into fixed number of equity instruments of the entity.

From the above paragraphs it is clear that OCPS issued by ABC Ltd. has a financial liability component as well as an equity component, making it a compound financial instrument.

As per paragraph 32, in case of compound financial instruments, the issuer first determines the carrying amount of the financial liability component by measuring the fair value of a similar liability that does not have an associated equity component. The carrying amount of the equity represented by (a) non-cumulative dividend feature and (b) option to convert the preference shares for fixed number of pre-determined ordinary
shares is then determined by deducting the fair value of the financial liability component from the fair value of the compound financial instrument as a whole.

Measurement and recognition (Calculations have been done at full scale):

At 7% market rate of interest, the fair value of the financial liability component of the OCPS is Rs. 71,29,862 [100,000 OCPS x Rs. 100 x (1/ (1+7%))5]

The fair value of the equity component is (residual value) Rs. 28,70,138 [Rs. 1,00,00,000 - Rs. 71,29,862]

Journal Entries

1st April, 20X1	**On Initial recognition**		
	Bank Dr.	1,00,00,000	
	To OCPS (Financial liability)		71,29,862
	To OCPS (Equity)		28,70,138
	(Being OCPS issued and recognised)		
31st March, 20X2	**<u>Interest expense – unwinding of discount</u>**		
	Interest expense@7% (Refer W.N.) Dr.	4,99,090	
	To OCPS (Financial liability)		4,99,090
	(Being interest recorded as per EIR)		
	Interest entry will be passed every year till conversion option is not exercised		
	Whenever the option is exercised by the holder to convert to equity shares		
	OCPS (Financial liability) Dr.	Balance on date of exercise of the option	
	To OCPS (Equity)		

As per paragraph 30, in case of a convertible financial instrument, the classification of the liability and equity components is not revised as a result of change in the likelihood that a conversion option will be exercised.

In other words, the amount attributable to equity component on initial recognition shall remain in equity and will not be reclassified even if the OCPS are ultimately redeemed in cash by the issuer.

31st March, 20X6	**If redeemed in cash on maturity**		
	OCPS (financial liability) (Refer W.N.) Dr.	1,00,00,000	
	To Bank		1,00,00,000
	(Being OCPS redeemed on maturity)		

Working Note:

Calculation of the amortised cost of the financial liability (at full scale):

Year	Opening Balance (Rs.)	Interest @ 7%	Repayment	Closing Balance (Rs.)
1	71,29,862	4,99,090	-	76,28,952
2	76,28,952	5,34,027		81,62,979
3	81,62,979	5,71,409		87,34,388
4	87,34,388	6,11,407		93,45,795
5	93,45,795	6,54,206	10,000,000	-

Thanks ....

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IND AS – 113 FAIR VALUE MEASUREMENT

CHAPTER - 21

Question 1 : Nov 2018 – PAPER

An asset is sold in 2 different active markets at different prices. An entity enters into transactions in both markets and can access the price in those markets for the asset at the measurement date.

In Market A:

The price that would be received is Rs.78, transaction costs in that market are Rs.9 and the costs to transport the asset to that market are Rs.6.

In Market B:

The price that would be received is Rs.75, transaction costs in that market are Rs.3 and the costs to transport the asset to that market are Rs.6.

You are required to calculate:

(i) The fair value of the asset, if market A is the principal market, and

(ii) The fair value of the asset, if none of the markets is principal market.

Solution :

(i) If Market A is the principal market

If Market A is the principal market for the asset (i.e., the market with the greatest volume and level of activity for the asset), the fair value of the asset would be measured using the price that would be received in that market, after taking into account transport costs.

Fair Value of the asset will be

	Rs.
Price receivable	78
Less: Transportation cost	(6)
Fair value of the asset	72

(ii) If neither of the market is the principal market

If neither of the market is the principal market for the asset, the fair value of the asset would be measured using the price in the most advantageous market. The most advantageous market is the market that maximises the amount that would be received to sell the asset, after taking into account transaction costs and transport costs (i.e., the net amount that would be received in the respective markets).

Determination of most advantageous market:

	Rs.	**Rs.**
	Market A	**Market B**
Price receivable	78	75

Less: Transaction cost	(9)	(3)
Less: Transportation cost	(6)	(6)
Fair value of the asset	63	66

Since the entity would maximise the net amount that would be received for the asset in Market B i.e. Rs.66, the fair value of the asset would be measured using the price in Market B.

Fair value of the asset will be

	Rs.
Price receivable	75
Less: Transportation cost	(6)
Fair value of the asset	69

Question 2 : Nov 2019 – RTP

Comment on the following by quoting references from appropriate Ind AS.

(i) DS Limited holds some vacant land for which the use is not yet determined. the land is situated in a prominent area of the city where lot of commercial complexes are coming up and there is no legal restriction to convert the land into a commercial land.

The company is not interested in developing the land to a commercial complex as it is not its business objective. Currently the land has been let out as a parking lot for the commercial complexes around.

The Company has classified the above property as investment property. It has approached you, an expert in valuation, to obtain fair value of the land for the purpose of disclosure under Ind AS.

On what basis will the land be fair valued under Ind AS?

(ii) DS Limited holds equity shares of a private company. In order to determine the fair value' of the shares, the company used discounted cash flow method as there were no similar shares available in the market.

Under which level of fair value hierarchy will the above inputs be classified?

What will be your answer if the quoted price of similar companies were available and can be used for fair valuation of the shares?

Solution :

(i) As per Ind AS 113, a fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The highest and best use of a non-financial asset takes into account the use of the asset that is physically possible, legally permissible and financially feasible, as follows:

(a) A use that is physically possible takes into account the physical characteristics of the asset that market participants would take into account when pricing the asset (eg the location or size of a property).

(b) A use that is legally permissible takes into account any legal restrictions on the use of the asset that market participants would take into account when pricing the asset (eg the zoning regulations applicable to a property).

(c) A use that is financially feasible takes into account whether a use of the asset that is physically possible and legally permissible generates adequate income or cash flows (taking into account the costs of converting the asset to that use) to produce an investment return that market participants would require from an investment in that asset put to that use.

Highest and best use is determined from the perspective of market participants, even if the entity intends a different use.

Therefore, the fair value of the land is the price that would be received when sold to a market participant who is interested in developing a commercial complex.

(ii) As per Ind AS 113, unobservable inputs shall be used to measure fair value to the extent that relevant observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. The unobservable inputs shall reflect the assumptions that market participants would use when pricing the asset or liability, including assumptions about risk.

In the given case, DS Limited adopted discounted cash flow method, commonly used technique to value shares, to fair value the shares of the private company as there were no similar shares traded in the market. Hence, it falls under Level 3 of fair value hierarchy. If an entity can access quoted price in active markets for identical assets or liabilities of similar companies which can be used for fair valuation of the shares without any adjustment, at the measurement date, then it will be considered as observable input and would be considered as Level 2 inputs.

Question 3 : Nov 2019 – PAPER

An asset is sold in two different active markets at different prices. Manor Ltd. enters into transactions in both markets and can access the price in those markets for the asset at the measurement date.

In Mumbai market, the price that would be received is Rs.290, transactions costs in that market are Rs.40 and the costs to transport the asset to that market are Rs.30. Thus the net amount that would be received is Rs.220.

In Kolkata market the price that would be received is Rs.280, transaction costs in that market are Rs.20 and the costs to transport the asset to that market are Rs.30. Thus, the net amount that would be received in Kolkata market is Rs.230.

(i) What should be the fair value of the asset if Mumbai Market is the principal market? What should be fair value if none of the markets is principle market?

(ii) If the net realisation after expenses is more in export market, say Rs.280 but Government allows only 15% of the production to be exported out of India. Discuss what would be fair value in such case.

Solution :

(i) Fair value :

(a) If Mumbai is the principal market

If Mumbai is the principal market for the asset (i.e., the market with the greatest volume and level of activity for the asset), the fair value of the asset would be measured using the price that would be received in that market, after taking into account transport costs.

Fair Value of the asset will be

	Rs.
Price receivable	290
Less: Transportation cost	(30)
Fair value of the asset	260

(b) If neither of them principal market

If neither of the market is the principal market for the asset, the fair value of the asset would be measured using the price in the most advantageous market. The most advantageous market is the market that maximises the amount that would be received to sell the asset, after taking into account transaction costs and transport costs (i.e., the net amount that would be received in the respective markets).

Determination of most advantageous market:

	Rs.	**Rs.**
	Mumbai	**Kolkata**
Price receivable	290	280
Less: Transaction cost	(40)	(20)
Less: Transportation cost	(30)	(30)
Fair value of the asset	220	230

Since Kolkata has maximum return fair value will be calculated using Kolkata.

Fair value of the asset will be

	Rs.
Price receivable	280
Less: Transportation cost	(30)
Fair value of the asset	250

(ii) As per Ind AS 113 Fair Value should be determined from principal market. Principal market is the one where highest volumes are traded.

So even if export market gives highest Net receivable value i.e. Rs.280 it cannot be considered as fair value because only 15% of production is allowed to be sold in export market.

Question 4 : Nov 2021 – RTP

On 1st January, 20X1, A Ltd assumes a decommissioning liability in a business combination. The reporting entity is legally required to dismantle and remove an offshore oil platform at the end of its useful life, which is estimated to be 10 years. The following information is relevant:

If A Ltd was contractually allowed to transfer its decommissioning liability to a market participant, it concludes that a market participant would use all of the following inputs, probability weighted as appropriate, when estimating the price it would expect to receive:

a. Labour costs

Labour costs are developed based on current marketplace wages, adjusted for expectations of future wage increases, required to hire contractors to dismantle and remove offshore oil platforms. A Ltd. assigns probability to a range of cash flow estimates as follows:

Cash Flow Estimates:	100 Cr	125 Cr	175 Cr
Probability:	25%	50%	25%

b. Allocation of overhead costs:

Assigned at 80% of labour cost

c. The compensation that a market participant would require for undertaking the activity and for assuming the risk associated with the obligation to dismantle and remove the asset. Such compensation includes both of the following:

i. Profit on labour and overhead costs:

A profit mark-up of 20% is consistent with the rate that a market participant would require as compensation for undertaking the activity

ii. The risk that the actual cash outflows might differ from those expected, excluding inflation:

A Ltd. estimates the amount of that premium to be 5% of the expected cash flows. The expected cash flows are 'real cash flows' / 'cash flows in terms of monetary value today'.

d. Effect of inflation on estimated costs and profits

A Ltd. assumes a rate of inflation of 4 percent over the 10-year period based on available market data.

e. Time value of money, represented by the risk-free rate: 5%

f. Non-performance risk relating to the risk that Entity A will not fulfill the obligation, including A Ltd.'s own credit risk: 3.5%

A Ltd, concludes that its assumptions would be used by market participants. In addition, A Ltd. does not adjust its fair value measurement for the existence of a restriction preventing it from transferring the liability.

You are required to calculate the fair value of the asset retirement obligation.

Solution :

Particulars	**Workings**	**Amount (In Cr)**
Expected Labour Cost (Refer W.N.)		131.25
Allocated Overheads	(80% x 131.25 Cr)	105.00
Profit markup on Cost	(131.25 + 105) x 20%	47.25
Total Expected Cash Flows before inflation		**283.50**
Inflation factor for next 10 years (4%)	$(1.04)^{10}$ =1.4802	
Expected cash flows adjusted for inflation	283.50 x 1.4802	419.65
Risk adjustment - uncertainty relating to cash flows	(5% x 419.65)	20.98
Total Expected Cash Flows	419.65+20.98)	440.63
Discount rate to be considered = risk-free rate entity's non-performance risk	5% + 3.5%	8.5%
Expected present value at 8.5% for 10 years	**440.63 / (1.085^{10}))**	**194.88**

Working Note:

Expected labour cost:

Cash Flows Estimates	**Probability**	**Expected Cash Flows**
100 Cr	25%	25.00 Cr
125 Cr	50%	62.50 Cr
175 Cr	25%	43.75 Cr
Total		**131.25 Cr**

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IND AS – 10 EVENTS AFTER REPORTING PERIOD

CHAPTER - 22

Question 1 : May 2019 – RTP

XYZ Ltd. was formed to secure the tenders floated by a telecom company for publication of telephone directories. It bagged the tender for publishing directories for Pune circle for 5 years. It has made a profit in 2013-2014, 2014-2015, 2015-2016 and 2016-2017. It bid in tenders for publication of directories for other circles – Nagpur, Nashik, Mumbai, Hyderabad but as per the results declared on 23rd April, 2017, the company failed to bag any of these. Its only activity till date is publication of Pune directory. The contract for publication of directories for Pune will expire on 31st December 2017. The financial statements for the F.Y. 2016-17 have been approved by the Board of Directors on July 10, 2017.

Whether it is appropriate to prepare financial statements on going concern basis?

Solution :

With regard to going concern basis to be followed for preparation of financial statements, Ind AS 10 provides as follows:

1) An entity shall not prepare its financial statements on a going concern basis if management determines after the reporting period either that it intends to liquidate the entity or to cease trading, or that it has no realistic alternative but to do so.
2) Deterioration in operating results and financial position after the reporting period may indicate a need to consider whether the going concern assumption is still appropriate. If the going concern assumption is no longer appropriate, the effect is so pervasive that this Standard requires a fundamental change in the basis of accounting, rather than an adjustment to the amounts recognised within the original basis of accounting."

In accordance with the above, an entity needs to change the basis of accounting if the effect of deterioration in operating results and financial position is so pervasive that management determines after the reporting period either that it intends to liquidate the entity or to cease trading, or that it has no realistic alternative but to do so.

In the instant case, since contract is expiring on 31st December 2017 and it is confirmed on 23rd April, 2017, i.e., after the end of the reporting period and before the approval of the financial statements, that no further contact is secured, implies that the entity's operations are expected to come to an end. Accordingly, if entity's operations are expected to come to an end, the entity needs to make a judgement as to whether it has any realistic possibility to continue or not. In case, the entity determines that it has no realistic alternative of continuing the business, preparation of financial statements for 2016-17 and thereafter on going concern basis may not be appropriate.

Question 2 : Nov 2019 – RTP

ABC Ltd. received a demand notice on 15th June, 2017 for an additional amount of Rs.28,00,000 from the Excise Department on account of higher excise duty levied by the Excise Department compared to the rate at which the company was creating provision and depositing the same. The financial statements for the year 2016-17 are approved on 10th August, 2017. In July, 2017, the company has appealed against the demand of Rs.28,00,000 and the company has expected that the demand would be settled at Rs.15,00,000 only. Show how the above event will have a bearing on the financial statements for the year 2016-17. Whether these events are adjusting or non-adjusting events and explain the treatment accordingly.

Solution :

Ind AS 10 defines 'Events after the Reporting Period' as follows:

Events after the reporting period are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are approved by the Board of Directors in case of a company, and, by the corresponding approving authority in case of any other entity for issue. Two types of events can be identified:

(a) those that provide evidence of conditions that existed at the end of the reporting period (adjusting events after the reporting period); and

(b) those that are indicative of conditions that arose after the reporting period (non-adjusting events after the reporting period)

In the instant case, the demand notice has been received on 15th June, 2017, which is between the end of the reporting period and the date of approval of financial statements. Therefore, it is an event after the reporting period. This demand for additional amount has been raised because of higher rate of excise duty levied by the Excise Department in respect of goods already manufactured during the reporting period. Accordingly, condition exists on 31st March, 2017, as the goods have been manufactured during the reporting period on which additional excise duty has been levied and this event has been confirmed by the receipt of demand notice. Therefore, it is an adjusting event.

In accordance with the principles of Ind AS 37, the company should make a provision in the financial statements for the year 2016-17, at best estimate of the expenditure to be incurred, i.e., Rs.15,00,000.

Question 3 : Nov 2019 – PAPER

Discuss with reasons whether these events are in nature of adjusting or non-adjusting and the treatment needed in light of accounting standard Ind AS 10.

(i) Moon Ltd. won an arbitration award on 25th April, 2019 for Rs.1 crore. From the arbitration proceeding, it was evident that the Company is most likely to win the arbitration award. The directors approved the financial statements of year ending 31.03.2019 on 1st May 2019. The management did not consider the effect of the above transaction in FY-2018-19, as it was favourable to the company and the award came after the end of the financial year.

(ii) Zoom Ltd. have a trading business of Mobile telephones. The Company has purchased 1000 mobiles phones at Rs.5,000 each on 15th March, 2019. The manufacturers of phone had announced the release of the new version on 1st March, 2019 but not announced the price. Zoom Ltd, has valued inventory at cost of Rs.5,000 each at the year ending 31st March, 2019.

Due to arrival of new advance version of Mobile Phone on 8th April, 2019, the selling prices of the mobile stocks remaining with company was dropped at Rs.4,000 each.

The financial statements of the company valued mobile phones @ Rs.5,000 each and not at the value @ Rs.4,000 less expenses on sales, as the price reduction in selling price was effected after 31.03.2019.

(iii) There was an old due from a debtor amounting to Rs.15 Lakhs against whom insolvency proceedings was instituted prior to the financial year ending 31st March, 2019. The debtor was declared in solvent on 15th April, 2019.

(iv) Assume that subsequence to the year end and before the financial statements are approved, Company's management announces that it will restructure the operations of the company. Management plans to make significant redundancies and to close a few divisions of company's business; however, there is not formal plan yet. Should management recognize a provision in the books if the company decides subsequent to end of the accounting year to restructure its operations?

Solution :

As per Ind AS 10, the treatment of stated issues would be as under:

(i) **Adjusting event:** It is an adjusting event as it is the settlement after the reporting period of a court case that confirms that the entity had a present obligation at the end of the reporting period. Even though winning of award is favorable to the company, it should be accounted in its books as receivable since it is an adjusting event.

(ii) **Adjusting event:** The sale of inventories after the reporting period may give evidence about their net realizable value at the end of the reporting period, hence it is an adjusting event as per Ind AS 10. Zoom Limited should value its inventory at Rs.40,00,000. Hence, appropriate provision must be made for Rs.15 lakh.

(iii) **Adjusting event:** As per Ind AS 10, the receipt of information after the reporting period indicating that an asset was impaired at the end of the reporting period, or that the amount of a previously recognised impairment loss for that asset needs to be adjusted.

The bankruptcy of a customer that occurs after the reporting period usually confirms that the customer was credit-impaired at the end of the reporting period.

(iv) **Non – adjusting event:**

Announcing or commencing the implementation of a major restructuring after reporting period is a non-adjusting event as per Ind AS 10. Though this is a non-adjusting event occurred after the reporting period, yet it would result in disclosure of the event in the financial statements, if restructuring is material.

This would not require provision since as per Ind AS 37, decision to restructure was not taken before or on the reporting date. Hence, it does not give rise to a constructive obligation at the end of the reporting period to create a provision.

Question 4 : May 2020 – RTP

A company manufacturing and supplying process control equipment is entitled to duty draw back if it exceeds its turnover above a specified limit. To claim duty drawback, the company needs to file application within 15 days of meeting the specified turnover. If application is not filed within stipulated time, the Department has discretionary power of giving duty draw back credit. For the year 20X1-20X2 the company has exceeded the specified limit of turnover by the end of the reporting period. However, duty drawback can be claimed on filing of application within the stipulated time or on discretion of the Department if filing of application is late. The application for duty drawback is filed on April 20, 20X2, which is after the stipulated time of 15 days of meeting the turnover condition. Duty drawback has been credited by the Department on June 28, 20X2 and financial statements have been approved by the Board of Directors of the company on July 26, 20X2. What would be the treatment of duty drawback credit as per the given information?

Solution :

In the instant case, the condition of exceeding the specified turnover was met at the end of the reporting period and the company was entitled for the duty drawback. However, the application for the same has been filed after the stipulated time. Therefore, credit of duty drawback was discretionary in the hands of the Department. Since the claim was to be accrued only after filing of application, its accrual will be considered in the year 20X2-20X3 only.

Accordingly, the duty drawback credit is a contingent asset as at the end of the reporting period 20X1-20X2, which will be realised when the Department credits the same.

As per para 35 of Ind AS 37, Provisions, Contingent Liabilities and Contingent Assets, contingent assets are assessed continually to ensure that developments are appropriately reflected in the financial statements. If it has become virtually certain that an inflow of economic benefits will arise, the asset and the related income are recognised in the financial statements of the period in which the change occurs. If an inflow of economic benefits has become probable, an entity discloses the contingent asset.

In accordance with the above, the duty drawback credit which was contingent asset for the F.Y. 20X1 -20X2 should be recognised as asset and related income should be recognized in the reporting period in which the change occurs. i.e., in the period in which realisation becomes virtually certain, i.e., F.Y. 20X2 - 20X3.

Question 5 : Nov 2020 – RTP

In one of the plant of PQR Ltd., fire broke out on 10.05.2020 in which the entire plant was damaged. PQR Ltd. estimated the loss of Rs.40,00,000 due to fire. The company filed a claim with the insurance company and expects recovery of Rs.27,00,000 from the claim. The financial statements for the year ending 31.03.2020 were approved by the Board of Directors on 12th June, 2020. Discuss the accounting treatment of the above situation.

Solution :

As per IND AS 10 – Evens after reporting period are those favourable or unfavourable, that occur between the end of reporting period and the date when financial statements are approved by board and director.

The event of fire is event after reporting period. If the event leads to deterioration of business that it lead to closure of business that Co. Needs to charge the base of accounting i.e. not follow going concern concept.

However if entity feels that business will continue through with some set back then note to the extent should be given in financial statements.

Question 6 : Jan 2021 – Paper

H Ltd. constructed a warehouse at a cost of Rs.10 lakhs in 2015. It first became available for use by H Ltd. on 1st January 2016. On 29th January 2020, H Ltd. discovered that its warehouse was damaged. During early February 2020, an investigation revealed that the damage was due to a structural fault in the construction of the warehouse. The fault became apparent when the warehouse building leaked severely after heavy rainfall in the week ended 27th January 2020. The discovery of the fault is an indication of impairment. So, H Ltd. was required to estimate the recoverable amount of its warehouse at 31st December 2019. This estimate was Rs.6,00,000. Furthermore, H Ltd. Reassessed the useful life of its warehouse at 20 years from the date that it was ready for use. Before discovering the fault, H Ltd. had depreciated the warehouse on the straight -line method to a nil residual value over its estimated 30-year useful life.

Seepage of rain water through the crack in the warehouse caused damage to inventory worth about Rs.1,00,000 (cost price) and became un-saleable. The entire damaged inventory was on hand as at 31st December, 2019. H Ltd. has not insured against any of the losses.

It accounts for all its property, plant and equipment under the cost model. H Ltd.'s annual financial statements for the year ended 31st December, 2019 were approved for issue by the Board of Directors on 28th February, 2020.

You are required to :

(i) Prepare accounting entries to record the effects of the events after the end of the reporting period in the accounting records of H Ltd. for the year ended 31st December, 2019. Kindly ignore tax impact;

(ii) Discuss disclosure requirement in above case as per relevant Ind AS; and

(iii) Will your answer be different if there was no structural fault and damage to the warehouse had been caused by an event that occurred after 31st December, 2019?

Solution :

(i) **Journal Entries on 31st December 2019**

		Rs.	Rs.
Depreciation expense A/c (W.N.1)	Dr.	19,608	
To Warehouse or Accumulated depreciation A/c			19,608

(Being additional depreciation expense recognised for the year ended 31st December 2019 arising from the reassessment of the useful life of the warehouse)			
Impairment loss A/c (W.N.2)	Dr.	2,47,059	
To Warehouse or Accumulated depreciation A/c			2,47,059
(Being impairment loss recognised due to discovery of structural fault in the construction of warehouse at 31st December 2019)			

(ii) (a) **The damage to warehouse is an adjusting event** (occurred after the end of the year 2019) for the reporting period 2019, since it provides evidence that the structural fault existed at the end of the reporting period. It is an adjusting event, in spite of the fact that fault has been discovered after the reporting date.

The effects of the damage to the warehouse are recognised in the year 2019 reporting period. Prior periods will not be adjusted because those financial statements were prepared in good faith (eg regarding estimate of useful life, assessment of impairment indicators etc) and had not affected the financials of prior years.

(b) Damage of inventory due to seepage of rainwater Rs.1,00,000 occurred during the year 2020. **It is a non-adjusting event** after the end of the 2019 reporting period since the inventory was in good condition at 31st December 2019. Hence, no accounting has been done for it in the year 2019.

H Ltd. must disclose the nature of the event (i.e. rain-damage to inventories) and an estimate of the financial effect (i.e. Rs.1,00,000 loss) in the notes to its 31st December 2019 annual financial statements.

(iii) If the damage to the warehouse had been caused by an event that occurred after 31st December 2019 and was not due to structural fault, **then it would be considered as a non-adjusting event** after the end of the reporting period 2019 as the warehouse would have been in a good condition at 31st December 2019.

Working Notes:

1. Calculation of additional depreciation to be charged in the year 2019

Original depreciation as per SLM already charged during the year 2019

= Rs.10,00,000/ 30 years = Rs.33,333.

Carrying value at the end of 2018 = 10,00,000 – (Rs.33,333 x 3 years) = Rs.9,00,000

Revised depreciation = 9,00,000 / 17 years = Rs.52,941

Additional depreciation to be recognised in the books in the year 2019

= Rs.52,941 – Rs.33,333 = Rs.19,608

2. Calculation of impairment loss in the year 2019

Carrying value after charging depreciation for the year 2019

= Rs.9,00,000 – Rs.52,941 = Rs.8,47,059

Recoverable value of the warehouse = Rs.6,00,000

Impairment loss = Carrying value - Recoverable value

= Rs.8,47,059 - Rs.6,00,000 = Rs.2,47,059

Question 7 : May 2022 – RTP

XYZ Ltd. sells goods to its customer with a promise to give discount of 5% on list price of the goods provided that the payments are received from customer within 15 days. XYZ Ltd. sold goods of Rs. 5 lakhs to ABC Ltd. between 17th March, 20X1 and 31st March, 20X1. ABC Ltd. paid the dues by 15th April, 20X1 with respect to sales made between 17th March, 20X1 and 31st March, 20X1. Financial statements were approved for issue by Board of Directors on 31st May, 20X1. State whether discount will be adjusted from the sales at the end of the reporting period.

Solution :

As per Ind AS 115, if the consideration promised in a contract includes a variable amount, an entity shall estimate the amount of consideration to which the entity will be entitled in exchange for transferring the promised goods or services to a customer.

In the instant case, the condition that sales have been made exists at the end of the reporting period and the receipt of payment within 15 days' time after the end of the reporting period and before the approval of the financial statements confirms that the discount is to be provided on those sales. Therefore, it is an adjusting event.

Accordingly, XYZ Ltd. should adjust the sales made to ABC Ltd. With respect to discount of 5% on the list price of the goods.

Thanks ....

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IND AS – 20 ACCOUNTING FOR GOVT. GRANT & DISCLOSURE OF GOVT. ASSISTANCE

CHAPTER - 23

Question 1 : Nov 2018 – PAPER

How will you recognize and present the grants received from the Government in the following cases as per Ind AS 20?

(i) A Ltd. received one acre of land to setup a plant in backward area (fair value of land Rs.12 lakh and acquired value by Government is Rs.8 lakhs).

(ii) B Ltd. received an amount of loan for setting up a plant at concessional rate of interest from the Government.

(iii) D Ltd. received an amount of Rs.25 lakh for immediate start-up of a business without any condition.

(iv) S Ltd. received Rs.10 lakh for purchase of machinery costing Rs.80 lakh. Useful life of machinery is 10 years. Depreciation on this machinery is to be charged on straight line basis.

(v) Government gives a grant of Rs.25 lakh to U Limited for research and development of medicine for breast cancer, even though similar medicines are available in the market but are expensive. The company is to ensure by developing a manufacturing process over a period of two years so that the cost comes down at least to 50%.

Solution :

(i) The land and government grant can be recognized at Fair Value or Nominal Value i.e. at either Rs.12,00,000 or Rs.8,00,000.

(ii) As per Ind AS 20 'Accounting for Government Grants and Disclosure of Government Assistance', loan at concessional rates of interest is to be measured at fair value and recognised as per Ind AS 109. Value of concession is the difference between the initial carrying value of the loan determined in accordance with Ind AS 109, and the proceeds received. The benefit is accounted for as Government grant.

(iii) Rs.25 lakh has been received by D Ltd. for immediate start-up of business. Since this grant is given to provide immediate financial support to an entity, it should be recognised in the Statement of Profit and Loss immediately.

(iv) Rs.10 lakh should be recognized by S Ltd. as deferred income and will be transferred to profit and loss over the useful life of the asset. In this case, Rs.1,00,000 [Rs.10 lakh / 10 years] should be credited to profit and loss each year over period of 10 years.

(v) As per Ind AS 20, the entire grant of Rs.25 lakh should be recognized immediately as deferred income and charged to profit and loss over a period of two years based on the related costs for which the grants are intended to compensate provided that there is reasonable assurance that U Ltd. will comply with the conditions attached to the grant.

Question 2 : Nov 2019 – PAPER

Arun Ltd. is an entity engaged in plantation and farming on a large scale and diversified across India. On 1st April, 2018, the company has received a government grant for Rs.20 lakhs subject to a condition that it will continue to engaged in plantation of eucalyptus tree for a coming period of five years.

The management has a reasonable assurance that the entity will comply with condition of engaging in the plantation of eucalypts tree for specified period of five years and accordingly it recognizes proportionate grant for Rs.4 lakhs in Statement of Profit and Loss as income following the principles laid down under Ind AS 20 Accounting for Government Grants and Disclosure of Government Assistance.

Required :

Evaluate whether the above accounting treatment made by the management is in compliance with the applicable Ind AS. If not, advise the correct treatment.

Solution :

As per Ind AS 20 Government grant should be recognised when there is reasonable assurance that

(a) the entity will comply with condition attaching to them and

(b) grant will be received.

The entity is reasonably sure to comply with condition and they are correct to recognise grand in proportionate amount i.e. 1/5 of 20,00,000 = Rs.4,00,000.

Question 3 : May 2020 – RTP

Rainbow Limited is carrying out various projects for which the company has either received government financial assistance or is in the process of receiving the same. The company has received two grants of Rs.1,00,000 each, relating to the following ongoing research and development projects:

(i) The first grant relates to the “Clean river project” which involves research into the effect of various chemicals waste from the industrial area in Madhya Pradesh. However, no major steps have been completed by Rainbow limited to commence this research as at 31st march, 20X2.

(ii) The second grant relates to the commercial development of a new equipment that can be used to manufacture eco-friendly substitutes for existing plastic products. Rainbow Limited is confident about the technical feasibility and financial viability of this new technology which will be available for sale in the market by April 20X3.

In September 20X1, due to the floods near one of its factories, the entire production was lost and Rainbow Limited had to shut down the factory for a period of 3 months. The State Government announced a compensation package for all the manufacturing entities affected due to the floods.

As per the scheme, Rainbow Limited is entitled to a compensation based on the average of previous three months' sales figure prior to the floods, for which the company is required to submit an application form on or before 30th June, 20X2 with necessary figures. The financial statements of Rainbow Limited are to be adopted on 31st May, 20X2, by which date the claim form would not have been filed with the State Government.

Suggest the accounting treatment of, if any, for the two grants received and the flood-related compensation in the books of accounts of Rainbow Limited as on 31st March, 20X2.

Solution :

Accounting treatment for:

1. **First Grant**

   The first grant for 'Clear River Project' involving research into effects of various chemicals waste from the industrial area in Madhya Pradesh, seems to be unconditional as no details regarding its refund has been mentioned. Even though the research has not been started nor any major steps have been completed by Rainbow Limited to commence the research, yet the grant will be recognised immediately in profit or loss for the year ended 31st March, 20X2.

   Alternatively, in case, the grant is conditional as to expenditure on research, the grant will be recognised in the books of Rainbow Limited over the year the expenditure is being incurred.

2. **Second Grant**

   The second grant related to commercial development of a new equipment is a grant related to depreciable asset. As per the information given in the question, the equipment will be available for sale in the market from April, 20X3. Hence, by that time, grant relates to the construction of an asset and should be initially recognised as deferred income.

   The deferred income should be recognised as income on a systematic and rational basis over the asset's useful life.

   The entity should recognise a liability on the balance sheet for the years ending 31st March, 20X2 and 31st March, 20X3. Once the equipment starts being used in the manufacturing process, the deferred grant income of Rs.100,000 should be recognised over the asset's useful life to compensate for depreciation costs.

   Alternatively, as per Ind AS 20, Rainbow Limited would also be permitted to offset the deferred income of Rs.100,000 against the cost of the equipment as on 1st April, 20X3.

3. **For flood related compensation**

   Rainbow Limited will be able to submit an application form only after 31st May, 20X2 i.e. in the year 20X2-20X3. Although flood happened in September, 20X1 and loss was incurred due to flood related to the year 20X1-20X2, the entity should recognise the income from the government grant in the year when the application form related to it is submitted and approved by the government for compensation.

   Since, in the year 20X1-20X2, the application form could not be submitted due to adoption of financials with respect to sales figure before flood occurred, Rainbow Limited should not recognise the grant income as it has not become receivable as on 31st March,20X2.

Question 4 : Nov 2020 – RTP

Entity A is awarded a government grant of Rs.60,000 receivable over three years (Rs.40,000 in year 1 and Rs.10,000 in each of years 2 and 3), contingent on creating 10 new jobs and maintaining them for three years. The employees are recruited at a total cost of Rs.30,000, and the wage bill for the first year is Rs.1,00,000, rising by Rs.10,000 in each of the subsequent years. Calculate the grant income and deferred income to be accounted for in the books for year 1, 2 and 3.

Solution :

The grant of 60,000 should be recognised over the 3 year period to compensate for the related cost.

1) Total Cost

Year	Total Cost		
1	30,000 + 1,00,000	=	1,30,000
2	Nil + 1,00,000 + 10,000	=	1,10,000
3	Nil + 1,00,000 + 20,000	=	1,20,000
			3,60,000

2) Grant to Recognised

Year	Total Cost		
1	60,000 / 3,60,000 × 1,30,000	=	21,667
2	60,000/3,60,000 × 1,10,000	=	18,333
3	60,000 / 3,60,000 × 1,20,000	=	20,000

3) Deferred Income

Year	Total Cost		
1	40,000 – 21,667	=	18,333
2	50,000 – 21,667 – 18,333	=	10,000
3	60,000 – 21,667 – 18,333 – 20,000	=	Nil

Question 5 : Nov 2021 – RTP

A Ltd. has been conducting its business activities in backward areas of the country and due to higher operating costs in such regions, it has collectively incurred huge losses in previous years. As per a scheme of government announced in March 20X1, the company will be partially compensated for the losses incurred by it to the extent of Rs. 10,00,00,000, which will be received in October 20X1. The compensation being paid by the government meets the definition of government grant as per Ind AS 20. Assume that no other conditions are to be fulfilled by the company to receive the compensation.

When should the grant be recognised in statement of profit and loss? Discuss in light of relevant Ind AS.

Solution :

Paragraph 7 of Ind AS 20 states that, Government grants, including non-monetary grants at fair value, shall not be recognised until there is reasonable assurance that:

(a) the entity will comply with the conditions attaching to them; and

(b) the grants will be received.

Further, paragraphs 20 and 22 of Ind AS 20 state as follows:

"A government grant that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs shall be recognised in profit or loss of the period in which it becomes receivable".

"A government grant may become receivable by an entity as compensation for expenses or losses incurred in a previous period. Such a grant is recognised in profit or loss of the period in which it becomes receivable, with disclosure to ensure that its effect is clearly understood."

In accordance with the above, in the given case, as at March 20X1, A Ltd. is entitled to receive government grant in the form of compensation for losses already incurred by it in the previous years. Therefore, even though the compensation will be received in the month of October 20X1, A Ltd. should recognise the compensation receivable by it as a government grant in the profit or loss for the period in which it became receivable, i.e., for the financial year 20X0-20X1 with disclosure to ensure that its effect is clearly understood.

Question 6 : May 2022 – RTP

A Limited is engaged in the manufacturing of certain specialized chemicals. During the manufacturing process, certain wastewater is produced which is released by A Limited in the nearby river. To reduce pollution of the rivers, the state government has introduced a scheme with the following salient features:

- If a manufacturer installs certain pre-approved wastewater treatment plant, the government will provide an interest free loan equal to 50% of the cost of the plant;
- Such loan will be repayable to the government in 5 years from the date of disbursal;
- The manufacturer availing the benefit of this scheme must treat the wastewater of its factory using the specified plant before releasing it to the river. If this condition is violated, the entire loan shall become immediately repayable to the government along with a penalty of Rs. 10 lakh.

Cost of the wastewater treatment plant to be installed to avail the benefit of the scheme is Rs. 50 lakh. A Limited decided to utilise this scheme because, if it were to obtain the similar loan from a bank, it would be available at a market interest rate of 12% per annum. Accordingly, A Limited applied for and obtained the government loan of Rs. 25 lakh on 1st April, 20X1. A Limited purchased and installed the plant such that it became ready for use on the same date.

A Limited has an accounting policy of recognising government grant in relation to depreciable assets in the proportion of depreciation expense. It has determined that the plant will be depreciated over a period of 5 years using straight-line method. In the month of March, 20X3, government officials conducted a surprise audit, and it was found that A Limited was not using the wastewater treatment plant as prescribed. Accordingly, on 31st March, 20X3, the government ordered A Limited to repay the entire loan along with penalty. A Limited repaid the loan with interest and penalty as per the order on 31st March, 20X3.

Measure the amount of government grant as on 1st April, 20X1. Determine the nature of the government grant and its accounting treatment (principally) for the year ended 31st March, 20X2. Also determine the impact on profit or loss if any, on account of revocation of government grant as on 31st March, 20X3.

Solution :

As per the principles of Ind AS 20 "Accounting for Government Grants and Disclosure of Government Assistance", the benefits of a government loan at a below market rate of interest is treated as a government grant. The loan shall be recognized and measured in accordance with Ind AS 109 "Financial Instruments". The benefit of the below market rate of interest shall be measured as the difference between the initial carrying value of the loan determined in accordance with Ind AS 109 and the proceeds received. The benefit is accounted for in accordance with Ind AS 20. As per Ind AS 109, the loan should be initially measured at its fair value.

Initial recognition of grant as on 1st April, 20X1

Fair value of loan = Rs. 25,00,000 x 0.567 (PVF @ 12%, 5th year) = Rs. 14,17,500

A Limited will recognize Rs. 10,82,500 (25,00,000 – 14,17,500) as the government grant and will make the following entry on receipt of loan:

Date	Particulars		Dr. (Rs.)	Cr. (Rs.)
1.4.20X1	Bank account	Dr.	25,00,000	
	To Deferred Grant Income			10,82,500
	To Loan account			14,17,500
	Being grant initially recorded at fair value)			

Accounting treatment for year ending 31st March, 20X2

As per para 3 of Ind AS 20, grants related to assets are government grants whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets.

As per para 24-27 of Ind AS 20, Government grants related to assets, including non-monetary grants at fair value, shall be presented in the balance sheet either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.

One method recognises the grant as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset.

The other method deducts the grant in calculating the carrying amount of the asset. The grant is recognised in profit or loss over the life of a depreciable asset as a reduced depreciation expense.

A Ltd. has adopted first method of recognising the grant as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset. Here, deferred income is recognised in profit or loss in the proportion in which depreciation expense on the asset is recognised.

Depreciation for the year (20X1-20X2) = Rs. 50,00,000 / 5 years = Rs. 10,00,000

As the loan is to finance a depreciable asset, Rs. 10,82,500 will be recognized in Profit or Loss on the same basis as depreciation.
Since the depreciation is provided on straight line basis by A Limited, it will credit Rs. 2,16,500 (10,82,500 / 5) equally to its statement of profit and loss over the 5 years.

Date	Particulars		Dr. (Rs.)	Cr. (Rs.)
31.3.20X2	Depreciation (Profit or Loss A/c)	Dr.	10,00,000	
	To Property, Plant & Equipment			10,00,000
	(Being depreciation provided for the year)			
	Deferred grant income	Dr.	2,16,500	
	To Profit or Loss			2,16,500
	(Being deferred income adjusted)			

Impact on profit or loss due to revocation of government grant as on 31st March 20X3
As per para 32 of Ind AS 20, a government grant that becomes repayable shall be accounted for as a change in accounting estimate. Repayment of a grant related to income shall be applied first against any unamortised deferred credit recognised in respect of the grant. To the extent that the repayment exceeds any such deferred credit, or when no deferred credit exists, the repayment shall be recognised immediately in profit or loss.

Amount payable to Government on account of principal loan = Rs. 25,00,000
Amount payable to Government on account of penalty = Rs. 10,00,000

Journal Entries

Date	Particulars		Dr. (Rs.)	Cr. (Rs.)
31.3.20X3	Deferred grant income	Dr.	2,16,500	
	To Profit or Loss			
	Being deferred income adjusted)			
	Loan account (W.N.1)	Dr.	17,78,112	
	Deferred grant income (W.N.2)	Dr.	6,49,500	
	Profit or Loss	Dr.	72,388	
	To Government grant payable			25,00,000
	Being refund of government grant)			
	Profit or Loss	Dr.	10,00,000	
	To Government grant payable			10,00,000
	Being penalty payable to government)			

Therefore, total impact on profit or loss on account of revocation of government grant as on 31st March, 20X3 will be Rs. 10,72,388 (10,00,000 + 72,388).
Circumstances giving rise to repayment of a grant related to an asset may require consideration to be given to the possible impairment of the new carrying amount of the asset.

Working Notes:

1. Amortisation Schedule of Loan

Year	Opening balance of Loan	Interest @ 12%	Closing balance of Loan
31.03.20X2	14,17,500	1,70,100	15,87,600
31.03.20X3	15,87,600	1,90,512	17,78,112

2. Deferred Grant Income

Year	Opening balance	Adjustment	Closing balance
31.03.20X2	10,82,500	2,16,500	8,66,000
31.03.20X3	8,66,000	2,16,500	6,49,500

Thanks ….

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IND AS – 12
INCOME TAXES

CHAPTER - 24

Question 1 : May 2018 – RTP

A's Ltd. profit before tax according to Ind AS for Year 20X1-20X2 is Rs.100 thousand and taxable profit for year 20X1-20X2 is Rs.104 thousand. The difference between these amounts arose as follows:

On 1st February, 20X2, it acquired a machine for Rs.120 thousand. Depreciation is charged on the machine on a monthly basis for accounting purpose. Under the tax law, the machine will be depreciated for 6 months. The machine's useful life is 10 years according to Ind AS as well as for tax purposes. In the year 20X1-20X2, expenses of Rs.8 thousand were incurred for charitable donations. These are not deductible for tax purposes.

You are required to prepare necessary entries as at 31st March 20X2, taking current and deferred tax into account. The tax rate is 25%.

Also prepare the tax reconciliation in absolute numbers as well as the tax rate reconciliation.

Solution :

1) Current Tax = Taxable Profit × Tax Rate

= 104 × 25% = 24 thousand

2) Deffered Tax :

a)

	A/c	**Tax**	
Asset - Cost	120	120	
- Depreciation	2	6	
CA	118	114	Tax Base

Taxable temporary difference = 4 × (118 – 114)

b) Charitable Donation

CA Nil

Tax bare Nil

∴ Total taxable difference = 4

Deferred tax liability = 4 × 25% = 1

3) Journal entries

a) Current tax

Profit & Loss A/c	Dr.	25	
To Current Tax			25

b) Deferred tax

Profit & Loss A/c Dr. 1
To Deferred Tax 1

4) Tax reconciliation in absolute No.

Tax Expenses (100 × 25%)	25
Add : Expenses (Donation) of deductible for tax (8 × 25%)	2
Less : Deferred tax (difference of Depreciation)	(1)
Current Tax	26

5) Tax Rate Reconciliation

Application Tax Rate	25%
Expenses not deductible for tax	2%
Effective tax rate	27%

Question 2 : Nov 2018 – RTP

X Ltd. prepares consolidated financial statements to 31st March each year. During the year ended 31st March 2018, the following events affected the tax position of the group:

(i) Y Ltd., a wholly owned subsidiary of X Ltd., made a loss adjusted for tax purposes of Rs.30,00,000. Y Ltd. is unable to utilise this loss against previous tax liabilities. Income-tax Act does not allow Y Ltd. to transfer the tax loss to other group companies. However, it allows Y Ltd. to carry the loss forward and utilise it against company's future taxable profits. The directors of X Ltd. do not consider that Y Ltd. will make taxable profits in the foreseeable future.

(ii) Just before 31st March, 2018, X Ltd. committed itself to closing a division after the year end, making a number of employees redundant. Therefore X Ltd. recognised a provision for closure costs of Rs.20,00,000 in its statement of financial position as at 31st March, 2018. Income-tax Act allows tax deductions for closure costs only when the closure actually takes place. In the year ended 31 March 2019, X Ltd. expects to make taxable profits which are well in excess of Rs.20,00,000. On 31st March, 2018, X Ltd. had taxable temporary differences from other sources which were greater than Rs.20,00,000.

(iii) During the year ended 31 March 2017, X Ltd. capitalised development costs which satisfied the criteria in paragraph 57 of Ind AS 38 'Intangible Assets'. The total amount capitalised was Rs.16,00,000. The development project began to generate economic benefits for X Ltd. from 1st January 2018. The directors of X Ltd. estimated that the project would generate economic benefits for five years from that date. The development expenditure was fully deductible against taxable profits for the year ended 31 March 2018.

(iv) On 1 April 2017, X Ltd. borrowed Rs.1,00,00,000. The cost to X Ltd. of arranging the borrowing was Rs.2,00,000 and this cost qualified for a tax deduction on 1 April 2017. The loan was for a three-year period. No interest was payable on the loan but the amount repayable on 31 March 2020 will be Rs.1,30,43,800. This equates to an effective annual interest rate of 10%. As per the Income-tax Act, a further tax deduction of Rs.30,43,800 will be claimable when the loan is repaid on 31st March, 2020.

Explain and show how each of these events would affect the deferred tax assets / liabilities in the consolidated balance sheet of X Ltd. group at 31 March, 2018 as per Ind AS. Assume the rate of corporate income tax is 20%.

Solution :

(i) The tax loss creates a potential deferred tax asset for the group since its carrying value is nil and its tax base is Rs.30,00,000.
However, no deferred tax asset can be recognised because there is no prospect of being able to reduce tax liabilities in the foreseeable future as no taxable profits are anticipated.

(ii) The provision creates a potential deferred tax asset for the group since its carrying value is Rs.20,00,000 and its tax base is nil.
This deferred tax asset can be recognised because X Ltd. is expected to generate taxable profits in excess of Rs.20,00,000 in the year to 31st March, 2019.
The amount of the deferred tax asset will be Rs.4,00,000 (Rs.20,00,000 x 20%).
This asset will be presented as a deduction from the deferred tax liabilities caused by the (larger) taxable temporary differences.

(iii) The development costs have a carrying value of Rs.15,20,000 (Rs.16,00,000 – (Rs.16,00,000 x 1/5 x 3/12)).
The tax base of the development costs is nil since the relevant tax deduction has already been claimed.
The deferred tax liability will be Rs.3,04,000 (Rs.15,20,000 x 20%). All deferred tax liabilities are shown as non-current.

(iv) The carrying value of the loan at 31st March, 2018 is Rs.1,07,80,000 (Rs.1,00,00,000 – Rs.2,00,000 + (Rs.98,00,000 x 10%)).
The tax base of the loan is Rs.1,00,00,000.
This creates a deductible temporary difference of Rs.7,80,000 (Rs.1,07,80,000 – Rs.1,00,00,000) and a potential deferred tax asset of Rs.1,56,000 (Rs.7,80,000 x 20%).
Due to the availability of taxable profits next year (see part (ii) above), this asset can be recognised as a deduction from deferred tax liabilities.

Question 3 : May 2019 – RTP

PQR Ltd., a manufacturing company, prepares consolidated financial statements to 31st March each year. During the year ended 31st March, 2018, the following events affected the tax position of the group:

- QPR Ltd., a wholly owned subsidiary of PQR Ltd., incurred a loss adjusted for tax purposes of Rs.30,00,000. QPR Ltd. is unable to utilise this loss against previous tax liabilities. Income-tax Act does not allow QPR Ltd. to transfer the tax loss to other group companies. However, it allows QPR Ltd. to carry the loss forward and utilise it against company's future taxable profits. The directors of PQR Ltd. do not consider that QPR Ltd. will make taxable profits in the foreseeable future.
- During the year ended 31st March, 2018, PQR Ltd. capitalised development costs which satisfied the criteria as per Ind AS 38 'Intangible Assets'. The total amount capitalised was Rs.16,00,000. The development project began to generate economic benefits for PQR Ltd.

from 1st January, 2018. The directors of PQR Ltd. estimated that the project would generate economic benefits for five years from that date. The development expenditure was fully deductible against taxable profits for the year ended 31st March, 2018.

- On 1st April, 2017, PQR Ltd. borrowed Rs.1,00,00,000. The cost to PQR Ltd. of arranging the borrowing was Rs.2,00,000 and this cost qualified for a tax deduction on 1st April 2017. The loan was for a three-year period. No interest was payable on the loan but the amount repayable on 31st March 2020 will be Rs.1,30,43,800. This equates to an effective annual interest rate of 10%. As per the Income-tax Act, a further tax deduction of Rs.30,43,800 will be claimable when the loan is repaid on 31st March, 2020.

  Explain and show how each of these events would affect the deferred tax assets / liabilities in the consolidated balance sheet of PQR Ltd. group at 31st March, 2018 as per Ind AS. The rate of corporate income tax is 30%.

Solution :

Impact on consolidated balance sheet of PQR Ltd. group at 31st March, 2018

- The tax loss creates a potential deferred tax asset for the PQR Ltd. group since its carrying value is nil and its tax base is Rs.30,00,000. However, no deferred tax asset can be recognised because there is no prospect of being able to reduce tax liabilities in the foreseeable future as no taxable profits are anticipated.
- The development costs have a carrying value of Rs.15,20,000 (Rs.16,00,000 – (Rs.16,00,000 × 1/5 × 3/12)). The tax base of the development costs is nil since the relevant tax deduction has already been claimed. The deferred tax liability will be Rs.4,56,000 (Rs.15,20,000 × 30%). All deferred tax liabilities are shown as non-current.
- The carrying value of the loan at 31st March, 2018 is Rs.1,07,80,000 (Rs.1,00,00,000 – Rs.200,000 + (Rs.98,00,000 × 10%)). The tax base of the loan is 1,00,00,000. This creates a deductible temporary difference of Rs.7,80,000 and a potential deferred tax asset of Rs.2,34,000 (Rs.7,80,000 × 30%).

Question 4 : Nov 2019 – RTP

An entity is finalising its financial statements for the year ended 31st March, 20X2. Before 31st March, 20X2, the government announced that the tax rate was to be amended from 40 per cent to 45 per cent of taxable profit from 30th June, 20X2.

The legislation to amend the tax rate has not yet been approved by the legislature. However, the government has a significant majority and it is usual, in the tax jurisdiction concerned, to regard an announcement of a change in the tax rate as having the substantive effect of actual enactment (i.e. it is substantively enacted).

After performing the income tax calculations at the rate of 40 per cent, the entity has the following deferred tax asset and deferred tax liability balances :

Deferred tax asset	Rs.80,000
Deferred tax liability	Rs.60,000

Of the deferred tax asset balance, Rs. 28,000 related to a temporary difference. This deferred tax asset had previously been recognised in OCI and accumulated in equity as a revaluation surplus.

The entity reviewed the carrying amount of the asset in accordance with para 56 of Ind AS 12 and determined that it was probable that sufficient taxable profit to allow utilisation of the deferred tax asset would be available in the future.
Show the revised amount of Deferred tax asset & Deferred tax liability and present the necessary journal entries.

Solution :

Calculation of Deductible temporary differences :

Deferred tax asset = Rs.80,000
Existing tax rate = 40%
Deductible temporary differences = 80,000/40%
= Rs.2,00,000

Calculation of Taxable temporary differences:

Deferred tax liability = Rs.60,000
Existing tax rate = 40%
Deductible temporary differences = 60,000/40%
= Rs.1,50,000

Of the total deferred tax asset balance of Rs.80,000, Rs.28,000 is recognized in OCI
Hence, Deferred tax asset balance of Profit & Loss is Rs.80,000 – Rs.28,000 = Rs.52,000
Deductible temporary difference recognized in Profit & Loss is Rs.1,30,000 (52,000 / 40%)
Deductible temporary difference recognized in OCI is Rs.70,000 (28,000 / 40%)
The adjusted balances of the deferred tax accounts under the new tax rate are:

Deferred tax asset		**Rs.**
Previously credited to OCI-equity	Rs.70,000 x 0.45	31,500
Previously recognised as Income	Rs.1,30,000 x 0.45	58,500
		90,000
Deferred tax liability		
Previously recognized as expense	Rs.1,50,000 x 0.45	67,500

The net adjustment to deferred tax expense is a reduction of Rs.2,500. Of this amount, Rs.3,500 is recognised in OCl and Rs.1,000 is charged to P&L.

An alternative method of calculation is :		**Rs.**
DTA shown in OCI	Rs.70,000 × (0.45 - 0.40)	3,500
DTA shown in Profit or Loss	Rs.1,30,000 × (0.45-0.40)	6,500
DTL shown in Profit or Loss	Rs.1,50,000 × (0.45 -0.40)	7,500

Journal Entries

	Rs.	**Rs.**
Deferred tax asset	3,500	
OCI –revaluation surplus		3,500
Deferred tax asset	6,500	
Deferred tax expense		6,500
Deferred tax expense	7,500	

Deferred tax liability		7,500

Alternatively, a combined journal entry may be passed as follows:

		Rs.	Rs.
Deferred tax asset	Dr.	10,000	
Deferred tax expense	Dr.	1,000	
To OCI –revaluation surplus			3,500
To Deferred tax liability			7,500

Question 5 : Nov 2020 – RTP

On 1 January 2020, entity H acquired 100% share capital of entity S for Rs.15,00,000. The book values and the fair values of the identifiable assets and liabilities of entity S at the date of acquisition are set out below, together with their tax bases in entity S's tax jurisdictions. Any goodwill arising on the acquisition is not deductible for tax purposes. The tax rates in entity H's and entity S's jurisdictions are 30% and 40% respectively.

Acquisitions	**Book values Rs.'000**	**Tax base Rs.'000**	**Fair values Rs.'000**
Land and buildings	600	500	700
Property, plant and equipment	250	200	270
Inventory	100	100	80
Accounts receivable	150	150	150
Cash and cash equivalents	130	130	130
Accounts payable	(160)	(160)	(160)
Retirement benefit obligations	(100)	-	(100)

You are required to calculate the deferred tax arising on acquisition of Entity S. Also calculate the Goodwill arising on acquisition.

Solution :

1) Calculation of Deferred tax as per IND AS 103

Net Assets	**Tax base**	**Fair Value**
Assets		
Land & Building	500	700
Property, Plant & Equipment	200	270
Inventory	100	80
Accounts Receivable	150	150
Cash & Cash Equivalent	130	130
	1080	1330
Liability		
Account payable	(160)	(160)
Retirement benefit ob.	–	(100)
Net Assets	920	1070

Difference (1070 – 920) = 150
Differed tax = 150 × 40% = 60

2) Calculating of goodwill

Purchase consideration	1500
Less : Fair value of Net Assets (1070 – 60)	1010
Goodwill	490

Question 6 : Nov 2020 – Paper

Lal Ltd. provides you the following information for financial year 2019-2020:
Estimated Income for the year ended 31 March 2020:

Gross Annual Income (inclusive of Estimated Capital Gains of Rs. 4,00,000)	Rs. 16,50,000
Quarter I	Rs. 3,50,000
Quarter II	Rs. 4,00,000
Quarter III (including Estimated Capital Gains of Rs. 4,00,000)	Rs. 6,00,000
Quarter IV	Rs. 3,00,000

Tax Rates	On Other Income	First Rs. 2,50,000	20%
		Balance Income	30%
	On Capital Gains		12%

Calculate the tax expense for each quarter, assuming that there is no difference between the estimated taxable income and the estimated accounting income.

Solution :

As per Ind AS 34 'Interim Financial Reporting', income tax expense is recognised in each interim period based on the best estimate of the weighted average annual income tax rate expected for the full financial year.

If different income tax rates apply to different categories of income (such as capital gains or income earned in particular industries) to the extent practicable, a separate rate is applied to each individual category of interim period pre-tax income.

	Rs.
Estimated annual income exclusive of estimated capital gain (16,50,000 – 4,00,000) (A)	12,50,000
Tax expense on other income:	
20% on Rs. 2,50,000	50,000
30% on remaining Rs. 10,00,000	3,00,000
(B)	3,50,000
Weighted average annual income tax rate = $\frac{B}{A} = \frac{3,50,000}{12,50,000}$ = 28%	

Tax expense to be recognised in each of the quarterly reports:

			Rs.
Quarter I -	Rs. 3,50,000 x 28%		98,000
Quarter II -	Rs. 4,00,000 x 28%		1,12,000
Quarter III -	Rs. (6,00,000 - 4,00,000) x 28%	56,000	
	Rs. 4,00,000 x 12%	48,000	1,04,000
Quarter IV -	Rs. 3,00,000 x 28%		84,000
			3,98,000

Question 7 : Jan 2021 – Paper

C Ltd. acquired the following assets and liabilities of D Ltd. in a business combination:

Rs. in '000s

	Fair Value	Carrying Amount	Temporary Difference
Plant & equipment	500	510	(10)
Inventory	130	150	(20)
Trade receivables	200	210	(10)
Loans and advances	80	85	(5)
	910	955	(45)
10% Debentures	200	200	
	710	755	
Consideration Paid	760	760	
Goodwill	50	5	45

Goodwill is deductible as permissible expenses under the existing tax law. Calculate Deferred Tax Asset / liability as per relevant Ind AS and also pass related journal entry in books of C Ltd. and assume tax rate at 25%.

Solution :

In this case there is a Deferred Tax Asset as the Tax base of assets acquired is higher by Rs. 45,000. Deferred Tax Asset would be Rs. 11,250 (45,000 x 25%)

Journal entry

Plant and equipment	Dr.	5,00,000	
Inventory	Dr.	1,30,000	
Trade receivables	Dr.	2,00,000	
Loans and advances	Dr.	80,000	
Goodwill (50,000 - 11,250)	Dr.	38,750	
Deferred Tax Asset	Dr.	11,250	
To 10% Debentures			2,00,000
To Bank			7,60,000

(Assets and liabilities taken over, goodwill and defer red tax asset have been recognised)

Question 8 : May 2021 – RTP

The entity has an identifiable asset ASSOTA with a carrying amount of Rs. 10,00,000. Its recoverable amount is Rs. 6,50,000. The tax base of ASSOTA is Rs. 8,00,000 and the tax rate is 30%. Impairment losses are not tax deductible. Entity expects to continue to earn profits in future. For the identifiable asset ASSOTA, what would be the impact on the deferred tax asset/ liability at the end of the period?

Solution :

As per Ind AS 36, the revised carrying amount of asset ASSOTA would be Rs.6,50,000.
The tax base of asset ASSOTA is given as Rs.8,00,000.

Carrying base of asset	= Rs.6,50,000
Tax base of asset	= Rs.8,00,000

Since tax base is greater than carrying base of asset, so deferred tax asset would be created on the temporary difference of Rs.1,50,000 (Rs.8,00,000 – Rs.6,50,000) at the given tax rate of 30%. Hence, Deferred tax asset for the asset ASSOTA would be Rs.1,50,000 x 30% = Rs.45,000.

Thanks ....

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IND AS – 24 RELATED PARTY DISCLOSURE

CHAPTER - 25

Question 1 : May 2018 – RTP

Mr. Atul is an independent director of a company X Ltd. He plays a vital role in the Management of X Ltd. and contributes in major decision making process of the organisation. X Ltd. pays sitting fee of Rs.2,00,000 to him for every Board of Directors' (BOD) meeting he attends. Throughout the year, X Ltd. had 5 such meetings which was attended by Mr. Atul.

Similarly, a non-executive director, Mr. Naveen also attended 5 BOD meetings and charged Rs.1,50,000 per meeting. The Accountant of X Ltd. believes that they being not the employees of the organisation, their fee should not be disclosed as per related party transaction in accordance with Ind AS 24.

Examine whether the sitting fee paid to independent director and non-executive director is required to be disclosed in the financial statements prepared as per Ind AS?

Solution :

As per Ind AS 24, Related Party Disclosures, "Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity."

Accordingly, key management personnel (KMP) includes any director of the entity who are having authority and responsibility for planning, directing and controlling the activities of the entity. Hence, independent director Mr. Atul and non-executive director Mr. Naveen are covered under the definition of KMP in accordance with Ind AS.

Also as per Ind AS 19, 'Employee Benefits', an employee may provide services to an entity on a full-time, part-time, permanent, casual or temporary basis. For the purpose of the Standard, Employees include directors and other management personnel.

Therefore, an entity shall disclose key management personnel compensation in total i.e. disclosure of directors' fee of (Rs.10,00,000 + Rs.7,50,000) Rs.17,50,000 is to be made as employees benefits (under various categories).

Question 2 : Nov 2018 – RTP

ABC Ltd. is a long-standing customer of XYZ Ltd. Mrs. P whose husband is a director in XYZ Ltd. purchased a controlling interest in entity ABC Ltd. on 1st June, 2017. Sales of products from XYZ Ltd. to ABC Ltd. in the two-month period from 1st April 2017 to 31st May 2017 totalled Rs.8,00,000. Following the shares purchased by Mrs. P, XYZ Ltd. began to supply the products at a discount of 20% to their normal selling price and allowed ABC Ltd. three months' credit

(previously ABC Ltd. was only allowed one month's credit, XYZ Ltd.'s normal credit policy). Sales of products from XYZ Ltd. to ABC Ltd. in the ten-month period from 1st June 2017 to 31st March 2017 totalled Rs.60,00,000. On 31st March 2018, the trade receivables of XYZ Ltd. included Rs.18,00,000 in respect of amounts owing by ABC Ltd.
Analyse and show how the above event would be reported in the financial statements of XYZ Ltd. for the year ended 31 March 2018 and mention the disclosure requirements also as per Ind AS.

Solution :

XYZ Ltd. would include the total revenue of Rs.68,00,000 (Rs.60,00,000 + Rs.8,00,000) from ABC Ltd. received / receivable in the year ended 31st March 2018 within its revenue and show Rs.18,00,000 within trade receivables at 31st March 2018.
Mrs. P would be regarded as a related party of XYZ Ltd. because she is a close family member of one of the key management personnel of XYZ Ltd.
From 1st June 2017, ABC Ltd. would also be regarded as a related party of XYZ Ltd. because from that date ABC Ltd. is an entity controlled by another related party.
Because ABC Ltd. is a related party with whom XYZ Ltd. has transactions, then XYZ Ltd. should disclose:

– The nature of the related party relationship.
– The revenue of Rs.60,00,000 from ABC Ltd. since 1st June 2017.
– The outstanding balance of rs.18,00,000 at 31st March 2018.

In the current circumstances it may well be necessary for XYZ Ltd. to also disclose the favourable terms under which the transactions are carried out.

Question 3 : Nov 2019 – RTP

Uttar Pradesh State Government holds 60% shares in PQR Limited and 55% shares in ABC Limited. PQR Limited has two subsidiaries namely P Limited and Q Limited. ABC Limited has two subsidiaries namely A Limited and B Limited. Mr. KM is one of the Key management personnel in PQR Limited.

(a) Determine the entity to whom exemption from disclosure of related party transactions is to be given. Also examine the transactions and with whom such exemption applies.

(b) What are the disclosure requirements for the entity which has availed the exemption?

Solution :

(a) As per Ind AS 24, 'Related Party Disclosures', if an entity had related party transactions during the periods covered by the financial statements, it shall disclose the nature of the related party relationship as well as information about those transactions and outstanding balances, including commitments, necessary for users to understand the potential effect of the relationship on the financial statements.

However, as per standard a reporting entity is exempt from the disclosure requirements in relation to related party transactions and outstanding balances, including commitments, with:

(i) a government that has control or joint control of, or significant influence over, the reporting entity; and

(ii) another entity that is a related party because the same government has control or joint control of, or significant influence over, both the reporting entity and the other entity

According to the above paras, for Entity P's financial statements, the exemption applies to:

(i) transactions with Government Uttar Pradesh State Government; and

(ii) transactions with Entities PQR and ABC and Entities Q, A and B.

Similar exemptions are available to Entities PQR, ABC, Q, A and B, with the transactions with UP State Government and other entities controlled directly or indirectly by UP State Government. However, that exemption does not apply to transactions with Mr. KM. Hence, the transactions with Mr. KM needs to be disclosed under related party transactions.

(b) It shall disclose the following about the transactions and related outstanding balances referred to :

(a) the name of the government and the nature of its relationship with the reporting entity (ie control, joint control or significant influence);

(b) the following information in sufficient detail to enable users of the entity's financial statements to understand the effect of related party transactions on its financial statements:

(i) the nature and amount of each individually significant transaction; and

(ii) for other transactions that are collectively, but not individually, significant, a qualitative or quantitative indication of their extent.

Question 4 : Nov 2020 – RTP

Mr. X owns 95% of entity A and is its director. He is also beneficiary of a trust that owns 100% of entity B, of which he is a director.

Whether entities A and B are related parties?

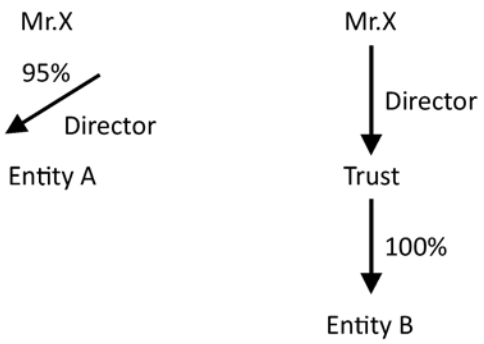
Would the situation be different if:

(a) Mr. X resigned as a director of entity A, but retained his 95% holding?

(b) Mr. X resigned as a director of entities A and B and transferred the 95% holding in entity A to the trust?

Solution :

1)



As per IND AS 24, Entity A and Entity B are related parties since Mr.X controls both entity A and B.

2) Mr.X resigns as director of A, but still controls A through 95% holding. He also continues to control B therefore Entity A and Entity controls to be related party.

3) Mr.X resigned as a director of A and B and transferred the 95% holding in entity A to the trust.
Since Mr.A control trust that will controls A and B. Entity A and Entity B will still continue to be related party.

Question 5 : May 2022 – RTP

Entity A owns 30% of the share capital of entity B and has the ability to exercise significant influence over it.
Entity B holds the following investments:

- 70% of the share capital of its subsidiary, entity C; and
- 30% of the share capital of entity D, with the ability to exercise significant influence.

Entity A transacts with entities C and D. Should entity A disclose these transactions as related party transactions in its separate financial statements? Also explain the disclosure of such transactions in the financial statements of C and D as related party transaction.

Solution :

Entity A should disclose its transactions with entity C in entity A's separate financial statements. Entity C is a related party of entity A, because entity C is the subsidiary of entity A's associate, entity B.
Entity A's management is not required to disclose entity A's transactions with entity D in its financial statements. Entity D is not a related party of entity A, because entity A has no ability to exercise control or significant influence over entity D.
Entity C is required to disclose its transactions with entity A in its financial statements, because entity A is a related partly.
Entity D is not required to disclose transactions with entity A, because they are not related parties.

Thanks ....

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IND AS – 33 EARNINGS PER SHARE

CHAPTER - 26

Question 1 : May 2018 – RTP

P Ltd. is a subsidiary company of ABC Ltd. It preparing both Separate financial statement (SFS) and consolidated financial statements (CFS) for the year ending on 31st March, 20XI. It has net profit after tax of Rs.20,00,000 as per SFS & Rs.16,00,000 as per CFS. Share capital of P Ltd. is 2,00,000 shares of Rs.10 each. ABC Ltd. has acquired 80% shares of P Ltd. Accountant of P Ltd. had calculated following Basic EPS for its SFS:

Calculation of Basic EPS in its SFS	
Net Profit after tax	Rs.16,00,000
Number of equity shares attributable to Parent company ABC Ltd. (2,00,000 x 80%) shares	1,60,000
Basic EPS	Rs.10 per share

Examine the correctness of the above presentation of Basic EPS.

Solution :

As per Ind AS 33 "Earnings per Share", when an entity presents both consolidated financial statements and separate financial statements prepared in accordance with Ind AS 110, Consolidated Financial Statements, and Ind AS 27, Separate Financial Statements, respectively, the disclosures required by this Standard shall be presented both in the consolidated financial statements and separate financial statements. In consolidated financial statements such disclosures shall be based on consolidated information and in separate financial statements such disclosures shall be based on information given in separate financial statements.

Hence, the presentation of Basic EPS by the Accountant of P Ltd. on the basis of consolidated financial statements in its separate financial statements is not correct. The correct presentation of Basic EPS would be as follows:

Calculation of Basic EPS of P Ltd. in SFS	
Net Profit after tax	Rs.20,00,000
No. of share issued	2,00,000 shares
Basic EPS	Rs.10 per share

Question 2 : May 2019 – RTP

An entity issues 2,000 convertible bonds at the beginning of Year 1. The bonds have a three-year term, and are issued at par with a face value of Rs.1,000 per bond, giving total proceeds of Rs. 2,000,000. Interest is payable annually in arrears at a nominal annual interest rate of 6 per cent. Each bond is convertible at any time up to maturity into 250 ordinary shares. The entity has an option to settle the principal amount of the convertible bonds in ordinary shares or in cash.

When the bonds are issued, the prevailing market interest rate for similar debt without a conversion option is 9 per cent. At the issue date, the market price of one ordinary share is Rs. 3. Income tax is ignored.

Calculate basic and diluted EPS when

Profit attributable to ordinary equity holders of the parent entity Year 1	Rs.1,000,000
Ordinary shares outstanding	1,200,000
Convertible bonds outstanding	2,000

Solution :

Allocation of proceeds of the bond issue:

Liability component (Refer Note 1)	Rs.1,848,122
Equity component	Rs.151,878
	Rs.2,000,000

The liability and equity components would be determined in accordance with Ind AS 32. These amounts are recognised as the initial carrying amounts of the liability and equity components. The amount assigned to the issuer conversion option equity element is an addition to equity and is not adjusted.

Basic earnings per share Year 1:

$$\frac{Rs.1{,}000{,}000}{1{,}200{,}000}$$ = Rs.0.83 per ordinary share

Diluted earnings per share Year 1:

It is presumed that the issuer will settle the contract by the issue of ordinary shares. The dilutive effect is therefore calculated in accordance with the Standard.

$$\frac{Rs.1{,}000{,}000 + Rs.166{,}331}{1{,}200{,}000 + 500{,}000}$$ = Rs.0.69 per ordinary share

Notes:

1. This represents the present value of the principal and interest discounted at 9% – Rs.2,000,000 payable at the end of three years; Rs.120,000 payable annually in arrears for three years.
2. Profit is adjusted for the accretion of Rs.166,331 (Rs.1,848,122 × 9%) of the liability because of the passage of time. However, it is assumed that interest @ 6% for the year has already been adjusted.
3. 500,000 ordinary shares = 250 ordinary shares × 2,000 convertible bonds.

Question 3 : May 2020 – RTP

CAB Limited is in the process of preparation of the consolidated financial statements of the group for the year ending 31st March, 20X3 and the extract of the same is as follows:

Particulars	Attributable to CAB Limited	Non-controlling interest	Total (Rs.in '000)
Profit for the year	39,000	3,000	42,000
Other Comprehensive Income	5,000	Nil	5,000

Total Comprehensive Income	44,000	3,000	47,000

The long-term finance of the company comprises of the following:

(i) 20,00,00,000 equity shares at the beginning of the year and the company has issued 5,00,00,000 shares on 1st July, 20X2 at full market value.

(ii) 8,00,00,000 irredeemable preference shares. These shares were in issue for the whole of the year ended 31st March, 20X3. The dividend on these preference shares is discretionary.

(iii) Rs.18 crores of 6% convertible debentures issued on 1st April, 20X1 and repayable on 31st March, 20X5 at par. Interest is payable annually. As an alternative to repayment at par, the holder on maturity can elect to exchange their convertible debentures for 10 crores ordinary shares in the company. On 1st April, 20X1, the prevailing market interest rate for four-year convertible debentures which had no right of conversion was 8%. Using an annual discount rate of 8%, the present value of Rs.1 payable in four years is 0.74 and the cumulative present value of Rs.1 payable at the end of years one to four is 3.31.

In the year ended 31st March, 20X3, CAB Limited declared an ordinary dividend of 0.10 paise per share and a dividend of 0.05 paise per share on the irredeemable preference shares.

Compute the following:

- the finance cost of convertible debentures and its closing balance as on 31st March, 20X3 to be presented in the consolidated financial statements.
- the basic and diluted earnings per share for the year ended 31st March, 20X3.

Assume that income tax is applicable to CAB Limited and its subsidiaries at 25%.

Solution :

Calculation of the liability and equity components on 6% Convertible debentures:

Present value of principal payable at the end of 4th year (Rs.1,80,000 thousand x 0.74) = Rs.1,33,200 thousand

Present value of interest payable annually for 4 years (Rs.1,80,000 thousand x 6% x 3.31) = Rs.35,748 thousand

Total liability component = Rs.1,68,948 thousand

Therefore, equity component = Rs.1,80,000 thousand – Rs.1,68,948 thousand = Rs.11,052 thousand

Calculation of finance cost and closing balance of 6% convertible debentures

Year	Opening balance Rs. in '000	Finance cost @ 8% Rs. in '000	Interest paid @ 6% Rs. in '000	Closing balance Rs. in '000
	a	b = a x 8%	c	d = a + b - c
31.3.20X2	1,68,948	13,515.84	10,800	1,71,663.84
31.3.20X3	1,71,663.84	13,733.11	10,800	1,74,596.95

Finance cost of convertible debentures for the year ended 31.3. 20X3 is **Rs.13,733.11** thousand and closing balance as on 31.3. 20X3 is **Rs.1,74,596.95** thousand.

Calculation of Basic EPS

Rs.in '000

Profit for the year	39,000
Less: Dividend on preference shares (80,000 thousand x Rs.0.05)	(4,000)
Profit attributable to equity shareholders	35,000

Weighted average number of shares = 20,00,00,000 + {5,00,00,000 x (9/12)}
= 23,75,00,000 shares or 2,37,500 thousand shares

Basic EPS = Rs.35,000 thousand / 2,37,500 thousand shares
= Rs.0.147

Calculation of Diluted EPS Rs. in '000

Profit for the year		39,000
Less: Dividend on preference shares (80,000 x 0.05)		(4,000)
		35,000
Add: Finance cost (as given in the above table)	13,733.11	
Less: Tax @ 25%	(3,433.28)	10,299.83
		45,299.83

Weighted average number of shares = 20,00,00,000 + {5,00,00,000 x (9/12)} + 10,00,00,000
= 33,75,00,000 shares or 3,37,500 thousand shares

Diluted EPS = Rs.45,299.83 thousand / 3,37,500 thousand shares
= Rs.0.134

Question 4 : Nov 2020 – Paper

The following information is available relating to Space India Limited for the Financial Year 2019-2020.

Net profit attributable to equity shareholders	Rs.90,000
Number of equity shares outstanding	16,000
Average fair value of one equity share during the year	Rs.90

Potential Ordinary Shares:

Options	900 options with exercise price of Rs. 75
Convertible Preference Shares	7,500 shares entitled to a cumulative dividend of Rs. 9 per share. Each preference share is convertible into 2 equity shares.
Applicable corporate dividend tax	8%
10% Convertible Debentures of Rs. 100 each	Rs. 10,00,000 and each debenture is convertible into 4 equity shares
Tax rate	25%

You are required to compute Basic and Diluted EPS of the company for the Financial Year 2019-2020.

Solution :

(i) Basic Earnings per share

		Year ended 31.3.2020
Net profit attributable to equity shareholders	(A)	Rs. 90,000
Number of equity shares outstanding	(B)	16,000
Earnings per share	(A/B)	Rs. 5.625

(ii) Diluted earnings per share

Options are most dilutive as their earnings per incremental share is nil. Hence, for the purpose of computation of diluted earnings per share, options will be considered first. 10% convertible debentures being second most dilutive will be considered next and thereafter convertible preference shares will be considered (as per W.N.).

	Net profit attributable to equity shareholders Rs.	No. of equity shares	Net Profit attributable per share Rs.	
Net profit attributable to equity shareholders	90,000	16,000	5.625	
Options	______	150		
	90,000	16,150	5.572	Dilutive
10% Convertible debentures	75,000	40,000		
	1,65,000	56,150	2.939	Dilutive
Convertible Preference Shares	72,900	15,000		
	2,37,900	71,150	3.344	Anti-Dilutive

Since diluted earnings per share is increased when taking the convertible preference shares into account (Rs. 2.939 to Rs. 3.344), the convertible preference shares are anti-dilutive and are ignored in the calculation of diluted earnings per share for the year ended 31 March 2020. Therefore, diluted earnings per share for the year ended 31 March 2020 is Rs. 2.939.

Working Note:

Calculation of incremental earnings per share and allocation of rank

	Increase in earnings (1)	Increase in number of equity shares (2)	Earnings per incremental share (3) = (1) ÷ (2)	Rank
	Rs.			
Options				
Increase in earnings	Nil		`	

No. of incremental shares issued for no consideration [900 x (90-75)/90]		150	Nil	1
Convertible Preference Shares				
Increase in net profit attributable to equity shareholders as adjusted by attributable dividend tax [(Rs.9 x 7,500) + 8% (Rs.9 x 7,500)]	72,900			
No. of incremental shares (2 x 7,500)		15,000	4.86	3
10% Convertible Debentures				
Increase in net profit [(` 10,00,000 x 10% x (1 – 0.25)]	75,000			
No. of incremental shares (10,000 x 4)		40,000	1.875	2

Note: Grossing up of preference share dividend has been ignored here. At present dividend distribution tax has been abolished. However, the question has been solved on the basis of the information given in the question.

Question 5 : July 2021 – Paper

At 31st March, 2019 the issues share capital of SB Limited consisted of 20,00,000 ordinary shares of Rs.1 each. On July 2019 the Company issued Rs.25,00,000 of 8% convertible loan stock for cash at par. Each Rs.100 nominal of the loan stock may be converted, at any time during the year ended 2024 to 2027, into the number of ordinary shares set out below :

- 31st March, 2024 : 135 Ordinary Shares
- 31st March, 2025 : 130 Ordinary Shares
- 31st March, 2026 : 125 Ordinary Shares
- 31st March, 2027 : 120 Ordinary Shares

If the loan stock is not converted by 2027, they would be redeemed at par.

It is assumed that the written equity conversion option is accounted for as a derivative liability and marked to market through profit or loss. The change in the options' fair value reported on 31st March, 2020 and 31st March 2021 amounted to losses of Rs.5,000 and Rs.5,300 respectively. Further, it is assumed that there are no tax consequences arising from these losses.

The profit before interest, fair value movements and taxation for the year ended 31st March, 2020 and 2021 amounted to Rs.16,50,000 and Rs.17,90,000 respectively and relate wholly to continuing operations. The rate of tax for both the periods is 33% (including cess and surcharge is any).

Calculate basis and Diluted EPS for 31st March 2020 and 31st March 2021.

Solution :

	2021	2020
Trading results	**Rs.**	**Rs.**
A. Profit before interest, fair value movements and tax	17,90,000	16,50,000
B. Interest on 8% convertible loan stock (2020: 9/12 × Rs. 2,00,000)	(2,00,000)	(1,50,000)
C. Change in fair value of embedded option	(5,300)	(5,000)
Profit before tax	15,84,700	14,95,000
Taxation @ 33% on (A-B)	(5,24,700)	(4,95,000)
Profit after tax	10,60,000	10,00,000
Calculation of basic EPS		
Number of equity shares outstanding	20,00,000	20,00,000
Earnings	10,60,000	10,00,000
Basic EPS	53 paise	50 paise

Calculation of diluted EPS

Test whether convertibles are dilutive:

The saving in after-tax earnings, resulting from the conversion of Rs. 100 nominal of loan stock, amounts to (Rs. 100 × 8% × 67%) + (Rs. 5,300 / 25,000) = Rs. 5.36 + Rs. 0.21 = Rs. 5.57.

There will then be 135 extra shares in issue.

Therefore, the incremental EPS is 4 paise (ie. Rs. 5.57 / 135). As this incremental EPS is less than the basic EPS at the continuing level, it will have the effect of reducing the basic EPS of 53 paise. Hence the convertibles are dilutive.

	2021	2020
Adjusted earnings	Rs.	Rs.
Profit for basic EPS	10,60,000	10,00,000
Add: Interest and other charges on earnings saved as a result of the conversion	(2,00,000 + 5,300) 2,05,300	(1,50,000 + 5,000) 1,55,000
Less: Tax relief on interest portion	(66,000)	(49,500)
Adjusted earnings for equity	11,99,300	11,05,500

Adjusted number of shares

From the conversion terms, it is clear that the maximum number of shares issuable on conversion of Rs. 25,00,000 loan stock after the end of the financial year would be at the rate of 135 shares per Rs. 100 nominal (that is, 33,75,000 shares).

	2021	2020
Number of equity shares for basic EPS	20,00,000	20,00,000
Maximum conversion at date of issue (33,75,000 × 9/12)	–	25,31,250
Maximum conversion after balance sheet date	33,75,000	–
Adjusted shares	53,75,000	45,31,250

Adjusted earnings for equity	11,99,300	11,05,500
Diluted EPS (approx.)	22 paise	24 paise

Question 6 : Nov 2021 – RTP

Following information pertains to an entity for the year ending 31st March 20X1:

Net profit for the year	Rs. 12,00,000
Weighted average number of equity shares outstanding during the year	5,00,000 shares
Average market price per share during the year	Rs. 20
Weighted average number of shares under option during the year	1,00,000 shares
Exercise price per share under option during the year	Rs. 15

Calculate basic and diluted earnings per share.

Solution :

	Earnings	Shares	Per share
Profit attributable to equity holders	Rs. 12,00,000		
Weighted average shares outstanding during year 20X1		5,00,000	
Basic earnings per share			**Rs. 2.40**
Weighted average number of shares under option		1,00,000	
Weighted average number of shares that would have been issued at average market price: (1,00,000 × Rs. 15.00) ÷ Rs. 20.00	Refer Note	(75,000)	
Diluted earnings per share	**Rs. 1,200,000**	**5,25,000**	**Rs. 2.29**

Note: Earnings have not increased because the total number of shares has increased only by the number of shares (25,000) deemed to have been issued for no consideration

Thanks ....

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IND AS – 102
SHARE BASED PAYMENTS

CHAPTER - 27

Question 1 : May 2018 – PAPER / Nov 2020 - Paper

ABC Limited issued 20,000 Share Appreciation Rights (SARs) that vest immediately to its employees on 1st April 2015. The SARs will be settled in cash. At that date it is estimated using an option pricing model, that the fair value of a SAR is Rs.95. SAR can be exercised any time up to 31st March 2018. At the end of 31st March 2016 it is expected that 95% of total employees will exercise the option, 92% of total employees will exercise the option at the end of next year and finally 89% will be vested only at the end of the 3rd year. Fair values at the end of each period have been given below:

Fair value of SAR	**Rs.**
31st March, 2016	110
31st March, 2017	107
31st March, 2018	112

Discuss the applicability of Cash Settled Share based payments under the relevant Ind AS and pass the journal entries.

Solution :

Applicability of cash settled share-based payment transactions

For cash-settled share-based payment transactions, the entity shall measure the goods or services acquired and the liability incurred at the fair value of the liability.

1. <u>When vesting conditions are attached to the share based payment plans</u>

   The recognition of such share based payment plans should be done by recognizing fair value of the liability at the time of goods/ services received and not at the date of grant.

2. <u>When no vesting period / condition is attached or to be fulfilled</u>

   Cash settled share based payment can be recognized in full at initial recognition itself.

   Until the liability is settled, the entity shall remeasure the fair value of the liability at the end of each reporting period date and difference in fair value will be charged to profit or loss for the period as employee benefit expenses.

   At the date of settlement, the liability is paid in cash based on the fair value on the date of settlement.

Calculation of expenses recognized during the year on account of change in the fair value of SARs

Period	Fair value	To be vested	Cumulative expenses	Expense / (benefit) for the current year
	a	b	c = a x b x 20,000	d = c-of current period – c of previous period
1st April, 2015	95	100%	19,00,000	19,00,000
31st March, 2016	110	95%	20,90,000	1,90,000
31st March, 2017	107	92%	19,68,800	(1,21,200)
31st March, 2018	112	89%	19,93,600	24,800
				19,93,600

Journal Entries

Date			Dr.(Rs.)	Cr.(Rs.)
1st April, 2015	Employee benefits expenses To Share based payment liability (Fair value of the SAR recognized initially)	Dr.	19,00,000	 19,00,000
31st March, 2016	Employee benefits expenses To Share based payment liability (Fair value of the SAR re-measured)	Dr.	1,90,000	 1,90,000
31st March, 2017	Share based payment liability To Employee benefits expenses (Fair value of the SAR re-measured & reversed)	Dr.	1,21,200	 1,21,200
31st March, 2018	Employee benefits expenses To Share based payment liability (Fair value of the SAR remeasured & recognized)	Dr.	24,800	 24,800
	Share based payment liability To Cash (Settlement of SARs in cash)	Dr.	19,93,600	 19,93,600

Question 2 : Nov 2018 – RTP / Nov 2019 – Paper

P Ltd. granted 400 stock appreciation rights (SAR) each to 75 employees on 1st April 2017 with a fair value Rs.200. The terms of the award require the employee to provide service for four years in order to earn the award. The fair value of each SAR at each reporting date is as follows:

31st March 2018	Rs.210
31st March 2019	Rs.220
31st March 2020	Rs.215
31st March 2021	Rs.218

What would be the difference if at the end of the second year of service (i.e. at 31st March 2019), P Ltd. modifies the terms of the award to require only three years of service. Answer on the basis of relevant Ind AS.

Solution :

a) Without modification of service period :

	31/03/2018	31/03/2019	31/03/2020	31/03/2021
Options	400	400	400	400
Employees	75	75	75	75
Fair value	210	220	215	218
Life	4 Years	4 Years	4 Years	4 Years

31/3/18 = $\frac{400 \times 75 \times 210}{4} \times 1$ = 15,75,000

31/3/19 = $\frac{400 \times 75 \times 220}{4} \times 2$ = 33,00,000 – 15,75,000 = 17,25,000

31/3/20 = $\frac{400 \times 75 \times 215}{4} \times 3$ = 48,37,500 – 33,00,000 = 15,37,500

31/3/21 = $\frac{400 \times 75 \times 218}{4} \times 4$ = 65,40,000 – 48,37,500 = 17,02,500

Journal Entries :

31/3/18	Employee Comp. Exp. (P&L)	15,75,000	
	To Liability for SAR		15,75,000
31/3/19	Employee Comp. Exp. (P&L)	17,25,000	
	To Liability for SAR		17,25,000
31/3/20	Employee Comp. Exp. (P&L)	15,37,500	
	To Liability for SAR		15,37,500
31/3/21	Employee Comp. Exp. (P&L)	17,02,500	
	To Liability for SAR		17,02,500

b) With modification of service period :

	31/03/2018	31/03/2019	31/03/2020
Options	400	400	400
Employees	75	75	75
Fair value	210	220	215
Life	4 Years	3 Years	3 Years

31/3/18 = $\frac{400 \times 75 \times 210}{4} \times 1$ = 15,75,000

31/3/19 = $\frac{400 \times 75 \times 220}{4} \times 2$ = 44,00,000 – 15,75,000 = 28,25,000

31/3/20 = $\frac{400 \times 75 \times 215}{4} \times 3$ = 64,50,000 – 44,00,000 = 20,50,000

Journal Entries :

31/3/18	Employee Comp. Exp. (P&L)	15,75,000	
	To Liability for SAR		15,75,000
31/3/19	Employee Comp. Exp. (P&L)	28,25,000	
	To Liability for SAR		28,25,000
31/3/20	Employee Comp. Exp. (P&L)	20,50,000	
	To Liability for SAR		20,50,000

Question 3 : Nov 2018 – PAPER

Golden Era Limited grants 200 shares to each of its 400 employees on 1st January, 2016. The employee should remain in service during the vesting period so as to be eligible. The shares will vest at the end of the

1st year - If the company's earnings increase by 12%.

2nd year - If the company's earnings increase by more than 20% over the two year period.

3rd year - If the company's earnings increase by more than 20% over the three year period.

The fair value per share (non-market related) at the grant date is Rs. 61. In 2016, earnings increased by 10% and 22 employees left the company. The company expects that earnings will continue at a similar rate in 2017 and expect that the shares will vest at the end of the year 2017. The company also expects that additional 18 employees will leave the organization in the year 2017 and that 360 employees will receive their shares at the end of the year 2017. At the end of 2017 company's earnings increased by 18% (over the 2 years period). Therefore, the shares did not vest. Only 16 employees left the organization during 2017.

The company believes that additional 14 employees will leave in 2020 and earnings will further increase so that the performance target will be achieved in 2018. At the end of the year 2018, only 9 employees have left the organization. Assume that the company's earnings increased to desired level and the performance target has been met.

You are required to determine the expense as per Ind AS for each year (assumed as financial year) and pass appropriate journal entries.

Solution :

Since the earnings of the entity is non-market related, hence it will not be considered in fair value calculation of the shares given. However, the same will be considered while calculating number of shares to be vested.

Calculation of yearly expenses to be charged :

		2016	2017	2018
(a)	Total employees	400	400	400
(b)	Employees left (Actual)	(22)	22+16=38	22+16+9=47
(c)	Employees expected to leave in the next year	(18)	(14)	-

(d)	Year end – No of employees (a-b-c)	360	348	353
(e)	Shares per employee	200	200	200
(f)	Fair value of a share at the grant date	61	61	61
	Conditional increase in earnings	12%	20%	20%
	Actual increase in earnings	10%	18%	20%
(g)	Vesting period	1/2	2/3	3/3
(h)	Expenses	$\frac{360 \times 200 \times 61}{2} \times 1$ = 21,96,000	$\frac{360 \times 200 \times 61}{3} \times 2$ = 28,30,400 – 21,96,000 6,34,400	$\frac{360 \times 200 \times 61}{3} \times 3$ = 43,06,600 – 28,30,400 14,76,200

Journal Entries

		Rs.	Rs.
31st March, 2016			
Employee benefits expenses A/c	Dr.	5,49,000	
To Share based payment reserve (equity) A/c			5,49,000
(Equity settled shared based payment based on conditional vesting period)			
Profit and Loss A/c	Dr.	5,49,000	
To Employee benefits expenses A/c			5,49,000
(Employee benefits expenses transferred to Profit and Loss A/c)			
31st March, 2017			
Employee benefits expenses	Dr.	18,05,600	
To Share based payment reserve (equity)			18,05,600
(Equity settled shared based payment based on conditional expected vesting period)			
Profit and Loss A/c	Dr.	18,05,600	
To Employee benefits expenses A/c			18,05,600
(Employee benefits expenses transferred to Profit and Loss A/c)			
31st March, 2018			
Employee benefits expenses	Dr.	8,44,850	
To Share based payment reserve (equity)			8,44,850
(Equity settled shared based payment based on conditional expected vesting period)			
Profit and Loss A/c	Dr.	8,44,850	
To Employee benefits expenses A/c			8,44,850
(Employee benefits expenses transferred to Profit and Loss A/c)			
31st March, 2019			
Employee benefits expenses	Dr.	11,07,150	
To Share based payment reserve (equity)			11,07,150

(Equity settled shared based payment based on conditional expected vesting period)		
Profit and Loss A/c Dr. To Employee benefits expenses A/c (Employee benefits expenses transferred to Profit and Loss A/c)	11,07,150	11,07,150
Share based payment reserve (equity) (353 x 200 x 61) Dr. To Share Capital (Share capital Issued)	43,06,600	43,06,600

Question 4 : May 2019 – RTP

A parent grants 200 share options to each of 100 employees of its subsidiary, conditional upon the completion of two years' service with the subsidiary. The fair value of the share options on grant date is Rs.30 each. At grant date, the subsidiary estimates that 80 percent of the employees will complete the two-year service period. This estimate does not change during the vesting period. At the end of the vesting period, 81 employees complete the required two years of service. The parent does not require the subsidiary to pay for the shares needed to settle the grant of share options.

Pass the necessary journal entries for giving effect to the above arrangement.

Solution :

As required by Ind AS 102, over the two-year vesting period, the subsidiary measures the services received from the employees in accordance, the requirements applicable to equity-settled share-based payment transactions. Thus, the subsidiary measures the services received from the employees on the basis of the fair value of the share options at grant date. An increase in equity is recognised as a contribution from the parent in the separate or individual financial statements of the subsidiary.

The journal entries recorded by the subsidiary for each of the two years are as follows:

Year 1	**Rs.**	**Rs.**
Remuneration expense Dr. (200 × 100 employees × Rs.30 × 80% × ½) To Equity (Contribution from the parent)	2,40,000	2,40,000
Year 2		
Remuneration expense Dr. [(200 x 81 employees x Rs.30) – 2,40,000] To Equity (Contribution from the parent)	2,46,000	2,46,000

Question 5 : Nov 2019 – RTP

QA Ltd. had on 1st April, 20X1 granted 1,000 share options each to 2,000 employees. The options are due to vest on 31st March, 20X4 provided the employee remains in employment till 31st March, 20X4.

On 1st April, 20X1, the Directors of Company estimated that 1,800 employees would qualify for the option on 31st March, 20X4. This estimate was amended to 1,850 employees on 31st March, 20X2 and further amended to 1,840 employees on 31st March, 20X3.
On 1st April, 20X1, the fair value of an option was Rs.1.20. The fair value increased to Rs.1.30 as on 31st March, 20X2 but due to challenging business conditions, the fair value declined thereafter. In September, 20X2, when the fair value of an option was Rs.0.90, the Directors repriced the option and this caused the fair value to increase to Rs.1.05. Trading conditions improved in the second half of the year and by 31st March, 20X3 the fair value of an option was Rs.1.25. QA Ltd. decided that additional cost incurred due to repricing of the options on 30th September, 20X2 should be spread over the remaining vesting period from 30th September, 20X2 to 31st March, 20X4.
The Company has requested you to suggest the suitable accounting treatment for these transaction as on 31st March, 20X3.

Solution :

a) Year 11 – 12

$$= \frac{1{,}850 \times 1{,}000 \times 1.2}{3} \times 1 \qquad = 7{,}40{,}000$$

b) Year 12 – 13

$$= \frac{1{,}840 \times 1{,}000 \times 1.2}{3} \times 2 \qquad = 14{,}72{,}000 - 7{,}40{,}000$$

$$= 7{,}32{,}000$$

$$= \frac{1{,}840 \times 1{,}000 \times (1.05 - 0.9)}{1.5} \times 0.5 \qquad = \underline{\quad 92{,}000}$$

$$8{,}24{,}000$$

Question 6 : May 2020 – RTP

An entity which follows its financial year as per the calendar year grants 1,000 share appreciation rights (SARs) to each of its 40 management employees as on 1st January 20X5. The SARs provide the employees with the right to receive (at the date when the rights are exercised) cash equal to the appreciation in the entity's share price since the grant date. All of the rights vest on 31st December 20X6; and they can be exercised during 20X7 and 20X8. Management estimates that, at grant date, the fair value of each SAR is Rs.11; and it estimates that overall 10% of the employees will leave during the two-year period. The fair values of the SARs at each year end are shown below:

Year	Fair value at year end
31 December 20X5	12
31 December 20X6	8
31 December 20X7	13
31 December 20X8	12

10% of employees left before the end of 20X6. On 31st December 20X7 (when the intrinsic value of each SAR was Rs.10), six employees exercised their options; and the remaining 30 employees

exercised their options at the end of 20X8 (when the intrinsic value of each SAR was equal to the fair value of Rs.12).
How much expense and liability is to be recognized at the end of each year? Pass Journal entries.

Solution :
The amount recognized as an expense in each year and as a liability at each year end) is as follows:

Year	Expense Rs.	Liability Rs.	Calculation of Liability
31 December 20X5	2,16,000	2,16,000	= 36 x 1,000 x 12 x ½
31 December 20X6	72,000	2,88,000	= 36 x 1,000 x 8
31 December 20X7	1,62,000*	3,90,000	= 30 x 1,000 x 13
31 December 20X8	(30,000)**	0	Liability extinguished

* Expense comprises an increase in the liability of Rs.102,000 and cash paid to those exercising their SARs of Rs.60,000 (6 x 1,000 x 10).
** Difference of opening liability (Rs.3,90,000) and actual liability paid [Rs.3,60,000 (30 x 1,000 x 12)] is recognised to Profit and loss i.e. Rs.30,000.

Journal Entries

31 December 20X5			
Employee benefits expenses To Share based payment liability (Fair value of the SAR recognized)	Dr.	2,16,000	 2,16,000
31 December 20X6			
Employee benefits expenses To Share based payment liability (Fair value of the SAR re-measured)	Dr.	72,000	 72,000
31 December 20X7			
Employee benefits expenses To Share based payment liability (Fair value of the SAR recognized)	Dr.	1,62,000	 1,62,000
Share based payment liability To Cash (Settlement of SAR)	Dr.	60,000	 60,000
31 December 20X8			
Share based payment liability To Employee benefits expenses (Fair value of the SAR recognized)	Dr.	30,000	 30,000
Share based payment liability To Cash (Settlement of SAR)	Dr.	3,60,000	 3,60,000

Note: Last two entries can be combined.

Question 7 : May 2021 – RTP

Company P is a holding company for company B. A group share-based payment is being organized in which Parent issues its own equity shares to the employees of company B. The details are as below –

Number of Employees of Company B	100
Grant date fair value of share	Rs.87
Number of shares granted to each employee	25
Vesting conditions	Immediately
Face value per share	Rs.10

Pass the journal entries in the books of company P & company B.

Solution :

Journal Entries

Books of Company P

Particulars		Debit (Rs.)	Credit (Rs.)
Investment in Company B Dr.	Dr.	2,17,500	
To Equity Share Capital A/c (2,500 shares x Rs.10)			25,000
To Securities Premium A/c (2,500 shares x Rs.77)			1,92,500
(Being allotment of 25 shares each to 100 employees of B at fair value of Rs. 87 per share)			

Books of Company B

Particulars		Debit (Rs.)	Credit (Rs.)
Employee Benefit Expense A/c	Dr.	2,17,500	
To Capital Contribution from Parent P			2,17,500
Being issue of shares by Parent to Employees pursuant to Group Share-based Payment Plan)			

Question 8 : July 2021 – Paper

Voya Limited issued 1,000 share options to each of its 200 employees for an exercise price of Rs.10. the employees are required to stay in employment for next 3 years. The fair value of the option is estimated at Rs.18.

90% of the employees are expected to vest the option.

The Company faced severe crisis during the 2nd year and it was decided to cancel the scheme with immediate effect. The market price of the share at the date of cancellation was Rs.15.

The following information is available :

Fair value of the option at the date of cancellation is Rs.12.

The company paid compensation to the employees at the rate of Rs.13.50. There were only 190 employees in the employment at that time.
You are required to show how cancellation will be recorded in the books of the Company as per relevant Ind AS.

Solution :

(A) Calculation of employee compensation expense

	Year 1	Year 2	
Expected employees to remain in the employment during the vesting period	180	190	
Fair value of option	18	18	
Number of options	1,000	1,000	
Total	32,40,000	34,20,000	
Expense weightage	3-Jan	3-Feb	Balance 2/3rd in full, as it is cancelled
Expense for the year	10,80,000	23,40,000	Remaining amount since cancelled

(B) Cancellation compensation to be charged in the year 2

Cancellation compensation		
Number of employees (A)	190	
Amount agreed to pay (B)	13.5	
Number of options/ employee (C)	1,000	
Compensation amount (A x B x C)		25,65,000
Less: Amount to be deducted from Equity		
Number of employees (D)	190	
Fair value of option (at the date of cancellation) (E)	12	
Number of options / employee (F)	1,000	
Amount to be deducted from Equity (D x E x F)		(22,80,000)
Balance transferred to Profit and Loss		2,85,000

Question 9 : May 2022 – RTP

New Age Technology Limited has entered into following Share Based payment transactions:

(i) On 1st April, 20X1, New Age Technology Limited decided to grant share options to its employees. The scheme was approved by the employees on 30th June, 20X1. New Age Technology Limited determined the fair value of the share options to be the value of the equity shares on 1st April, 20X1.

(ii) On 1st April, 20X1, New Age Technology Limited entered into a contract to purchase IT equipment from Bombay Software Limited and agreed that the contract will be settled by issuing equity instruments of New Age Technology Limited. New Age Technology Limited received the IT equipment on 30th July, 20X1. The share-based payment transaction was measured based on the fair value of the equity instruments as on 1st April, 20X1.

(iii) On 1st April, 20X1, New Age Technology Limited decided to grant the share options to its employees. The scheme was approved by the employees on 30th June, 20X1.
The issue of the share options was however subject to the same being approved by the shareholders in a general meeting. The scheme was approved in the general meeting held on 30th September, 20X1. The fair value of the equity instruments for measuring the share-based payment transaction was taken on 30th September, 20X1.

Identify the grant date and measurement date in all the 3 cases of Share based payment transactions entered into by New Age Technology Limited, supported by appropriate rationale for the determination?

Solution :

Ind AS 102 defines grant date and measurement dates as follows:

(a) **Grant date:** The date at which the entity and another party (including an employee) agree to a share-based payment arrangement, being when the entity and the counterparty have a shared understanding of the terms and conditions of the arrangement. At grant date the entity confers on the counterparty the right to cash, other assets, or equity instruments of the entity, provided the specified vesting conditions, if any, are met. If that agreement is subject to an approval process (for example, by shareholders), grant date is the date when that approval is obtained.

(b) **Measurement date:** The date at which the fair value of the equity instruments granted is measured for the purposes of this Ind AS. For transactions with employees and others providing similar services, the measurement date is grant date. For transactions with parties other than employees (and those providing similar services), the measurement date is the date the entity obtains the goods or the counterparty renders service.

Applying the above definitions in the given scenarios following would be the conclusion based on the assumption that the approvals have been received prospectively:

Scenario	Grant date	Measurement date	Base for grant date	Base for measurement date
i)	30th June, 20X1	30th June, 20X1	The date on which the scheme was approved by the employees	For employees, the measurement date is grant date

ii)	1st April, 20X1	30th July, 20X1	The date when the entity and the counterparty entered a contract and agreed for settlement by equity instruments	The date when the entity obtains the goods from the counterparty
iii)	30th September, 20X1	30th September, 20X1	The date when the approval by shareholders was obtained	For employees, the measurement date is grant date

Thanks ....

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IND AS – 19 EMPLOYEES BENEFITS

CHAPTER - 28

Question 1 : Nov 2018 – RTP / Nov 2019 – RTP

A Ltd. prepares its financial statements to 31st March each year. It operates a defined benefit retirement benefits plan on behalf of current and former employees. A Ltd. receives advice from actuaries regarding contribution levels and overall liabilities of the plan to pay benefits. On 1st April, 2017, the actuaries advised that the present value of the defined benefit obligation was Rs.6,00,00,000. On the same date, the fair value of the assets of the defined benefit plan was Rs.5,20,00,000. On 1st April, 2017, the annual market yield on government bonds was 5%. During the year ended 31st March, 2018, A Ltd. made contributions of Rs.70,00,000 into the plan and the plan paid out benefits of Rs.42,00,000 to retired members. Both these payments were made on 31st March, 2018.

The actuaries advised that the current service cost for the year ended 31st March, 2018 was Rs.62,00,000. On 28th February, 2018, the rules of the plan were amended with retrospective effect. These amendments meant that the present value of the defined benefit obligation was increased by Rs.15,00,000 from that date.

During the year ended 31st March, 2018, A Ltd. was in negotiation with employee representatives regarding planned redundancies. The negotiations were completed shortly before the year end and redundancy packages were agreed. The impact of these redundancies was to reduce the present value of the defined benefit obligation by Rs.80,00,000. Before 31st March, 2018, A Ltd. made payments of Rs.75,00,000 to the employees affected by the redundancies in compensation for the curtailment of their benefits. These payments were made out of the assets of the retirement benefits plan.

On 31st March, 2018, the actuaries advised that the present value of the defined benefit obligation was Rs.6,80,00,000. On the same date, the fair value of the assets of the defined benefit plan were Rs.5,60,00,000.

Examine and present how the above event would be reported in the financial statements of A Ltd. for the year ended 31st March, 2018 as per Ind AS.

Solution :

Step 1 : Determine deficit / Surplus

A) Defined benefit obligation :

Opening (1/4/2017)	6,00,00,000
+ Interest @ 5% (P/L)	30,00,000

+ Current Service Cost (P/L)	62,00,000
+ Past Service Cost (P/L)	15,00,000
– Benefits Paid (Bank)	(42,00,000)
– Redundancies	(80,00,000)
	5,85,00,000
Closing (31/3/2018)	6,80,00,000
Difference (OCI)	95,00,000

B) Plan Assets

Opening (1/4/2017)	5,20,00,000
+ Interest @ 5% (P/L)	26,00,000
+ Contributions (Bank)	70,00,000
– Benefits Paid (Bank)	(42,00,000)
– Redundancies	(75,00,000)
	4,99,00,000
Closing (31/3/2018)	5,60,00,000
Difference (OCI)	61,00,000

Step 2 : Determination of Net Defined benefit

Defined benefit obligation	6,80,00,000
– Plan Assets	5,60,00,000
Net Defined benefit liability	1,20,00,000

Step 3 : Determination of the amount to be recognised in P/L

Current Service Cost		62,00,000
Past Service Cost		15,00,000
Net Finance Cost	30,00,000	
	– 26,00,000	4,00,000
Gain on settlement of Redundancies (80 – 75)		(5,00,000)
		76,00,000

Step 4 : Determination of amount to be recognised in OCI

Remeasurement of DBO	95,00,000
– Remeasurement of Plan Assets	61,00,000
	34,00,000

Question 2 : Nov 2018 – PAPER

Sun Shine India Limited has a capital base of Rs.150 Lakh and has earned profits to the tune of Rs.17 lakh. The Return on Investment (ROI) of the particular industry to which the company belongs is 14%. If the services of a particular executive are acquired by the company, it is expected that the profit will increase by Rs.3 lakh over and above the target profit.

Determine the amount of maximum bid price for that particular executive and the maximum salary that could be offered to him.

Solution :

EITHER

Capital Base	=	Rs.1,50,00,000
Actual Profit	=	Rs.17,00,000
Target Profit @ 14%	=	Rs.21,00,000

Expected Profit on employing the particular executive

= Rs.21,00,000 + Rs.3,00,000 = Rs.24,00,000

Additional Profit = Expected Profit – Actual Profit

= Rs.24,00,000 – Rs.17,00,000 = Rs.7,00,000

Maximum bid price = $\frac{\text{Additional Profit}}{\text{Rate of Return on Investment}} = \frac{7,00,000}{14\%} \times 100$ = Rs.50,00,000

Maximum salary that can be offered = 14% of Rs.50,00,000 i.e., Rs.7,00,000

Maximum salary can be offered to that particular executive upto the amount of additional profit i.e., Rs.7,00,000.

Question 3 : May 2019 – RTP

ABC Limited operates a defined benefit plan which provides to the employees covered under the plan a pension benefit which is equal to 0.75% final salary for each year of completed service. An employee needs to complete minimum of five years' service for becoming eligible to the benefit. On 1st April, 2015, the entity improves the pension benefit to 1% of final salary for each year of service, including prior years. The present value of the defined benefit obligation is therefore, increased by Rs.80 million. Given below is the composition of this amount:

Employees with more than 5 years' of service at 1st April, 2015	Rs.60 million
Employees with less than 5 years' of service at 1st April, 2015	Rs.20 million

The employees in the second category have completed average 2 and half years of service. Hence, they need to complete another two and half year of service until vesting.

Comment on the treatment of Rs.80 million of the defined benefit obligation in the financial statements both as per AS 15 and Ind AS 19.

Solution :

Under AS 15, a past service cost of Rs.60 million needs to be recognized immediately, as those benefits are already vested. The remaining Rs.20 million cost is recognized on a straight line basis over the vesting period, i.e., period to two and half years commencing from 1st April, 2015.

Under Ind AS 19, the entire past service cost of Rs.80 million needs to be recognized and charged in profit or loss immediately. ABC Ltd. cannot defer any part of this cost.

Question 4 : May 2020 – RTP

On 1 April 20X1, the fair value of the assets of XYZ Ltd's defined benefit plan were valued at Rs.20,40,000 and the present value of the defined obligation was Rs.21,25,000. On 31st March, 20X2 the plan received contributions from XYZ Ltd amounting to Rs.4,25,000 and paid out benefits of Rs.2,55,000. The current service cost for the financial year ending 31 March 20X2 is Rs.5,10,000. An interest rate of 5% is to be applied to the plan assets and obligations. The fair value of the plan's assets at 31 March 20X2 was Rs.23,80,000, and the present value of the defined benefit obligation was Rs.27,20,000. Provide a reconciliation from the opening balance to the closing balance for Plan assets and Defined benefit obligation. Also show how much amount should be recognised in the statement of profit and loss, other comprehensive income and balance sheet?

Solution :

Reconciliation of Plan assets and Defined benefit obligation

	Plan Assets Rs.	**Defined benefit obligation Rs.**
Fair value/present value as at 1st April 20X1	20,40,000	21,25,000
Interest @ 5%	1,02,000	1,06,250
Current service cost		5,10,000
Contributions received	4,25,000	-
Benefits paid	(2,55,000)	(2,55,000)
Return on gain (assets) (balancing figure)	68,000	-
Actuarial Loss (balancing figure)	-	2,33,750
Closing balance as at March 31,20X2	23,80,000	27,20,000

In the Statement of Profit and loss, the following will be recognised:

	Rs.
Current service cost	5,10,000
Net interest on net defined liability (Rs.1,06,250 – Rs.1,02,000)	4,250

Defined benefit re-measurements recognised in Other Comprehensive Income:

	Rs.
Loss on defined benefit obligation	(2,33,750)
Gain on plan assets	68,000
	(1,65,750)

In the Balance sheet, the following will be recognised :

	Rs.
Net defined liability (Rs.27,20,000 – Rs.23,80,000)	3,40,000

Question 5 : Nov 2020 – Paper

Diamond Pvt. Ltd, has a headcount of around 1,000 employees in the organisation in financial year 2019-2020. As per the company's policy, the employees are given 35 days of privilege leave (PL), 15 days of sick leave (SL) and 10 days of casual leave. Out of the total PL and sick leave, 10 PL leave and 5 sick leave can be carried forward to next year. On the basis of past trends, it has been noted that 200 employees will take 5 days of PL and 2 days of SL and 800 employees will avail 10 days of PL and 5 days of SL.

Also the company has been earning profits since 2010. It has decided in financial year 2019-2020 to distribute profits to its employees @ 4% during the year. However, due to the employee turnover in the organisation, the expected pay-out of the Diamond Pvt. Ltd. is expected to be around 3.5%. The profits earned during the financial year 2019-2020 are Rs. 4,000 crores.

Diamond Pvt. Ltd. has a post-employment benefit plan which is in the nature of defined contribution plan where contribution to the fund amounts to Rs. 200 crores which will fall due within 12 months from the end of accounting period.

The company has paid Rs. 40 crores to this plan in financial year 2019-2020.

What would be the treatment of the short-term compensating absences, profit-sharing plan and the defined contribution plan in the books of Diamond Pvt. Ltd.?

Solution :

(i) **Treatment of short term compensating absences:** Diamond Pvt. Ltd. will recognise a liability in its books to the extent of 5 days of PL for 200 employees and 10 days of PL for remaining 800 employees and 2 days of SL for 200 employees and 5 days of SL for remaining 800 employees in its books as an unused entitlement that has accumulated in 2019-2020 as short-term compensated absences.

(ii) **Treatment of profit sharing plan:** Diamond Pvt. Ltd. will recognise Rs. 140 crores (4,000 x 3.5%) as a liability and expense in its books of account.

(iii) **Treatment of defined contribution plan:** When an employee has rendered service to an entity during a period, the entity shall recognise the contribution payable to a defined contribution plan in exchange for that service.

Under Ind AS 19, the amount of Rs. 160 crores (200-40) will be recognised as a liability (accrued expense), after deducting any contribution already paid i.e. Rs. 40 crores (with contribution of Rs. 200 crores to the plan) and an expense in the statement of profit and loss.

It can also be seen that the contributions are payable within 12 months from the end of the year in which the employees render the related service; hence, they will not be discounted.

Question 6 : May 2021 – RTP

At 1 April, 20X0, the fair value of the Plan Assets was Rs. 10,00,000. The Plan paid benefits of Rs. 1,90,000 and received contributions of Rs. 4,90,000 on 30 September, 20X0. The company computes the Fair Value of Plan Assets to be Rs. 15,00,000 as on 31 March, 20X1 and the Present Value of the Defined Benefit Obligation to amount to Rs. 14,79,200 on the same date. Actuarial losses on defined benefit obligation were Rs. 6,000.

Compounding happens half-yearly. The normal interest rate for 6 months period is 10% per annum, while the effective interest rate for 12 months period is based on the following data:

At 1 April, 20X0, the company made the following estimates based on market prices at that date:

Particulars	%
Interest and Dividend Income, after tax payable by the fund	9.25
Add: Realized and Unrealized Gains on Plan Assets (after tax)	2.00
Less: Administration Costs	(1.00)
Expected Rate of Return	10.25

Determine actual return and expected return on plan asset. Also compute amount to be recognized in 'Other Comprehensive Income' in this case.

Solution :

Computation of Expected Return on Plan Assets

Particulars	Rs.
Return on Rs. 10,00,000 for 20X0-20X1 at 10.25% = Rs. 10,00,000 x 10.25%	1,02,500
Add: Return on Rs. 3,00,000 for 6 months at 10% Normal Rate = [3,00,000 (Inflow Rs. 4,90,000 less Payments Rs. 1,90,000) x 10% x 6/12]	15,000
Expected Return on Plan Assets	**1,17,500**

Computation of Actual Return on Plan Assets

Particulars	Rs.
Fair Value of Plan Assets at the year-end – 31 March 20X1	15,00,000
Less: Fair Value of Plan Assets at the beginning – 1 April 20X0	(10,00,000)

Less: Contributions received during the year 20X0-20X1	(4,90,000)
Add: Benefits paid during the year 20X0-20X1	1,90,000
Actual Return on Plan Assets	**2,00,000**

Computation of Net Actuarial Gain

Particulars	**Rs.**
Actual Return on Plan Assets	2,00,000
Less: Expected Return on Plan Assets	(1,17,500)
Actuarial Gain on Plan Assets	82,500
Less: Actuarial Loss on Defined Benefit Obligation (given)	(6,000)
Net Actuarial Gain to be recognized in 'Other Comprehensive Income'	**76,500**

Thanks ….

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IND AS – 115 REVENUE FROM CONTRACT WITH CUSTOMER

CHAPTER - 29

Question 1 : May 2018 – RTP

Mac Ltd. purchased goods on credit from Toy Ltd. for Rs.580 lakhs for export. The export order was cancelled. Mac Ltd. decided to sell the same goods in the local market with a price discount. Toy Ltd. was requested to offer a price discount of Rs.10%. Toy Ltd. wants to adjust the sales figure to the extent of the discount requested by Mac Ltd. Discuss whether such a treatment in the books of Toy Ltd. is justified as per the provisions of the relevant Ind AS.

Also, Toy Ltd. entered into a sale deed for its Land on 15th March, 20X1. But registration was done with the registrar on 20th April, 20X1. But before registration, is it possible to recognize the sale and the gain at the balance sheet date? Give reasons in support of your answer.

Solution :

Toy Ltd. had sold goods to Mac Ltd on credit worth for Rs.580 lakhs and the sale was completed in all respects. Mac Ltd.'s decision to sell the same in the domestic market at a discount does not affect the amount recorded as sales by Toy Ltd.

The price discount of 10% offered by Toy Ltd. after request of Mac Ltd. was not in the nature of a discount given during the ordinary course of trade because otherwise the same would have been given at the time of sale itself. However, there appears to be an uncertainty relating to the collectability of the debt, which has arisen subsequent to sale. Therefore, it would be appropriate to make a separate provision to reflect the uncertainty relating to collectability rather than to adjust the amount of revenue originally recorded. Hence such discount should be charged to the Statement of Profit and Loss and not shown as deduction from the sales figure.

With respect to sale of land, both sale and gain on sale of land earned by Toy Ltd. shall be recognized in the books at the balance sheet date. In substance, the land was transferred with significant risk & rewards of ownership to the buyer before the balance sheet date and what was pending was merely a formality to register the deed. The registration post the balance sheet date only confirms the condition of sale at the balance sheet date as per Ind AS 10 “Events after the Reporting Period.”

Question 2 : May 2018 – RTP

ABC is a construction contract company involved in building commercial properties. Its current policy for determining the percentage of completion of its contracts is based on the proportion of cost incurred to date compared to the total expected cost of the contract.

One of ABC’s contracts has an agreed price of Rs.250 crores and estimated total costs of Rs.200 crores. The cumulative progress of this contract is:

Year ended	31st March 20X1	31st March 20X2
Cost incurred	80	145
Work certified and billed	75	160
Amount received against bills	70	150

ABC prepared and published its financial statements for the year ended 31st March 20X1. Relevant extracts are:

	Rs.in Crores
Revenue [(80/200) x 250]	100
Cost of sales	(80)
Profit	20

Balance Sheet (Extracts)

	Rs.Crores
Current assets	
Amount due from customers	
Contract cost to date	80
Profit recognized	20
	100
Progress billing to date	(75)
Billing to be done	25
Contract asset (amount receivable) (75-70)	5

ABC has received some adverse publicity in the financial press for taking its profit too early in the contract process, leading to disappointing profits in the later stages of contracts. Most of ABC's competitors take profit based on the percentage of completion as determined by the work certified compared to the contract price.

Required

(a) Assume that ABC changes its method of determining the percentage of completion of contracts to that used by its competitors, as this would represent a change in an accounting estimate. Prepare equivalent extracts to the above for the year ended 31st March 20X2.

(b) Identify, whether the above change represents a change in accounting estimate or a change in accounting policy and why?

Solution :

(i) ABC's income statement (extracts) for the year ended:

	31 March 20X2
	Rs.Crores
Revenue (based on work certified) (160-100)	60
Cost of sales (balancing figure)	(48)
Profit [(160/250) x (250-200)] - 20	12

Statement of financial position (extracts) as on

	31 March 20X2
	Rs.Crores
Current assets	
Amount due from customers	
Contract cost to date	145
Profit recognized (20+12)	32
	177
Progress billing	(160)
Billing to be done	17
Contract assets (amount receivable) (160-150)	10

(ii) The relevant issue here is what constitutes the accounting policy for construction contracts. Where there is uncertainty in the outcome of a contract, the appropriate accounting policy would be the completed contract basis (i.e. no profit is taken until the contract is completed). Similarly, any expected losses should be recognised immediately. Where the outcome of a contract is reasonably foreseeable, the appropriate accounting policy is to accrue profits by the percentage of completion method. If this is accepted, it becomes clear that the different methods of determining the percentage of completion of construction contracts are different accounting estimates. Thus the change made by ABC in the year to 31 March 20X2 represents a change of accounting estimate.

Question 3 : Nov 2018 – PAPER

Deluxe bike manufactured by Zed Limited is sold with an extended warranty of 2 years for Rs.87,300 while an identical Deluxe bike without the extended warranty is sold in the market for Rs.80,000 and equivalent warranty is given in the market for Rs.10,000. How should Zed Limited recognize and measure revenue in the books on the sale of the bikes and warranty?

Solution :

As per Ind As 115 Zed Ltd. has sold two products viz Deluxe bike and the extended warranty. Revenue earned on sale of each product should be recognised separately.

Calculation of Revenue attributable to both the components :

Total fair value of Deluxe bike and extended warranty (80,000+10,000)	Rs.90,000
Less: Sale price of the Deluxe bike with extended warranty	(Rs.87,300)
Discount	Rs.2,700
Discount and revenue attributable to each component of the transaction:	
Proportionate discount attributable to sale of Deluxe bike (2,700 x 80,000 / 90,000)	Rs.2,400
Revenue from sale of Deluxe bike (80,000 – 2,400)	Rs.77,600
Proportionate discount attributable to extended warranty (2,700 x 10,000 / 90,000)	Rs.300
Revenue from extended warranty (10,000 - 300)	Rs.9,700

Revenue in respect of sale of Deluxe bike of Rs. 77,600 should be recognised immediately and revenue from warranty of Rs.9,700 should be recognised over the period of warranty ie. 2 years.

Question 4 : Nov 2018 – PAPER

Future Limited undertakes a contract for construction of a Bridge on 01.04.2017. The contract was to be completed in two years. The following details are given below:
Contract Price Rs.1250 Lakh
Cost incurred up to 31.03.2018 Rs.780 Lakh
The company estimated that a further cost of Rs.520 lakh would be incurred for completing the project.
What amount should be charged to revenue for the financial year 2017-18 as per the provisions of Ind AS 115 "Construction Contracts"?
Show the extracts of Profit and Loss account in the books of Future Limited.

Solution :

Statement showing the amount to be charged to Revenue as per Ind AS 11

	Rs.in lakh
Cost of construction incurred upto 31.03.2018	780
Add: Estimated future cost	520
Total estimated cost of construction	1,300
Degree of completion (780/1,300 x 100)	60%

	Rs.in lakh
Revenue recognized (1,250 x 60%)	750
Total foreseeable loss (1,300 – 1,250)	50
Less: Expense for the current year (780 – 750)	(30)
Loss to be provided for	20

Profit and Loss Account (Extract)

		Rs.in lakh			**Rs.in lakh**
To	Construction Costs	780	By	Contract Price	750
To	Provision for loss	20	By	Net loss	50
		800			**800**

Question 5 : May 2019 – RTP

KK Ltd. runs a departmental store which awards 10 points for every purchase of Rs.500 which can be discounted by the customers for further shopping with the same merchant. Each point is redeemable on any future purchases of KK Ltd.'s products within 3 years. Value of each point is Rs.0.50. During the accounting period 2017-2018, the entity awarded 1,00,00,000 points to various customers of which 18,00,000 points remained undiscounted (to be redeemed till 31st March, 2020). The management expects only 80% of the remaining will be discounted in future.

The Company has approached your firm with the following queries and has asked you to suggest the accounting treatment (Journal Entries) under the applicable Ind AS for these award points:

(a)	How should the recognition be done for the sale of goods worth Rs.10,00,000 on a particular day?
(b)	How should the redemption transaction be recorded in the year 2017-2018? The Company has requested you to present the sale of goods and redemption as independent transaction. Total sales of the entity is Rs.5,000 lakhs.
(c)	How much of the deferred revenue should be recognised for year 2018-19 / 19-20 because of the estimation that only 80% of the outstanding points will be redeemed?
(d)	In the next year 2018-2019, 60% of the outstanding points were discounted Balance 40% of the outstanding points of 2017-2018 still remained outstanding. How much of the deferred revenue should the merchant recognize in the year 2018-2019 and what will be the amount of balance deferred revenue?
(e)	How much revenue will the merchant recognized in the year 2019-2020, if 3,00,000 points are redeemed in the year 2019-2020?

Solution :

(a) As per Ind AS 115

(i) On sale of Rs.10,00,000, 20,000 points shall be amended

$$\frac{10,00,000}{500} \times 10 = 20,000$$

(ii) Every point cost Rs.05, so 20,000 points shall be converted Rs.10,000.

(iii) So as sale the consideration shall be allocated to sale of goods and points in ratio of its stand alone price.

	Standalone Price	**Consideration Allocated**
Sale of goods	10,00,000	9,90,099
Points (Rs.)	10,000	9,901
	10,10,000	**10,00,000**

(b) As per Ind AS 115

(i) On sale of Rs.50,00,00,000, 1,00,00,000 points should be awarded.

i.e. $\frac{50,00,00,000}{500} \times 10 = 1,00,00,000$ points

Amount of points = 1,00,00,000 $\times$ 0.5 = 50,00,000.

Allocation of Consideration

	Price	**Allocated**
Goods	50,00,00,000	49,50,49,505
Points	50,00,000	49,50,495
	50,50,00,000	**50,00,00,000**

Bank	50,00,00,000	
To Revenue (Sales)		49,50,49,505
To Points		49,50,495

(ii) Entity awarded 1,00,00,000 o customer out of which 18,00,000 remain undiscounted till march, 2020.

$\therefore$ Undiscounted points estimated to be recognized in next year = 18,00,000 $\times$ 80% = 14,40,000

$\therefore$ Revenue to be recognised i.e. 1,00,00,000 – 18,00,000 + 14,40,000 = 96,40,000.

Revenue to be recognized with respect to point discounted

$$= 49{,}50{,}495 \times \frac{82{,}00{,}000}{96{,}40{,}000} = 42{,}11{,}002$$

i.e. Points	42,11,002	
To Revenue		42,11,002

Note : Balance = 7,39,493 (49,50,495 – 42,11,002) shall be defined beyond March, 2017.

(c) Revenue Recognised in 18-19/19-2000 should be 42,11,002.

(d) If 60% of outstanding points are discounted

Points discounted = 18,00,000 $\times$ 60% = 10,80,000.

Total points discounted = 82,00,000 + 10,80,000 = 92,80,000

Total Revenue to be recognized = $49{,}50{,}495 \times \frac{92{,}80{,}000}{96{,}40{,}000} = 47{,}65{,}622$

Revenue already recognised = 42,11,002

Revenue to be recognised = 47,65,622 – 42,11,002 = 5,54,620

Points	5,54,620	
To Revenue		5,54,620

Balance Outstanding = 7,39,493 – 5,54,620 = 1,84,873

(e) In the year 2019-2020 the merchant will be recognised the balance of Rs.1,84,873 irrespective of points redeemed became it is last year.

Points	1,84,873	
To Revenue		1,84,873

Question 6 : Nov 2019 – RTP

An entity G Ltd. enters into a contract with a customer P Ltd. for the sale of a machinery for Rs.20,00,000. P Ltd. intends to use the said machinery to start a food processing unit. The food processing industry is highly competitive and P Ltd. has very little experience in the said industry. P Ltd. pays a non-refundable deposit of Rs.1,00,000 at inception of the contract and enters into a long-term financing agreement with G Ltd. for the remaining 95 per cent of the agreed consideration which it intends to pay primarily from income derived from its food processing unit as it lacks any other major source of income. The financing arrangement is provided on a non-recourse basis, which means that if P Ltd. defaults then G Ltd. can repossess the machinery but cannot seek further compensation from P Ltd., even if the full value of the amount owed is not recovered from the machinery. The cost of the machinery for G Ltd. is Rs.12,00,000. P Ltd. obtains control of the machinery at contract inception.

When should G Ltd. recognise revenue from sale of machinery to P Ltd. in accordance with Ind AS 115?

Solution :

As per Ind AS 115, "An entity shall account for a contract with a customer that is within the scope of this Standard only when all of the following criteria are met:

(a) the parties to the contract have approved the contract (in writing, orally or in accordance with other customary business practices) and are committed to perform their respective obligations;

(b) the entity can identify each party's rights regarding the goods or services to be transferred;

(c) the entity can identify the payment terms for the goods or services to be transferred;

(d) the contract has commercial substance (ie the risk, timing or amount of the entity's future cash flows is expected to change as a result of the contract); and

(e) it is probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. In evaluating whether collectability of an amount of consideration is probable, an entity shall consider only the customer's ability and intention to pay that amount of consideration when it is due. The amount of consideration to which the entity will be entitled may be less than the price stated in the contract if the consideration is variable because the entity may offer the customer a price concession".

Paragraph (e) above, requires that for revenue to be recognised, it should be probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. In the given case, it is not probable that G Ltd. will collect the consideration to which it is entitled in exchange for the transfer of the machinery. P Ltd.'s ability to pay may be uncertain due to the following reasons:

(a) P Ltd. intends to pay the remaining consideration (which has a significant balance) primarily from income derived from its food processing unit (which is a business involving significant risk because of high competition in the said industry and P Ltd.'s little experience);

(b) P Ltd. lacks sources of other income or assets that could be used to repay the balance consideration; and

(c) P Ltd.'s liability is limited because the financing arrangement is provided on a non-recourse basis.

In accordance with the above, the criteria in Ind AS 115 are not met.

Further, it states that when a contract with a customer does not meet the criteria in paragraph 9 and an entity receives consideration from the customer, the entity shall recognise the consideration received as revenue only when either of the following events has occurred:

(a) the entity has no remaining obligations to transfer goods or services to the customer and all, or substantially all, of the consideration promised by the customer has been received by the entity and is non-refundable; or

(b) the contract has been terminated and the consideration received from the customer is non-refundable.

In accordance with the above, in the given case G Ltd. should account for the non-refundable deposit of Rs.1,00,000 payment as a deposit liability as none of the events described in paragraph 15 have occurred—that is, neither the entity has received substantially all of the consideration nor it has terminated the contract. Consequently, in accordance with paragraph 16, G Ltd. Will continue to account for the initial deposit as well as any future payments of principal and interest as a deposit liability until the criteria in paragraph 9 are met (i.e. the entity is able to conclude that it is probable that the entity will collect the consideration) or one of the events in paragraph 15 has occurred. Further, G Ltd. will continue to assess the contract in accordance with paragraph 14 to determine whether the criteria in paragraph 9 are subsequently met or whether the events in paragraph 15 of Ind AS 115 have occurred.

Question 7 : Nov 2019 – PAPER

Nivaan Limited commenced work on two long-term contracts during the financial year 31st March, 2019.

The first contract with A & Co. commences on 1st June, 2018 and had a total sales value of Rs.40 lakhs. It was envisaged that the contract would run two years and that the total expected costs would be Rs.32 lakhs. On 31st March, 2019. Navaan Limited revised its estimate of the total expected cost Rs.34 lakhs on the basis of the additional rectification cost of Rs.2 Lakhs incurred on the contract during the current financial year. An independent surveyor has estimated at 31st March, 2019 that the contract is 30% complete. Nivaan Limited has incurred cots up to 31st March, 2019 of Rs.16 lakhs and has received payments on account of Rs.13 lakhs.

The second contract with B & co. commenced on 1st Sept., 2018 and was for 18 months. The total sales value of contract was Rs.30 lakhs ad the total expected costs rs.24 lakhs. Payments on account already received were Rs.9.50 lakhs and total costs incurred to date were Rs.8 lakhs. Navaan Limited had insisted on a large deposit from B and Co. because the companies had not traded together prior to the contract. The independent surveyor estimated that 31st March, 2019 the contract was 20% complete.

The two contracts meet the requirement of Ind AS-115 'Revenue from Contracts with Customers' to recognize revenue over time as the performance obligations are satisfied over time.

The company also has several other contracts of between twelve and eighteen months in duration. Some of these contracts fall into two accounting period and were not completed as at 31st March, 2019. In absence of any financial data relating to the other contracts, you are advised

to ignore these other contracts while preparing the financial statements of the company for the year ended 31st March, 2019.
Prepare financial statements extracts for Nivaan Limited in respect of the two construction contracts for the year ending 31st March, 2019.

Solution :

(a) Extracts of Balance Sheet of Nivaan Ltd. as on 31stMarch, 2019

	Rs. in lakh
Current Assets	
Contract Assets- Work-in-progress (Refer W.N. 3)	9.0
Current Liabilities	
Contract Liabilities (Advance from customers) (Refer W.N. 2)	4.5

Extracts of Statement of Profit and Loss of Nivaan Ltd. as on 31stMarch, 2019

	Rs. in lakh
Revenue from contracts (Refer W.N. 1)	18
Cost of Revenue (Refer W.N. 1)	(16.4)
Net Profit on Contracts (Refer W.N. 1)	1.6

Working Notes:

1. Table showing calculation of total revenue, expenses and profit or loss on contract for the year

Rs.in lakh

	A & Co.	**B & Co.**	**Total**
Revenue from contracts	(40 x 30%) = 12	(30 x 20%) = 6	18
Expenses due for the year	(34* x 30%) = 10.2	(24 x 20%) = 4.8	15
Profit or loss on contract	1.8	1.2	3

***Note:** Additional rectification cost of Rs.2 lakh has been treated as normal cost. Hence total expected cost has been considered as Rs.34 lakh. However, in case this Rs.2 lakh is treated as abnormal cost then expense due for the year would be Rs.11.6 lakh (i.e. 30% of Rs.32 lakh plus Rs.2 lakh). Accordingly, with respect to A & Co., the profit for the year would be Rs.0.4 lakh and work-in-progress recognised at the end of the year would be Rs.4.4 lakh.

2. Calculation of amount due from / (to) customers

Rs.in lakh

	A & Co.	**B & Co.**	**Total**
Billing on the basis of revenue recognised in the books	12	6	18
Payments received from the customers	(13)	(9.5)	(22.5)
Advance received from the customers	1	3.5	4.5

3. Work in Progress recognised as part of contract asset at the end of the year

Rs.in lakh

	A & Co.	B & Co.	Total
Total actual cost incurred during the year	16	8	24
Less: Cost recognised in the books for the year 31.3.2019	(10.2)	(4.8)	(15)
Work-in-progress recognised at the end of the year	5.8	3.2	9

Question 8 : May 2020 – RTP

(a) Entity I sells a piece of machinery to the customer for RS.2 million, payable in 90 days. Entity I is aware at contract inception that the customer might not pay the full contract price. Entity I estimates that the customer will pay atleast Rs.1.75 million, which is sufficient to cover entity I's cost of sales (rs.1.5 million) and which entity I is willing to accept because it wants to grow its presence in this market. Entity I has granted similar price concessions in comparable contracts.

Entity I concludes that it is highly probable that it will collect Rs.1.75 million, and such amount is not constrained under the variable consideration guidance.

What is the transaction price in this arrangement?

(b) On 1 January 20x8, entity J enters into a one-year contract with a customer to deliver water treatment chemicals. The contract stipulates that the price per container will be adjusted retroactively once the customer reaches certain sales volume, defined, as follows:

Price per container	Cumulative sales volume
Rs.100	1 - 1,000,000 containers
Rs.90	1,000,001 - 3,000,000 containers
Rs.85	3,000,001 containers and above

Volume is determined based on sales during the calendar year. There are no minimum purchase requirements. Entity J estimates that the total sales volume for the year will be 2.8 million containers, based on its experience with similar contracts and forecasted sales to the customer.

Entity J sells 700,000 containers to the customer during the first quarter ended 31 March 20X8 for a contract price of Rs.100 per container.

How should entity J determine the transaction price?

(c) Entity K sells electric razors to retailers for C 50 per unit. A rebate coupon is included inside the electric razor package that can be redeemed by the end consumers for C 10 per unit.

Entity K estimates that 20% to 25% of eligible rebates will be redeemed, based on its experience with similar programmes and rebate redemption rates available in the market for similar programmes. Entity K concludes that the transaction price should incorporate an assumption of 25% rebate redemption, as this is the amount for which it is highly probable that a significant reversal of cumulative revenue will not occur if estimates of the rebates change.

How should entity K determine the transaction price?

(d) A manufacturer enters into a contract to sell goods to a retailer for Rs.1,000. The manufacturer also offers price protection, whereby it will reimburse the retailer for any difference between the sale price and the lowest price offered to any customer during the following six months. This clause is consistent with other price protection clauses offered in the past, and the manufacturer believes that it has experience which is predictive for this contract.

Management expects that it will offer a price decrease of 5% during the price protection period. Management concludes that it is highly probable that a significant reversal of cumulative revenue will not occur if estimates change.

How should the manufacturer determine the transaction price?

Solution :

(a) Entity I is likely to provide a price concession and accept an amount less than Rs.2 million in exchange for the machinery. The consideration is therefore variable. The transaction price in this arrangement is Rs.1.75 million, as this is the amount which entity I expects to receive after providing the concession and it is not constrained under the variable consideration guidance. Entity I can also conclude that the collectability threshold is met for Rs.1.75 million and therefore contract exists.

(b) The transaction price is Rs.90 per container based on entity J's estimate of total sales volume for the year, since the estimated cumulative sales volume of 2.8 million containers would result in a price per container of Rs.90. Entity J concludes that based on a transaction price of Rs.90 per container, it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty is resolved. Revenue is therefore recognised at a selling price of Rs.90 per container as each container is sold. Entity J will recognise a liability for cash received in excess of the transaction price for the first 1 million containers sold at Rs.100 per container (that is, Rs.10 per container) until the cumulative sales volume is reached for the next pricing tier and the price is retroactively reduced.

For the quarter ended 31st March, 20X8, entity J recognizes revenue of Rs.63 million (700,000 containers x Rs.90) and a liability of Rs.7 million [700,000 containers x (Rs.100 – Rs.90)].

Entity J will update its estimate of the total sales volume at each reporting date until the uncertainty is resolved.

(c) Entity K records sales to the retailer at a transaction price of Rs.47.50 (Rs.50 less 25% of Rs.10). The difference between the per unit cash selling price to the retailers and the transaction price is recorded as a liability for cash consideration expected to be paid to the end customer. Entity K will update its estimate of the rebate and the transaction price at each reporting date if estimates of redemption rates change.

(d) The transaction price is Rs.950, because the expected reimbursement is Rs.50. The expected payment to the retailer is reflected in the transaction price at contract inception, as that is the amount of consideration to which the manufacturer expects to be entitled after the price protection. The manufacturer will recognise a liability for the difference between the invoice price and the transaction price, as this represents the cash that it expects to refund to the retailer. The manufacturer will update its estimate of expected reimbursement at each reporting date until the uncertainty is resolved.

Question 9 : Nov 2020 – RTP

A contractor enters into a contract with a customer to build an asset for Rs.1,00,000, with a performance bonus of Rs.50,000 that will be paid based on the timing of completion. The amount of the performance bonus decreases by 10% per week for every week beyond the agreed-upon completion date. The contract requirements are similar to those of contracts that the contractor has performed previously, and management believes that such experience is predictive for this contract. The contractor concludes that the expected value method is most predictive in this case. The contractor estimates that there is a 60% probability that the contract will be completed by the agreed-upon completion date, a 30% probability that it will be completed one week late, and a 10% probability that it will be completed two weeks late.

Determine the transaction price.

Solution :

As per IND AS 116, transaction price is the total of fixed + variable component = Variable component should be evaluated by the two method.

1) Expected value approach
2) Most likely approach

The entity in this case uses the expected value approach.

$\therefore$ Transaction price is equal to

1)	Fixed Contract Price			1,00,000
2)	Variable Contract Price			
	$50,000 \times 60\%$	=	30,000	
	$45,000 \times 30\%$	=	13,500	
	$40,000 \times 10\%$	=	4,000	47,500
				1,47,500

Note : The contractor will update its estimate at each reporting date.

Question 10 : Nov 2020 – Paper

ABC Limited supplies plastic buckets to wholesaler customers. As per the contract entered into between ABC Limited and a customer for the financial year 2019-2020, the price per plastic bucket will decrease retrospectively as sales volume increases within the stipulated time of one year.

The price applicable for the entire sale will be based, on sales volume bracket during the year. Price

Price per unit (INR)	Sale Volume
90	0 - 10,000 units
80	10,001 - 35,000 units
70	35,001 units & above

All transactions are made in cash.

(i) Suggest how revenue is to be recognised in the books of accounts of ABC Limited as per expected value method, considering a probability of 15%, 75% and 10% for sales volumes of 9,000 units, 28,000 units and 36,000 units respectively. For workings, assume that ABC Limited achieved the same number of units of sales to the customer during the year as initially estimated under expected value method for the financial year 2019-2020.

(ii) In case ABC Limited decides to measure revenue, based on most likely method instead of expected value method, how will be the revenue recognised in the books of accounts of ABC Limited based on above available information? For workings, assume that ABC Limited achieved the same number of units of sales to the customer during the year as initially estimated under most likely value method for the financial year 2019-2020.

(iii) You are required to pass Journal entries in the books of ABC Limited if the revenue is accounted for as per expected value method for financial year 2019-2020.

Solution :

(i) Determination of how revenue is to be recognised in the books of ABC Ltd. as per expected value method

Calculation of probability weighted sales volume

Sales volume (units)	Probability	Probability-weighted sales volume (units)
9,000	15%	1,350
28,000	75%	21,000
36,000	10%	3,600
		25,950

Calculation of probability weighted sales value

Sales volume (units)	Sales price per unit (Rs.)	Probability	Probability-weighted sales value (Rs.)
9,000	90	15%	1,21,500
28,000	80	75%	16,80,000
36,000	70	10%	2,52,000
			20,53,500

Average unit price = Probability weighted sales value/ Probability weighted sales volume
= 20,53,500 / 25,950 = Rs.79.13 per unit

Revenue is recognised at Rs. 79.13 for each unit sold. First 10,000 units sold will be booked at Rs. 90 per unit and liability is accrued for the difference price of Rs. 10.87 per unit (Rs. 90 – Rs. 79.13), which will be reversed upon subsequent sales of 15,950 units (as the question states that ABC Ltd. achieved the same number of units of sales to the customer during the year as initially estimated under the expected value method for the financial year 2019-2020). For, subsequent sale of 15,950 units, contract liability is accrued at Rs. 0.87 (80 – 79.13) per unit and revenue will be deferred.

(ii) Determination of how revenue is to be recognised in the books of ABC Ltd. as per most likely method

Note: It is assumed that the sales volume of 28,000 units given under the expected value method, with highest probability is the sales estimated under most likely method too.

Transaction price will be:

28,000 units x Rs. 80 per unit = Rs. 22,40,000

Average unit price applicable = Rs. 80

First 10,000 units sold will be booked at Rs. 90 per unit and liability of Rs. 1,00,000 is accrued for the difference price of Rs. 10 per unit (Rs. 90 – Rs. 80), which will be reversed upon subsequent sales of 18,000 units (as question states that ABC Ltd. achieved the same number of units of sales to the customer during the year as initially estimated under the most likely method for the financial year 2019-2020).

Note: Alternatively, the question may be solved based on 25,950 units (as calculated under expected value method assuming that the targets were met) as follows:

Transaction price will be :

25,950 units x Rs. 80 per unit = Rs. 20,76,000

Average unit price applicable = Rs. 80.

First 10,000 units sold will be booked at Rs. 90 per unit and liability is accrued for the difference price of Rs. 10 per unit (Rs. 90 – Rs. 80), which will be reversed upon subsequent sales of 15,950 units.

(iii) Journal Entries in the books of ABC Ltd.

(when revenue is accounted for as per expected value method for financial year 2019-2020)

			Rs.	Rs.
1	Bank A/c (10,000 x Rs. 90)	Dr.	9,00,000	
	To Revenue A/c (10,000 x Rs. 79.13)			7,91,300
	To Liability (10,000 x Rs. 10.87)			1,08,700
	(Revenue recognised on sale of first 10,000 units)			
2	Bank A/c [(25,950 x Rs. 80)- 9,00,000]	Dr.	11,76,000	
	Liability	Dr.	86,124	
	To Revenue A/c (15,950 x Rs. 79.13)			12,62,124
	(Revenue recognised on sale of remaining 15,950 units (25,950 - 10,000). Amount paid by the customer will be the balance amount after adjusting the excess paid earlier since, the customer falls now in second slab)			
3	Liability (1,08,700 – 86,124)	Dr.	22,576	
	To Revenue A/c [25,950 x (80-79.13)]			22,576
	(On reversal of liability at the end of the financial year 2019-2020 i.e. after completion of stipulated time)			

Alternatively, in place of first two entries, one consolidated entry may be passed as follows:

		Rs.	Rs.
Bank A/c (25,950 x Rs. 80)	Dr.	20,76,000	
To Revenue A/c (25,950 x Rs. 79.13)			20,53,424
To Liability (25,950 x Rs. 0.87)			22,576
(Revenue recognised on sale of 25,950 units)			

Note: In 2nd journal entry, it is assumed that the customer had paid balance amount of Rs. 11,76,000 after adjusting excess Rs. 1,00,000 paid with first lot of sale of 10,000 unit. However, one can pass journal entry with total sales value of Rs. 12,76,000 (15,950 units x Rs. 80 per unit) and later on pass third entry for refund. In such a situation, alternatively, 2nd and 3rd entries would be as follows:

		Rs.	Rs.
Bank A/c (15,950 x Rs. 80)	Dr.	12,76,000	
To Revenue A/c (15,950 x Rs. 79.13)			12,62,124
To Liability			13,876
(Revenue recognised on sale of remaining 15,950 units (25,950 - 10,000))			
Liability (1,08,700 + 13,876)	Dr.	1,22,576	
To Revenue A/c [25,950 x (80-79.13)]			22,576
To Bank			1,00,000
(On reversal of liability at the end of the financial year 2019-2020 i.e. after completion of stipulated time and excess amount refunded)			

Question 11 : Jan 2021 – Paper

A Ltd. is a company which is in the business of manufacturing engineering machines and providing after sales services. The company entered into a contract with Mr. Anik to supply and install a machine, namely 'model pi' on 1st April 2018 and to service this machine on 30th September 2018 and 1st April 2019. The cost of manufacturing the machine to A Ltd. was Rs.1,60,000.

It is possible for a customer to purchase both the machine 'model pi' and the maintenance services separately. Mr. Anik is contractually obliged to pay A Ltd Rs.4,00,000 on 1st April, 2019. The prevailing rate for one-year credit granted to trade customers in the industry is 5 percent per six-month period.

As per the experience, the servicing of the machine 'model pi' sold to Mr. Anik is expected to cost A Ltd. Rs.30,000 to perform the first service and Rs.50,000 to perform the second service. Assume actual costs equal expected costs. When A Ltd. provides machine services to customers in a separate transaction it earns a margin of 50% on cost. On 1st April, 2018, the cash selling price of the machine 'model pi' sold to Mr. Anik is Rs.2,51,927.

The promised supply of machine 'model pi' and maintenance service obligations are satisfactorily carried out in time by the company.

You are required to:

(i) Segregate the components of the transaction that A Ltd. shall apply to the revenue recognition criteria separately as per Ind AS 115;

(ii) Calculate the amount of revenue which A Ltd. must allocate to each component of the transaction;

(iii) Prepare journal entries to record the information set out above in the books of accounts of A Ltd. for the years ended 31st March·2019 and 31st March 2020; and

(iv) Draft an extract showing how revenue could be presented and disclosed in the financial statements of A Ltd. for the year ended 31st March 2019 and 31st March 2020.

Solution :

(i) As per para 27 of Ind AS 115, a good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to them. A readily available resource is a good or service that is sold separately (by the entity or another entity) or that the customer has already obtained from the entity or from other transactions or events; and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract.

Factors that indicate that two or more promises to transfer goods or services to a customer are separately identifiable include, but are not limited to, the following:

(a) significant integration services are not provided (i.e. the entity is not using the goods or services as inputs to produce or deliver the combined output called for in the contract)

(b) the goods or services does not significantly modify or customize other promised goods or services in the contract.

(c) the goods or services are not highly inter-dependent or highly interrelated with other promised goods or services in the contract

Accordingly, on 1st April, 2018, entity A entered into a single transaction with three identifiable separate components:

1. Sale of a good (i.e. engineering machine);
2. Rendering of services (i.e. engineering machine maintenance services on 30th September, 2018 and 1st April, 2019); and
3. Providing finance (i.e. sale of engineering machine and rendering of services on extended period credit).

(ii) Calculation and allocation of revenue to each component of the transaction

Date	Opening balance	Finance income	Goods	Services	Payment received	Closing balance
1st April, 2018	–	–	2,51,927	–	–	2,51,927
30th September, 2018	2,51,927	12,596 (Note 1)	–	45,000	–	3,09,523
31st March, 2019	3,09,523	15,477	–	–	–	3,25,000

		(Note 2)				
1st April, 2019	3,25,000	–	–	75,000	- 4,00,000	

Notes:

1. Calculation of finance income as on 30th September, 2018
   = 5% x 2,51,927 = Rs.12,596
2. Calculation of finance income as on 31st March, 2019
   = 5% x 3,09,523 = Rs.15,477

(iii) **Journal Entries**

Date	**Particulars**	**Dr. (Rs.)**	**Cr. (Rs.)**
1st April, 2018	Mr. Anik Dr. To Revenue - sale of goods (Profit or loss A/c) (Being revenue recognised from the sale of the machine on credit)	2,51,927	 2,51,927
	Cost of goods sold (Profit or loss) Dr. To Inventories (Being cost of goods sold recognised)	1,60,000	 1,60,000
30th September, 2018	Mr. Anik Dr. To Finance Income (Profit or loss) (Being finance income recognised)	12,596	 12,596
	Mr. Anik Dr. To Revenue- rendering of services (Profit or loss) (Being revenue from the rendering of maintenance services recognised)	45,000	 45,000
	Cost of services (Profit or loss) Dr. To Cash/Bank or payables (Being the cost of performing maintenance services recognised)	30,000	 30,000
31st March, 2019	Mr. Anik Dr. To Finance Income (Profit or loss) (Being finance income recognised)	15,477	 15,477
1st April, 2019	Mr. Anik Dr. To Revenue - rendering of services (Profit or loss) (Being revenue from the rendering of maintenance services recognised)	75,000	 75,000
	Cost of services (Profit or loss) Dr. To Cash/Bank or payables (Being the cost of performing maintenance services recognised)	50,000	 50,000
	Cash/Bank Dr. To Mr. Anik	4,00,000	 4,00,000

	(Being the receipt of cash from the customer recognised)		

(iv) Extract of Notes to the financial statements for the year ended 31st March, 2019 and 31st March, 2020

Note on Revenue

	2019-2020 Rs.	**2018-2019 Rs.**
Sale of goods	–	2,51,927
Rendering of machine - maintenance services	75,000	45,000
Finance income	–	28,073
	75,000	3,25,000

Question 12 : May 2021 – RTP

A property sale contract includes the following:

(a) Common areas
(b) Construction services and building material
(c) Property management services
(d) Golf membership
(e) Car park
(f) Land entitlement

Analyse whether the above items can be considered as separate performance obligations as per the requirements of Ind AS 115?

Solution :

Ind AS 115 provides that at contract inception, an entity evaluates the promised goods or services to determine which goods or services (or bundle of goods or services) are distinct and therefore constitute a performance obligation.

A performance obligation is a promise in a contract to transfer to the customer either:

- a good or service (or a bundle of goods or services) that is distinct; and
- series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

As per paragraph 27 of Ind AS 115, a good or service that is promised to a customer is distinct if both of the following criteria are met:

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (i.e. the good or service is capable of being distinct); and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (i.e. the promise to transfer the good or service is distinct within the context of the contract).

Each performance obligation is required to be accounted for separately.

Based on the above guidance, the following table discusses whether the common goods and services in property sale contract should be considered as separate performance obligation or not:

Goods/Service	Whether a separate Performance obligation (PO) or not	Reason
Common areas	Unlikely to be separate PO	Common areas are unlikely to be a separate performance obligation because the interests received in common areas are typically undivided interests that are not separable from the property itself. However, if the common areas were sold separately by the developer, then they could be considered as a separate performance obligation provided that it is distinct in the context of the contract.
Construction services and building material	Unlikely to be separate PO	Construction services and building materials can meet the first criterion as they are items that can be used in conjunction with other readily available goods or services. However, the developer would be considered to be providing a significant integration service as it is bringing together all the separate elements to deliver a complete building.
Property management services and Golf membership	Likely to be separate PO	Property management services and golf membership are likely to be separate performance obligations as they may be used in isolation or with the property already acquired, i.e., management services can be used with the property. These types of services are not significantly customised, integrated with, or dependent on the property. This is because there is no change in their function with or without the property. Also, a property management service could be undertaken by a third party.
Car park and Land entitlement	Analysis required	Items such as car parks and land entitlements generally meet the first criterion – i.e., capable of being distinct – as the buyer benefits from them on their own. Whether the second criterion is met depends on the facts and circumstances. For example, if the land entitlement can be sold separately or pledged as security as a separate item, it may indicate that it is not highly dependent on, or integrated with,

		other rights received in the contract. In an apartment scenario, the customer can receive an undivided interest in the land on which the apartment block sits. This type of right is generally considered as highly inter-related with the apartment itself.*

* However, if title to the land is transferred to the buyer separately – for example in a single party development – then the separately identifiable criterion may be met.

PS: Other facts and circumstances of each contract should also be carefully examined to determine performance obligations.

Question 13 : July 2021 – Paper

GTM Limited has provided the following 3 independent scenarios. You are advised to respond to the queries mentioned at the end of each scenario. Support your answer with the relevant extracts of the applicable Ind Ass.

Scenario 1

GTM Limited enters into a contract with a customer to sell product G, T and M in exchange for Rs.1,90,000. GTM Limited will satisfy the performance obligations for each of the product at different points in time. GTM Limited regularly sells product G separately and therefore the stand-along selling price is directly observable. The stand-alone selling prices of product T and M are not directly observable.

Because the stand-alone selling prices for Product T and M are not directly observable, the company has to estimate them. To estimate the stand-alone selling prices, the Company uses the adjusted market assessment approach for product T and the expected cost plus a margin approach for product M. In making these estimates, the Company maximizes the use of observable inputs.

The entity estimated the stand-along selling prices as follows :

Product	**Stand-alone selling price (Rs.)**
Product G	90,000
Product T	44,000
Product M	66,000
Total	2,00,000

Determine the transaction price allocated to each Product.

Scenario 2

GTM Limited regularly sells products G, T and M individually. The stand alone selling prices are as under :

Product	**Stand-alone selling price (Rs.)**
Product G	90,000
Product T	44,000
Product M	66,000

Total	2,00,000

In addition the Company regularly sells Products T and M together for Rs.1,00,000.
The Company enters into a contract with an another customer to sell Products G, T and M in exchange for Rs.1,90,000. GTM Limited will satisfy the performance obligations for each of the products at different points in time; or Product T and M at same point in time.
Determine the allocation of transactions price to Product T and M.

Scenario 3
GTM Limited enters into a contract with a customer to sell products G, T and M as described in scenario 2. The contract also includes a promise to transfer product 'Hope'. Total consideration in the contract is Rs.2,40,000. The stand-alone selling price for product 'Hope' is highly variable because the company sells product 'Hope' to different customers for a broad range of amounts (Rs.40,000 to Rs.65,000)
Determine the selling price of Products G, T, m and Hope using the residual approach.

Scenario 4
The same facts as in scenario 3 applies to scenario 4 except that the transaction price is Rs.2,25,000 instead of Rs.2,40,000.
Discuss how the transaction price should be allocated.

Solution :
Scenario 1
The customer receives a discount for purchasing the bundle of goods because the sum of the stand-alone selling prices (Rs. 2,00,000) exceeds the promised consideration (Rs. 1,90,000). The entity considers that there is no observable evidence about the performance obligation to which the entire discount belongs. The discount is allocated proportionately across Products G, T and M. The discount, and therefore the transaction price, is allocated as follows:

Product	**Allocated transaction price**	
	Rs.	
Product G	85,500	(Rs. 90,000 ÷ Rs. 2,00,000 × Rs. 1,90,000)
Product T	41,800	(Rs. 44,000 ÷ Rs. 2,00,000 × Rs. 1,90,000)
Product M	62,700	(Rs. 66,000 ÷ Rs. 2,00,000 × Rs. 1,90,000)
Total	1,90,000	

Scenario 2
The contract includes a discount of Rs. 10,000 on the overall transaction, which would be allocated proportionately to all three performance obligations when allocating the transaction price using the relative stand-alone selling price method.
However, because the entity regularly sells Products T and M together for Rs. 1,00,000 and Product G for Rs. 90,000, it has evidence that the entire discount of Rs. 10,000 should be allocated to the promises to transfer Products T and M in accordance with paragraph 82 of Ind AS 115.

If the entity transfers control of Products T and M at the same point in time, then the entity could, as a practical matter, account for the transfer of those products as a single performance obligation. That is, the entity could allocate Rs. 90,000 of the transaction prices to the single performance obligation of G and recognise revenue of Rs. 1,00,000 when Products T and M simultaneously transfer to the customer.

If the contract requires the entity to transfer control of Products T and M at different points in time, then the allocated amount of Rs. 1,00,000 is individually allocated to the promises to transfer Product T (stand-alone selling price of Rs. 44,000) and Product M (stand-alone selling price of Rs. 66,000) as follows:

Product	**Allocated transaction price**	
	Rs.	
Product G	40,000	(Rs.44,000 ÷ Rs.1,10,000 total stand-alone selling price × Rs.1,00,000)
Product T	60,000	(Rs. 66,000 ÷ Rs.1,10,000 total stand-alone selling price × Rs.1,00,000)
Total	1,00,000	

Scenario 3

Before estimating the stand-alone selling price of Product Hope using the residual approach, the entity determines whether any discount should be allocated to the other performance obligations in the contract.

As in Scenario 2, because the entity regularly sells Products T and M together for Rs. 1,00,000 and Product G for Rs. 90,000, it has observable evidence that Rs. 1,90,000 should be allocated to those three products and Rs. 10,000 discount should be allocated to the promises to transfer Products T and M in accordance with paragraph 82 of Ind AS 115.

Using the residual approach, the entity estimates the stand-alone selling price of Product Hope to be Rs. 50,000 as follows:

Product	**Stand-alone selling price Rs.**	**Method**
Product G	90,000	Directly observable
Products T and M	1,00,000	Directly observable with discount
Product Hope	50,000	Residual approach
Total	2,40,000	

The entity observes that the resulting Rs. 50,000 allocated to Product Hope is within the range of its observable selling prices (Rs. 40,000 to Rs. 65,000).

Scenario 4

The same facts as in Scenario 3 apply to Scenario 4 except the transaction price is Rs. 2,25,000 instead of Rs. 2,40,000. Consequently, the application of the residual approach would result in a stand-alone selling price of Rs. 35,000 for Product Hope (Rs. 2,25,000 transaction price less Rs. 1,90,000 allocated to Products G, T and M).

The entity concludes that Rs. 35,000 would not faithfully depict the amount of consideration to which the entity expects to be entitled in exchange for satisfying its performance obligation to transfer Product Hope, because Rs. 35,000 does not approximate the stand-alone selling price of Product Hope, which ranges from Rs. 40,000 to Rs. 65,000.
Consequently, the entity reviews its observable data, including sales and margin reports, to estimate the stand-alone selling price of Product Hope using another suitable method. The entity allocates the transaction price of Rs. 2,25,000 to Products G, T, M and Hope using the relative stand-alone selling prices of those products in accordance with paragraphs 73–80 of Ind AS 115.

Question 14 : Nov 2021 – RTP

Prime Ltd. is a technology company and regularly sells Software S, Hardware H and Accessory A. The stand-alone selling prices for these items are stated below:
Software S – Rs. 50,000
Hardware H – Rs.1,00,000 and
Accessory A – Rs. 20,000.
Since the demand for Hardware H and Accessory A is low, Prime Ltd. sells H and A together at Rs. 100,000. Prime Ltd. enters into a contract with Zeta Ltd. to sell all the three items for a consideration of Rs.1,50,000.
What will be the accounting treatment for the discount in the financial statements of Prime Ltd., considering that the three items are three different performance obligations which are satisfied at different points in time? Further, what will be the accounting treatment if Prime Ltd. would have transferred the control of Hardware H and Accessory A at the same point in time.

Solution :

Paragraph 82 of Ind AS 115 states that, "An entity shall allocate a discount entirely to one or more, but not all, performance obligations in the contract if all of the following criteria are met:

(a) the entity regularly sells each distinct good or service (or each bundle of distinct goods or services) in the contract on a stand-alone basis;

(b) the entity also regularly sells on a stand-alone basis a bundle (or bundles) of some of those distinct goods or services at a discount to the stand-alone selling prices of the goods or services in each bundle; and

(c) the discount attributable to each bundle of goods or services described in paragraph 82(b) is substantially the same as the discount in the contract and an analysis of the goods or services in each bundle provides observable evidence of the performance obligation (or performance obligations) to which the entire discount in the contract belongs".

In the given case, the contract includes a discount of Rs. 20,000 on the overall transaction, which should have been allocated proportionately to all three performance obligations when allocating the transaction price using the relative stand-alone selling price method (in accordance with paragraph 81 of Ind AS 115). However, as Prime Ltd. meets all the criteria specified in paragraph 82 above, i.e., it regularly sells Hardware H and Accessory A together for Rs. 1,00,000 and Software S for Rs. 50,000, accordingly, it is evident that the entire discount should be allocated to the promises to transfer Hardware H and Accessory A.

In the given case, since the contract requires the entity to transfer control of Hardware H and Accessory A at different points in time, then the allocated amount of Rs. 1,00,000 should be individually allocated to the promises to transfer Hardware H (stand-alone selling price of Rs. 1,00,000) and Accessory A (stand-alone selling price of Rs.20,000)

Product	Allocated transaction price (Rs.)
Hardware H	83,333 (1,00,000/ 120,000 x 100,000)
Accessory A	16,667 (20,000/120,000 x 100,000)
Total	1,00,000

However, if Prime Ltd. would have transferred the control of Hardware H and Accessory A at the same point in time, then the Prime Ltd. could, as a practical matter, account for the transfer of those products as a single performance obligation. That is, Prime Ltd. could allocate Rs. 1,00,000 of the transaction price to the single performance obligation and recognise revenue of Rs. 1,00,000 when Hardware H and Accessory A simultaneously transfer to Zeta Ltd.

Question 15 : May 2022 – RTP

On 1st April, 20X1, S Limited enters into a contract with Corp Limited to construct heavy-duty equipment for a promised consideration of rupees with a bonus of rupees if the equipment is completed within 24 months. At the inception of the contract, S Limited correctly accounts for the promised bundle of goods and services as a single performance obligation in accordance with Ind AS 115. At the inception of the contract, the Company expects the costs to be rupees and concludes that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will occur. Completion of the heavy-duty equipment is highly susceptible to factors outside of the Company's influence, mainly due to difficulties with the supply of components.

At 31st March, 20X2, S Limited has satisfied 65% of its performance obligation on the basis of costs incurred to date and concludes that the variable consideration is still constrained in accordance with Ind AS 115. However, on 4 June 20X2, the contract is modified with the result that the fixed consideration and expected costs increase by Rs. 1,50,000 and Rs. 80,000 respectively. The time allowable for achieving the bonus is extended by six months with the result that S Limited concludes that it is highly probable that the bonus will be achieved and that the contract remains a single performance obligation.

S Limited wants your opinion on the accounting treatment of contract with Corp Limited in light of Ind AS 115, for the year 20X1-20X2 and 20X2-20X3.

Solution :

For the year 20X1-20X2

S Limited accounts for the promised bundle of goods and services as a single performance obligation satisfied over time in accordance with Ind AS 115. At the inception of the contract, S Limited expects the following:

Transaction price	– Rs. 20,00,000
Expected costs	– Rs. 11,00,000
Expected profit (45%)	– Rs. 9,00,000

At contract inception, S Limited excludes the Rs. 2,50,000 bonus from the transaction price because it cannot conclude that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur. Completion of the heavy-duty equipment is highly susceptible to factors outside the entity's influence.

By the end of the first year, the entity has satisfied 65% of its performance obligation on the basis of costs incurred to date. Costs incurred to date are therefore Rs. 7,15,000 and S Limited reassesses the variable consideration and concludes that the amount is still constrained. Therefore at 31st March, 20X2, the following would be recognised:

Revenue	(A)	– Rs. 13,00,000 (Rs. 20,00,000 x 65%)
Costs	(B)	– Rs. 7,15,000 (Rs. 11,00,000 x 65%)
Gross profit (C) i.e.(A-B)		– Rs. 5,85,000

For the year 20X2-20X3

On 4th June, 20X2, the contract is modified. As a result, the fixed consideration and expected costs increase by Rs. 1,50,000 and Rs. 80,000, respectively.

The total potential consideration after the modification is Rs. 24,00,000 which is Rs. 21,50,000 fixed consideration + Rs. 2,50,000 completion bonus. In addition, the allowable time for achieving the bonus is extended by six months with the result that S Limited concludes that it is highly probable that including the bonus in the transaction price will not result in a significant reversal in the amount of cumulative revenue recognised in accordance with Ind AS 115. Therefore, the bonus of Rs. 2,50,000 can be included in the transaction price.

S Limited also concludes that the contract remains a single performance obligation. Thus, S Limited accounts for the contract modification as if it were part of the original contract. Therefore, S Limited updates its estimates of costs and revenue as follows:

S Limited has satisfied 60.60% of its performance obligation (Rs. 7,15,000 actual costs incurred compared to Rs. 11,80,000 total expected costs). The entity recognises additional revenue of Rs. 1,54,400 [(60.60% of Rs. 24,00,000) – Rs. 13,00,000 revenue recognised to date] at the date of modification i.e. on 4th June, 20X2 as a cumulative catch-up adjustment.

Thanks ....

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IND AS – 101
FIRST TIME ADOPTION

CHAPTER - 30

Question 1 : May 2018 – RTP

ABC Ltd is a government company and is a first-time adopter of Ind AS. As per the previous GAAP, the contributions received by ABC Ltd. from the government (which holds 100% shareholding in ABC Ltd.) which is in the nature of promoters' contribution have been recognised in capital reserve and treated as part of shareholders' funds in accordance with the provisions of AS 12, Accounting for Government Grants.

State whether the accounting treatment of the grants in the nature of promoters' contribution as per AS 12 is also permitted under Ind AS 20 Accounting for Government Grants and Disclosure of Government Assistance. If not, then what will be the accounting treatment of such grants recognised in capital reserve as per previous GAAP on the date of transition to Ind AS.

Solution :

Ind AS 20, "Accounting for Government Grants and Disclosure of Government Assistance" inter alia states that the Standard does not deal with government participation in the ownership of the entity.

Since ABC Ltd. is a Government company, it implies that government has 100% shareholding in the entity. Accordingly, the entity needs to determine whether the payment is provided as a shareholder contribution or as a government. Equity contributions will be recorded in equity while grants will be shown in the Statement of Profit and Loss.

Where it is concluded that the contributions are in the nature of government grant, the entity shall apply the principles of Ind AS 20 retrospectively as specified in Ind AS 101 'First Time Adoption of Ind AS'. Ind AS 20 requires all grants to be recognised as income on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate. Unlike AS 12, Ind AS 20 requires the grant to be classified as either a capital or an income grant and does not permit recognition of government grants in the nature of promoter's contribution directly to shareholders' funds.

Where it is concluded that the contributions are in the nature of shareholder contributions and are recognised in capital reserve under previous GAAP, the provisions of paragraph 10 of Ind AS 101 would be applied which states that, which states that except in certain cases, an entity shall in its opening Ind AS Balance Sheet:

(a) recognise all assets and liabilities whose recognition is required by Ind AS;

(b) not recognise items as assets or liabilities if Ind AS do not permit such recognition;

(c) reclassify items that it recognised in accordance with previous GAAP as one type of asset, liability or component of equity, but are a different type of asset, liability or component of equity in accordance with Ind AS; and

(d) apply Ind AS in measuring all recognised assets and liabilities."

Accordingly, as per the above requirements of paragraph 10(c) in the given case, contributions recognised in the Capital Reserve should be transferred to appropriate category under 'Other Equity' at the date of transition to Ind AS.

Question 2 : May 2019 – RTP

XYZ Pvt. Ltd. is a company registered under the Companies Act, 2013 following Accounting Standards notified under Companies (Accounting Standards) Rules, 2006. The Company has decided to voluntary adopt Ind AS w.e.f 1st April, 2018 with a transition date of 1st April, 2017.

The Company has one Wholly Owned Subsidiary and one Joint Venture which are into manufacturing of automobile spare parts.

The -consolidated financial statements of the Company under Indian GAAP are as under:

Consolidated Financial Statements

(Rs.in Lakhs)

Particulars	**31.03.2018**	**31.03.2017**
Shareholder's Funds		
Share Capital	7,953	7,953
Reserves & Surplus	16,547	16,597
Non-Current Liabilities		
Long Term Borrowings	1,000	1,000
Long Term Provisions	1,101	691
Other Long-Term Liabilities	5,202	5,904
Current Liabilities		
Trade Payables	9,905	8,455
Short Term Provisions	500	475
Total	**42,208**	**41,075**
Non-Current Assets		
Property Plant & Equipment	21,488	22,288
Goodwill on Consolidation of subsidiary and JV	1,507	1,507
Investment Property	5,245	5,245
Long Term Loans & Advances	6,350	6,350
Current Assets		
Trade Receivables	4,801	1,818
Investments	1,263	3,763
Other Current Assets	1,554	104
Total	**42,208**	**41,075**

Additional Information :

The Company has entered into a joint arrangement by acquiring 50% of the equity shares of ABC Pvt. Ltd. Presently, the same has been accounted as per the proportionate consolidated method. The proportionate share of assets and liabilities of ABC Pvt. Ltd. included in the consolidated financial statement of XYZ Pvt. Ltd. is as under:

Particulars	**Rs.in Lakhs**
Property, Plant & Equipment	1,200
Long Term Loans & Advances	405
Trade Receivables	280
Other Current Assets	50
Trade Payables	75
Short Term Provisions	35

The Investment is in the nature of Joint Venture as per Ind AS 111.

The Company has approached you to advice and suggest the accounting adjustments which are required to be made in the opening Balance Sheet as on 1st April, 2017.

Solution :

As per paras D31AA and D31AB of Ind AS 101, when changing from proportionate consolidation to the equity method, an entity shall recognise its investment in the joint venture at transition date to Ind AS.

That initial investment shall be measured as the aggregate of the carrying amounts of the assets and liabilities that the entity had previously proportionately consolidated, including any goodwill arising from acquisition. If the goodwill previously belonged to a larger cash-generating unit, or to a group of cash-generating units, the entity shall allocate goodwill to the joint venture on the basis of the relative carrying amounts of the joint venture and the cash-generating unit or group of cash-generating units to which it belonged. The balance of the investment in joint venture at the date of transition to Ind AS, determined in accordance with paragraph D31AA above is regarded as the deemed cost of the investment at initial recognition.

Accordingly, the deemed cost of the investment will be

Property, Plant & Equipment	1,200
Goodwill (Refer Note below)	119
Long Term Loans & Advances	405
Trade Receivables	280
Other Current Assets	50
Total Assets	2054
Less: Trade Payables	75
Short Term Provisions	35
Deemed cost of the investment in JV	1944

Calculation of proportionate goodwill share of Joint Venture ie ABC Pvt. Ltd.

Property, Plant & Equipment	22,288
Goodwill	1,507
Long Term Loans & Advances	6,350
Trade Receivables	1,818
Other Current Assets	104
Total Assets	32,067

Less:	Trade Payables	8,455
	Short Term Provisions	475
		23,137

Proportionate Goodwill of Joint Venture
= [(Goodwill on consolidation of subsidiary and JV/Total relative net asset) × Net asset of JV]
= (1507 / 23,137) × 1825 = 119 (approx.)
Accordingly, the proportional share of assets and liabilities of Joint Venture will be removed from the respective values assets and liabilities appearing in the balance sheet on 31.3.2017 and Investment in JV will appear under non-current asset in the transition date balance sheet as on 1.4.2017.

Adjustments made in I GAAP balance sheet to arrive at Transition date Ind AS Balance Sheet

Particulars	**31.3.2017**	**Ind AS Adjustment**	**Transition date Balance Sheet as per Ind AS**
Non-Current Assets			
Property Plant & Equipment	22,288	(1,200)	21,088
Intangible assets - Goodwill on Consolidation	1507	(119)	1,388
Investment Property	5,245	-	5,245
Long Term Loans & Advances	6,350	(405)	5,945
Non- current investment in JV	-	1,944	1,944
Current Assets			
Trade Receivables	1,818	(280)	1,538
Investments	3,763	-	3,763
Other Current Assets	104	(50)	54
Total	**41,075**	**(110)**	**40,965**
Shareholder's Funds			
Share Capital	7,953	-	7,953
Reserves & Surplus	16,597	-	16,597
Non-Current Liabilities			
Long Term Borrowings	1,000		1,000
Long Term Provisions	691		691
Other Long-Term Liabilities	5,904		5,904
Current Liabilities			
Trade Payables	8,455	(75)	8,380
Short Term Provisions	475	(35)	440
Total	**41,075**	**(110)**	**40,965**

Question 3 : Nov 2019 – RTP

Mathur India Private Limited has to present its first financials under Ind AS for the year ended 31st March, 20X3. The transition date is 1st April, 20X1.
The following adjustments were made upon transition to Ind AS:

(a) The Company opted to fair value its land as on the date on transition.
The fair value of the land as on 1st April, 20X1 was Rs.10 crores. The carrying amount as on 1st April, 20X1 under the existing GAAP was Rs.4.5 crores.

(b) The Company has recognised a provision for proposed dividend of Rs.60 lacs and related dividend distribution tax of Rs.18 lacs during the year ended 31st March, 20X1. It was written back as on opening balance sheet date.

(c) The Company fair values its investments in equity shares on the date of transition. The increase on account of fair valuation of shares is Rs.75 lacs.

(d) The Company has an Equity Share Capital of Rs.80 crores and Redeemable Preference Share Capital of Rs.25 crores.

(e) The reserves and surplus as on 1st April, 20X1 before transition to Ind AS was Rs.95 crores representing Rs.40 crores of general reserve and Rs.5 crores of capital reserve acquired out of business combination and balance is surplus in the Retained Earnings.

(f) The company identified that the preference shares were in nature of financial liabilities.

What is the balance of total equity (Equity and other equity) as on 1st April, 20X1 after transition to Ind AS? Show reconciliation between total equity as per AS (Accounting Standards) and as per Ind AS to be presented in the opening balance sheet as on 1st April, 20X1.
Ignore deferred tax impact.

Solution :

Computation of balance total equity as on 1st April, 20X1 after transition to Ind AS

			Rs. in crore
Share capital- Equity share Capital			80
Other Equity			
General Reserve		40	
Capital Reserve		5	
Retained Earnings (95-5-40)	50		
Add: Increase in value of land (10 – 4.5)	5.5		
Add: De recognition of proposed dividend (0.6 + 0.18)	0.78		
Add: Increase in value of Investment	0.75	57.03	102.03
Balance total equity as on 1st April, 20X1 after transition to Ind AS			182.03

Reconciliation between Total Equity as per AS and Ind AS to be presented in the opening balance sheet as on 1st April, 20X1

		Rs. in crore
Equity share capital		80
Redeemable Preference share capital		25
		105
Reserves and Surplus		95
Total Equity as per AS		200
Adjustment due to reclassification		

Preference share capital classified as financial liability		(25)
Adjustment due to derecognition		
Proposed Dividend not considered as liability as		0.78
1st April 20X1		
Adjustment due to remeasurement		
Increase in the value of Land due to remeasurement at fair value	5.5	
Increase in the value of investment due to remeasurement at fair value	0.75	6.25
Equity as on 1st April, 20X1 after transition to Ind AS		182.03

Question 4 : May 2020 – RTP

On April 1, 20X1, Sigma Ltd. issued 30,000 6% convertible debentures of face value of Rs.100 per debenture at par. The debentures are redeemable at a premium of 10% on March 31, 20X5 or these may be converted into ordinary shares at the option of the holder. The interest rate for equivalent debentures without conversion rights would have been 10%. The date of transition to Ind AS is April 1, 20X3.

Suggest how should Sigma Ltd. account for this compound financial instrument on the date of transition.

The present value of Re. 1 receivable at the end of each year based on discount rates of 6% and 10% can be taken as:

End of year	6%	10%
1	0.94	0.91
2	0.89	0.83
3	0.84	0.75
4	0.79	0.68

Solution :

Ind AS 32, 'Financial Instruments: Presentation', requires an entity to split a compound financial instrument at inception into separate liability and equity components. If the liability component is no longer outstanding, retrospective application of Ind AS 32 would involve separating two portions of equity. The first portion is recognised in retained earnings and represents the cumulative interest accreted on the liability component. The other portion represents the original equity component. However, in accordance with Ind AS 101, a first-time adopter need not separate these two portions if the liability component is no longer outstanding at the date of transition to Ind AS.

In the present case, since the liability is outstanding on the date of transition, Sigma Ltd. will need to split the convertible debentures into debt and equity portion on the date of transition. Accordingly, we will first measure the liability component by discounting the contractually determined stream of future cash flows (interest and principal) to present value by using the discount rate of 10% p.a. (being the market interest rate for similar debentures with no conversion option).

	Rs.
Interest payments p.a. on each debenture	6
Present Value (PV) of interest payment on each debenture for years 1 to 4 (6 x 3.17) (Note 1)	19.02
PV of principal repayment on each debenture (including premium) 110 x 0.68 (Note 2)	74.80
Total liability component on each debenture (A)	93.82
Total equity component per debenture (Balancing figure) (B) = (C) – (A)	6.18
Face value per debenture (C)	100.00
Equity component per debenture	6.18
Total equity component for 30,000 debentures	1,85,400
Total debt amount (30,000 x 93.82)	28,14,600

Thus, on the date of transition, the amount of Rs.30,00,000 being the amount of debentures will be split as under:

Debt Rs.28,14,600

Equity Rs.1,85,400

Notes:

1. 3.17 is annuity factor of present value of Re. 1 at a discount rate of 10% for 4 years.
2. On maturity, Rs.110 will be paid (Rs.100 as principal payment + Rs.10 as premium)

Question 7 : May 2021 – RTP

HIM Limited having net worth of Rs. 250 crores is required to adopt Ind AS from 1 April, 20X2 in accordance with the Companies (Indian Accounting Standard) Rules 2015.

Rahul, the senior manager, of HIM Ltd. has identified following issues which need specific attention of CFO so that opening Ind AS balance sheet as on the date of transition can be prepared:

Issue 1 : As part of Property, Plant and Equipment, Company has elected to measure land at its fair value and want to use this fair value as deemed cost on the date of transition. The carrying value of land as on the date of transition was Rs. 5,00,000. The land was acquired for a consideration of Rs. 5,00,000. However, the fair value of land as on the date of transition was Rs. 8,00,000.

Issue 2 : Under Ind AS, the Company has designated mutual funds as investments at fair value through profit or loss. The value of mutual funds as per previous GAAP was Rs. 4,00,000 (at cost). However, the fair value of mutual funds as on the date of transition was Rs. 5,00,000.

Issue 3 : Company had taken a loan from another entity. The loan carries an interest rate of 7% and it had incurred certain transaction costs while obtaining the same. It was carried at cost on its initial recognition. The principal amount is to be repaid in equal instalments over the period of loan. Interest is also payable at each year end. The fair value of loan as on the date of transition is Rs. 1,80,000 as against the carrying amount of loan which at present equals Rs. 2,00,000.

Issue 4 : The company has declared dividend of Rs. 30,000 for last financial year. On the date of transition, the declared dividend has already been deducted by the accountant from the company's 'Reserves & Surplus' and the dividend payable has been grouped under 'Provisions'. The dividend was only declared by board of directors at that time and it was not approved in the annual general meeting of shareholders. However, subsequently when the meeting was held it was ratified by the shareholders.

Issue 5 : The company had acquired intangible assets as trademarks amounting to Rs. 2,50,000. The company assumes to have indefinite life of these assets. The fair value of the intangible assets as on the date of transition was Rs. 3,00,000. However, the company wants to carry the intangible assets at Rs. 2,50,000 only.

Issue 6 : After consideration of possible effects as per Ind AS, the deferred tax impact is computed as Rs. 25,000. This amount will further increase the portion of deferred tax liability. There is no requirement to carry out the separate calculation of deferred tax on account of Ind AS adjustments.

Management wants to know the impact of Ind AS in the financial statements of company for its general understanding.

Prepare Ind AS Impact Analysis Report (Extract) for HIM Limited for presentation to the management wherein you are required to discuss the corresponding differences between Earlier IGAAP (AS) and Ind AS against each identified issue for preparation of transition date balance sheet. Also pass journal entry for each issue.

Solution :

Preliminary Impact Assessment on Transition to Ind AS in HIM Limited's Financial Statements

Issue 1: Fair value as deemed cost for property plant and equipment:

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
As per AS 10, Property, Plant and Equipment is recognised at cost less depreciation.	Ind AS 101 allows entity to elect to measure Property, Plant and Equipment on the transition date at its fair value or previous GAAP carrying value (book value) as deemed cost.	The company has decided to adopt fair value as deemed cost in this case. Since fair value exceeds book value, so the book value should be brought up to fair value. The resulting impact of fair valuation of land Rs. 3,00,000 should be adjusted in other equity.

Journal Entry on the date of transition

Particulars		Debit (Rs.)	Credit (Rs.)
Property Plant and Equipment Dr.	Dr.	3,00,000	
To Revaluation Surplus (OCI- Other Equity)			3,00,000

Issue 2: Fair valuation of Financial Assets:

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
As per Accounting Standard, investments are measured at lower of cost and fair value.	On transition, financial assets including investments are measured at fair values except for investments in subsidiaries, associates and JVs' which are recorded at cost.	All financial assets (other than Investment in subsidiaries, associates and JVs' which are recorded at cost) are initially recognized at fair value. The subsequent measurement of such assets are based on its categorization either Fair Value through Profit & Loss (FVTPL) or Fair Value through Other Comprehensive Income (FVTOCI) or at Amortised Cost based on business model assessment and contractual cash flow characteristics. Since investment in mutual fund are designated at FVTPL, increase of Rs. 1,00,000 in mutual funds fair value would increase the value of investments with corresponding increase to Retained Earnings.

Journal Entry on the date of transition

Particulars		Debit (Rs.)	Credit (Rs.)
Investment in mutual funds	Dr.	1,00,000	
To Retained earnings			1,00,000

Issue 3: Borrowings - Processing fees/transaction cost:

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
As per AS, such expenditure is charged to Profit and loss account or capitalised as the case may be	As per Ind AS, such expenditure is amortised over the period of the loan. Ind AS 101 states that if it is impracticable for an entity to apply retrospectively the effective interest method in Ind AS 109, the fair value of the financial asset or the financial liability at the date of transition to Ind AS shall be the new gross carrying amount of that financial asset or the new amortised cost of that financial liability.	Fair value as on the date of transition is Rs. 1,80,000 as against its book value of Rs. 2,00,000. Accordingly, the difference of Rs. 20,000 is adjusted through retained earnings.

Journal Entry on the date of transition

Particulars		Debit (Rs.)	Credit (Rs.)
Borrowings / Loan payable	Dr.	20,000	
To Retained earnings			20,000

Issue 4: Proposed dividend:

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
As per AS, provision for proposed divided is made in the year when it has been declared and approved.	As per Ind AS, liability for proposed dividend is recognised in the year in which it has been declared and approved.	Since dividend should be deducted from retained earnings during the year when it has been declared and approved. Therefore, the provision declared for preceding year should be reversed (to rectify the wrong entry). Retained earnings would increase proportionately due to such adjustment

Journal Entry on the date of transition

Particulars		Debit (Rs.)	Credit (Rs.)
Provisions	Dr.	30,000	
To Retained earnings			30,000

Issue 5 : Intangible assets:

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
The useful life of an intangible asset cannot be indefinite under IGAAP principles. The Company amortised brand/trademark on a straight line basis over maximum of 10 years as per AS 26.	The useful life of an intangible asset like brand/trademark can be indefinite. Not required to be amortised and only tested for impairment. Company can avail the exemption given in Ind AS 101 as on the date of transition to use the carrying value as per previous GAAP.	Consequently, there would be no impact as on the date of transition since company intends to use the carrying amount instead of book value at the date of transition.

Issue 6: Deferred tax

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
As per AS, deferred taxes are accounted as per income statement approach.	As per Ind AS, deferred taxes are accounted as per balance sheet approach.	On date of transition to Ind AS, deferred tax liability would be increased by Rs. 25,000.

Journal Entry on the date of transition

Particulars	Debit (Rs.)	Credit (Rs.)
Retained earnings Dr.	25,000	
To Deferred tax liability		25,000

Question 8 : Nov 2021 – RTP

While preparing an opening balance sheet on the date of transition, an entity is required to:

(a) recognise all assets and liabilities whose recognition is required by Ind AS;

(b) reclassify items that it recognised in accordance with previous GAAP as one type of asset, liability or component of equity, but are a different type of asset, liability or component of equity in accordance with Ind AS; and

(c) apply Ind AS in measuring all recognised assets and liabilities.

Give examples for each of the above 4 categories.

Solution :

The examples of the items that an entity may need to recognise, derecognise, remeasure, reclassify on the date of transition are as under:

(a) recognise all assets and liabilities whose recognition is required by Ind AS:

- (i) customer related intangible assets if an entity elects to restate business combinations
- (ii) share-based payment transactions with non-employees
- (iii) recognition of deferred tax on land

(b) reclassify items that it recognised in accordance with previous GAAP as one type of asset, liability or component of equity, but is a different type of asset, liability or component of equity in accordance with Ind AS:

- (i) redeemable preference shares that would have earlier been classified as equity;
- (ii) non-controlling interests which would have been earlier classified outside equity; and

(c) apply Ind ASs in measuring all recognised assets and liabilities:

- (i) discounting of long-term provisions
- (ii) measurement of deferred income taxes for all temporary differences instead of timing differences.

Question 9 : May 2022 – RTP

GG Ltd., a listed company, prepares its first Ind AS financial statements for the year ending 31st March, 20X3. The date of transition is 1st April, 20X1. The functional and presentation currency is Rupee. The financial statements as at and for the year ended 31st March, 20X3 contain an explicit and unreserved statement of compliance with Ind AS. Previously it was using Indian GAAP (AS) as base.
It has already published its first interim results of quarter 1, quarter 2 and quarter 3 of 20X2- 20X3 in accordance with Ind AS 34 and Ind AS 101. The interim financial report included the reconciliations both of total comprehensive income and of equity that are required by Ind AS 101. Since issuing the interim financial report, its management has concluded that one of accounting policy choices applied at the interim should be changed for the full year.
How should GG Ltd. deal with the change in accounting policy under Ind AS framework?

Solution :
The first annual Ind AS financial statements are prepared in accordance with the specific requirements of Ind AS 101. Subject to certain specified exemptions and exceptions, paragraph 7 of Ind AS 101 requires the entity to use the same accounting policies in its opening Ind AS balance sheet and throughout all periods presented. This override Ind AS 8's requirements for disclosures about changes in accounting policies do not apply in an entity's first Ind AS financial statements.
GG Ltd. should include an explanation of the change in policy that it has made since the interim financial report, in the notes to the annual financial statements, in accordance with paragraph 27A of Ind AS 101. The disclosure note is likely to include information, similar to what Ind AS 8 would otherwise require, to help users of the financial statements to understand the changes that have been made. The entity should also ensure that the reconciliations of total comprehensive income and of equity, presented in the first Ind AS financial statements in accordance with paragraph 24 of Ind AS 101 are updated from those included in the interim financial report to reflect the amended accounting policy

Thanks ....

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ANALYSIS OF FINANCIAL STATEMENTS

CHAPTER - 31

Question 1 : May 2022 – RTP

Defense Innovators Limited is a public sector undertaking and is engaged in the construction of warships and submarines. XYZ Private Limited approached Defense Innovators Limited for construction of "specially designed" ships for it, which will be used by XYZ Private Limited for transportation of specific goods. The offer was accepted by the Defense Innovators Limited and both the companies entered into an agreement for the construction and delivery of 3 specially designed ships on 'Fixed Price' basis with variable component in respect to certain items.

Base and depot (B & D) spares for all three ships shall be procured by Defense Innovators Limited and will be paid on the cost of the item with certain percentage.

The contract states that "certain equipment" out of variable cost items, will be supplied by XYZ Private Limited at 'free of cost' for installation on board of ship. It is, therefore, to be noted as under:

(i) Some equipment are procured by Defense Innovators Limited in the presence of the XYZ Private Limited's representative for technical scrutiny as well as negotiating the prices. The vendors of these equipment are paid by Defense Innovators Limited. The cost of the equipment along with the cost of installation and profit thereon is claimed and reimbursed by XYZ Private Limited to Defense Innovators Limited.

(ii) There are certain other equipment for which orders are directly placed and also paid by the XYZ Private Limited. These equipment are known as 'Buyer Furnished Equipment (BFE)' and are delivered to the company 'free of cost' for installing in the ship. The labour cost of Installation of these are already included in the price component of the contract. BFEs are returned to the buyer after completion of the ship.

The period required for construction of one ship was approximately four years.

Whether the cost of Buyer Furnished Equipment's (BFE's) supplied by XYZ Private Limited to Defense Innovators Limited for-installing the same in the ships can be considered as 'inventory' by Defense Innovators Limited and then on delivery of ship will be recognised as revenue in its books of account? Elaborate.

Solution :

Before any item can be recognised as an inventory, it should meet the definition of 'asset' as given in the Conceptual Framework for Financial Reporting under Ind AS, issued by the Institute of Chartered Accountants of India as follows:

"An asset is a present economic resource controlled by the entity as a result of past events and economic resource is a right that has the potential to produce economic benefits".

The orders in respect of Buyer Furnished Equipment's (BFEs) are directly placed by the buyer and payment in respect of them is made by the buyer. These are then supplied to the company for installing in the ship and the buyer pays installation charges which are included in the contract price. Thus, the company has neither incurred any cost on BFEs nor any amount is recoverable on account of such equipment except installation charges. Accordingly, such equipment are not 'assets' that may be considered as a part of its contract work-in progress.

In fact, after installation in the ship, BFEs are returned to the buyer after completion of the ship. Thus, these are only held by the company in the capacity of a bailee. Since, it cannot be considered as an 'asset', therefore, it can neither be considered as 'inventory' nor as 'work-in-progress'.

Further, it can also not be considered as a part of sale value or revenue of the company as no consideration would be receivable with respect to the cost of such equipment.

On the basis of the above, it can be concluded that:

(i) The BFEs cannot be considered as inventories / Work-in-progress for Defense Innovators Limited.

(ii) The BFE's cost cannot be considered as part of sales value / contract revenue to Defense Innovators Limited.

Thanks ….

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CORPORATE SOCIAL RESPONSIBILITY

CHAPTER - 32

Question 1 : May 2018 – PAPER

What are the provisions of section 135 of the Companies Act, 2013 regarding constitution of a Corporate Social Responsibility (CSR) Committee. Also explain the role of Corporate Social Responsibility (CSR) Committee and Board.

XYZ Limited is a company which has net worth of Rs.250 crore. It manufactures parts for automobiles. The sales of the company are affected due to low demand of the products. The previous year's financial state of company are as below:

(Rs.in crore)

	31st March 2018 (Current Year)	31st March 2017	31st March 2016	31st March 2015
Net Profit	4.25	8.00	3.50	3.25
Turnover	500.00	900.00	400.00	350.00

Examine, whether the company has an obligation to form a CSR committee since the applicability criteria is not satisfied in the current financial year.

Solution :

A. As per section 135 of the Companies Act 2013

Every company having either

- ❖ net worth of Rs.500 crore or more, or
- ❖ turnover of Rs.1,000 crore or more or
- ❖ a net profit of Rs.5 crore or more

during any financial year shall constitute a Corporate Social Responsibility (CSR) Committee of the Board consisting of three or more directors (including at least one independent director).

B. Role of Corporate Social Responsibility (CSR) Committee

The CSR Committee shall—

(a) formulate and recommend to Board-

a. a CSR Policy indicating the activities to be undertaken by the company as specified in Schedule VII;

b. the amount of expenditure to be incurred on the above activities and

(b) monitor the CSR Policy of the company from time to time.

C. Role of Board

Board shall disclose-

(a) The composition of CSR Committee in its report
(b) Approve the recommended CSR Policy for the company
(c) Disclose the contents of such Policy in its report and place it on the company's website
(d) Ensure that the activities included in CSR Policy of the company are duly executed by the company
(e) Ensure that the company spends, in every financial year, at least two percent of the average net profits of the company made during the three immediately preceding financial years by giving preference to the local area and areas around it where it operates
(f) In case the company fails to spend such amount, the Board shall specify the reasons for not spending the amount.

D. In the given scenario

The MCA has clarified that 'any financial year' referred to under sub-section (1) of section 135 of the Act read with Rule 3(2) of Companies CSR Rule, 2014, implies 'any of the three preceding financial years'.

A company which meets the 'net worth', 'turnover' or 'net profits' criteria in any of the preceding three financial years, but which does not meet the criteria in the relevant financial year, is still required to constitute a CSR Committee and comply with provisions of sections 135 of the Companies Act, 2013.

As per the criteria to constitute CSR committee -

1) <u>Net worth greater than or equal to Rs.500 Crore:</u> This criterion is not satisfied.
2) <u>Sales greater than or equal to Rs.1000 Crore:</u> This criterion is not satisfied.
3) <u>Net Profit greater than or equal to Rs.5 Crore:</u> This criterion is satisfied in financial year ended March 31, 2017 when the net profit was Rs.8 crore.

Hence, the XYZ Ltd. is required to form a CSR committee.

Question 2 : Nov 2018 – PAPER

Baby Limited manufactures consumable goods for infants like bath soap, cream, powder, oil etc. As part of its CSR policy, it has decided that for every pack of these goods sold, Rs.0.75 will go towards the "Swachh Bharat Foundation" which will qualify as a CSR spend as per Schedule VII. Consequently, at the year end, the company sold 40,000 such packs and a total of Rs.30,000 was recognized as CSR expenditure. However, this amount was not paid to the Foundation at the end of the financial year. Will the amount of Rs.30,000 qualify to be CSR expenditure?

Solution :

Baby Ltd. has earmarked 75 paise per pack to spend as CSR activities. However, only by earmarking the amount from such sale for CSR expenditure, the company cannot show it as CSR expenditure. To qualify the amount as CSR expenditure, it has to be spent. Hence, Rs.30,000 will not be automatically considered as CSR expenditure till the time it is spent on CSR activities i.e it is deposited to 'Swachh Bharat Foundation'.

Question 3 : May 2019 – RTP

ABC Ltd. is a company which has a net worth of INR 200 crores, it manufactures rubber parts for automobiles. The sales of the company are affected due to low demand of its products.
The previous year's financial state:

(Rs.in Crore)

	March 31, 2019 (Current year)	March 31, 2018	March 31, 2017	March 31, 2016
Net Profit	3.00	8.50	4.00	3.00
Sales (turnover)	850	950	900	800

Does the Company have an obligation to form a CSR committee since the applicability criteria is not satisfied in the current financial year?

Solution :

It has been clarified that 'any financial year' referred to under sub-section (1) of section 135 of the Act read with Rule 3(2) of Companies CSR Rule, 2014, implies 'any of the three preceding financial years'.

A company which meets the net worth, turnover or net profits criteria in any of the preceding three financial years, but which does not meet the criteria in the relevant financial year, will still need to constitute a CSR Committee and comply with provisions of sections 135(2) to (5) read with the CSR Rules.

As per the criteria to constitute CSR committee -

1) Net worth greater than or equal to INR 500 Crores: This criterion is not satisfied.
2) Sales greater than or equal to INR 1000 Crores: This criterion is not satisfied.
3) Net Profit greater than or equal to INR 5 Crores: This criterion is satisfied in financial year ended March 31, 2018.

Hence, the Company will be required to form a CSR committee.

Question 4 : Nov 2020 – RTP

In order to encourage companies and organisations to generously contribute to the Government's COVID-19 relief fund, taxation laws have been amended to reckon these contributions as deductible for the financial year ending 31st March, 2020 even if the contributions are made after the year end but within three months after year end. Government of India issued the notification on 31st March, 2020 by way of an Ordinance. Such contributions to COVID-19 funds are considered for compliance with annual spends on corporate social responsibility (CSR) for the current accounting year under the Companies Act, 2013. In this scenario, whether the contributions to COVID-19 Relief Funds made subsequent to reporting date of the current accounting period can be provided for as expenses of the current accounting period? Also show its impact on deferred tax, if any.

Solution :

According to Ind AS 37, a provision shall be made if:

(a) an entity has a present obligation (legal or constructive) 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. If these conditions are not met as of reporting date, no provision shall be recognised for that financial year.

Government of India issued the notification on 31st March, 2020 by way of an Ordinance and hence, it is most unlikely for any entity to have a present obligation on 31st March, 2020, for such a commitment. As these conditions are not met as of reporting date of financial year 2019 - 2020, no provision should be recognised in the financial statements for that financial year.

In the fact pattern given above, the accounting implications for the financial year 2019-2020 is as follows:

- Do not recognize expense / liability for the contribution to be made subsequent to the year ended 31st March, 2020 as it does not meet the criteria of a present obligation as at the balance sheet date. However, the expected spend may be explained in the notes to the accounts as the same will also be considered in measurement of deferred tax liability.
- If the entity claims a deduction in the Income Tax return for the financial year 2019 - 2020 for that contribution made subsequent to 31st March, 2020, recognise Deferred Tax Liability as there would be a tax saving in financial year 2019 - 2020 for a spend incurred in subsequent year.

Question 5 : Nov 2020 – Paper

Royal Ltd. is a company which has a net worth of Rs. 200 crore engaged in the manufacturing of rubber products. The sales of the company are badly affected due to pandemic during the Financial year 2019-2020.

Relevant financial details of the following financial years are as follows: (Rs. in crore)

Particulars	31 March 2020 (Current year) estimated	31-Mar-19	31-Mar-18	31-Mar-17
Net Profit	3.00	8.50	4.00	3.00
Sales (turnover)	850	950	900	800

During the pandemic period (till 31 March 2020) various commercial activities were undertaken with considerable concessions/discounts, along the related affected areas. The management intends to highlight the expenditure incurred on such activities as expenditure incurred, on activities undertaken to discharge corporate social responsibility, while publishing its financial statements for the year 2019-2020.

You are requested to advise CFO of Royal Ltd on the below points along with reasons for your advise:

(i) Whether the Company has an obligation to form a CSR committee since the applicability criteria are not satisfied in the current financial year?

(ii) The accounting of expenditure during the pandemic period is to be treated as expenditure on CSR in the financial statement according to the view of the accountant of the company.

Solution :

(i) A company which meets the net worth, turnover or net profits criteria in immediate preceding financial year will need to constitute a CSR Committee and comply with provisions of sections 135(2) to (5) read with the CSR Rules.

As per the criteria to constitute CSR committee -

(1) Net worth should be greater than or equal to ` 500 Crore: This criterion is not satisfied as per the facts given in the question.

(2) Sales should be greater than or equal to ` 1000 Crore: This criterion is not satisfied as per the facts given in the question.

(3) Net profit should be greater than or equal to ` 5 Crore: as per the facts given in the question, this criterion is satisfied in financial year ended 31 March 2019 i.e. immediate preceding financial year.

Hence, the Company will be required to form a CSR committee.

(ii) The Companies Act, 2013 mandated the corporate entities that the expenditure incurred for Corporate Social Responsibility (CSR) should not be the expenditure incurred for the activities in the ordinary course of business. If expenditure incurred is for the activities in the ordinary course of business, then it will not be qualified as expenditure incurred on CSR activities.

Further, it is presumed that the commercial activities performed at concessional rates are the activities done in the ordinary course of business of the company other than the activities defined in Schedule VII of the Companies Act, 2013. Therefore, the treatment done by the Management by showing the expenditure incurred on such commercial activities in its financial statements as the expenditure incurred on activities undertaken to discharge CSR, is not correct.

Question 6 : Jan 2021 – Paper

Sun Shine Limited is a company which seems to be covered under the ambit of CSR rules. As part of its CSR contribution an amount of Rs.40,000 p.m. was spent by way of adoption of 2 families of drought hit area.

The average net profits of immediately preceding financial year was Rs.1,80,00,000. Please note that the company commenced its commercial activities only on the first day of the immediately preceding financial year. The Accountant of the company says that CSR provisions are not applicable to his company since it is one year old and in case if it is applicable he wants to carry forward the excess amount spent on account of CSR activities to future years.

You are required to comment with the figures, whether the contention of the Accountant is correct in context of CSR provisions?

Solution :

As per section 135 of the Companies Act 2013, every company having either

- net worth of Rs.500 crore or more, or
- turnover of Rs.1,000 crore or more or
- a net profit of Rs.5 crore or more

during the immediately preceding financial year shall constitute a Corporate Social Responsibility (CSR) Committee.

In the given case, the average net profits of immediate preceding financial year of Sun Shine Limited is Rs.1,80,00,000 (i.e. Rs.1.80 crore). Hence, net profit criteria is not met.

Company is covered under the ambit of CSR rules (assuming that net worth or turnover criteria is met):

Since it is given in the question that the company seems to be covered under the ambit of CSR rules, it is assumed that either the net worth of Sun Shine Limited might have exceeded Rs.500 crore or more, or turnover might have exceeded Rs.1,000 crore or more during immediate preceding financial year. Accordingly, CSR provisions are applicable to Sun Shine Limited irrespective of the fact that the company is in second year of6 operations.

If the company meets any one of the thresholds in the immediately preceding previous year, then the contention of accountant is incorrect that CSR provisions will not be applicable to the company as it is only one year old.

The accountant wants to carry forward the excess amount spent on account of CSR activities to future years which is Rs.1,20,000 [Rs.40,000 x 12 - (Rs.1,80,00,000 x 2%)]. However, there is no provision to carry forward the excess CSR expenditure spent* in a particular year. Hence, here also the contention of the accountant is incorrect. The excess expenditure made shall be considered as voluntary made by the entity.

*The amendments in section of CSR has been made effective from January, 2021. Hence not applicable for January, 2021 examination.

Question 7 : July 2021 – Paper

Government of India provides loans to MSMEs at a below – market rate of interest to fund the set – up a new manufacturing facility. Sikshma Limited's date of transition to Ind AS is 1st April 2020.

In financial year 2014-15, the Company had receive a loan of Rs.2.0 crores at a below – market rate of interest from the government. Under Indian GAAP, the Company had accounted for the loan as equity and the carrying amount was Rs.2.0 crores at the date of transition. The amount repayable on 31st March 2024 will be Rs.2.50 crores.

The Company has been advised to recognize the difference of Rs.0.50 crores in equity by correspondingly increasing the value of various assets under property, plant and equipment by an equivalent amount on proportionate basis. Further, on 31st March 2024 when the loan has to be repaid, Rs.2.50 crores should be presented as a deduction from property, plant and equipment.

Discuss the above treatment and share your views as per applicable Ind Ass.

Solution :

Requirement as per Ind AS:

A first-time adopter shall classify all government loans received as a financial liability or an equity instrument in accordance with Ind AS 32. A first-time adopter shall apply the requirements in Ind AS 109 and Ind AS 20, prospectively to government loans existing at the date of transition to Ind AS and shall not recognise the corresponding benefit of the government loan at a below-market rate of interest as a government grant.

Treatment to be done:

Consequently, if a first-time adopter did not, under its previous GAAP, recognise and measure a government loan at a below-market rate of interest on a basis consistent with Ind AS requirements, it shall use its previous GAAP carrying amount of the loan at the date of transition to Ind AS as the carrying amount of the loan in the opening Ind AS Balance Sheet. An entity shall apply Ind AS 109 to the measurement of such loans after the date of transition to Ind AS.

In the instant case, the loan meets the definition of a financial liability in accordance with Ind AS 32. Company therefore reclassifies it from equity to liability. It also uses the previous GAAP carrying amount of the loan at the date of transition as the carrying amount of the loan in the opening Ind AS balance sheet.

It calculates the annual effective interest rate (EIR) starting 1st April 2020 as below:

EIR = Amount / Principal(1/t) i.e. 2.50/2(1/4) i.e. 5.74%. approx.

At this rate, Rs. 2 crore will accrete to Rs. 2.50 crore as at 31st March 2024.

During the next 4 years, the interest expense charged to statement of profit and loss shall be:

Year ended	**Opening amortised cost (Rs.)**	**Interest expense for the year (Rs.) @ 5.74% p.a. approx.**	**Closing amortised cost (Rs.)**
31st March 2021	2,00,00,000	11,48,000	2,11,48,000
31st March 2022	2,11,48,000	12,13,895	2,23,61,895
31st March 2023	2,23,61,895	12,83,573	2,36,45,468
31st March 2024	2,36,45,468	13,54,532	2,50,00,000

An entity may apply the requirements in Ind AS 109 and Ind AS 20 retrospectively to any government loan originated before the date of transition to Ind AS, provided that the information needed to do so had been obtained at the time of initially accounting for that loan.

The accounting treatment is to be done as per above guidance and the advice which the company has been provided is not in line with the requirements of Ind AS 101.

Thanks ….

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IND AS – 28 INVESTMENTS IN JOINT VENTURE & ASSOCIATES

CHAPTER - 33

Question 1 : Nov 2018 – RTP

As provided in Ind- AS 111 - Joint Arrangements - this is a joint arrangement because two or more parties have joint control of the property under a contractual arrangement. The arrangement will be regarded as a joint operation because Alpha Ltd. and Gama Ltd. have rights to the assets and obligations for the liabilities of this joint arrangement. This means that the company and the other investor will each recognise 50% of the cost of constructing the asset in property, plant and equipment.

The borrowing cost incurred on constructing the property should under the principles of Ind AS 23 'Borrowing Costs', be included as part of the cost of the asset for the period of construction. In this case, the relevant borrowing cost to be included is Rs.50,00,000 (Rs.10,00,00,000 x 10% x 6/12).

The total cost of the asset is Rs.40,50,00,000 (Rs.40,00,00,000 + Rs.50,00,000) Rs.20,25,00,000 crores is included in the property, plant and equipment of Alpha Ltd. and the same amount in the property, plant and equipment of Gama Ltd.

The depreciation charge for the year ended 31 March 2018 will therefore be Rs.1,01,25,000 (Rs.40,50,00,000 x 1/20 x 6/12) Rs.50,62,500 will be charged in the statement of profit or loss of the company and the same amount in the statement of profit or loss of Gama Ltd.

The other costs relating to the arrangement in the current year totalling Rs.54,00,000 (finance cost for the second half year of Rs.50,00,000 plus maintenance costs of Rs.4,00,000) will be charged to the statement of profit or loss of Alpha Ltd. and Gama Ltd. in equal proportions- Rs.27,00,000 each.

Solution :

As provided in Ind- AS 111 - Joint Arrangements - this is a joint arrangement because two or more parties have joint control of the property under a contractual arrangement. The arrangement will be regarded as a joint operation because Alpha Ltd. and Gama Ltd. have rights to the assets and obligations for the liabilities of this joint arrangement. This means that the company and the other investor will each recognise 50% of the cost of constructing the asset in property, plant and equipment.

The borrowing cost incurred on constructing the property should under the principles of Ind AS 23 'Borrowing Costs', be included as part of the cost of the asset for the period of construction. In this case, the relevant borrowing cost to be included is Rs.50,00,000 (Rs.10,00,00,000 x 10% x 6/12).

The total cost of the asset is Rs.40,50,00,000 (Rs.40,00,00,000 + Rs.50,00,000) Rs.20,25,00,000 crores is included in the property, plant and equipment of Alpha Ltd. and the same amount in the property, plant and equipment of Gama Ltd.
The depreciation charge for the year ended 31 March 2018 will therefore be Rs.1,01,25,000 (Rs.40,50,00,000 x 1/20 x 6/12) Rs.50,62,500 will be charged in the statement of profit or loss of the company and the same amount in the statement of profit or loss of Gama Ltd.
The other costs relating to the arrangement in the current year totalling Rs.54,00,000 (finance cost for the second half year of Rs.50,00,000 plus maintenance costs of Rs.4,00,000) will be charged to the statement of profit or loss of Alpha Ltd. and Gama Ltd. in equal proportions-Rs.27,00,000 each.

Question 2 : May 2020 – RTP

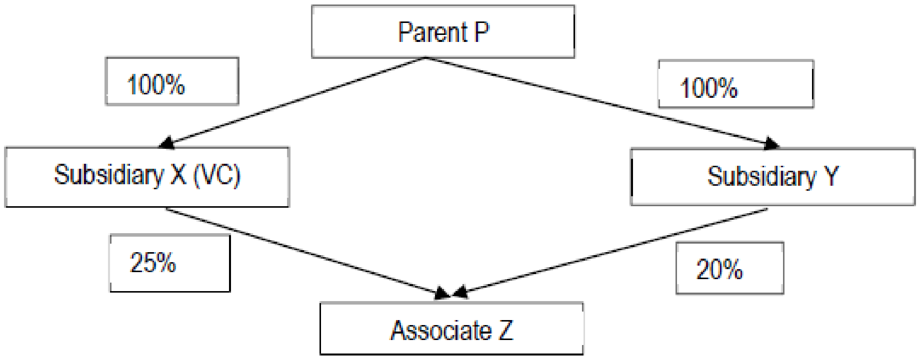
An entity P (parent) has two wholly-owned subsidiaries - X and Y, each of which has an ownership interest in an 'associate', entity Z. Subsidiary X is a venture capital organisation. Neither of the investments held in associate Z by subsidiaries X and Y is held for trading. Subsidiary X and Y account for their investment in associate Z at fair value through profit or loss in accordance with Ind AS 109 and using the equity method in accordance with Ind AS 28 respectively.
How should P account for the investment in associate Z in the following scenarios:
Scenario 1: Where both investments in the associate result in significant influence on a stand-alone basis - Subsidiary X and Y ownership interest in associate Z is 25% and 20% respectively.
Scenario 2: When neither of the investments in the associate results in significant influence on a stand-alone basis, but do provide the parent with significant influence on a combined basis - Subsidiary X and Y ownership interest in associate Z is 10% each.
Scenario 3: When one of the investments in the associate results in significant influence on a stand-alone basis and the other investment in the associate does not result in significant influence on a stand-alone basis - Subsidiary X and Y ownership interest in associate Z is 30% and 10% respectively.
Assume there is significant influence if the entity has 20% or more voting rights.

Solution :

Paragraph 18 of Ind AS 28 states that, "when an investment in an associate or a joint venture is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure investments in those associates and joint ventures at fair value through profit or loss in accordance with Ind AS 109. An entity shall make this election separately for each associate or joint venture, at initial recognition of the associate or joint venture."
Paragraph 19 of Ind AS 28 provides that, "'when an entity has an investment in an associate, a portion of which is held indirectly through a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure that portion of the investment in the associate at fair value through profit or loss in accordance with Ind AS 109 regardless of whether the venture capital organisation has significant influence over that portion of the investment. If the entity makes that election, the entity shall apply the equity method to any remaining portion of its investment in an associate that is not

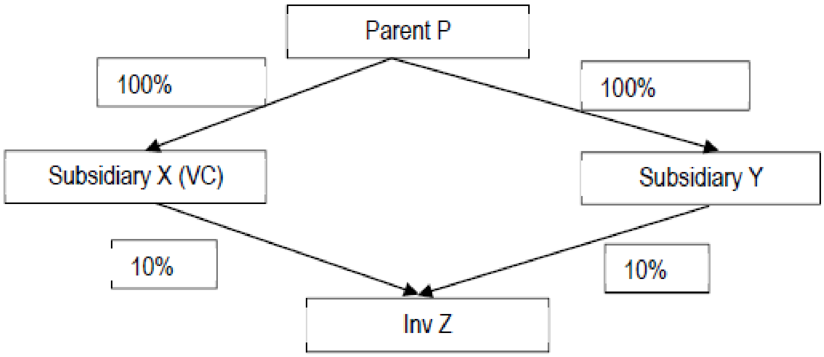
held through a venture capital organisation". Therefore, fair value exemption can be applied partially in such cases.

Scenario 1: Where both investments in the associate result in significant influence on a stand-alone basis.



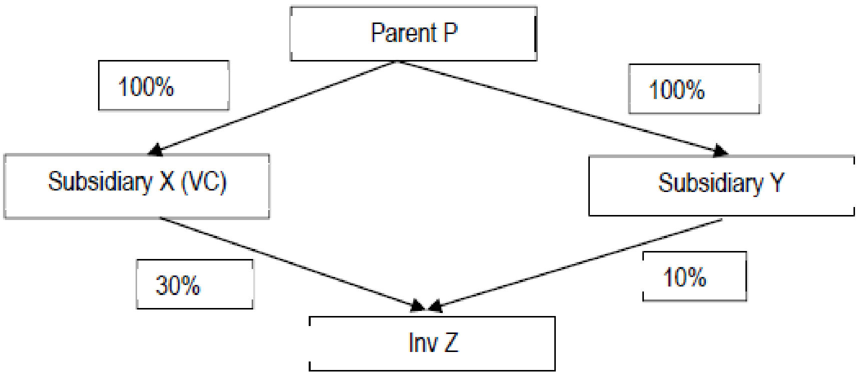
In the present case, in accordance with paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 20% interest held by Y. Under the partial use of fair value exemption, P may elect to measure the 25% interest held by X at fair value through profit or loss.

Scenario 2: When neither of the investments in the associate results in significant influence on a stand-alone basis, but do provide the parent with significant influence on a combined basis.



In the present case in accordance with the paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 10% interest held by Y, even though Y would not have significant influence on a stand-alone basis. Under the partial use of fair value exemption, P may elect to measure the 10% interest held by X at fair value through profit or loss.

Scenario 3: When one of the investments in the associate results in significant influence on a stand-alone basis and the other investment in the associate does not result in significant influence on a stand-alone basis



In the present case, in accordance with paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 10% interest held by Y, even though Y would not have significant influence on a stand-alone basis. Under the partial use of fair value exemption, the P may elect to measure the 30% interest held by X at fair value through profit or loss.

Question 3 : Nov 2020 – RTP

On 1st April 2019, Investor Ltd. acquires 35% interest in another entity, XYZ Ltd. Investor Ltd. determines that it is able to exercise significant influence over XYZ Ltd. Investor Ltd. has paid total consideration of Rs.47,50,000 for acquisition of its interest in XYZ Ltd. At the date of acquisition, the book value of XYZ Ltd.'s net assets was
Rs.90,00,000 and their fair value was Rs.1,10,00,000. Investor Ltd. has determined that the difference of Rs.20,00,000 pertains to an item of property, plant and equipment (PPE) which has remaining useful life of 10 years.
During the year, XYZ Ltd. made a profit of Rs.8,00,000. XYZ Ltd. paid a dividend of Rs.12,00,000 on 31st March, 2020. XYZ Ltd. also holds a long-term investment in equity securities. Under Ind AS, investment is classified as at FVTOCI in accordance with Ind AS 109 and XYZ Ltd. recognized an increase in value of investment by Rs.2,00,000 in OCI during the year. Ignore deferred tax implications, if any.
Calculate the closing balance of Investor Ltd.'s investment in XYZ Ltd. as at 31st March, 2020 as per the relevant Ind AS.

Solution :

Calculation of Investor Ltd.'s investment in XYZ Ltd. under equity method:

	Rs.	Rs.
Acquisition of investment in XYZ Ltd.		
Share in book value of XYZ Ltd.'s net assets (35% of Rs.90,00,000)	31,50,000	
Share in fair valuation of XYZ Ltd.'s net assets [35% of (Rs.1,10,00,000 – Rs.90,00,000)]	7,00,000	
Goodwill on investment in XYZ Ltd. (balancing figure)	9,00,000	
Cost of investment		**47,50,000**
Profit during the year		
Share in the profit reported by XYZ Ltd. (35% of Rs.8,00,000)	2,80,000	
Adjustment to reflect effect of fair valuation [35% of (Rs.20,00,000/10 years)]	-70,000	
Share of profit in XYZ Ltd. recognised in income by Investor Ltd.		**2,10,000**
Long term equity investment		
FVTOCI gain recognised in OCI (35% of Rs.2,00,000)		70,000
Dividend received by Investor Ltd. during the year [35% of Rs.12,00,000]		(4,20,000)
Closing balance of Investor Ltd.'s investment in XYZ Ltd.		**46,10,000**

Question 4 : Nov 2020 – Paper

Entity K is owned by three institutional investors - M Limited, N Limited and C Limited - holding 40%, 40% and 20% equity interest respectively. A contractual arrangement between M Limited and N Limited gives them joint control over the relevant activities of Entity K. It is determined that Entity K is a joint operation (and not a joint venture). C Limited is not a party to the arrangement between M Limited and N Limited. However, like M Limited and N Limited, C Limited also has rights to the assets, and obligations for the liabilities, relating to the joint operation in proportion of its equity interest in Entity K.

Would the manner of accounting to be followed by M Limited and N Limited on the one hand and C Limited on the other in respect of their respective interests in Entity K be the same or different? You are required to explain in light of the relevant provisions in the relevant standard in this regard.

OR

An entity negotiates with major airlines to purchase tickets at reduced rates compared with the price of tickets sold directly by the airlines to the public. The entity agrees to buy a specific number of tickets and will pay for those tickets even if it is not able to resell them. The reduced rate paid by the entity for each ticket purchased is negotiated and agreed in advance. The entity determines the prices at which the airline tickets will be sold to its customers. The entity sells the tickets and collects the consideration from customers when the tickets are sold; therefore, there is no credit risk to the entity.

The entity also assists the customers in resolving complaints with the service provided by airlines. However, each airline is responsible for fulfilling obligations associated with the ticket, including remedies to a customer for dissatisfaction with the service.

Determine whether the entity is a principal or an agent with suitable explanation in light with the provisions given in the relevant standard.

Solution :

Ind AS 111 states that a joint operator shall recognise in relation to its interest in a joint operation:

(a) its assets, including its share of any assets held jointly;
(b) its liabilities, including its share of any liabilities incurred jointly;
(c) its revenue from the sale of its share of the output arising from the joint operation;
(d) its share of the revenue from the sale of the output by the joint operation; and
(e) its expenses, including its share of any expenses incurred jointly.

A joint operator shall account for the assets, liabilities, revenues and expenses relating to its interest in a joint operation in accordance with the Ind AS applicable to the particular assets, liabilities, revenues and expenses.

Further, Ind AS 111 states that a party that participates in, but does not have joint control of a joint operation shall also account for its interest in the arrangement in accordance with above provisions of the standard, if that party has rights to the assets, and obligations for the liabilities, relating to the joint operation.

In the given case, all three investors (M Limited, N Limited and C Limited) share in the assets and liabilities of the joint operation in proportion of their respective equity interest. Accordingly, both

M Limited and N Limited (which have joint control) and C Limited (which does not have joint control but participates) shall recognise their interest in joint operation as per above guidance while accounting for their respective interests in Entity K in their respective separate financial statements as well as in the consolidated financial statements.

OR

To determine whether the entity's performance obligation is to provide the specified goods or services itself (i.e. the entity is a principal) or to arrange for another party to provide those goods or services (i.e. the entity is an agent), the entity considers the nature of its promise as per Ind AS 115.

The entity determines that its promise is to provide the customer with a ticket, which provides the right to fly on the specified flight or another flight if the specified flight is changed or cancelled. The entity considers the following indicators for assessment as principal or agent under the contract with the customers:

(a) the entity is primarily responsible for fulfilling the contract, which is providing the right to fly. However, the entity is not responsible for providing the flight itself, which will be provided by the airline.

(b) the entity has inventory risk for the tickets because they are purchased before they are sold to the entity's customers and the entity is exposed to any loss as a result of not being able to sell the tickets for more than the entity's cost.

(c) the entity has discretion in setting the sales prices for tickets to its customers.

The entity concludes that its promise is to provide a ticket (i.e. a right to fly) to the customer. On the basis of the indicators, the entity concludes that it controls the ticket before it is transferred to the customer. Thus, the entity concludes that it is a principal in the transaction and recognises revenue in the gross amount of consideration to which it is entitled in exchange for the tickets transferred.

Question 5 : Jan 2021 – Paper

On 1st April 2019, Big Limited acquired a 35 interest in Dig Limited and achieved a significant influence. The cost of the investment was Rs.3,00,000. Dig Limited has net assets of Rs.5,50,000 as on 1st April 2019. The fair value of those net assets is Rs.6,50,000, since the fair value of property, plant and equipment is Rs.1,00,000 higher than its book value. This property, plant and equipment have a remaining useful life of 8 years. For the financial year 2019-2020, Dig Limited earned a profit (after tax) of Rs.1,00,000 and paid a dividend of Rs.11,000 out of these profits. Dig Ltd. has also recognized the loss of Rs.15,000, that arose from re-measurement of defined benefit directly in 'Other Comprehensive Income'.

Calculate Big Ltd.'s interest in Dig Ltd. as at the year ended 31st March 2020 under the relevant method.

Solution :

Calculation of Big Ltd.'s interest in Dig Ltd at the year ended 31st March, 2020 as per Equity method:

	Amount (Rs.)
Cost of investment (35%)	3,00,000
Share in profit after adjustment (Refer Working Note)	30,625
Dividend received by Big Ltd from Dig Ltd (35% x Rs.11,000)	(3,850)
Big Ltd.'s share of loss in OCI w.r.t Dig Ltd .'s loss from remeasurement of defined benefit liability (35% x Rs.15,000)	(5,250)
Big Ltd.'s interest in Dig Ltd at the end of the year	3,21,525

Working Note:

Computation of Share in profit after adjustment

	Amount (Rs.)
Big Ltd.'s share of Dig Ltd.'s after tax profit (35% x Rs.1,00,000)	35,000
Less: Big Ltd.'s share of depreciation based on fair value (35% x Rs.12,500)	(4,375)
Share in profit after adjustment	30,625

Thanks ....

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IND AS – 111
JOINT ARRANGEMENTS

CHAPTER - 34

Question 1 : May 2020 – RTP

AB Limited and BC Limited establish a joint arrangement through a separate vehicle PQR, but the legal form of the separate vehicle does not confer separation between the parties and the separate vehicle itself. Thus, both the parties have rights to the assets and obligations for the liabilities of PQR. As neither the contractual terms nor the other facts and circumstances indicate otherwise, it is concluded that the arrangement is a joint operation and not a joint venture.

Both the parties own 50% each of the equity interest in PQR. However, the contractual terms of the joint arrangement state that AB Limited has the rights to all of Building No. 1 owned by PQR and the obligation to pay all of the debt owed by PQR to a lender XYZ. AB Limited and BC Limited have rights to all other assets in PQR, and obligations for all other liabilities of PQR in proportion of their equity interests (i.e. 50% each).

PQR's summarized balance sheet is as follows:

(Rs. in crore)

	Amount
Building 1	240
Building 2	200
Cash	40
Total Assets	**480**
Equity	140
Debt owed to XYZ	240
Employee benefit plan obligation	100
Total Liabilities	**480**

How would AB Limited present its interest in PQR in its financial statements?

Solution :

Ind AS 111 states that "a joint operator shall recognise in relation to its interest in a joint operation:

(a) its assets, including its share of any assets held jointly;

(b) its liabilities, including its share of any liabilities incurred jointly;

(c) its revenue from the sale of its share of the output arising from the joint operation;

(d) its share of the revenue from the sale of the output by the joint operation; and

(e) its expenses, including its share of any expenses incurred jointly."

The rights and obligations, as specified in the contractual arrangement, that an entity has with respect to the assets, liabilities, revenue and expenses relating to a joint operation might differ

from its ownership interest in the joint operation. Thus a joint operator needs to recognise its interest in the assets, liabilities, revenue and expenses of the joint
operation on the basis (bases) specified in the contractual arrangement, rather than in proportion of its ownership interest in the joint operation.

Thus, AB Limited would record the following in its financial statements, to account for its rights to the assets of PQR and its obligations for the liabilities of PQR.

	Rs. in crore
Assets	
Cash	20
Building 1*	240
Building 2	100
Liabilities	
Debt owned to XYZ (third party)**	240
Employees benefit plan obligation	50

* Since AB Limited has the rights to all of Building No. 1, it records the amount in its entirety.

** AB Limited has obligation for the debt owed by PQR to XYZ in its entirety.

Question 2 : May 2022 – RTP

Identify the type of joint arrangements in each of the following scenarios:

(i) X Ltd and Y Ltd, manufacturing similar type of mobile phones, form a joint arrangement to manufacture and sell mobile phones. Under the terms of the arrangement, both X Ltd and Y Ltd are to use their own assets to manufacture the mobile phones and both are responsible for liabilities related to their respective manufacture. The arrangement also lays down the distribution revenues from the sale of the mobile phones and expenses incurred thereof. X Ltd however has exclusive control over the marketing and distribution functions and does not require the consent of Y Ltd in this aspect. No separate entity is created for the arrangement.

(ii) Continuing with (i) above, what would be the classification of the joint arrangement if X Ltd and Y Ltd both jointly control all the relevant activities of the Joint arrangement including the marketing and the distribution functions?

(iii) What would be the classification of the joint arrangement if under the terms of the arrangement, a separate entity is created to manufacture the mobile phones.

(iv) Continuing with (iii) above, the joint arrangement is a means of manufacturing mobile phones on a common platform but the output of the joint arrangement is purchased by both X Ltd and Y Ltd in the ratio of 50:50. The joint arrangement cannot sell output to third parties. The price of the output sold to X Ltd and Y Ltd is set by both the parties to the arrangement to cover the production costs and other administrative costs of the joint arrangement entity.

(v) Would your answer in (iv) above be different if X Ltd and Y Ltd sold their respective share of output to third parties?

(vi) Assume that in (iv) above, the contractual terms of the arrangement were modified so that the joint arrangement entity is not obliged to sell the output to X Ltd and Y Ltd but was able to sell the output to third parties.

Solution :

For a joint arrangement to be either a *joint operation* or *joint venture*, it depends on whether the parties to the joint arrangement have rights to the assets and obligations for liabilities (will be a joint operation) OR whether the parties to the joint arrangement have rights to the net assets of the arrangement (will be joint venture).

(i) In order to fit into the definition of a joint arrangement, the parties to the joint arrangement should have joint control over the arrangement. In the given case, decisions relating to relevant activities, ie, marketing and distribution, are solely controlled by X Ltd and such decisions do not require the consent of Y Ltd. Hence, the joint control test is not satisfied in this arrangement and the arrangement does not fit into the definition of a joint arrangement in accordance with the Standard.

(ii) Where X Ltd and Y Ltd both jointly control all the relevant activities of the arrangement and since no separate entity is formed for the arrangement, the joint arrangement is in the nature of a *joint operation.*

(iii) Where under a joint arrangement, a separate vehicle is formed to give effect to the joint arrangement, then the joint arrangement can either be a *joint operation* or a *joint venture.* Hence in the given case, if:

  (a) The contractual terms of the joint arrangement, give both X Ltd and Y Ltd rights to the assets and obligations for the liabilities relating to the arrangement, and the rights to the corresponding revenues and obligations for the corresponding expenses, *then the joint arrangement will be in the nature of a joint operation.*

  (b) The contractual terms of the joint arrangement, give both X Ltd and Y Ltd. rights to the net assets of the arrangement, *then the joint arrangement will be in the nature of a joint venture.*

(iv) Where the rights to assets and liabilities to obligations are not clear from the contractual arrangement, then other facts and circumstances also need to be considered to determine whether the joint arrangement is a joint operation or a joint venture.

When the provision of the activities of the joint venture is primarily to produce output and the output is available / distributed only to the parties to the joint arrangement in some pre-determined ratio, then this indicates that the parties have substantially all the economic benefits of the assets of the arrangement. The only source of cash flows to the joint arrangement is receipts from parties through their purchases of the output and the parties also have a liability to fund the settlement of liabilities of the separate entity. Such an arrangement indicates that the joint arrangement is in the nature of *a joint operation.*

In the given case, the output of the joint arrangement is exclusively used by X Ltd. and Y Ltd. and the joint arrangement is not allowed to sell the output to outside parties. Hence, the joint arrangement between X Ltd. and Y Ltd. is in the nature of *a joint operation.*

(v) It makes no difference whether the output of the joint arrangement is exclusively for use by the parties to the joint arrangement or the parties to the arrangement sold their share of the output to third parties.
Hence, even if X Ltd. and Y Ltd. sold their respective share of output to third parties, the fact still remains that the joint arrangement cannot sell output directly to third parties. Hence, the joint arrangement will still be deemed to be in the nature of *a joint operation*.

(vi) Where the terms of the contractual arrangement enable the separate entity to sell the output to third parties, this would result in the separate entity assuming demand, inventory and credit risks. Such facts and circumstances would indicate that the arrangement is a joint venture.

Thanks ….

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IND AS – 27 SEPARATE FINANCIAL STATEMENTS

CHAPTER - 35

Question 1 : Nov 2020 – RTP

A company, AB Ltd. holds investments in subsidiaries and associates. In its separate financial statements, AB Ltd. wants to elect to account its investments in subsidiaries at cost and the investments in associates as financial assets at fair value through profit or loss (FVTPL) in accordance with Ind AS 109, Financial Instruments. Whether AB Limited can carry investments in subsidiaries at cost and investments in associates in accordance with Ind AS 109 in its separate financial statements?

Solution :

Ind AS 27, Separate Financial Statements inter-alia provides that, when an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109, Financial Instruments in its separate financial statements. Further, the entity shall apply the same accounting for each category of investments.

It may be noted that although the 'category' is used in number of Standards, it is not defined in any of the Ind AS. It seems that subsidiaries, associates and joint ventures would qualify as separate categories. Thus, the same accounting policies are applied for each category of investments - i.e. each of subsidiaries, associates and joint ventures. However, paragraph 10 of Ind AS 27 should not be read to mean that, in all circumstances, all investments in associates are one 'category' of investment and all investments in joint ventures or an associate are one 'category' of investment. These categories can be further divided into sub-categories provided the sub-category can be defined clearly and objectively and results in information that is relevant and reliable. For example, an investment entity parent can have investment entity subsidiary (at fair value through profit or loss) and non-investment entity subsidiary (whose main purpose is to provide services that relate to the investment entity's investment activities) as separate categories in its separate financial statements. In the present case, investment in subsidiaries and associates are considered to be different categories of investments. Further, Ind AS 27 requires to account for the investment in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109 for each category of Investment. Thus, AB Limited can carry its investments in subsidiaries at cost and its investments in associates as financial assets in accordance with Ind AS 109 in its separate financial statements.

Question 2 : Nov 2020 – Paper

Entity H holds a 20% equity interest in Entity S (an associate) that in turn has a 100% equity interest in Entity T. Entity S recognised net assets relating to Entity T of Rs. 10,000 in its consolidated financial statements. Entity S sells 20% of its interest in Entity T to a third party (a non-controlling shareholder) for Rs. 3,000 and recognises this transaction as an equity transaction in accordance with the provisions of Ind AS 110, resulting in a credit in Entity S's equity of Rs.1,000.

The financial statements of Entity H and Entity S are summarised as follows before and after the transaction:

Before

H's consolidated financial statements

Assets	**(Rs.)**	**Liabilities**	**(Rs.)**
Investment in S	2,000	Equity	2,000
Total	2,000	Total	2,000

S's consolidated financial statements

Assets	**(Rs.)**	**Liabilities**	**(Rs.)**
Assets (from T)	10,000	Equity	10,000
Total	10,000	Total	10,000

The financial statements of S after the transaction are summarised below:

After

S's consolidated financial statements

Assets	**(Rs.)**	**Liabilities**		**(Rs.)**
Assets (from T)	10,000	Equity	10,000	
Cash	3,000	Equity transaction Impact with non- controlling interest	1,000	
		Equity attributable to owners		11,000
		Non-controlling interest		2,000
Total	**13,000**	**Total**		**13,000**

Although Entity H did not participate in the transaction, Entity H's share of net assets in Entity S increased as a result of the sale of S's 20% interest in T. Effectively, H's share in S's net assets is now Rs. 2,200 (20% of Rs. 11,000) i.e., Rs. 200 in addition to its previous share.

How this equity transaction that is recognised in the financial statements of Entity S reflected in the consolidated financial statements of Entity H that uses the equity method to account for its investment in Entity S?

Solution :

Ind AS 28 defines the equity method as "a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition change in the investor's share of the investee's net assets. The investor's profit or loss includes its share of the investee's profit or loss and the investor's other comprehensive income includes its share of the investee's other comprehensive income."

Ind AS 28, states, inter alia, that when an associate or joint venture has subsidiaries, associates or joint ventures, the profit or loss, other comprehensive income, and net assets taken into account in applying the equity method are those recognised in the associate's or joint venture's financial statements (including the associate's or joint venture's share of the profit or loss, other comprehensive income and net assets of its associates and joint ventures), after any adjustments necessary to give effect to uniform accounting policies.

The change of interest in the net assets / equity of the associate as a result of the investee's equity transaction is reflected in the investor's financial statements as 'share of other changes in equity of investee' (in the statement of changes in equity) instead of gain in Statement of profit and loss, since it reflects the post-acquisition change in the net assets of the investee as per the provisions of Ind AS 28 and also faithfully reflects the investor's share of the associate's transaction as presented in the associate's consolidated financial statements.

Thus, in the given case, Entity H recognises Rs. 200 as change in other equity instead of in statement of profit and loss and maintains the same classification as of its associate, Entity S, i.e., a direct credit to equity as in its consolidated financial statements.

Question 3 : Nov 2021 – RTP

A company, AB Ltd. holds investments in subsidiaries and associates. In its separate financial statements, AB Ltd. wants to elect to account its investments in subsidiaries at cost and the investments in associates as financial assets at fair value through profit or loss (FVTPL) in accordance with Ind AS 109, Financial Instruments.

Whether AB Limited can carry investments in subsidiaries at cost and investments in associates in accordance with Ind AS 109 in its separate financial statements?

Solution :

Paragraph 10 of Ind AS 27 'Separate Financial Statements' *inter-alia* provides that, when an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109 'Financial Instruments' in its separate financial statements. Further, the entity shall apply the same accounting for each category of investments.

It may be noted that although the 'category' is used in number of Standards, it is not defined in any of the Ind AS. It seems that subsidiaries, associates and joint ventures would qualify as separate categories. Thus, the same accounting policies are applied for each category of investments - i.e. each of subsidiaries, associates and joint ventures. However, paragraph 10 of Ind AS 27 should not be read to mean that, in all circumstances, all investments in associates are one 'category' of investment and all investments in joint ventures or an associate are one 'category' of investment. These categories can be further divided into sub-categories provided the sub-category can be defined clearly and objectively and results in information that is relevant and reliable. For example, an investment entity parent can have investment entity subsidiary (at fair value through profit or loss) and non-investment entity subsidiary (whose main purpose is to provide services that relate to the investment entity's investment activities) as separate categories in its separate financial statements.

In the present case, investment in subsidiaries and associates are considered to be different categories of investments. Further, Ind AS 27 requires to account for the investment in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109 for each category of Investment. Thus, AB Limited can carry its investment in subsidiaries at cost and its investments in associates as financial assets in accordance with Ind AS 109 in its separate financial statements.

Thanks ....

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ABOUT THE AUTHOR

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