



VOLUME - II

CA FINAL

FINANCIAL REPORTING

# COMPILER 4.0

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PYP | RTP | MTP



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# IND AS – 12 INCOME TAXES

## CHAPTER - 15

### 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	<u>2</u>	<u>6</u>
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	
<b>4)</b>	<b>Tax reconciliation in absolute No.</b>			
	Tax Expenses (100 × 25%)			25
	<b>Add :</b> Expenses (Donation) of deductible for tax (8 × 25%)			2
	<b>Less :</b> Deferred tax (difference of Depreciation)			<u>(1)</u>
	Current Tax			26
<b>5)</b>	<b>Tax Rate Reconciliation</b>			
	Application Tax Rate			25%
	Expenses not deductible for tax			<u>2%</u>
	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	$Rs.70,000 \times 0.45$	31,500
Previously recognised as Income	$Rs.1,30,000 \times 0.45$	<u>58,500</u>
		<u>90,000</u>
Deferred tax liability		
Previously recognized as expense	$Rs.1,50,000 \times 0.45$	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 OCI and Rs.1,000 is charged to P&L.

**An alternative method of calculation is :**

		Rs.
DTA shown in OCI	$Rs.70,000 \times (0.45 - 0.40)$	3,500
DTA shown in Profit or Loss	$Rs.1,30,000 \times (0.45-0.40)$	6,500
DTL shown in Profit or Loss	$Rs.1,50,000 \times (0.45 -0.40)$	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
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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
<u>Assets</u>		
Land & Building	500	700
Property, Plant & Equipment	200	270
Inventory	100	80
Accounts Receivable	150	150
Cash & Cash Equivalent	<u>130</u>	<u>130</u>
	<u>1080</u>	<u>1330</u>
<u>Liability</u>		
Account payable	(160)	(160)
Retirement benefit ob.	<u>—</u>	<u>(100)</u>

Net Assets	920	1070
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Difference (1070 – 920) = 150

Differed tax = 150 × 40% = 60

## 2) Calculating of goodwill

Purchase consideration	1500
Less : Fair value of Net Assets (1070 – 60)	<u>1010</u>
Goodwill	<u>490</u>

### 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.

	<b>Rs.</b>
Estimated annual income exclusive of estimated capital gain (16,50,000 – 4,00,000) (A)	<u>12,50,000</u>
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%	<u>48,000</u>	1,04,000
Quarter IV - Rs. 3,00,000 x 28%		<u>84,000</u>
		<u>3,98,000</u>

### 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	<u>80</u>	<u>85</u>	<u>(5)</u>
	<u>910</u>	<u>955</u>	<u>(45)</u>
10% Debentures	<u>200</u>	<u>200</u>	
	<u>710</u>	<u>755</u>	
Consideration Paid	<u>760</u>	<u>760</u>	
Goodwill	<u>50</u>	<u>5</u>	<u>45</u>

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 deferred 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.

**Question 9 : Nov 2022 – RTP**

Following is the summarized statement of profit and loss of EARTH Limited as per Ind AS for the year ended 31st March 20X1:

Particulars	Rs. in Crore
Revenue from operations	1,160.00
Other income	56.00
Total Income (A)	1,216.00
Purchase of stock-in-trade	40.00
Changes in inventories of stock-in-trade	6.00
Employee benefits expense	116.00
Finance costs	130.00
Depreciation and amortization expense	30.00
Other expenses	300.00
Total Expenses (B)	622.00
Profit Before Tax (A-B)	594.00
Current tax	165.40
Deferred tax	1.50
Tax Expenses	166.90
Profit after Tax	427.10

Additional information:

- Corporate income tax rate applicable to EARTH Limited is 30%.
- Other income includes long-term capital gains of Rs. 10 crore which are taxable at the rate of 10%.

- Other expenses include the following items which are not deductible for income tax purposes:

Item	Rs. in Crore
Penalties	1.00
Impairment of goodwill	44.00
Corporate Social Responsibility expense	6.00

- Other expenses include research and development (R & D) expenditure of Rs. 8 crore in respect of which a 200% weighted deduction is available under income tax laws.
- Other income includes dividends of Rs. 4 crore, which is exempt from tax.
- Profit before tax of Rs. 594 crore includes (i) agriculture income of Rs. 55 crore which is exempt from tax; and (ii) profit of Rs. 60 crore earned in the USA on which EARTH Limited is required to pay tax at the rate of 20%.
- Depreciation as per income tax laws is Rs. 25.0 crore.

During review of the financial statements of EARTH Limited, the CFO multiplied profit before tax by the income tax rate and arrived at Rs. 178.2 crore as the tax expense (Rs. 594 crore x 30% = Rs. 178.2 crore). However, actual income tax expense appearing in the summarized statement of profit and loss is Rs. 166.9 crore.

The CFO has sought your help in reconciling the difference between the two tax expense amounts. Prepare a reconciliation containing the disclosure as required under the relevant Ind AS.

**Solution :**

**Reconciliation of income tax expense and current tax as per accounting profit  
for the year ended 31st March, 20X1**

Particulars		Rs. in crore
Accounting profit		<u>594.00</u>
Tax at the applicable tax rate of 30%		178.20
Tax effect of expenses that are not deductible in determining taxable profits:		
Penalties (1.00 x 30%)	0.30	
Impairment of goodwill (44.00 x 30%)	13.20	
Corporate social responsibility expense (6.00 x 30%)	<u>1.80</u>	15.30
Tax effect of expenses that are deductible in determining taxable profits:		
Research and development expenses (8.00 x 30%)		(2.40)
Tax effect of income that are exempted in determining taxable profits:		
Dividend income (Exempt) (4.00 x 30%)	1.20	
Agriculture income (Exempt) (55.00 x 30%)	<u>16.50</u>	(17.70)
Tax effect of income on which different tax rates are used for determining taxable profits:		

Differential income tax on long term capital gain [10.00 x (30% - 10%)]	2.00	
Foreign income in USA [60.00 x (30%-20%)]	<u>6.00</u>	<u>-8.00</u>
Income tax expense (Current) reported in the Statement of Profit and Loss for the current year		<u>165.40</u>

#### Reconciliation of deferred tax:

Particulars	Rs. in crore
Particulars	
Deferred tax in relation to depreciation and amortization [(30 – 25) x 30%]	1.50
Tax expense (deferred) reported in the Statement of Profit or Loss for the current year	1.50

#### Question 10 : Nov 2022 – Paper

Following is the summarized statement of profit and loss of New Age Ltd. as per Ind AS for the year ended 31.03.2022 :

Particulars	Rs. In lakhs
Revenue from operations	1,450.00
Other income	70.00
<b>(A) Total Income</b>	<b>1,520.00</b>
Purchase of stock in trade	50.00
Change in inventories of stock in trade	20.00
Employee benefit expenses	145.00
Finance costs	180.00
Other expenses	375.00
<b>(B) Total expenses</b>	<b>770.00</b>
<b>(C) Profit before tax (A – B)</b>	<b>750.00</b>
<b>(D) Current tax expense</b>	<b>211.65</b>
<b>(E) Profit after tax (C – D)</b>	<b>538.35</b>

#### Additional Information :

- (1) Consider that Income tax rate applicable to New Age Ltd. in India is 30%.
- (2) Other Expenses include the following expenses which are not deductible for income tax purpose :
  - (i) Penalties Rs.1.50 lakh
  - (ii) Donations Rs.55.00 lakhs
  - (iii) Impairment of goodwill Rs.7.00 lakhs
- (3) Other expenses also include expenditure on Scientific Research amounting to Rs.10 lakhs in respect of which a 150% weighted deduction is available under income tax laws.
- (4) Other income includes :
  - (i) Dividend of Rs.5 lakhs, which is exempt from tax.

- (ii) Long term capital gains of Rs.12 lakhs which are taxable at the rate of 10%.
- (5) Profit before tax of Rs.750 lakhs includes :
- (i) Agriculture income of Rs.65 lakhs which is exempt from tax; and
- (ii) Profit of Rs.75 lakhs earned in USA on which New Age Ltd. has paid tax at rate of 20%.

During review of financial statements of New Age Ltd., the CFO multiplied profit before tax by the income tax rate and arrived at Rs.225 lakhs as the tax expenses. However, the actual income tax expenses appearing in the summarized statement of profit and loss is Rs.211.65 lakhs. You are required to help the CFO of the company in reconciling the difference between the two tax expense amount.

**Solution :**

**Reconciliation of income tax expense and current tax as per accounting profit  
for the year ended 31st March 2022**

Particulars		Rs. in lakhs
Accounting profit		<u>750.00</u>
Tax at the applicable tax rate of 30%		225.00
Tax effect of expenses that are not deductible in determining taxable profits:		
Penalties (1.5 x 30%)	0.45	
Impairment of goodwill (7 x 30%)	2.10	
Donations (55 x 30%)	<u>16.50</u>	19.05
Tax effect of expenses that are deductible in determining taxable profits:		
Expenditure on scientific research (10.00 x 50% x 30%)		-1.50
Tax effect of income that are exempted in determining taxable profits:		
Dividend income (Exempt) (5.00 x 30%)	1.50	
Agriculture income (Exempt) (65.00 x 30%)	<u>19.50</u>	(21.00)
Tax effect of income on which different tax rates are used for determining taxable profits:		
Differential income tax on long term capital gain [12.00 x (30% - 10%)]	2.40	
Foreign income in USA [75.00 x (30% - 20%)]	<u>7.50</u>	<u>(9.90)</u>
Income tax expense (Current) reported in the Statement of Profit and Loss for the current year		<u>211.65</u>

**Question 11 : Nov 2023 – RTP**

On 1st April, 20X1, an entity paying tax at 30% acquired a non-tax-deductible office building for Rs. 1,00,000 in circumstances in which Ind AS 12 prohibits recognition of the deferred tax liability

associated with the temporary difference of Rs. 1,00,000. The building is depreciated over 10 years at Rs. 10,000 per year to a residual value of zero. The entity's financial year ends on 31st March.

On 1st April, 20X2, the carrying amount of the building is Rs. 90,000, and it is revalued upwards by Rs. 45,000 to its current market value of Rs. 1,35,000. There is no change to the estimated residual value of zero, or to the useful life of the building after revaluation.

Determine the carrying amount, depreciation for the year ended 31st March, 20X3 and defer tax thereafter till the useful life of the building. Further analyse the treatment and impact of defer tax since 31st March, 20X3 till the useful life of the building.

**Solution :**

Since there is no change to the estimated residual value of zero, or to the useful life of the building after revaluation, at the end of the 2nd year i.e. 31st March 20X3, the building will be depreciated over the next 9 years at Rs. 15,000 per year.

Following the revaluation, the temporary difference associated with the building is Rs. 1,35,000. Of this amount, only Rs. 90,000 arose on initial recognition, since Rs. 10,000 of the original temporary difference of Rs. 1,00,000 arising on initial recognition of the asset has been eliminated through depreciation of the asset. The carrying amount (which equals the temporary difference, since the tax base is zero) and depreciation during the year ended 31st March, 20X3 and thereafter may then be analysed as follows:

Year	Carrying amount a	Tax base b	Gross temporary difference (c = a-b)	Unrecognised temporary difference d	Recognised temporary difference (e = c-d)	Deferred tax liability f = e @ 30%
0	1,00,000	-	1,00,000	1,00,000	-	-
1	90,000	-	90,000	90,000	-	-
Reval	1,35,000	-	1,35,000	90,000	45,000	13,500
2	1,20,000	-	1,20,000	80,000	40,000	12,000
3	1,05,000	-	1,05,000	70,000	35,000	10,500
4	90,000	-	90,000	60,000	30,000	9,000
5	75,000	-	75,000	50,000	25,000	7,500
6	60,000	-	60,000	40,000	20,000	6,000
7	45,000	-	45,000	30,000	15,000	4,500
8	30,000	-	30,000	20,000	10,000	3,000
9	15,000	-	15,000	10,000	5,000	1,500
10	-	-	-	-	-	-

**Note:** The depreciation is allocated pro rata to the cost element and revalued element of the total carrying amount.

On 31st March, 20X3, the entity recognises a deferred tax liability based on the temporary difference of Rs. 45,000 arising on the revaluation (i.e., after initial recognition) giving a deferred tax expense of Rs. 13,500 (Rs. 45,000 @ 30%) recognised in Other Comprehensive Income (OCI).

This has the result that the effective tax rate shown in the financial statements for the revaluation is 30% (Rs. 45,000 gain with deferred tax expense of Rs. 13,500).

As can be seen from the table above, as at 31st March, 20X4 (year 3), Rs. 40,000 of the total temporary difference arose after initial recognition. The entity, therefore, provides for deferred tax of Rs. 12,000 (Rs. 40,000 @ 30%), and a deferred tax credit of Rs. 1,500 (the reduction in the liability from Rs. 13,500 to Rs. 12,000) is recognised in profit or loss.

The deferred tax credit can be explained as the tax effect at 30% of the additional Rs. 5,000 depreciation relating to the revalued element of the building.

**Question 12 : May 2024 – RTP**

Joy Ltd. wishes to calculate tax base of its assets and liabilities as on 31st March 20X5. The Balance Sheet has been adjusted by current tax expense.

Summarised Balance Sheet as on 31st March 20X5:

<b>ASSETS</b>	<b>Rs.</b>
<b>Non-current Assets</b>	
Property, Plant and Equipment	12,00,000
Intangible Assets-Product Development Costs	60,000
Investment in Subsidiary - Pall Ltd.	4,40,000
<b>Current Assets</b>	
Trade Investments	2,08,000
Trade Receivables	6,26,000
Inventories	3,04,000
Cash and Cash Equivalentents	<u>1,80,000</u>
<b>TOTAL ASSETS</b>	<b><u>30,18,000</u></b>
<b>EQUITY &amp; LIABILITIES</b>	<b>Rs.</b>
<b>Equity</b>	
Share Capital	12,00,000
Accumulated Profits	7,37,438
Revaluation Surplus	88,000
<b>Non-current Liabilities</b>	
Deferred Income - Government Grants	40,000
Liability for Product Warranty Costs	16,000
Deferred Tax Liability (From 20X3-20X4)	22,162
<b>Current Liabilities</b>	
Trade Payables	7,64,000
Health Care Benefits for Employees	70,000
Current Tax Liability	<u>80,400</u>
<b>TOTAL EQUITY &amp; LIABILITIES</b>	<b><u>30,18,000</u></b>

**Notes:**

- (a) Depreciation expense for the year 20X4-20X5 allowable in accordance with tax laws is Rs. 2,06,000. Accounting depreciation included in operating costs is Rs. 1,70,000. Cost of PPE is Rs. 16,00,000 and Joy Ltd has deducted expenses of Rs. 4,16,000 in its tax returns prior to the financial year 20X4-20X5. Moreover, as on 31st March 20X5, Joy Ltd for the first time revalued its property, plant and equipment to fair value of Rs. 12,00,000 (revaluation surplus = Rs. 88,000).
- (b) In 20X1-20X2, Joy Ltd incurred product development costs of Rs. 1,00,000. These costs were recognized as an asset and being amortized over useful period of 10 years. For tax purposes, Joy Ltd deducted full product development costs in 20X1-20X2.
- (c) Trading investments were acquired in 20X3-20X4 with cost of Rs. 2,30,000. These investments are classified at fair value through profit and loss and thus recognized at their fair value. Fair value adjustments are not tax deductible.
- (d) Bad debt provision amounts to Rs. 1,30,000 and relates to 2 debtors:
- o Debtor A - Rs. 80,000 (receivable originated in 20X2-20X3 and 100% provision was recognized in 20X3-20X4) and
  - o Debtor B - Rs. 50,000 (receivable originated in 20X3-20X4 and 100% provision was recognized in 20X4-20X5).
- Tax law allows deduction of 20% of provision for debtors overdue for more than 1 year, another 30% for debtors overdue for more than 2 years and remaining 50% for debtors overdue for more than 3 years.
- (e) Joy Ltd accounts for inventory obsolescence provision. New provision created in 20X4-20X5 was Rs. 10,800 (total provision: Rs. 18,000). This provision is not tax deductible, as it is a general provision.
- (f) Government grants are not taxable. Government grant received in 20X4-20X5 is appearing in the balance sheet.
- (g) In 20X4-20X5, Joy Ltd made a further provision for product warranty of Rs. 5,000. Such provisions for product warranty costs are not tax deductible until the claims are paid or settled. During the year 20X4-20X5, warranty claims were paid/settled for Rs. 6,200.
- (h) During the year 20X4-20X5, Joy Ltd has introduced health care benefits for employees. The expenses are allowable as deduction in tax only when benefits are paid but in line with Ind AS 19, such liability is recognized in profit or loss when employees provide service. Calculate temporary differences and deferred tax for Joy Ltd as on 31st March 20X5 assuming the tax rate is 32%.

### Solution :

#### Calculation of temporary differences and deferred tax for Joy Ltd. as on 31st March, 20X5

Amount in Rs.

Item	Carrying amount	Tax base	Temporary Difference	Taxable/ Deductible	DTA / (DTL) at 32%
Property Plant & Equipment	12,00,000	9,78,000 (W.N.1)	2,22,000	Taxable	(71,040)
Product Development Costs	60,000	0	60,000	Taxable	(19,200)
Trading investments	2,08,000	2,30,000	(22,000)	Deductible	7,040

Trade receivables	6,26,000	7,06,000 (W.N.2)	(80,000)	Deductible	25,600
Inventories	3,04,000	3,22,000	(18,000)	Deductible	5,760
Deferred income – Government grants	(40,000)	0	(40,000)	Excluded	0
Liability for product warranty costs	(16,000)	0	(16,000)	Deductible	5,120
Health care benefits for employees	(70,000)	0	(70,000)	Deductible	22,400
Total Deferred Tax Asset					65,920
Total Deferred Tax Liability					(90,240)
Net Deferred Tax Liability					(24,320)

**Working Notes:**

**1. Property Plant & Equipment as per tax records**

	Rs.
Cost of PPE	16,00,000
Less: Current tax depreciation	(2,06,000)
Less: Previous year tax depreciation	<u>(4,16,000)</u>
Tax base	<u>9,78,000</u>

**2. Trade receivables – Provision for doubtful debts:**

		Rs.
<b>Calculation of cost for tax records</b>		
Carrying amount		6,26,000
Add back: Bad debt provision		<u>1,30,000</u>
Cost		A
Debtor A – Rs. 80,000 from 20X2-20X3		
>1 year – 20% deducted in 20X3-20X4		16,000
>2 years – 30% deducted in 20X4-20X5		<u>24,000</u>
Already deducted for tax		40,000
Debtor B- Rs. 50,000 from 20X3-20X4		
>1 year – 20% deducted in 20X4-20X5		<u>10,000</u>
Total deduction for tax purpose		B
Tax base of trade receivables		A-B
		<u>-50,000</u>
		<u>7,06,000</u>

**Question 13 : Nov 2024 – RTP**

X Ltd., an Indian company owns a freehold land with carrying value of Rs.10,00,000 which is not depreciated for tax purposes but is indexed for inflation. Indexed value and fair value of such land is Rs. 15,00,000 and Rs.22,00,000 respectively as of the reporting date. What will be the tax base for such freehold land for measurement of deferred tax if:

- (i) X Ltd. intends to sell it as a part of slump sale of business eventually after using it for business purpose
- (ii) X Ltd. intends to sell the land individually and not on a slump sale basis
- (iii) X Ltd. has classified such land as investment property and intends to sell it individually and not on a slump sale basis

- (iv) X Ltd. follows a revaluation model for freehold land and intends to sell it individually and not on a slump sale

As per the applicable tax laws in the jurisdiction, indexation benefit is not available if the freehold land is sold as a part of slump sale of business, but indexation benefit is available if freehold land is sold individually.

### **Solution :**

Paragraphs 51 and 51A of Ind AS 12, state that the measurement of deferred tax liabilities and deferred tax assets shall reflect the tax consequences that would follow from the manner in which the entity expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

In some jurisdictions, the manner in which an entity recovers (settles) the carrying amount of an asset (liability) may affect either or both of:

- (a) the tax rate applicable when the entity recovers (settles) the carrying amount of the asset (liability); and
- (b) the tax base of the asset (liability).

In such cases, an entity measures deferred tax liabilities and deferred tax assets using the tax rate and the tax base that are consistent with the expected manner of recovery or settlement.”

The expectation of the entity at the end of the reporting period with regard to the manner of recovery or settlement of its assets and liabilities will require exercise of judgement based on evaluation of facts and circumstances in each case. It may be relevant to consider that there is substance to management’s expectation of the entity being able to recover the asset through slump sale or otherwise.

Depending on the facts and circumstances, it is generally assumed that the Company will act in the most economically advantageous way.

If a non-depreciable asset is measured using the revaluation model, then an entity is required to measure the DTA/DTL considering the tax consequences of recovering the carrying amount through sale.

Accordingly, based on assumption around supporting facts and circumstances to support management expectation around recovery or settlement, following will be the tax base for computing the deferred tax assets/ liability, in the given case:

- (i) X Ltd. intends to sell it as slump sale eventually after using it for business purpose  
If it is concluded based on evaluation of facts that the freehold land will be sold through slump sale, then the tax base of the land will be the same as the carrying amount of the land, as indexation benefit is not available in case of slump sale and hence there will not be any temporary difference.
- (ii) X Ltd. intends to sell the land individually and not on a slump sale basis  
In the given scenario, the company intends to sell the land individually and not on a slump sale such that the company would get indexation benefit.  
Thus, book base of land, i.e. carrying amount of freehold land in the balance sheet is Rs. 10,00,000. As per paragraph 51A of Ind AS 12, the tax base (amount that will be deductible for tax purposes against any taxable economic benefits that will flow to the entity when it recovers the carrying amount of the asset) is the indexed valued of Rs. 15,00,000 since the

company intends to sell the land individually and not on slump sale and thus get indexation benefit. Deferred tax assets will be set up, subject to recoverability, on a deductible tax difference of Rs. 5,00,000.

- (iii) X Ltd. has classified such land as investment property and intends to sell it individually and not on a slump sale

Paragraph 56 of Ind AS 40, *Investment property*, requires that after initial recognition, an entity shall measure all of its investment properties in accordance with the requirement for cost model as per Ind AS 16, other than those that meet the criteria to be classified as held for sale in accordance with Ind AS 105, *Non-current Assets Held for Sale and Discontinued Operations*. Ind AS 40 does not allow fair value model. Accordingly, freehold land classified as investment property will be measured at cost.

Thus, book base of land, i.e. carrying amount of freehold land in the balance sheet is Rs. 10,00,000. The Company intends to sell the land individually and not on a slump sale and thus get indexation benefit. Hence, as per paragraph 51A of Ind AS 12, the tax base (amount that will be deductible for tax purposes against any taxable economic benefits that will flow to the entity when it recovers the carrying amount of the asset) is the indexed valued of Rs. 15,00,000. Accordingly, deferred tax assets will be set up, subject to recoverability, on deductible tax difference of Rs. 5,00,000.

- (iv) X Ltd. follows a revaluation model for freehold land and intends to sell it individually and not on a slump sale. If X Ltd. follows a revaluation model, carrying amount of freehold land in the balance sheet would be Rs. 22,00,000. Thus, book base of land is Rs. 22,00,000.

The Company intends to sell the land individually and not on a slump sale and thus get indexation benefit. Hence, as per paragraph 51A of Ind AS 12, the tax base (amount that will be deductible for tax purposes against any taxable economic benefits that will flow to the entity when it recovers the carrying amount of the asset) is the indexed valued of Rs. 15,00,000. Accordingly, deferred tax liability will be set up on taxable temporary difference of Rs. 7,00,000.

As per paragraph 39 of Ind AS 16, 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. Accordingly, the effect of deferred tax liability should also be recognised in other comprehensive income as per paragraph 57 and 61A of Ind AS 12.

#### Question 14 : Nov 2024 – Paper

Mahadev Ltd. has a block of assets with a written down value of Rs.5,00,000 on 1st April, 2022 for tax purposes. The book value of the assets for accounting purposes is also Rs.5,00,000. Depreciation is charged on written down value @ 20% p.a. for both accounting and tax purposes. Of the entire block, assets costing Rs.50,000 on 1st April, 2022 were sold for Rs.1,00,000 on 31st March, 2024. You are required to compute the deferred tax asset/liability assuming tax rate of 35%.

#### Solution :

#### Computation of tax base

Particulars	Carrying amount (Rs.)	Taxbase (Rs.)
Carrying balance on 1st April, 2022	5,00,000	5,00,000
Less: Depreciation	(1,00,000)	(1,00,000)
Balance as on 31st March, 2023	4,00,000	4,00,000
No Temporary difference as on 31st March, 2023	--	--
Less: Carrying amount on the date of disposal to be reversed (accounting record) (Refer W.N.)	(32,000)	
Less: Sale proceeds of the asset to be deducted as per tax records		(1,00,000)
Less: Depreciation		
Accounting depreciation (4,00,000 x 20%)	(80,000)	
Tax depreciation {(4,00,000 - 1,00,000) x 20%}		(60,000)
Balance of the asset as on 31st March, 2024	2,88,000	2,40,000

**Working Note:**

Accounting book value on 31st March, 2024 = Rs. 50,000 - Rs. 10,000 - Rs. 8,000  
= Rs. 32,000

Carrying amount is greater than Tax base which leads to Deferred Tax Liability i.e. Temporary difference = Rs. 2,88,000 - Rs. 2,40,000 = Rs. 48,000

Deferred Tax Liability = Rs. 48,000 x 35% = Rs. 16,800

**Question 15 : May 2025 – RTP**

On 1st January, 20X1, H Ltd. acquired all of the share capital of S Ltd. for Rs. 15,00,000. The book values and the fair values of the identifiable assets and liabilities of S Ltd. at the date of acquisition are set out below, together with their tax bases in S Ltd.'s tax jurisdictions. Any goodwill arising on the acquisitions is not deductible for tax purposes. The tax rates in H Ltd.'s and S Ltd.'s tax jurisdictions are 30% and 40% respectively.

Net assets acquired	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
Total assets	1,230	1,080	1,330
Accounts payable	(160)	(160)	(160)
Retirement benefit obligations	(100)	-	(100)
Net assets before deferred tax liability	970	920	(1070)

Deferred tax liability on differences between book values and tax bases (Rs. 50 @ 40%)	(20)	-	-
Net assets at acquisition	950	920	1,070

Calculate deferred tax arising on acquisition of S Ltd. and goodwill based on the above information.

**Solution :**

**Calculation of deferred tax arising on acquisition of S Ltd. and goodwill**

	Rs.'000	Rs.'000
Fair values of S Ltd.'s identifiable assets and liabilities (excluding deferred tax)		1,070
Less: Tax base		<u>(920)</u>
Temporary difference arising on acquisition		150
Net deferred tax liability arising on acquisition of S Ltd. (Rs. 1,50,000 @ 40%)– replaces book deferred tax		60
Purchases consideration		1,500
Fair values of S Ltd.'s identifiable assets and liabilities (excluding deferred tax)	1,070	
Deferred tax	<u>(60)</u>	<u>1,010</u>
Goodwill arising on acquisition		<u>490</u>

The tax base of the goodwill is nil, so a taxable temporary difference of Rs. 4,90,000 arises on the goodwill. No deferred tax is recognised on the goodwill. The deferred tax on other temporary differences arising on acquisitions is provided at 40% (not 30%), because taxes will be payable or recoverable in S Ltd.'s tax jurisdictions when the temporary differences are reversed.

Thanks ...



# IND AS – 19

## EMPLOYEES BENEFITS

### CHAPTER - 16

#### 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	<u>(80,00,000)</u>
	5,85,00,000
Closing (31/3/2018)	<u>6,80,00,000</u>
Difference (OCI)	<u>95,00,000</u>

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	<u>(75,00,000)</u>
	4,99,00,000
Closing (31/3/2018)	<u>5,60,00,000</u>
Difference (OCI)	<u>61,00,000</u>

**Step 2 : Determination of Net Defined benefit**

Defined benefit obligation	6,80,00,000
– Plan Assets	<u>5,60,00,000</u>
Net Defined benefit liability	<u>1,20,00,000</u>

**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	
	<u>– 26,00,000</u>	4,00,000
Gain on settlement of Redundancies (80 – 75)		<u>(5,00,000)</u>
		<u>76,00,000</u>

**Step 4 : Determination of amount to be recognised in OCI**

Remeasurement of DBO	95,00,000
– Remeasurement of Plan Assets	<u>61,00,000</u>
	<u>34,00,000</u>

**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

$$= \text{Rs.21,00,000} + \text{Rs.3,00,000} = \text{Rs.24,00,000}$$

Additional Profit = Expected Profit – Actual Profit

$$= \text{Rs.24,00,000} - \text{Rs.17,00,000} = \text{Rs.7,00,000}$$

$$\text{Maximum bid price} = \frac{\text{Additional Profit}}{\text{Rate of Return on Investment}} = \frac{7,00,000}{14\%} \times 100 = \text{Rs.50,00,000}$$

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:**

	<b>Rs.</b>
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	<u>68,000</u>
	<u>(1,65,750)</u>

**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	<u>(1.00)</u>
Expected Rate of Return	<u>10.25</u>

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
<b>Expected Return on Plan Assets</b>	<b>1,17,500</b>

#### 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
<b>Actual Return on Plan Assets</b>	<b>2,00,000</b>

#### Computation of Net Actuarial Gain

Particulars	Rs.
Actual Return on Plan Assets	2,00,000
Less: Expected Return on Plan Assets	<u>(1,17,500)</u>
Actuarial Gain on Plan Assets	82,500
Less: Actuarial Loss on Defined Benefit Obligation (given)	(6,000)
<b>Net Actuarial Gain to be recognized in 'Other Comprehensive Income'</b>	<b>76,500</b>

### Question 7 : May 2022 – Paper

On 1<sup>st</sup> April, 2021, the fair value of the assets of Raj 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 31<sup>st</sup> March, 2022 the plan received contributions from Raj Ltd. amounting to Rs.4,75,000 and paid out benefits of Rs.2,65,000. The current service cost for the financial year ending 31<sup>st</sup> March, 2022 is Rs.5,10,000. An interest rate of 5% per annum is to be applied to the plan assets and obligations. The fair value of the plan assets at 31<sup>st</sup> March, 2022 was Rs.23,90,000, 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 recognized 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, 2021	20,40,000	21,25,000
Interest @ 5%	1,02,000	1,06,250
Current service cost		5,10,000
Contributions received	4,75,000	-
Benefits paid	(2,65,000)	(2,65,000)
Return on gain (assets) (balancing figure)	38,000	-
Actuarial Loss (balancing figure)	-	2,43,750
Closing balance as at 31st March, 2022	23,90,000	27,20,000

**In the Statement of Profit and Loss, followings will be recognised:**

	<b>Rs.</b>
Current service cost	5,10,000
Net interest on net defined liability (Rs. 1,06,250 – Rs. 1,02,000)	4,250

**In Other Comprehensive Income, following Defined Benefits re-measurements will be recognised :**

	<b>Rs.</b>
Loss on defined benefit obligation	(2,43,750)
Gain on plan assets	<u>38,000</u>

(2,05,750)

In the Balance Sheet, following Net Defined Liability will be recognised :

	Rs.
Net defined liability (Rs. 27,20,000 – Rs. 23,90,000)	3,30,000

**Question 8 : May 2023 – RTP**

From the following particulars, compute the net defined benefit liability and expense to be recognized in Profit and Loss account.

(Rs. In lakhs)

Particulars	Defined benefit obligation		Plan Assets	
	31st Dec. 20X2	31st Dec. 20X1	31st Dec. 20X2	31st Dec. 20X1
Balance at the beginning of the year	63.25	47.08	21.80	14.65
Current service cost	5.84	4.97	-	-
Interest cost	4.27	3.56	-	-
Changes in demographic assumptions	0.62	1.86	-	-
Changes in financial assumptions	3.58	1.93	-	-
Experience variance	(2.49)	4.46	-	-
Benefits paid	-	(0.61)	-	(0.61)
Investment income	-	-	1.47	1.12
Employers' contribution	-	-	8.00	7.00
Return on plan assets	-	-	2.12	(0.35)

**Solution :**

**Computation of defined benefit liability and expenses to be charged to Statement of Profit and Loss:**

Particulars	Defined benefit obligation		Plan Assets	
	31st Dec. 20X2	31st Dec. 20X1	31st Dec. 20X2	31st Dec. 20X1
Balance at the beginning of the year	63.25	47.08	21.80*	14.65
Current service cost	5.84	4.97	-	-
Interest cost	4.27	3.56	-	-
Changes in demographic assumptions	0.62	1.86	-	-
Changes in financial assumptions	3.58	1.93	-	-
Experience variance	(2.49)	4.46	-	-
Benefits paid	-	(0.61)	-	(0.61)
Investment income	-	-	1.47	1.12
Employers' contribution	-	-	8.00	7.00
Return on plan assets	-	-	<u>2.12</u>	(0.35)
Balance at the end of year	<u>75.07</u>	<u>63.25</u>	2.12	<u>21.81*</u>

\*Difference is due to approximation.

In the **BALANCE SHEET**, the following will be recognised:

Net defined liability to be recognised for the period ending 31st December, 20X1:  
= Rs. 41.44 lakhs (Rs. 63.25 lakhs – Rs. 21.81 lakhs)

Net defined liability to be recognised for the period ending 31st December, 20X2:  
= Rs. 41.68 lakhs (Rs. 75.07 lakhs – Rs. 33.39 lakhs)

In the **STATEMENT OF PROFIT AND LOSS**, the following will be recognised:

Particulars	Defined benefit obligation (Rs. In lakhs)		Plan Assets (Rs. In lakhs)	
	31st Dec. 20X2	31st Dec. 20X1	31st Dec. 20X2	31st Dec. 20X1
Current service cost	5.84	4.97	-	-
Interest cost	4.27	3.56	-	-
Investment income	-	-	(1.47)	(1.12)
Total	<u>10.11</u>	<u>8.53</u>	<u>(1.47)</u>	<u>(1.12)</u>

Expense to be recognised in the Statement of Profit and Loss for the period ending 31st December, 20X1 = Rs. 7.41 lakhs (Rs. 8.53 lakhs – Rs. 1.12 lakhs)

Expense to be recognised in the Statement of Profit and Loss for the period ending 31st December, 20X2 = Rs. 8.64 lakhs (Rs. 10.11 lakhs – Rs. 1.47 lakhs).

### Question 9 : Nov 2023 – RTP

Arunachalam Ltd. operates a Defined Retirement Benefits Plan for its current and former employees. Given the large size of the company, it engaged a firm of Actuaries for advice on the Contribution Levels and overall Liabilities of the Plan to pay benefits. Following details are given:

- On 1st April, 20X1, the actuarial valuation of the present value of the defined benefit obligation was Rs. 15 crores. On the same date, the fair value of the assets of the Defined Benefit Plan was Rs. 13 crores. On 1st April, 20X1, the annual market yield based on Government Bonds was 5%.
- During the year ended 31st March, 20X2, Arunachalam made contributions of Rs. 1.75 crore into the Plan and the Plan paid out benefits of Rs. 1.05 crore to retired members. Assume that both these payments were made on 31st March, 20X2.
- The Actuarial Firm estimated that the current service cost for the year ended 31st March, 20X2 would be Rs. 1.55 crores. On 28th February, 20X2, the rules of the Plan were amended with retrospective effect which led to an increase in the present value of the defined benefit obligation by Rs. 37.5 lakhs from that date.
- During the year ended 31st March, 20X2, Arunachalam was in negotiation with employee representatives regarding planned redundancies. These negotiations were completed shortly before the year end and the redundancy packages were agreed. The impact of these redundancies was to reduce the present value of the defined benefit obligation by Rs. 2 crores. Before 31st March, 20X2, Arunachalam made payments of Rs. 1.875 crores to

the employees affected by the redundancies in compensation for a curtailment of their benefits. These payments were made out of the assets of the Retirement Benefits Plan.

- (e) On 31st March, 20X2, the present value of the defined benefit obligation was Rs. 17 crores and the fair value of the assets of the Defined Benefit Plan was Rs. 14 crores.

Discuss how the above will be accounted in the books of Arunachalam Ltd. for the year 20X1-20X2. Also give the extracts of financial statements affected due to above transactions.

**Solution :**

**1. Extract of Balance Sheet (Net Amount in the Balance Sheet) (Rs. in lakhs)**

	<b>31.3.20X2</b>	<b>1.4.20X1</b>
PV of Defined Benefit Obligation (given)	(1,700.00)	(1,500.00)
FV of Plan Assets (given)	<u>1,400</u>	<u>1,300</u>
Net Defined Benefit Liability (under Long-term Provision)	<u>(300.00)</u>	<u>(200.00)</u>

**2. Extract of Statement of Profit and Loss**

	<b>(Rs. in lakhs)</b>
Current service cost (given)	155.00
Past service cost (given)	37.50
Gain on settlement (Rs. 200 lakhs – Rs. 187.50 lakhs)	(12.50)
Net interest on net defined benefit liability [Rs. 75 lakhs – Rs. 65 lakhs]	<u>10.00</u>
<b>Total to Statement of Profit and Loss</b>	<b><u>190.00</u></b>

**3. Extract of Other Comprehensive Income (Remeasurements)**

	<b>(Rs. in lakhs)</b>
Actuarial loss on defined benefit obligation (W.N.1)	(237.50)
Return on plan assets other than expected return (W.N.2)	<u>152.50</u>
<b>Total</b>	<b><u>(85.00)</u></b>

**Working Notes:**

**1. Defined Benefit Obligation Account**

Particulars	Rs. in lakhs	Particulars	Rs. in lakhs
To Plan Assets (benefits paid)	105.00	By Balance b/f (given) [balance as on 1.4.20X1]	1,500.00
To Curtailment and Settlement	200.00	By Current Service Cost	155.00
To Balance c/d (given) [balance as on 31.3.20X2]	<u>1,700.00</u>	By Interest Cost [5% on Opening balance]	75.00
		By Past service cost	37.50

		By Actuarial Loss (balancing figure)	237.50
	<b><u>2,005.00</u></b>		<b><u>2,005.00</u></b>

2.

**Plan Assets Account**

Particulars	Rs. in lakhs	Particulars	Rs. in lakhs
To Balance b/f (given) [balance as on 1.4.20X1]	1,300.00	By Defined Benefit Obligation [benefits paid]	105.00
To Expected Return [5% on Opening balance]	65.00	By Payments on curtailment and settlement	187.50
To Bank (contributions paid)	175.00	By Balance c/d (given) [balance as on 31.3.20X2]	1,400.00
To Actuarial Gain (balancing figure)	<u>152.50</u>		
	<b><u>1,692.50</u></b>		<b><u>1,692.50</u></b>

The above Defined Benefit Obligation Account and Plan Assets Account can alternatively be presented in a statement form as follows:

Defined Benefit Obligation		Plan Assets	
Particulars	Rs. in lakhs	Particulars	Rs. in lakhs
PV of Obligation b/f.	1,500.00	FV of Plan Assets b/f.	1,300
Interest Cost [Rs. 1,500 x 5%	75.00	Interest Income [Rs. 1,300 x 5%]	65.00
Current Service Cost	155.00	Contribution during 20X1-20X2	175.00
Benefits paid during 20X1-20X2	(105.00)	Benefits paid during 20X1-20X2	(105.00)
Plan Curtailment and Settlement	(200.00)	Payment towards settlement	(187.50)
Past Service Cost	37.50	Remeasurement Gain (balancing figure)	<u>152.50</u>
Remeasurement Loss (balancing figure)	<u>237.50</u>		
PV of Obligation c/f.	<b><u>1,700.00</u></b>	FV of Plan Assets c/f.	<b><u>1,400.00</u></b>

**Question 10 : Nov 2023 – RTP**

On 1st January, 20X2, the directors of Johansen Ltd. decided to terminate production at one of the company's divisions. This decision was publicly announced on 31st January, 20X2. The activities of the division were gradually reduced from 1st April, 20X2 and closure is expected to be complete by 30th September, 20X2.

At 31st January, 20X2, the directors prepared the following estimates of the financial implications of the closure:

- (i) Redundancy costs were initially estimated at Rs. 2 million. Further expenditure of Rs. 8,00,000 will be necessary to retrain employees who will be affected by the closure but remained with Johansen Ltd. in different divisions. This retraining will begin in early July 20X2. Latest estimates are that redundancy costs will be Rs. 1.9 million, with retraining costs of Rs. 8,50,000.
- (ii) Plant and equipment having an expected carrying value at 31st March, 20X2 of Rs. 8 million will have a recoverable amount Rs. 1.5 million. These estimates remain valid.
- (iii) The division is under contract to supply goods to a customer for the next three years at a pre-determined price. It will be necessary to pay compensation of Rs. 6,00,000 to this customer. The compensation actually paid, on 31st May, 20X2, was Rs. 5,50,000.
- (iv) The division will make operating losses of Rs. 3,00,000 per month in the first three months of 20X2-20X3 and Rs. 2,00,000 per month in the next three months of 20X2-20X3. This estimate proved accurate for April, 20X2 and May, 20X2.
- (v) The division operates from a leasehold premise. The lease is a non-cancellable operating lease with an unexpired term of five years from 31st March, 20X2. The annual lease rentals (payable on 31st March in arrears) are Rs. 1.5 million. The landlord is not prepared to discuss an early termination payment.

Following the closure of the division it is estimated that Johansen Ltd. would be able to sub-let the property from 1st October, 20X2.

Johansen Ltd. could expect to receive a rental of Rs. 3,00,000 for the six-month period from 1st October, 20X2 to 31st March, 20X3 and then annual rentals of Rs. 5,00,000 for each period ending 31st March, 20X4 to 31st March, 20X7. All rentals will be received in arrears.

Any discounting calculations should be performed using a discount rate of 5% per annum. You are given the following data for discounting at 5% per annum:

Present value of Rs. 1 received at the end of year 1 = Rs. 0.95

Present value of Rs. 1 received at the end of year 1–2 inclusive = Rs. 1.86

Present value of Rs. 1 received at the end of year 1–3 inclusive = Rs. 2.72

Present value of Rs. 1 received at the end of year 1–4 inclusive = Rs. 3.54

Present value of Rs. 1 received at the end of year 1–5 inclusive = Rs. 4.32

Compute the amounts that will be included in the Statement of Profit and Loss for the year ended 31st March, 20X2 in respect of the decision to close the division of Johansen Ltd.

### **Solution :**

As per Ind AS 37 'Provisions, Contingent Liabilities and Contingent Assets', closure of a division is a restructuring exercise. Ind AS 37 states that a constructive obligation to proceed with the restructuring arises when at the reporting date the entity has:

- Commenced activities connected with the restructuring; or
- Made a public announcement of the main features of the restructuring to those affected by it. In this case a public announcement has been made and so a provision will be necessary at 31st March, 20X2.

This will result in the following charges to the Statement of Profit and Loss:

Estimate of redundancy costs of Rs. 1.9 million is the best estimate of the expenditure at the date the financial statements are authorized for issue. Changes in estimates after the reporting date

are taken into account for this purpose as an adjusting event after the reporting date. No charge is necessary for the retraining costs as these are not incurred in 20X1-20X2 and cannot form part of a restructuring provision as they are related to the ongoing activities of the entity.

Impairment of plant and equipment of Rs. 6.5 million is although not strictly part of the restructuring provision the decision to restructure before the year-end means that related assets need to be reviewed for impairment. In this case the recoverable amount of the plant and equipment is only Rs. 1.5 million. As per Ind AS 36 'Impairment of Assets', property, plant and equipment should be written down to this amount, resulting in a charge of Rs. 6.5 million to the income statement.

For compensation for breach of contract of Rs. 0.55 million, same principle applies here as applied to the redundancy costs.

No charge is recognized in 20X1-20X2 with respect to future operating losses of 20X2-20X3. Future operating losses relate to future events and provisions are made only for the consequences of past events.

Ind AS 37 states that an onerous contract is one for which the expected cost of fulfilling the contract exceeds the benefits expected from the contract. Provision is made for the lower of the expected net cost of fulfilling the contract and the cost of early termination (not available in this case).

### Question 11 : May 2024 – Paper

Based on the advice from actuaries regarding contribution levels and overall liabilities of the defined benefit retirement plan to pay benefits to past and present employees, the Accountant Mr. Krishna of TUNA Limited provides the following information:

- (i) On 1st April, 2023, the actuaries of the company advised that the present value of the defined obligation was Rs. 2,88,420. On the same date, the fair value of the assets of the defined benefit plan was Rs. 2,49,670 and the annual market yield on government bonds was 8%.
- (ii) During the year ended 31st March, 2024, TUNA Limited made contributions of Rs. 33,650 into the plan and the plan paid out benefits of Rs. 20,160 to retired members. Both these payments were made on 31st March 2024
- (iii) The actuaries advised that the current service cost for the year ended 31st March, 2024 was Rs. 29,760. On 28th February 2024, the rules of the plan were amended with retrospective effect. These amendments meant that the present value of the defined obligation was increased by Rs. 7,280 from that date.
- (iv) During the year ended 31st March, 2024, TUNA Limited 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. 38,390. Before 31st March, 2024, TUNA Limited made payments of Rs. 36,270 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.

- (v) On 31st March, 2024, the actuaries advised that the present value of the defined benefit obligation was Rs. 3,26,480. On the same date, the fair value of the assets of the defined benefits plan were Rs. 2,68,340.

Examine and present how the above events would be reported in the financial statements of TUNA Ltd. for the year ended 31st March, 2024 as per Ind AS. Please note that the finance cost is to be computed on the opening balance.

**Solution :**

**Remeasurement of gain or loss**

	Rs.
Liability at the start of the year (Rs. 2,88,420 -Rs. 2,49,670)	38,750
Current service cost	29,760
Past service cost	7,280
Net finance cost	3,100
Gain on settlement	(2,120)
Contributions to plan	(33,650)
Benefits paid	NIL
Remeasurement loss (balancing figure)	<u>15,020</u>
Liability at the end of the year (Rs. 3,26,480 - Rs. 2,68,340)	<u>58,140</u>

On 31st March 2024, Tuna Ltd. will report a net pension liability in the balance sheet. The amount of the liability will be Rs. 58,140 (Rs. 3,26,480 – Rs. 2,68,340).

For the year ended 31st March 2024, Tuna Ltd. will report the current service cost as an operating cost in the statement of profit or loss. The amount reported will be Rs. 29,760. The same treatment applies to the past service cost of Rs. 7,280.

For the year ended 31st March 2024, Tuna Ltd. will report a finance cost in profit or loss at the start of the year of Rs. 38,750 (Rs. 2,88,420 - Rs. 2,49,670).

The amount of the finance cost will be Rs. 3,100 (Rs. 38,750 x 8%).

The redundancy programme represents the partial settlement of the curtailment of a defined benefit obligation. The gain on settlement of Rs. 2,120 (Rs. 38,390 – Rs. 36,270) will be reported in the statement of profit and loss.

Other movements in the net pension liability will be reported as remeasurement gains or losses in other comprehensive income.

For the year ended 31st March, 2024, the remeasurement loss will be Rs. 15,020 (Refer above table).

**In the Statement of Profit and loss, the following will be recognised:**

	Rs.
Current service cost	29,760
Net interest on net defined liability (Rs. 23,074 – Rs. 19,974)	3,100
Gain on settlement (Rs. 38,390 – 36,270)	2,120

**Defined benefit re-measurements recognised in Other Comprehensive Income:**

	Rs.
Loss on defined benefit obligation	(36,496)
Gain on plan assets	<u>21,476</u>
Gain on remeasurement	(15,020)

**In the Balance Sheet, the following will be recognised:**

	Rs.
Net defined benefit liability (Rs. 3,26,480 – Rs. 2,68,340)	58,140

**Question 12 : Sept 2025 – Paper**

XYZ Ltd. operates a defined retirement benefits plan on behalf of current and former employees. XYZ Ltd. receives advice from actuaries regarding contribution levels and overall liabilities of the plan to pay benefits. On 1st April, 2024, the actuaries advised that the present value of the defined benefit obligation was Rs. 90 lakhs. On the same day, the fair value of the assets of the defined benefit plan was Rs. 78 lakhs. On 1st April, 2024, the annual market yield on high quality corporate bonds\* was 6%. During the year ended 31st March, 2025, XYZ Ltd. made contributions of Rs. 10,50,000 into the plan and the plan paid out benefits of Rs. 6,30,000 to retired members. Assume that both these payments were made on 31st March, 2025. The actuaries advised that the current service cost for the year ended 31st March, 2025 was Rs. 9,30,000.

On 28th February, 2025, the rules of the plan were amended with retrospective effect. These amendments meant that the present value of defined benefit obligation was increased by Rs. 2,25,000 from that date. During the year ended 31st March, 2025, XYZ Ltd. was in negotiation with employees' representatives regarding redundancies. The negotiations were completed shortly before the year and the redundancy packages were agreed. The impact of these redundancies was to reduce the present value of the defined benefit obligation by Rs. 12,00,000. Before 31st March, 2025, XYZ Ltd. made payments of Rs. 11,25,000 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, 2025, the actuaries advised that the present value of the defined benefit obligation was Rs. 1,02,00,000. On the same day, the fair value of the assets of the defined benefit plan were Rs. 84,00,000.

You are required to suggest the accounting treatment of the above under the provisions of relevant Ind AS. Please note that the finance cost is to be computed on the opening balance.

**Solution :**

On 31st March 2025, XYZ Ltd. will report a net pension liability in the Balance sheet. The amount of the liability will be Rs. 18,00,000 (Rs. 1,02,00,000 – Rs. 84,00,000).

For the year ended 31st March 2025, XYZ Ltd. will report the current service cost as an operating cost in the statement of profit and loss. The amount reported will be Rs. 9,30,000. The same treatment applies to the past service cost of Rs. 2,25,000.

For the year ended 31st March 2025, XYZ Ltd. will report a finance cost in profit or loss based on the net pension liability at the start of the year of Rs. 12,00,000 (Rs. 90,00,000 – Rs. 78,00,000). The amount of the finance cost will be Rs. 72,000 (Rs. 12,00,000 x 6%).

The redundancy programme represents the partial settlement of the curtailment of a defined benefit obligation. The gain on settlement of Rs. 75,000 (Rs. 12,00,000 – Rs. 11,25,000) will be reported in the statement of profit and loss.

Other movements in the net pension liability will be reported as remeasurement gains or losses in other comprehensive income.

For the year ended 31st March 2025, the remeasurement loss will be Rs. 4,98,000 (Refer W. N.).

**Working Note:**

**Remeasurement of gain or loss**

	Rs.
Liability at the start of the year (Rs. 90,00,000 – Rs. 78,00,000)	12,00,000
Current service cost	9,30,000
Past service cost	2,25,000
Net finance cost	72,000
Gain on settlement	(75,000)
Contributions to plan	(10,50,000)
Remeasurement loss (balancing figure)	4,98,000
Liability at the end of the year (Rs. 1,02,00,000 – Rs. 84,00,000)	18,00,000

**In the Statement of Profit and loss, the following will be recognised:**

	Rs.
Current service cost	9,30,000
Finance Cost (Net interest) on net defined liability [(Rs. 90,00,000 – Rs. 78,00,000) x 6%]	72,000
Past Service Cost	2,25,000
Gain on Settlement	(75,000)

**Defined benefit re-measurements recognised in Other Comprehensive Income:**

	Rs.
Loss on defined benefit obligation	(4,98,000)

**In the Balance sheet, the following will be recognised:**

	Rs.
Defined benefit liability (Rs. 1,02,00,000 – Rs. 84,00,000)	18,00,000

**Note:**

Alternatively, one may work out remeasurement gain/loss by making statement or ledger account of defined benefit obligation and plan assets as follows:

**Statement to Calculate Actuarial Gain or Loss on Defined Benefit Liability and Plan Assets**

	Plan Assets Rs.	Defined Benefit obligation Rs.
Fair Value/Present Value as on 1st April, 2024	78,00,000	90,00,000
Interest @ 6%	4,68,000	5,40,000

Current Service Cost		9,30,000
Past Service Cost		2,25,000
Redundancy benefit	(11,25,000)	(12,00,000)
Contribution received	10,50,000	
Contribution paid	(6,30,000)	(6,30,000)
Return on Plan Assets (Balancing Figure)	8,37,000	
Actuarial loss (Balancing Figure)		<u>13,35,000</u>
Closing Balance as on 31st March, 2025	<u>84,00,000</u>	<u>1,02,00,000</u>

Thanks ....



# IND AS – 20

## ACCOUNTING FOR GOVT. GRANT & DISCLOSURE OF GOVT. ASSISTANCE

### CHAPTER - 17

#### 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 1<sup>st</sup> 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.  $\frac{1}{5}$  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	=	<u>1,20,000</u>
			<u>3,60,000</u>

## 2) Grant to Recognised

Year	Total Cost		
1	$60,000 / 3,60,000 \times 1,30,000$	=	21,667
2	$60,000 / 3,60,000 \times 1,10,000$	=	18,333
3	$60,000 / 3,60,000 \times 1,20,000$	=	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. To Property, Plant & Equipment (Being depreciation provided for the year)	10,00,000	10,00,000
	Deferred grant income Dr. To Profit or Loss (Being deferred income adjusted)	2,16,500	2,16,500

**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. To Profit or Loss (Being deferred income adjusted)	2,16,500	
	Loan account (W.N.1) Dr. Deferred grant income (W.N.2) Dr. Profit or Loss Dr. To Government grant payable (Being refund of government grant)	17,78,112 6,49,500 72,388	25,00,000
	Profit or Loss Dr. To Government grant payable (Being penalty payable to government)	10,00,000	10,00,000

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

**Question 7 : May 2022 – Paper**

Shagun Ltd. received two different grants from State government as per details below :

- (i) A cash grant of Rs.24 lakhs was received on 31<sup>st</sup> March, 2020 towards the skill development of employees over a period of 18 months, starting from 1<sup>st</sup> April, 2020. Actual costs of the skills development program in financial year 2020-2021 was Rs.30 lakhs and in financial year 2021-2022 was Rs.20 lakhs.

State, how this grant should be accounted for in the books of account in financial year 2019-20, 2020-21 and 2021-22?

- (ii) A grant of Rs.10 lakhs receivable over three years (Rs.5 lakhs in financial year 2019-20, Rs.2 lakhs in financial year 2020-21 and Rs.3 lakhs in financial year 2021-22), contingent on developing 5 gardens and maintaining them for three years. The gardens are developed in financial year 2019-20 at a total cost of Rs.6 lakhs, and the maintenance cost for financial year 2019-20 is Rs.12 lakhs, for financial year 2020-21 is Rs.15 lakhs and for financial year 2021-22 is Rs.17 lakhs.

Calculate the grant income and deferred income to be accounted for in the books for financial years 2019-20, 2020-21 and 2021-22.

**Solution :**

- (i) At 31<sup>st</sup> March, 2020 the grant would be recognised as a liability and presented in the balance sheet as a split between current and non-current amounts.

Rs. 16 lakh [(12 months / 18 month) x 24 lakh] is current and would be recognised in profit and loss for the year ended 31<sup>st</sup> March, 2021. The balance amount of Rs. 8 lakh will be shown as non-current.

At the end of the year 2020-2021, there would be a current balance of Rs. 8 lakh (being the non-current balance at the end of year 2019-2020 reclassified as current) in the balance sheet. This would be recognised as profit in the statement of profit and loss for the year ended on 2021-2022.

**Balance Sheet (extracts) as at**

	31st March,2020	31st March,2021	31st March,2022
<b>Current liabilities</b>			

Deferred income	16 lakh	8 lakh	-
<b>Non-current liabilities</b>			
Deferred income	8 lakh	-	-

**Statement of Profit and Loss (extracts) for the year ended**

	31st March, 2021	31st March, 2022
Method 1 (As per para 29 of Ind AS 20)		
Other Income - Government grant received	16 lakh	8 lakh
Training costs	(30 lakh)	(20 lakh)
Method 2 (Alternative) (As per para 29 of Ind AS 20)		
Training costs (30 lakh – 16 lakh)	14 lakh	
Training costs (20 lakh – 8 lakh)		12 lakh

- (ii) The income of Rs. 10 lakh should be recognised over the three-year period to compensate for the related costs. Since the receipt of grant is depending on fulfilling the contract, it is assumed that on initial date certainty to fulfil the conditions by the entity could not be established. Hence, the grant is recognised in the books on receipt basis.

**Calculation of Grant Income and Deferred Income: (Rs. in lakh)**

Year	Maintenance Cost a	Grant Income b = [(10/50) x a]	Grant received during the year c	Deferred Income d
2019-2020	18	3.6	5	(5 – 3.6)1.4
2020-2021	15	3.0	2	[(5 + 2) – (3.6 + 3.0)] 0.4
2021-2022	<u>17</u>	<u>3.4</u>	3	[(5 + 2 + 3) – (3.6+ 3.0 + 3.4)] –
	<u>50</u>	<u>10.0</u>		

Therefore, Grant income to be recognised in Profit & Loss for years 2019-2020, 2020-2021 and 2021-2022 will be Rs. 3.6 lakh, Rs. 3.0 lakh and Rs. 3.4 lakh respectively.

Amount of grant that has not yet been credited to profit & loss i.e. deferred income will be reflected in the balance sheet. Hence, deferred income balance as at year end 2019-2020, 2020-2021 and 2021-2022 will be Rs. 1.4 lakh, Rs. 0.4 lakh and Nil respectively.

**Question 8 : Nov 2022 – RTP**

To encourage entities to expand their operations in a specified development zone, the government provides interest-free loans to fund the purchase of manufacturing equipment. In accordance with the development scheme, an entity receives an interest-free loan of Rs. 5,00,000 from the government for a period of three years. The market rate of interest for similar loans for 3 years is 5% per year.

There are no future performance conditions attached to the interest-free loan.

Discuss how to account for the above loan. Pass necessary journal entries in the entity's books of accounts from year 1 to year 3, as per relevant Ind AS.

**Solution :**

The entity measures the loan on initial recognition at Rs. 4,32,000, which is the present value of the loan (financial liability) — Rs. 5,00,000/(1.05)<sup>3</sup>. Rs. 68,000, the difference between the loan proceeds received Rs. 5,00,000 (the loan's face value) and present value of the loan Rs. 4,32,000, is a government grant and is recognised immediately as there are no specified future performance conditions.

The amount recognised on day one will accrete to Rs. 5,00,000 over the three-year term using the effective interest method.

**Journal Entries**

**On initial recognition :**

		Rs.	Rs.
Cash/Bank (financial asset)	Dr.	5,00,000	
To Loan (financial liability)			4,32,000
To Income (profit or loss)			68,000
(Being interest-free loan recognised at fair value and the receipt of a government grant)			

**At the end of**

**Year 1 :**

		Rs.	Rs.
Finance cost (profit or loss)	Dr.	21,600	
To Loan (financial liability)			21,600
(Being accretion of time value recognised on the financial liability)			

**Year 2 :**

		Rs.	Rs.
Finance cost (profit or loss)	Dr.	22,680	
To Loan (financial liability)			22,680
(Being accretion of time value recognised on the financial liability)			

**Year 3**

		Rs.	Rs.
Finance cost (profit or loss)	Dr.	23,720	
To Loan (financial liability)			23,720
(Being accretion of time value recognised on the financial liability)			

Immediately after all the accretions are recognised, the carrying amount of the loan is equal to its face value of Rs. 5,00,000, which is also the amount payable to the government.

		Rs.	Rs.
Loan (financial liability)	Dr.	5,00,000	
To Cash/Bank			5,00,000
(Being loan repaid to the government)			

**Working Note:**

Calculation of Amortised Cost

Year	Opening balance (A)	Interest at 5% (B) = (A) x 5%	Cash flow (C)	Closing balance (A) + (B) – (C)
1	4,32,000	21,600	–	4,53,600
2	4,53,600	22,680	–	4,76,280
3	4,76,280	23,720*	(5,00,000)	–

\* Difference is due to approximation.

**Question 9 : May 2023 – RTP**

A Ltd. received a government grant of Rs. 10,00,000 to defray expenses for environmental protection. Expected environmental costs to be incurred is Rs. 3,00,000 per annum for the next 5 years. How should A Ltd. present such grant related to income in its financial statements?

**Solution :**

As per paragraph 29 of Ind AS 20 ‘Accounting for Government Grants and Disclosure of Government Assistance’, grants related to income are presented as part of profit or loss, either separately or under a general heading such as ‘Other income’.

Alternatively, they are deducted in reporting the related expense.

In accordance with the above, presentation of grants related to income under both the methods would be as follows:

**Method 1: Credit in the Statement of Profit and Loss**

The entity can recognise the grant as income on a straight-line basis i.e., Rs. 2,00,000 per year in the statement of profit and loss either separately or under the head “Other Income”.

This method considered on the contention that it would be inappropriate to present income and expense items on a net basis and that separation of the grant from the expense would facilitate comparison with other expenses not affected by a grant.

**Method 2: As a deduction in reporting the related expense**

Since the grant relates to environmental expenses incurred/to be incurred by the entity, it can present the grant by reducing the grant amount every year from the related expense i.e., environmental expense of Rs. 1,00,000 (i.e., net expense Rs. 3,00,000 – Rs. 2,00,000).

This method is considered based on the contention that the expenses might well not have been incurred by the entity if the grant had not been available and presentation of the expense without offsetting the grant might therefore be misleading.

The Standard regards both the methods as acceptable for the presentation of grants related to income. However, method 2 may be more appropriate when the company can relate the grant to a specific expenditure.

The Standard also provides that disclosure of the grant may be necessary for a proper understanding of the financial statements. Disclosure of the effect of the grants on any item of income or expense which is required to be separately disclosed is usually appropriate

**Question 10 : Nov 2023 – RTP**

An entity opens a new factory and receives at the beginning of the year a government grant of Rs. 15,000 in respect of capital equipment costing Rs. 1,00,000. It depreciates all plant and machinery at 20% p.a. using straight-line method. Assume that there is reasonable assurance that the conditions attached to the grant will be fulfilled.

For year 1, pass the necessary Journal Entries and show the presentation of the effect of this grant in both Balance Sheet and Statement of Profit and Loss under both methods permitted under paragraph 24 of Ind AS 20?

**Solution :**

Paragraph 24 of Ind AS 20 provides that 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. In accordance with the above, journal entries and presentation of grants related to assets under both the methods are as follows:

**Method 1: When the deferred income account is set-up with the amount of government grant**  
**(I) Journal Entries**

S. No.	Particulars	Nature of Account	Dr./ Cr.	Amount (in Rs.)	Amount (in Rs.)
(i)	Bank A/c  To Government Grant Deferred Income A/c (Being grant received and deferred income set up)	Balance Sheet (Asset) Balance Sheet (Liability)	Dr.  Cr.	15,000	15,000
(ii)	Government Grant Deferred Income A/c To Government Grant Income A/c (Being amortisation of the grant in Profit and loss A/c for the current year)	Balance Sheet (Liability) Income (P/L)	Dr.  Cr.	3,000	3,000
(iii)	Depreciation A/c To Accumulated Depreciation A/c	Expense (P/L) Balance Sheet (Asset)	Dr.  Cr.	20,000	20,000

	(Being depreciation charge of the asset for the current year)				
(iv)	Government Grant Income A/c To Profit and Loss A/c (Being transfer of government grant income to profit and loss A/c)	Income (P/L) P/L	Dr. Cr.	3,000	3,000
(v)	Profit and Loss A/c To Depreciation A/c (Being the charge of depreciation transferred to profit and loss A/c)	P/L Expense (P/L)	Dr. Cr.	20,000	20,000

**(II) Presentation in Balance Sheet and Statement of Profit and Loss**

**Extract of Statement of Profit and Loss**

Particulars	Amount (in Rs.)
<b>Income</b>	
Government grant (Refer W.N.1)	3,000
<b>Expenses</b>	
Depreciation (1,00,000 x 20%)	<u>(20,000)</u>
<b>Net effect on profit and loss</b>	<u>(17,000)</u>

**Presentation in Balance Sheet (Year 1)**

Particulars	Amount (in Rs.)
<b>Non-current Assets</b>	
<b>Property, Plant and Equipment</b>	
Plant & machinery	1,00,000
Accumulated depreciation (1,00,000 × 20%)	<u>(20,000)</u>
	<u>80,000</u>
<b>Non-current liabilities</b>	
Government grant (Refer W.N.1)	9,000
<b>Current liabilities</b>	
Government grant (Refer W.N.1)	3,000

**Working Note 1: Presentation in Balance Sheet as current and non-current liability**

Particulars	Amount (in Rs.)
Portion to be amortised in next 12 months (15,000 x 20%)	3,000 <u>9,000</u>
Portion to be amortised after 12 months	12,000
Total Balance	

**Method 2: When the government grant is deducted from the cost of the asset**

**(I) Journal Entries**

S. No.	Particulars	Nature of Account	Dr./ Cr.	Amount (in Rs.)	Amount (in Rs.)
(i)	Bank A/c	Balance Sheet (Asset)	Dr.	15,000	
	To Government Grant A/c (Being grant received)	Balance Sheet (Liability)	Cr.		15,000
(ii)	Government Grant A/c	Balance Sheet (Liability)	Dr.	15,000	
	To Plant & Machinery A/c (Being cost of asset reduced with grant received)	Balance Sheet (Asset)	Cr.		15,000
(iii)	Depreciation A/c (85,000 x 20%)	Expense (P/L)	Dr.	17,000	
	To Accumulated Depreciation A/c (Being depreciation charge of the asset for the current year)	Balance Sheet (Asset)	Cr.		17,000
(iv)	Profit and Loss A/c	P/L Expense (P/L)	Dr.	17,000	
	To Depreciation A/c (Being the charge of depreciation transferred to profit and loss A/c)		Cr.		17,000

**(II) Presentation in Balance Sheet and Statement of Profit and Loss**  
**Extract of Statement of Profit and Loss (Year 1)**

Particulars	Amount (in Rs.)
Depreciation (Rs. 85,000 x 20%)	(17,000)

**Extract of Balance Sheet (Year 1)**

Particulars	Amount (in Rs.)
<b>Non-current Assets</b>	
<b>Property, Plant and Equipment</b>	
Plant & machinery	
Original cost	1,00,000
Less: Government Grant	<u>(15,000)</u>
Adjusted cost	85,000
Accumulated depreciation	<u>(17,000)</u>
Carrying amount	<u>68,000</u>

**Question 11 : May 2024 – Paper**

ABC Limited has received the following grants for its newly started venture of manufacturing defense equipment in the defense corridor:

- (i) Rs. 25 lakhs received as an incentive for setting up industry in the defense corridor without any further condition.
- (ii) Rs. 50 lakhs received for carrying out research and development in the field of innovation of defense equipment.
- (iii) Besides ABC Limited is awarded a government grant of Rs. 6 lakhs payable over three years (Rs. 4 lakhs in the first year, Rs. 1 lakh each in year 2 and 3), on the condition of creating 10 new jobs and maintaining them for 3 years. The employees are recruited at a cost of Rs. 3,60,000 and the wage bill for the first year is Rs. 8,00,000, rising by Rs. 80,000 in each of the next 2 years. ABC Limited has a reasonable assurance that it will comply with the conditions. attached to them and the grants will be received.

How should ABC Limited account for the above grants including the deferred income if any in its books of account?

**Solution :**

ABC Ltd. should recognise the grants in the following manner:

- (i) Rs. 25 lakhs have been received as an incentive for setting up industry in the defence corridor. This should be recognised in Statement of Profit and Loss immediately as there are no further conditions attached to the grant.
- (ii) Rs. 50 lakhs should be recognised in profit or loss immediately assuming that no further conditions are attached to the grant.

**Alternatively,** in case it is assumed that grant for carrying out research and development in the field of innovation of defense equipment has conditions attached to it, then Rs. 50 lakhs should be recognised in profit or loss on a systematic basis over the periods in which ABC Ltd. recognises as expense the Research and Development costs for which the grant is intended to compensate.

- (iii) Since there is reasonable assurance that the entity will comply with the conditions attaching to them and the grant will be received, the grant of Rs. 6,00,000 should be recognised at the beginning of the first year as receivable and will be compensated for the related costs over three years.

Therefore, grant income to be recognised in the Statement of Profit and Loss for the years 1,2 and 3 would be Rs. 2,32,000, Rs. 1,76,000 and Rs. 1,92,000 respectively. (Refer W.N 1 below)

The amount of grant that has not yet been credited to the statement of profit and loss i.e. deferred income is to be shown on the balance sheet. Hence, deferred income balance as at end of year 1, 2 and 3 are Rs. 3,68,000, Rs. 1,92,000 and Nil respectively. (Refer W.N.1 below)

**Working Note:**

**Calculation of grant income and deferred income:**

Year	Labour Cost Rs.	Grant Income Rs.	Computation of Grant Income Rs.	Deferred Income at the end of the year Rs.	Computation of deferred income at the end of the year Rs.
1	11,60,000	2,32,000	$6,00,000 \times (1,160/3,000)$	3,68,000	$(6,00,000 - 2,32,000)$
2	8,80,000	1,76,000	$6,00,000 \times (880/3,000)$	1,92,000	$(3,68,000 - 1,76,000)$
3	9,60,000	1,92,000	$6,00,000 \times (960/3,000)$	Nil	$(1,92,000 - 1,92,000)$
	30,00,000	6,00,000			

Thanks ....



# IND AS – 21

## THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATE

### CHAPTER - 18

#### 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
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### 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 $(1,36,00,000 \times \frac{1}{4} \times \frac{3}{12})$	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 March, 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	=	<u>2,00,000 FCY</u>
		<u>58,00,000 FCY</u>

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.

$$\begin{aligned} \text{Loan to be converted in INR} &= 58,00,000 \text{ FCY} \times \text{Rs.}2.50/\text{FCY} \\ &= \text{Rs.}1,45,00,000 \end{aligned}$$

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)
	<b>A</b>	<b>B</b>	<b>C</b>	<b>A + B – C</b>
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 cater 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 1<sup>st</sup> 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. 31<sup>st</sup> 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 1<sup>st</sup> February, 2021                      1 Euro = Rs.85

Exchange rate on 31<sup>st</sup> 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 To Sales (Being revenue recorded on initial recognition)	Dr.	850	850
31.3.2021	UB Ltd. A/c To Foreign exchange difference (unrealised) (Being foreign exchange difference recorded at year end)	Dr.	30	30

### Accounting treatment in the books of UB Ltd (Functional currency EURO)

Date			in Euros	in Euros
1.2.2021	Purchase account To SB limited (Being purchased recorded at the date of transaction)	Dr.	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)			

### Question 10 : May 2022 – Paper

GEM Ltd., an Indian company acquired 75% of the share capital of VEW Ltd., on 30<sup>th</sup> September, 2020, an entity registered as company in USA. The functional currency of GEM Ltd. is Rupee and its financial year end on 31<sup>st</sup> March, 2021. The functional currency of VEW Ltd. is USD.

- On 30<sup>th</sup> September, 2020, the fair value of the Net Assets of VEW Ltd. was USD 10 million and the purchase consideration paid was USD 7.8 million. The exchange rate as at 30<sup>th</sup> September, 2020 was Rs.71.5 per USD and 31<sup>st</sup> March, 2021 was Rs.73.5 per USD.
- VEW Ltd. sold goods costing USD 1.9 million to GEM Ltd. for USD 3.1 million during the year ended 31<sup>st</sup> March, 2021. The exchange rate on the date of purchase by GEM Ltd. was Rs.70.5 per USD and on 31<sup>st</sup> March, 2021 was Rs.73.5 per USD. 50% of the goods purchased by GEM Ltd. from VEW Ltd. were unsold as at 31<sup>st</sup> March, 2021.

For (i) determine the value at which the Goodwill should be recognized in the financial statements GEM Ltd as at 31<sup>st</sup> March, 2021.

For (ii) determine the unrealized profit to be eliminated in the preparation of consolidated financial statements of GEM Ltd. for the year ending on 31<sup>st</sup> March, 2021.

### 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.

**When NCI is measured at proportionate share of net assets, the amount of goodwill will be as follows:**

Net identifiable asset	Dr.	USD 10 million	
Goodwill (bal. fig.)	Dr.	USD 0.30 million	
To Bank (Purchase consideration)			USD 7.80 million

To NCI (10 x 25%) USD 2.50 million  
 Thus, goodwill on reporting date in the books of GEM Ltd. would be  
 = USD 0.30 million x Rs. 73.50 = Rs. 22.05 million

**Alternatively, when NCI is measured at fair value, the amount of goodwill will be as follows:**

Net identifiable asset	Dr.	USD 10 million	
Goodwill (bal. fig.)	Dr.	USD 0.40 million	
To Bank (Purchase consideration)			USD 7.80 million
To NCI (7.8/75*25)			USD 2.60 million

Thus, goodwill on reporting date in the books of GEM Ltd. would be  
 = USD 0.40 million x Rs. 73.50 = Rs. 29.40 million

**(ii) Calculation of unrealised profit**

Particulars	USD in million
Sale price of inventory	3.1
Cost of inventory	1.9
Profit earned by VEW Ltd.	1.2
Unrealised profit (1.20 x 50%) [a]	0.6

Exchange rate as on date of purchase of inventory [b] Rs. 70.50 / USD  
 Unrealised profit to be eliminated [a x b] = USD 0.60 million x Rs. 70.50  
 = Rs. 42.30 million

As per para 39 of 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. Hence, the exchange rate on the date of purchase of inventory is taken for calculation of unrealised profit which is to be eliminated while preparation of consolidated financial statements.

**Question 11 : Nov 2023 – RTP**

Infotech Global Ltd. (a stand-alone entity) has a functional currency of USD and needs to translate its financial statements into the presentation currency (INR). The following is the draft financial statements of Infotech Global Ltd. prepared in accordance with its functional currency.

**Balance Sheet**

Particulars	31st March, 20X3	31st March, 20X2
	USD	USD
Property, plant and equipment	50,000	55,000
Trade Receivables	68,500	56,000
Inventory	8,000	5,000
Cash	<u>40,000</u>	<u>35,000</u>
<b>Total assets</b>	<b><u>1,66,500</u></b>	<b><u>1,51,000</u></b>
Share Capital	50,000	50,000

Retained earnings	<u>29,500</u>	<u>18,000</u>
<b>Total Equity</b>	<b><u>79,500</u></b>	<b><u>68,000</u></b>
Trade payables	40,000	38,000
Loan	<u>47,000</u>	<u>45,000</u>
<b>Total liabilities</b>	<b><u>87,000</u></b>	<b><u>83,000</u></b>
<b>Total equity and liabilities</b>	<b><u>1,66,500</u></b>	<b><u>1,51,000</u></b>

**Statement of Profit and Loss**

Particulars	USD
Revenue	1,77,214
Cost of sales	<u>1,13,100</u>
<b>Gross Profit</b>	<b>64,114</b>
Distribution costs	2,400
Administrative expenses	18,000
Other expenses	11,000
Finance costs	<u>12,000</u>
<b>Profit before tax</b>	<b>20,714</b>
Income tax expense	<u>6,214</u>
<b>Profit for the year</b>	<b><u>14,500</u></b>

**Extracts from Statement of Changes in Equity**

Particulars	31st March, 20X3 (USD)
Retained earnings at the beginning of the year	18,000
Profit for the year	14,500
Dividends	<u>(3,000)</u>
Retained earnings at the end of the year	<u>29,500</u>

- Share capital was issued when the exchange rate was USD 1 = INR 70.
- Retained earnings on 1st April, 20X1 was INR 4,00,000.
- At 31st March, 20X2, a cumulative gain of INR 4,92,000 has been recognised in the foreign exchange reserve, which is due to translation of entity's financial statements into INR in the previous years.
- Entity paid a dividend of USD 3,000 when the rate of exchange was USD 1 = INR 73.5
- Profit for the year 20X1-20X2 of USD 8,000, translated in INR at INR 5,72,000.
- Profit for the year 20X2-20X3 of USD 14,500, translated in INR at INR 10,72,985.

For the sake of simplicity, items of income and expense are translated at weighted average monthly rate as there has been no significant exchange rate fluctuation during the entire year and the business of the entity is not cyclical in nature.

Relevant exchange rates are as follows:

- Rate at 31st March, 20X2 USD 1= INR 73
- Rate at 31st March, 20X3 USD 1= INR 75

Prepare financial statements of Infotech Global Ltd. translated from functional currency (USD) to presentation currency (INR)

**Solution :**

As per paragraph 39 of Ind AS 21, all assets and liabilities are translated at the closing exchange rate, which is USD 1 = INR 73 on 31st March, 20X2 and USD 1 = INR 75 on 31st March, 20X3.

In the given case, share capital is translated at the historical rate USD 1 = INR 70. The share capital will not be restated at each year end. It will remain unchanged.

Accordingly, the translated financial statements will be as follows:

**Note 1: Retained earnings at 31st March, 20X3 and 31st March, 20X2:**

Particulars	31st March, 20X3	31st March, 20X2
	INR	INR
Opening retained earnings	9,72,000	4,00,000
Profit for the year	10,72,985	5,72,000
Dividends paid (USD 3,000 x INR 73.5)	<u>(2,20,500)</u>	-
<b>Closing retained earnings</b>	<u>18,24,485</u>	<u>9,72,000</u>

**Balance Sheet**

Particulars	31st March, 20X3			31st March, 20X2		
	USD	Rate	INR	USD	Rate	INR
Property, plant and equipment	50,000	75	37,50,000	55,000	73	40,15,000
Trade Receivables	68,500	75	51,37,500	56,000	73	40,88,000
Inventory	8,000	75	6,00,000	5,000	73	3,65,000
Cash	<u>40,000</u>	75	<u>30,00,000</u>	<u>35,000</u>	73	<u>25,55,000</u>
<b>Total assets</b>	<b>1,66,500</b>		<b>1,24,87,500</b>	<b>1,51,000</b>		<b>1,10,23,000</b>
Share Capital	50,000	70	35,00,000	50,000	70	35,00,000
Retained earnings (Refer note 1)	29,500		18,24,485	18,000		9,72,000
Foreign Exchange reserve (Balancing figure)			<u>6,38,015</u>	-		<u>4,92,000</u>
<b>Total Equity</b>	<b>79,500</b>		<b>59,62,500</b>	<b>68,000</b>		<b>49,64,000</b>
Trade payables	40,000	75	30,00,000	38,000	73	27,74,000
Loan	<u>47,000</u>	75	<u>35,25,000</u>	<u>45,000</u>	73	<u>32,85,000</u>
<b>Total liabilities</b>	<b>87,000</b>		<b>65,25,000</b>	<b>83,000</b>		<b>60,59,000</b>
<b>Total equity and liabilities</b>	<b>1,66,500</b>		<b>1,24,87,500</b>	<b>1,51,000</b>		<b>1,10,23,000</b>

The foreign exchange reserve is the exchange difference resulting from translating income and expense at the average exchange rate and assets and liabilities at the closing rate.

**Other Comprehensive Income**

Exchange differences on translating from USD to INR	INR 1,46,015
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(6,38,015 - 4,92,000)	
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**Statement of Changes in Equity (INR)**

Particulars	Share capital	Retained Earnings	Foreign exchange reserve	Total
Balance at 1st April, 20X2	35,00,000	9,72,000	4,92,000	49,64,000
Dividends	-	(2,20,500)	-	(2,20,500)
Profit for the year	-	10,72,985	-	10,72,985
Exchange difference (transferred to OCI)	-	-	<u>1,46,015</u>	<u>1,46,015</u>
Balance at 31st March, 20X3	<u>35,00,000</u>	<u>18,24,485</u>	<u>6,38,015</u>	<u>59,62,500</u>

**Question 12 : Nov 2023 – Paper**

N Ltd. is engaged in the business of manufacturing of bottles for both, pharmaceutical companies and non-pharmaceutical companies. It has a wholly owned subsidiary, H Ltd., which is engaged in the business of pharmaceuticals. H Ltd. purchases the pharmaceutical bottles from its parent company. The demand of H Ltd. is very high and hence to cater to its shortfall, H Ltd. also purchases the bottles from other companies. Purchases are made at competitive prices.

N Ltd. sold pharmaceuticals bottles to H Ltd. for Euro 24 lakhs on 1st February, 2023. The cost of these bottles was Rs. 1660 lakhs in the books of N Ltd. at the time of sale. As at 31st March, 2023, all these bottles were lying as closing stock in the books of H Limited. Also as at 31st March, 2023, the entire amount against the supply of these bottles was payable by H Ltd.

The functional currency of:

- H Limited is Euro; and
- N Limited is INR.

Following additional information is available

Exchange rate on 1st February, 2023	1 Euro = Rs. 83
Exchange rate on 31st March, 2023	1 Euro = Rs. 85

Provide the journal entries in the books of N Ltd. and H Ltd. on the transaction date(s) as well as 31st March, 2023, if any. Assume net realizable value of stock was always equal to its cost.

**Solution :**

**Accounting treatment in the books of N Ltd. (Functional Currency INR)**

N Ltd. will recognize sales of Rs. 1,992 lakhs (24 lakhs Euro x Rs. 83)

Profit on sale of inventory = Rs. 1,992 lakhs – Rs. 1,660 lakhs = Rs. 332 lakhs.

On balance sheet date, receivable from H Ltd. will be translated at closing rate i.e. 1 Euro = Rs. 85.

Therefore, unrealised forex gain will be recorded in standalone profit and loss of Rs. 48 lakhs [i.e. (Rs. 85 – Rs. 83) x 24 lakhs]

**Journal Entries**

		(Rs. in lakhs)	(Rs. in lakhs)
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1st February, 2023	H Ltd. A/c To Sales (Being revenue recorded on initial recognition)	Dr.	1,992	1,992
31st March, 2023	H Ltd. A/c To Foreign exchange difference (unrealised) (Being foreign exchange difference recorded at year end)	Dr.	48	48

### Accounting treatment in the books of H Ltd. (Functional currency EURO)

H Ltd. will recognize inventory on 1st February, 2023 of Euro 24 lakhs which will also be its closing stock at year end.

#### Journal Entries

			(in Euros)	(in Euros)
1st February, 2023	Purchase To N Ltd.	Dr.	24 lakhs	24 lakhs

### Question 13 : May 2025 – RTP

P Ltd., incorporated in India owns 70% interest in foreign entity, S Ltd. P Ltd. has INR (Rs.) as its functional currency while S Ltd. has US dollars as its functional currency. P Ltd. sells its entire investment in S Ltd. for Rs. 3,200 thousand. The following information is provided:

(Rs. in thousand)

Particulars	S's Total	P's share (70%)	NCI (30%)
Net assets	4,000	2,800	1,200
Foreign currency translation reserve gain	900	630	270

#### Required:

How does an entity account for cumulative translation adjustment (CTA) on disposal of a foreign subsidiary?

#### Solution :

As per paragraphs 48 and 48B of Ind AS 21, on the disposal of a foreign operation, the cumulative amount of the exchange differences relating to that foreign operation, recognised in other comprehensive income and accumulated in the separate component of equity, shall be reclassified from equity to profit or loss (as a reclassification adjustment) when the gain or loss on disposal is recognised (see Ind AS 1, Presentation of Financial Statements).

Further, the standard states that on disposal of a subsidiary that includes a foreign operation, the cumulative amount of the exchange differences relating to that foreign operation that have been attributed to the non-controlling interests shall be derecognised, but shall not be reclassified to profit or loss.

Where the subsidiary is partially owned (that is, where a non-controlling interest exists) and the parent has sold its entire interest, the amount of the CTA that has been allocated to the non-controlling interest is derecognised, but it is not transferred to profit or loss. Derecognition of the

non-controlling interest (that includes the non-controlling interest’s share of CTA) will form part of the journal entry to recognise the gain or loss on disposal of the subsidiary.

In P Ltd.’s consolidated financial statements, the following amounts (Rs. in thousand) have been recognised in relation to its investment in S Ltd.:

- net assets of Rs. 4,000 and associated non-controlling interests of Rs. 1,200;
- foreign exchange gains of Rs. 900 were recognised in other comprehensive income, of which Rs. 270 was attributable to non- controlling interests and is therefore included in the Rs. 1,200 non- controlling interests;
- Rs. 630 of foreign exchange gains have been accumulated in a separate component of equity relating to P Ltd.'s 70% share in S Ltd.

P Ltd. sells its 70% interest in S Ltd. for Rs. 3,200 and records the following amounts:

Cash/Bank A/c	Dr.	3,200	
NCI	Dr.	1,200	
Foreign Currency Translation Reserve (OCI)	Dr.	630	
To Net assets			4,000
To Profit on disposal {630+(3,200-2,800)}			1,030

It can be seen that Rs. 630 of the foreign currency gains previously recognised in OCI, i.e. the amount attributed to P Ltd. is reclassified to profit or loss (profit on disposal) and adjusted from OCI. However, Rs. 270 of such gains attributed to the non-controlling interests is not reclassified to profit or loss and is derecognised as a part of the NCI balance.

#### Question 14 : Sept 2025 – RTP

PQR Ltd. has entered into a fixed price contract on 1st February, 20X2 to provide annual maintenance services worth USD 10,000 which is rendered uniformly throughout the year over a period of two years (1st April, 20X2 – 31st March 20X4) to a foreign customer. As per the terms of the contract, it has received advance payment of USD 3,000 on 1st February, 20X2 and the balance is to be received on 31st March, 20X4.

The entity recognises revenue at the end of every year.

How should the entity account for the said transactions, where the consideration is received in advance?

#### Solution :

If the advance received from the customer is determined to be in the nature of prepayments or progress payments, these are treated as non-monetary items.

Accordingly, in the instant case, PQR Ltd. receives the advance payment of USD 3,000 on 1st February which it translates into its functional currency using the exchange rate on 1st February, 20X2. Applying paragraph 23(b) of Ind AS 21, the entity does not update the translated amount of the nonmonetary liability.

Applying Ind AS 115, Revenue from Contracts with Customers, it recognises revenue over a period of two years.

Since, the entity recognises revenue at the end of the year, revenue of USD 5,000 will be recognised at the end of the first year.

PQR Ltd. has determined that the consideration of USD 3,000 relates to the service it has rendered in the first year. At the end of year 1, the entity is entitled to an unconditional right to USD 2,000 of the remaining consideration.

Accordingly, at the end of the first year, on 31st March 20X3, it recognises revenue of USD 5,000 out of which USD 3,000 will be recognised by derecognising the contract liability and no exchange fluctuation will be involved. Balance of USD 2,000 revenue will be recognised by translating the exchange rate at the date of transaction and a receivable (monetary asset) will be recognised and translated at the exchange rate as at 31st March 20X3.

It will update the translated amount of the receivable until the receivable is settled on 31st March 20X4 and recognises the corresponding gain or loss in profit or loss.

At the end of the second year on 31st March 20X4, it recognises the balance revenue of USD 5,000 using the exchange rate at the date of the transaction.

### Question 15 : Sept 2025 – Paper

Drape Ltd. took a long-term loan of USD 30,000 from an entity registered in U.S.A. on 1st April, 2024. Interest of USD 2,400 is payable annually on 31st March, starting from 31st March, 2025. The loan is repayable in USD on 31st March, 2030 and the effective annual interest rate implicit in the loan is 11%. The appropriate measurement basis for this loan is amortised cost. Relevant exchange rates are as follows:

- 1st April, 2024-USD 1 = Rs. 74.
- 31st March, 2025-USD 1 = Rs. 78.
- Average rate for the year ended 31st March, 2025 - USD 1 = Rs. 72.

The functional currency of the group is Indian Rupee.

Calculate (a) the initial measurement amount for the loan, (b) finance cost for the year 2024-2025, (c) closing balance of loan as at 31st March 2025 and (d) exchange gain / loss for the year 2024-2025.

### Solution :

#### (i) Initial carrying amount of loan in books

Loan amount received = USD 30,000

Present value of loan

Cash flow of interest USD 30,000 x 8% = 2,400 for 6 years.

PV of cash flow of interest USD 2,400 x 4.2305 = 10,153.20

PV of Repayment of loan USD 30,000 x 0.5346 = 16,038.00

Total 26,191.20

When effective interest rate is different from the contractual rate, it results into transaction cost due to which the initial present value of the loan is different from the transaction price. Accordingly, here difference of USD 3,808.80 (USD 30,000 – USD 26,191.20) will be recorded as transaction cost.

As per Ind AS 21, foreign currency transactions are initially recorded at the rate of exchange in force when the transaction was first recognized.

Loan to be converted in Rupees (Rs.) = USD 26,191.20 x Rs. 74/ USD = Rs. 19,38,149

Therefore, the loan would initially be recorded at Rs. 19,38,149.

**(ii) Calculation of Finance Cost for the year 2024-2025**

The finance cost = USD 26,191.20 x 11% = USD 2,881

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 financial year 2024-2025 in Rupees (Rs.) is Rs. 2,07,432 (USD 2,881 x Rs. 72/USD)

The actual payment of interest would be recorded at USD 2,400 x Rs. 78/ USD = Rs. 1,87,200

**(iii) Calculation of closing balance of loan as at 31st March 2025**

Period	Opening Financial Liability (USD) A	Interest @ 11% EIR (USD) B	Cash outflow (USD) C	Closing balance of loan (USD) A+B-C
2024-2025	26,191.20	2,881	2,400	26,672.20

**(iv) Computation of Exchange Gain/Loss for the year 2024-2025**

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 Rupees (Rs.) is USD 26,672.20 x Rs. 78/USD = Rs. 20,80,432

In this case, the exchange difference is Rs. [20,80,432 - (19,38,149 + 2,07,432 – 1,87,200)] = Rs. 1,22,051.

This exchange loss of Rs. 1,22,051 is taken to profit and loss account.

**Note:**

Effective interest rate is more than the contractual rate of interest in general when an entity incurs any transaction cost or repayment of loan is not at par value. Since in the question, there is no transaction cost or no repayment information different from par value, effective interest rate should have been equivalent to contractual interest rate.

The above solution has been drawn considering Effective Interest Rate of 11%, leading to calculation of initial recognition of loan amount on the date of acquisition of loan and difference being treated as transaction cost.

However, alternatively one may draw the solution considering Effective Interest Rate of 11% (as given) only for calculation of finance cost without change in the initial recognition of loan amount on the date of acquisition of loan or considering interest rate of 8%.

In both the case the solutions will be drawn as follows:

**Alternative: Considering Effective Interest Rate of 11% (as given) only for calculation of finance cost without change in the initial recognition of loan amount on the date of acquisition of loan**

**(i) Initial carrying amount of loan in books**

Loan amount received = USD 30,000

As per Ind AS 21, foreign currency transactions are initially recorded at the rate of exchange in force when the transaction was first recognized.

Loan to be converted in Rupees (Rs.) = USD 30,000 x Rs. 74 / USD = Rs. 22,20,000

Therefore, the loan would initially be recorded at Rs. 22,20,000.

**(ii) Calculation of Finance Cost for the year 2024-2025**

The finance cost = USD 30,000 x 11% = USD 3,300

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 financial year 2024-2025 in Rupees (Rs.) is Rs. 2,37,600 (USD 3,300 x Rs. 72 / USD)

The actual payment of interest would be recorded at USD 2,400 x Rs. 78/ USD = Rs. 1,87,200

**(iii) Calculation of closing balance of loan as at 31st March, 2025**

Period	Opening Financial Liability (USD) A	Interest @ 11% EIR (USD) B	Cash outflow (USD) C	Closing balance of loan (USD) A+B-C
2024-2025	30,000	3,300	2,400	30,900

**(iv) Computation of Exchange Gain/Loss for the year 2024-2025**

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 Rupees (Rs.) is USD 30,900 x Rs. 78 / USD = Rs. 24,10,200

In this case, the exchange difference is Rs. [24,10,200 - (22,20,000 + 2,37,600 - 1,87,200)] = Rs. 1,39,800

This exchange loss of Rs. 1,39,800 is taken to profit and loss account.

**Alternative: Considering Interest rate of 8% (as computed)**

**(i) Initial carrying amount of loan in books**

Loan amount received = USD 30,000

As per Ind AS 21, foreign currency transactions are initially recorded at the rate of exchange in force when the transaction was first recognized.

Loan to be converted in Rupees (Rs.) = USD 30,000 x Rs. 74 USD  
= Rs. 22,20,000

Therefore, the loan would initially be recorded at Rs. 22,20,000.

**(ii) Calculation of Finance Cost for the year 2024-2025**

The finance cost = USD 2,400 as given in the question

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 financial year 2024-2025 in Rupees (Rs.) is Rs. 1,72,800 (USD 2,400 x Rs. 72/ USD)

The actual payment of interest would be recorded at USD 2,400 x Rs. 78/ USD = Rs. 1,87,200

**(iii) Calculation of closing balance of loan as at 31st March, 2025**

Period	Opening Financial Liability (USD) A	Interest @ 8% (USD) B	Interest paid C	Closing Financial Liability (USD) A+B-C
2024-2025	30,000	2,400	2,400	30,000

**(iv) Computation of Exchange Gain/Loss for the year 2024-2025**

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 Rupees (Rs.) is  $USD\ 30,000 \times Rs.\ 78/USD = Rs.\ 23,40,000$

In this case, the exchange difference is  $Rs.\ [23,40,000 - (22,20,000 + 1,72,800 - 1,87,200)] = Rs.\ 1,34,400$

This exchange loss of Rs. 1,34,400 is taken to profit and loss.

**Question 16 : Jan 2026 – RTP**

Parent A Ltd. is the reporting entity that has net investment in foreign operations in its two foreign Subsidiaries, B Ltd. and C Ltd.

In all the following scenarios, loans made between group entities are permanent in nature (that is, settlement is neither planned nor likely to occur):

**Scenario 1**

Parent A Ltd., with sterling as its functional currency, is preparing its financial statements to 31st March, 20X5. It has a loan receivable of US\$ 1 million from its Subsidiary C Ltd. that has been outstanding for some time. The parent notified the subsidiary at the beginning of the financial year that no repayment of the amount will be requested for the foreseeable future.

The relevant exchange rate are as follows:

	<b>31st March, 20X5</b>	<b>31st March, 20X4</b>
£1=	US\$1.82	US\$1.45

**Scenario 2**

The facts are the same as in the above Scenario 1, except that Parent A Ltd. has a loan receivable from Subsidiary C Ltd. of £ 2,00,000 that has been outstanding for some time. The loan is treated by Parent A Ltd. as forming part of its net investment in Subsidiary C Ltd.

Required:

Determine the treatment of exchange differences in Standalone Financial Statements of both subsidiary and parent company and in Consolidated Financial Statements of parent company under both the scenarios.

**Solution :**

**Scenario 1**

The following exchange differences will arise in the financial statements of the individual entities if the loan is re-translated at the closing rate:

	<b>31st March, 20X5</b>
<b>Standalone Financial Statements of Subsidiary C Ltd.</b> No exchange difference arises in the foreign subsidiary because the loan payable is denominated in its functional currency	
<b>Standalone Financial Statements of Parent A Ltd.</b> Exchange difference on long-term loan receivable:	£
On closing rate - US\$ 1 million / \$ 1.82/£	5,49,450
On opening rate - US\$ 1 million / \$ 1.45/£	6,89,655

Exchange loss	1,40,205
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In Parent A Ltd.'s separate financial statements, the loan is regarded as a monetary item and any exchange difference is taken to profit or loss.

On consolidation, the re-translated long-term loan is regarded as part of the net investment in Subsidiary C Ltd., so the related exchange loss is recognised in other comprehensive income and accumulated as a separate component of equity as per para 32 of Ind AS 21. There would also be a corresponding exchange gain included in other comprehensive income, arising as part of the re-translation of the net assets (which include the US dollar loan creditor) of Subsidiary C Ltd. under the closing rate/net investment method.

### Scenario 2

In the financial statements of the individual entities, the following exchange differences will arise if the loan is re-translated at the closing rate.

#### Parent A Ltd.

There is no exchange difference in the parent's financial statements in respect of the loan because it is denominated in sterling.

#### Subsidiary C Ltd.

Exchange difference on long-term loan payable:

	US \$
On closing rate – £ 2,00,000 @ \$ 1.82/£	3,64,000
On opening rate - £ 2,00,000 @ \$ 1.45/£	<u>2,90,000</u>
Exchange loss	<u>74,000</u>
Exchange loss translated in £ at the closing rate @ \$ 1.82/£	£ 40,659

The exchange loss of US \$ 74,000 on the sterling loan is recognised in Subsidiary C Ltd.'s income statement, because the subsidiary is exposed to the foreign currency risk.

On consolidation, the inter-company loan will be cancelled. However, because the long-term loan is regarded as part of the net investment in the subsidiary, the exchange loss of £ 40,659 is recognised in other comprehensive income and accumulated as a separate component of equity in the consolidated financial statements. There is a corresponding exchange gain included in other comprehensive income, arising as part of the re-translation of the net assets of Subsidiary C Ltd. The effect is that the consolidated income statement will not reflect any exchange difference on the loan, which is consistent with the fact that the loan has no impact on group cash flows, unless the investment is sold.

Thanks ....



# IND AS – 24

## RELATED PARTY

### DISCLOSURE

## CHAPTER - 19

#### 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 2018 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.

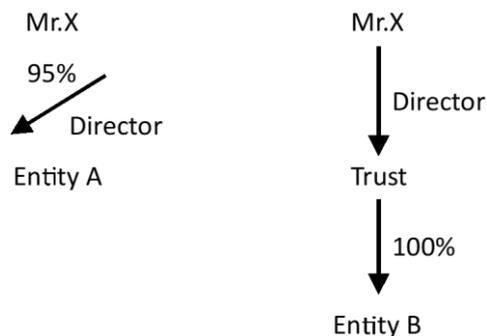
Whether entities A and B are related parties?

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 party.

Entity D is not required to disclose transactions with entity A, because they are not related parties.

#### Question 6 : May 2023 – Paper

Mr. M has an investment in X Limited and Y lim . . . .

- (i) Under what circumstances Mr. M is a related party of X Limited and Y Limited?
- (ii) Will X Limited and Y Limited be related parties if Mr. M has only significant influence over both X Limited and Y Limited ?

#### Solution :

- (i) As per para 9(a) of Ind AS 24, Mr. M will be considered as a related party to X Limited, when

1. Mr. M has control or joint control over X Limited
2. Mr. M has significant influence over X Limited

Similar will be the circumstances for Mr. M being considered as related party to Y Limited.

- (ii) Even if Mr. X has only significant influence over both the entities i.e., X Limited & Y Limited, then both the entities (X Limited & Y Limited) will not be considered as related party, if no direct or indirect control is exercised on each other in any of the manner.

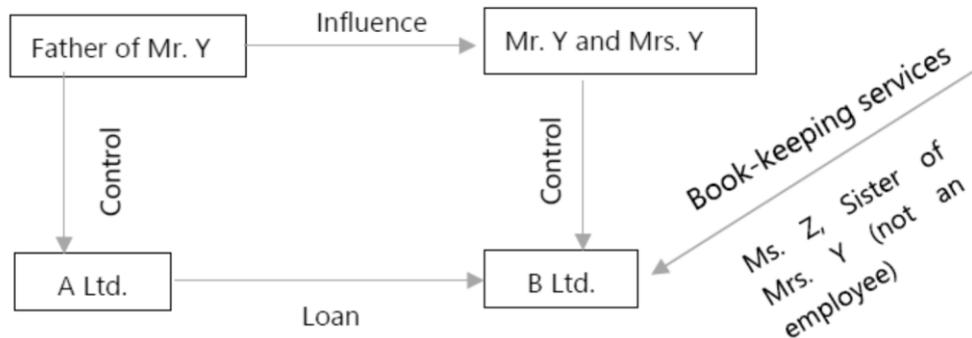
**Question 7 : May 2025 – RTP**

Mr. Y’s father owns 100% of the shares in A Ltd. Mr. Y and Mrs. Y own 100% of the shares in B Ltd. Ms. Z who is Mrs. Y’s sister, provides book-keeping services from time to time to B Ltd. However, Ms. Z is not an employee of B Ltd. A Ltd. has increased its loan of Rs. 1,50,000 to B Ltd. to Rs. 2,00,000 during the year, for which A Ltd. charges a below market rate of interest.

**Required:**

- (i) State whether Mr. Y’s father & Mrs. Y’s sister are related party of B Ltd.
- (ii) What disclosure is to be made in the financial statements of both A Ltd. & B Ltd. with respect to the loan given by A Ltd. to B Ltd.?
- (iii) Whether B Ltd. is required to disclose the dealings with the sister of Mrs. Y in its financial statements?

**Solution :**



- (i) Mr. Y’s father and Mrs. Y’s sister are related parties of B Ltd., if they are ‘close family’ of either Mr. Y or Mrs. Y. They are close family if they might be expected to influence, or be influenced by, Mr. Y or Mrs. Y in their dealing with B Ltd. Mr. Y’s father and Mr. Y and Mrs. Y are ‘close family’, so Mr. Y’s father is a related party of B Ltd., which is controlled by Mr. Y and Mrs. Y.  
Mr. Y’s father has a controlling interest in A Ltd. A Ltd. is a related party of B Ltd.
- (ii) Both entities should disclose the necessary details regarding the increase in the loan to Rs. 2,00,000 in their financial statements. A Ltd. should also disclose the amounts due to it from B Ltd. on the balance sheet date, together with any provisions and amounts written off. B Ltd. should disclose the amount that it owes to A Ltd. at the balance sheet date alongwith the concessional rate of interest at which the loan was given to B Ltd.
- (iii) B Ltd. would have to disclose the transactions with Mrs. Y’s sister if the sister might be expected to influence, or be influenced by, either Mr. Y or Mrs. Y in their dealings with B Ltd. based on further facts of the case. In case the influence exists, disclosure to be made as per para 18 of Ind AS 24 about the transactions and the outstanding balances.

**Question 8 : Jan 2026 – RTP**

Mr. A, Mr. B and Mr. C have direct interests of 40%, 10% and 10% respectively, of Trust T. The remaining 40% interest in Trust T is held by 20 unrelated investors.

Mr. A, Mr. B and Mr. C wish to control the trust, and so they enter into a contractual arrangement to act together. In this situation, assume that 1% interest constitutes one voting right.

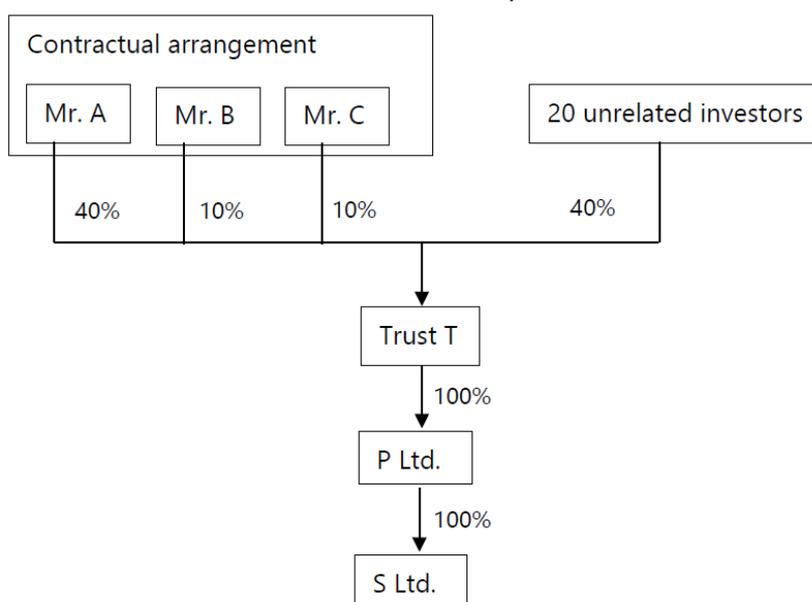
S Ltd. is a wholly owned subsidiary of P Ltd. and P Ltd. is wholly owned by Trust T.

Required:

Should a group of persons be disclosed as the ultimate controlling party where they have a contractual arrangement to act together?

**Solution :**

The following diagram shows the structure of the Group:



S Ltd.’s management should disclose Mr. A, Mr. B and Mr. C as the ultimate controlling party (as a group) of S Ltd. where they have a contractual arrangement to act together, irrespective of whether there were transactions between them and S Ltd. during the year.

The agreement between Mr. A, Mr. B and Mr. C provided them with a collective control over 60% (40%+10%+10%) of Trust T’s voting rights. Mr. A, Mr. B and Mr. C form a group that controls Trust T, which controls P Ltd. and S Ltd.

Trust T should also be disclosed as the ultimate parent entity of S Ltd. in the notes to the financial statements, if this information is not disclosed elsewhere in information published with the financial statements.

Trust T would be the ultimate controlling party of S Ltd. and only Mr. A would be a related party of S Ltd. if the contractual arrangement to act together did not exist. Mr. A is related to S Ltd. because his 40% interest in Trust T gives him significant influence over S Ltd.

Thanks ....



# IND AS – 33

## EARNINGS PER SHARE

### CHAPTER - 20

#### 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:

$$\frac{\text{Rs.1,000,000}}{1,200,000} = \text{Rs.0.83 per ordinary share}$$

#### 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.

$$\frac{\text{Rs.1,000,000} + \text{Rs.166,331}}{1,200,000 + 500,000} = \text{Rs.0.69 per ordinary share}$$

#### Notes:

- 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.
- 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.
- 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
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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)	<u>(4,000)</u>
Profit attributable to equity shareholders	<u>35,000</u>

Weighted average number of shares =  $20,00,00,000 + \{5,00,00,000 \times (9/12)\}$   
 = 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)		<u>(4,000)</u>
		35,000
Add: Finance cost (as given in the above table)	13,733.11	
Less: Tax @ 25%	<u>(3,433.28)</u>	<u>10,299.83</u>
		<u>45,299.83</u>

Weighted average number of shares =  $20,00,00,000 + \{5,00,00,000 \times (9/12)\} + 10,00,00,000$   
 = 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**

	<b>Year ended 31.3.2020</b>
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.).

	<b>Net profit attributable to equity shareholders  Rs.</b>	<b>No. of equity shares</b>	<b>Net Profit attributable per share  Rs.</b>	
Net profit attributable to equity shareholders	90,000	16,000	5.625	
Options	<u>          </u>	<u>150</u>		
	90,000	16,150	5.572	Dilutive
10% Convertible debentures	<u>75,000</u>	<u>40,000</u>		
	1,65,000	56,150	2.939	Dilutive
Convertible Preference Shares	<u>72,900</u>	<u>15,000</u>		
	<u>2,37,900</u>	<u>71,150</u>	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**

	<b>Increase in earnings</b>	<b>Increase in number of equity shares</b>	<b>Earnings per incremental share</b>	<b>Rank</b>
	(1)	(2)	(3) = (1) ÷ (2)	
	Rs.			
<b>Options</b>				
Increase in earnings	Nil			

No. of incremental shares issued for no consideration [900 x (90-75)/90]		150	Nil	1
<b>Convertible Preference Shares</b>				
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
<b>10% Convertible Debentures</b>				
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 31<sup>st</sup> 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 :

- 31<sup>st</sup> March, 2024 : 135 Ordinary Shares
- 31<sup>st</sup> March, 2025 : 130 Ordinary Shares
- 31<sup>st</sup> March, 2026 : 125 Ordinary Shares
- 31<sup>st</sup> 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 31<sup>st</sup> March, 2020 and 31<sup>st</sup> 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 31<sup>st</sup> 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 31<sup>st</sup> March 2020 and 31<sup>st</sup> March 2021.

**Solution :**

	<b>2021</b>	<b>2020</b>
<b>Trading results</b>	<b>Rs.</b>	<b>Rs.</b>
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	<u>(5,300)</u>	<u>(5,000)</u>
Profit before tax	15,84,700	14,95,000
Taxation @ 33% on (A-B)	<u>(5,24,700)</u>	<u>(4,95,000)</u>
Profit after tax	<u>10,60,000</u>	<u>10,00,000</u>
<b>Calculation of basic EPS</b>		
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  $(Rs. 100 \times 8\% \times 67\%) + (Rs. 5,300 / 25,000) = Rs. 5.36 + Rs. 0.21 = Rs. 5.57$ .

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.

	<b>2021</b>	<b>2020</b>
	<b>Rs.</b>	<b>Rs.</b>
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	<u>(66,000)</u>	<u>(49,500)</u>
Adjusted earnings for equity	<u>11,99,300</u>	<u>11,05,500</u>

**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).

	<b>2021</b>	<b>2020</b>
Number of equity shares for basic EPS	20,00,000	20,00,000
Maximum conversion at date of issue ( $33,75,000 \times 9/12$ )	–	25,31,250

Maximum conversion after balance sheet date	<u>33,75,000</u>	—
Adjusted shares	<u>53,75,000</u>	<u>45,31,250</u>
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	
<b>Basic earnings per share</b>			<b>Rs. 2.40</b>
Weighted average number of shares under option		1,00,000	
Weighted average number of shares that would have been issued at average market price: $(1,00,000 \times \text{Rs. } 15.00) \div \text{Rs. } 20.00$	Refer Note	(75,000)	
<b>Diluted earnings per share</b>	<b>Rs. 1,200,000</b>	<b>5,25,000</b>	<b>Rs. 2.29</b>

**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

### Question 7 : May 2022 – Paper

GOLD Ltd, a manufacturing company, prepares its financial statements on 31<sup>st</sup> March every year. On 1<sup>st</sup> April, 2021, it had issued (a) 10,00,000 ordinary shares and (b) 6% convertible bonds amounting to Rs.100,000, the terms of conversion being 120 ordinary shares for every Rs.100. On 30<sup>th</sup> June, 2021, Rs.50,000 bonds converted to ordinary shares. The profit for the year ended 31<sup>st</sup> March, 2022 is Rs.250,000. The applicable tax rate is 25%.

Calculate basic and diluted EPS. Ignore the need to split the convertible bonds into liability and equity element.

### Solution :

	Number of shares	Profit (Rs.)
Profit		2,50,000
Outstanding ordinary shares	10,00,000	
New shares on conversion (weighted average) [(9/12 x Rs. 50,000 / 100 x 120)]	<u>45,000</u>	
Figures for basic EPS	10,45,000	2,50,000
<b>Basic EPS is</b> (Rs. 2,50,000 / 10,45,000 shares) = Rs. 0.239 per share		
<b>Dilution adjustments</b>		
Unconverted shares (Rs. 50,000 / 100 x 120)	60,000	
Interest (Rs. 50,000 x 6% x 0.75 net of tax)		2,250
Converted shares pre conversion adjustment (3/12 x Rs. 50,000 / 100 x 120)	15,000	
Interest: [3/12 x Rs. 50,000 x 6% x 0.75 net of tax]		562.50
	11,20,000	2,52,812.50
<b>Diluted EPS is</b> (Rs. 2,52,812.50 / 11,20,000 shares) = Rs. 0.226 per share		

#### Question 8 : Nov 2022 – RTP

Company S is a subsidiary of Company P.

Following facts are in respect of Company S:

- Company S has 10,000 ordinary shares and 1,000 options outstanding, of which Company P owns 9,000 shares and 500 options, respectively.
- The options have an exercise price of Rs. 40.
- The average market price of Company S's ordinary share was Rs. 50 in 20X1.
- In 20X1, Company S's profit was Rs. 30,000.

Following facts are in respect of Company P:

- Company P has 5,000 ordinary shares outstanding.
- In 20X1, Company P's profit (excluding any distributed and undistributed earnings of subsidiaries) was Rs. 7,000.
- The options outstanding are dilutive at P's level.

Determine the diluted EPS of Company P for the year 20X1. Ignore income tax.

#### Solution :

To determine the diluted EPS of Company P, the diluted EPS of Company S has to be calculated first.

#### Calculation of Company S's diluted EPS:

Company S's earnings for the period	Rs. 30,000
Weighted average ordinary shares	10,000
Incremental shares (refer W.N.)	200
Company S's diluted EPS	Rs. 30,000/ (10,000 + 200)

Rs. 2.94

Calculation of Company P's diluted EPS:

Company P's earning for the period Rs. 7,000

Company P's share of Company S's earning attributable to ordinary shares Rs. 26,460

$[(9,000 / 10,000) \times (2.94 \times 10,000)]$

Company P's share of Company S's earning attributable to options Rs. 294

$[(500 / 1,000) \times (2.94 \times 200)]$

Company P's weighted average ordinary shares outstanding 5,000

Company P's diluted EPS =  $(7,000 + 26,460 + 294) / 5,000$  Rs. 6.75

**Working Note:**

**Computation of Incremental shares related to weighted average options outstanding:**

All options are dilutive because their exercise price is below the average market price of Company S's ordinary shares for the period.

The incremental shares are calculated as follows:

Shares issued on assumed exercise of options 1,000

Less: Shares that would be issued at average market Price  $[(40 \times 1,000) / 50]$  (800)

Incremental shares 200

### Question 9 : May 2023 – RTP

Company P has both ordinary shares and equity-classified preference shares in issue. The reconciliation of the number of shares during Year 1 is set out below:

Dates in Year 1	Transaction	Number of shares		
		Ordinary shares	Treasury shares	Preference shares
1st April	Balance	30,00,000	(5,00,000)	5,00,000
15th April	Bonus issue – 5% (no corresponding changes in resources)	1,50,000	(25,000)	-
1st May	Repurchase of shares for cash	-	(2,00,000)	-
1st November	Shares issued for cash	<u>4,00,000</u>	-	-
31st March	Balance	<u>35,50,000</u>	<u>(7,25,000)</u>	<u>5,00,000</u>

The following additional information is relevant for Year 1.

- Company P's net profit for the year is Rs. 46,00,000.
- On 15th February, non-cumulative preference dividends of Rs. 1.20 per share were declared. The dividends were paid on 15th March. Preference shares do not participate in additional dividends with ordinary shares.
- Dividends on non-cumulative preference shares are deductible for tax purposes. The applicable income tax rate is 30%.

The financial year of Company P ends on 31st March.

Determine the Basic EPS of the Company P for Year 1. Use the number of months or part of months, rather than the number of days in the calculation of EPS.

**Solution :**

**Determination of numerator for calculation of Basic EPS**

The first step in the basic EPS calculation is to determine the profit or loss that is attributable to ordinary shareholders of Company P for the period.

Non-cumulative dividends paid on equity-classified preference shares are not deducted in arriving at net profit or loss for the period, but they are not returns to ordinary shareholders. Accordingly, these dividends are deducted from net profit or loss for the period in arriving at the numerator.

		Rs.
Net profit		46,00,000
Preference dividends (5,00,000 shares x 1.2)	(6,00,000)	
Related tax (Rs. 6,00,000 x 30%)	<u>1,80,000</u>	<u>(4,20,000)</u>
Profit or loss attributable to P's ordinary shareholders		<u><b>41,80,000</b></u>
Accordingly, the numerator for calculation of Basic EPS is Rs. 41,80,000		

**Determination of denominator for calculation of Basic EPS**

The second step in the basic EPS calculation is to determine the weighted-average number of ordinary shares outstanding for the reporting period.

Number of shares	Time weighting	Weight	Weighted average number of shares
1st April – opening balance (30,00,000 – 5,00,000)	25,00,000	1	
15th April – bonus issue (1,50,000 – 25,000)	<u>1,25,000</u>		
1st April to 30th April	26,25,000	1/12	2,18,750
1st May – repurchase of shares	<u>(2,00,000)</u>		
1st May to 31st October	24,25,000	6/12	12,12,500
1st November – new shares issued	4,00,000		
1st November to 31st March	<u>28,25,000</u>	5/12	<u>11,77,083</u>
<b>Weighted average number of shares for the year</b>			<u><b>26,08,333</b></u>

The denominator for calculation of Basic EPS is 26,08,333 shares.

**Basic EPS** = Rs. 41,80,000 / 26,08,333 shares = Rs. 1.60 per share (approx.).

**Question 10 : May 2025 – Paper**

Following information is given to you in respect of A Ltd. and B Ltd.:

Particulars	A Ltd.	B Ltd.
	Amount (Rs.)	Amount (Rs.)
Income (loss) from continuing operations	5,04,000	(3,60,000)

Income (loss) from discontinued operations	(8,40,000)	6,51,840
Net income (loss)	(3,36,000)	2,91,840
Weighted average number of shares outstanding	1,60,000	1,92,000
Incremental common share outstanding relating to stock options	32,000	51,200

From the above information, you are required to calculate the following:

- (i) Basic and Diluted EPS of A Ltd. and
- (ii) Diluted EPS of B Ltd.

**Solution :**

**(i) Basic EPS of A Ltd.**

Basic EPS (Continued Operations)	=	Profit from continued operations/Weighted average number of shares outstanding Rs. 5,04,000 / 1,60,000 = Rs. 3.15
Basic Loss per share (Discontinued operations)	=	Loss from discontinued operations / Weighted average number of shares outstanding (Rs. 8,40,000) / 1,60,000 = (Rs. 5.25)
Overall Basic Loss per share	=	(Rs. 3,36,000) / 1,60,000 = (Rs. 2.10)

**Diluted EPS of A Ltd.**

Diluted EPS = Profit for the year / Adjusted weighted average number of shares outstanding

DEPS (Continued Operations)	=	Profit from continued operations / Adjusted weighted average number of shares outstanding Rs. 5,04,000 / 1,92,000 = Rs. 2.625
Diluted Loss per share (Discontinued operations)	=	Loss from discontinued operations/ Adjusted weighted average number of shares outstanding (Rs. 8,40,000) / 1,92,000 = (Rs. 4.375)
Overall Diluted Loss per share	=	(Rs. 3,36,000) / 1,92,000 = (Rs. 1.75)

- (ii)** In case of B Ltd.'s loss from continuing operations, the potential shares are excluded since including those shares would result into anti-dilution effect on the control number (loss from continuing operations).

Therefore, the Diluted EPS of B Ltd will be calculated as under:

Diluted EPS	=	Profit for the year / Adjusted weighted average number of shares outstanding
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Overall Profit	=	Loss from continuing operations + Gain from discontinued operations (Rs. 3,60,000) + Rs. 6,51,840 = Rs. 2,91,840
Weighted average number of shares outstanding	=	1,92,000
Diluted EPS	=	Rs. 1.52

**Question 11 : Sept 2025 – Paper**

On 31st March, 2024, Vanshika Ltd. granted options to its employees that gave them right to subscribe for equity shares in next 3 years at Rs. 112 per share. It also issued 2 lakhs warrants convertible into shares at Rs. 84.

As on 31st March, 2025:

Options outstanding	1,40,000
Profit after Tax, attributable to equity shareholders	Rs. 91,20,000
Average market price of equity shares	Rs. 140
Issued Equity share capital (Face value Rs. 10 each)	Rs. 50,00,000

There were no grants, exercises or lapses of options during the year. Also, none of the warrants was converted into shares during the year.

You are required to calculate Basic and Diluted EPS as at 31st March, 2025.

**Solution :**

**Calculation of Basic Earnings Per Share (EPS)**

	2024-2025
Profit after tax	Rs. 91,20,000
Number of shares (Rs. 50,00,000 / Rs. 10 per share)	5,00,000
Basic EPS	Rs. 18.24

**Calculation of Diluted EPS**

<b>(i) Adjusted number of shares</b>	
<b>a. Number of shares under options:</b>	
Issued at full market price	
$[(1,40,000 \times 112) / 140] = 1,12,000$	
Options issued at nil consideration (dilutive)	28,000
$(1,40,000 - 1,12,000)$	
<b>b. Number of shares under warrants:</b>	
Issued at full market price	
$[(2,00,000 \times 84) / 140] = 1,20,000$	
Warrants issued at nil consideration (dilutive)	
$(2,00,000 - 1,20,000)$	<u>80,000</u>
Number of dilutive shares under options and warrants	<u>1,08,000</u>

<b>(ii) Calculation of Diluted EPS:</b>		
Number of equity shares for basic EPS		5,00,000
Number of dilutive shares under options and warrants		1,08,000
Adjusted number of shares	(A)	<u>6,08,000</u>
Profit after tax	(B)	Rs. 91,20,000
Diluted EPS	(B/A)	Rs. 15

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Thanks ....



# IND AS – 34 INTERIM FINANCIAL REPORTING

## CHAPTER - 21

### 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	<u>Rs.4,50,000</u>

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)
<b>Annual</b>	<b>0</b>		<b>0</b>

**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
<b>Under recovery year to date (Rs.)</b>	<b>50,000</b>	<b>20,000</b>	<b>NIL</b>	<b>60,000</b>

#### 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.

#### Question 6 : Nov 2022 – RTP

PQR Ltd. is preparing its interim financial statements for quarter 3 of the year. How the following transactions and events should be dealt with while preparing its interim financials:

- (i) It makes employer contributions to government-sponsored insurance funds that are assessed on an annual basis. During Quarter 1 and Quarter 2 larger amount of payments for this contribution were made, while during the Quarter 3 minor payments were made (since contribution is made upto a certain maximum level of earnings per employee and hence for higher income employees, the maximum income reaches before year end).
- (ii) The entity intends to incur major repair and renovation expense for the office building. For this purpose, it has started seeking quotations from vendors. It also has tentatively identified a vendor and expected costs that will be incurred for this work.
- (iii) The company has a practice of declaring bonus of 10% of its annual operating profits every year. It has a history of doing so.

#### Solution :

Paragraph 28 of Ind AS 34, Interim Financial Reporting states that an entity shall apply the same accounting recognition and measurement principles in its interim financial statements as are applied in its annual financial statements.

Further, paragraphs 32 and 33 of Ind AS 34, Interim Financial Reporting state that for assets, the same tests of future economic benefits apply at interim dates and at the end of an entity's financial year. Costs that, by their nature, would not qualify as assets at financial year-end would not qualify at interim dates either. Similarly, a liability at the end of an interim reporting period must represent an existing obligation at that date, just as it must at the end of an annual reporting period.

An essential characteristic of income (revenue) and expenses is that the related inflows and outflows of assets and liabilities have already taken place. If those inflows or outflows have taken place, the related revenue and expense are recognised otherwise not. The Conceptual Framework does not allow the recognition of items in the balance sheet which do not meet the definition of assets or liabilities.

Considering the above guidance, while preparing its interim financials, the transactions and events of the given case should be dealt with as follows:

- (i) If employer contributions to government-sponsored insurance funds are assessed on an annual basis, the employer's related expense is recognised using an estimated average annual effective contribution rate in its interim financial statements, even though a large portion of the payments have been made early in the financial year. Accordingly, it should

work out an average effective contribution rate and account for the same accordingly, in its interim financials.

- (ii) The cost of a planned overhaul expenditure that is expected to occur in later part of the year is not anticipated for interim reporting purposes unless an event has caused the entity to have a legal or constructive obligation. The mere intention or necessity to incur expenditure related to the future is not sufficient to give rise to an obligation.
- (iii) A bonus is anticipated for interim reporting purposes, if and only if,
  - (a) the bonus is a legal obligation or past practice would make the bonus a constructive obligation for which the entity has no realistic alternative but to make the payments, and
  - (b) a reliable estimate of the obligation can be made. Ind AS 19, Employee Benefits provides guidance in this regard.

A liability for bonus may arise out of legal agreement or constructive obligation because of which it has no alternative but to pay the bonus and accordingly, needs to be accrued in the annual financial statements.

Bonus liability is accrued in interim financial statements on the same basis as they are accrued for annual financial statements. In the instant case, bonus liability of 10% of operating profit for the year to date may be accrued.

In the given case, since the company has past record of declaring annual bonus every year, the same may be accrued using a reasonable estimate (applying the principles of Ind AS 19, Employee Benefits) while preparing its interim results.

### Question 7 : May 2023 – RTP

The entity's financial year ends on 31st March. What are the "reporting periods" for which financial statements (condensed or complete) in the interim financial report of the entity as on 30th September, 20X1 are required to be presented, if:

- (i) Entity publishes interim financial reports quarterly
- (ii) Entity publishes interim financial reports half-yearly.

### Solution :

Paragraph 20 of Ind AS 34, Interim Financial Reporting states as follows:

"Interim reports shall include interim financial statements (condensed or complete) for periods as follows:

- a) balance sheet as of the end of the current interim period and a comparative balance sheet as of the end of the immediately preceding financial year.
- b) statements of profit and loss for the current interim period and cumulatively for the current financial year to date, with comparative statements of profit and loss for the comparable interim periods (current and year-to-date) of the immediately preceding financial year.
- c) statement of changes in equity cumulatively for the current financial year to date, with a comparative statement for the comparable year-to-date period of the immediately preceding financial year.

- d) statement of cash flows cumulatively for the current financial year to date, with a comparative statement for the comparable year-to-date period of the immediately preceding financial year.

Accordingly, periods for which interim financial statements are required to be presented are provided herein below:

**(i) Entity publishes interim financial reports quarterly**

The entity will present the following financial statements (condensed or complete) in its interim financial report of 30th September, 20X1

Balance sheet at	30th September 20X1	31st March 20X1	-	-
Statement of profit and loss for	3 months ended 30th September 20X1	3 months ended 30th September 20X0	6 months ended 30th September 20X1	6 months ended 30th September 20X0
Statement of changes in equity for	6 months ended 30th September 20X1	6 months ended 30th September 20X0		
Statement of cash flows for	6 months ended 30th September 20X1	6 months ended 30th September 20X0	-	-

**(ii) Entity publishes interim financial reports half-yearly**

The entity's financial year ends 31st March. The entity will present the following financial statements (condensed or complete) in its half-yearly interim financial report of 30th September, 20X1:

<b>Balance sheet at</b>	30th September 20X1	31st March 20X1
<b>Statement of profit and loss for</b>	6 months ending 30th September 20X1	6 months ending 30th September 20X0
<b>Statement of changes in equity for</b>	6 months ending 30th September 20X1	6 months ending 30th September 20X0
<b>Statement of cash flows for</b>	6 months ending 30th September 20X1	6 months ending 30th September 20X0

Dhruv Limited, a production company, sells television to various companies all over India. Company's financial year ends on 31st March. For the financial year 2022-2023, the company had a net profit after taxes of Rs. 2.4 crores. It prepares and publishes an interim financial report for each quarter of the year. The net profit of the company for the second quarter of 2023-2024 is Rs. 56 Lakhs.

Following adjustments are to be made while computing the net profit of second quarter:

- (i) The company has a practice of declaring bonus of 5% of its profit after taxes of previous financial year. It has a history of doing so and the amount is recognised equally in each quarter. It declared bonus on 1st June 2023 but recognised the full amount in second quarter.
- (ii) The company intends to incur major repair and renovation expense for the office building. For this purpose, it has started seeking quotations from vendors. It also has tentatively identified a vendor and expected costs are Rs. 34 lakhs. It provided for the same in this quarter.
- (iii) Exceptional loss of Rs. 4.2 Lakhs incurred during the second quarter due to workers' strike. 50% of exceptional loss has been deferred to next quarter.

Ascertain the correct net profit with reasons to be shown in the Interim Financial Report of second quarter to be presented to the Board of Directors.

### **Solution :**

In the instant case, the quarterly net profit has not been correctly stated. As per Ind AS 34, Interim Financial Reporting, the quarterly net profit should be adjusted and restated as follows:

- (i) A liability for bonus may arise out of legal agreement or constructive obligation because of which it has no alternative but to pay the bonus and accordingly, needs to be accrued in the annual financial statements. Bonus liability is accrued in interim financial statements on the same basis as they are accrued for annual financial statements.  
In the given case, since the company has past record of declaring annual bonus every year, the same may be accrued using a reasonable estimate (applying the principles of Ind AS 19, Employee Benefits) while preparing its interim results.  
Accordingly, Bonus amount to be charged in the second quarter would be Rs. 2,40,00,000 x 5% x  $\frac{1}{4}$  = Rs. 3,00,000.  
Bonus of Rs. 9,00,000 (Rs. 12,00,000 – Rs. 3,00,000) must be reversed.
- (ii) The cost of a planned major repair and renovation that is expected to occur in later part of the year is not considered for interim reporting purposes unless an event has caused the entity to have a legal or constructive obligation. The mere intention or necessity to incur expenditure related to the future is not sufficient to give rise to an obligation.  
Hence, Rs. 34,00,000 provided in the second quarter must be reversed.
- (iii) Treatment of exceptional loss is not as per the principles of Ind AS 34, as the entire amount of Rs. 4,20,000 incurred during the second quarter should be recognized in the same quarter.  
Hence, Rs. 2,10,000 which was deferred should be deducted from the profits of second quarter only.

Thus, considering the above, the correct net profits to be shown in Interim Financial Report of the second quarter shall be:

Rs. 96,90,000 (Rs. 56,00,000 + Rs. 9,00,000 + Rs. 34,00,000 - Rs. 2,10,000).

### Question 9 : Nov 2024 – Paper

Spicer Ltd., a listed company, prepares interim financial reports at the end of each quarter. Following information is provided:

- (i) On 1st April' 2023, Spicer Ltd. has brought forward losses of Rs.620 lakh under Income Tax Act. No Deferred Tax Asset has been recognized by the management of the company on such losses in view of the uncertainty over company's ability to earn profits in the foreseeable future and set off these losses.
  - (ii) Due to sudden change in government policies, the company's business turned around and it has reported quarterly earnings of Rs.650 lakh and Rs.360 lakh respectively for the first two quarters of financial year 2023-24 and anticipates net earnings of Rs.720 lakh in the coming half year ended March' 2024 of which Rs.160 lakh will be the loss in the quarter ended December' 2023.
  - (iii) The tax rate for the company is 25% with a 10% surcharge.
- You are required to calculate the amount of Tax Expenses to be reported for each quarter of financial year 2023-24.

### Solution :

It is assumed that net profit for all the quarters of the year 2023-2024 excludes the brought forward losses of Rs. 620 lakh.

#### Computation of estimated total earnings for the year 2023-2024

Quarter	Earnings before tax (in lakhs)
1	650 (actual)
2	360 (actual)
3	(160) (estimated)
4	720 + 160 = <u>880</u> (estimated)
	<u>1,730</u> (estimated)

Tax rate for the company = 25 x 110% = 27.5%

#### Computation of Average Annual Effective Tax Rate

The estimated payment of the annual tax on earnings for the current year:

= (1,730-620) x 27.5% = Rs. 305.25 lakhs.

As per Ind AS 34, 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.

Thus, average annual effective tax rate = (305.25 / 1,730) × 100

= 17.645% (approx.)

Tax expense to be shown in each quarter.

Quarter	Earnings before tax (in lakhs)	Tax expense @ 17.645%
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1	650 (actual)	114.69
2	360 (actual)	63.52
3	(160) (estimated)	(28.23)
4	720 + 160 = <u>880</u> (estimated)	155.27
	<u>1730</u> (estimated)	305.25

### Question 9 : May 2025 – Paper

Hero Ltd. reported a profit before tax of Rs. 8 lakhs for the third quarter ending 31st December 2024. On enquiry, you observe the following:

- Dividend income of Rs. 8 lakhs received during the quarter has been recognized to the extent of Rs. 2 lakhs only.
- 60% of sales promotion expenses of Rs. 30 lakhs incurred in the third quarter has been deferred to the fourth quarter as the sales in fourth quarter are expected to be high.
- Rs. 4 lakhs extraordinary gain received in third quarter was allocated equally to the third and fourth quarter.
- Cumulative loss of Rs. 30 lakhs resulting from change in method of inventory valuation was recognized in the third quarter. Out of this loss, Rs. 10 lakhs relate to previous quarters.
- Sale of investment in the first quarter resulted in a gain of Rs. 40 lakhs. The company had apportioned this equally to the four quarters.

You are required to discuss the treatment of the above observations and ascertain the adjusted profit /loss before tax for the third quarter.

### Solution :

As per para 37 and para 39 of Ind AS 34 “Interim Financial Reporting”, seasonal or occasional revenue and cost within a financial year should not be anticipated or deferred as of interim date if it would not be appropriate to anticipate or defer the same at the end of the entity’s financial year. Therefore, dividend income, extraordinary gain, and gain on sale of investment received during 3rd quarter should be recognised in the 3rd quarter only.

Similarly, sales promotion expenses incurred in the 3rd quarter should also be charged in the 3rd quarter only.

Further, as per the standard, if there is change in the accounting policy within the current financial year, then such a change should be applied retrospectively by restating the financial statements of prior interim periods of the current financial year.

The change in the method of inventory valuation is a change in the accounting policy. Therefore, the prior interim periods’ financial statements should be restated by applying the change in the method of valuation retrospectively.

Accordingly, the adjusted profit before tax for the 3rd quarter will be as follows:

#### Statement showing Adjusted Profit Before Tax for the Third Quarter ending 31st December, 2024

	(Rs. in lakhs)
Profit before tax (as reported)	8

Add: Dividend income Rs. (8-2) lakhs	6
Extraordinary gain Rs. (4-2) lakhs	2
Cumulative loss due to change in the method of inventory valuation should be applied retrospectively	<u>10</u>
	26
Less: Sales promotion expenses (60% of Rs. 30 lakhs)	(18)
Gain on sale of investment (occasional gain should not be deferred)	<u>(10)</u>
Adjusted Profit before tax for the third quarter	<u>(2)</u>

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Thanks ....



# IND AS – 37

## PROVISIONS, CONTINGENT LIABILITIES & CONTINGENT ASSETS

### CHAPTER - 22

#### 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	4,00,00	
	.	0	
To Provision for Onerous Contract Liability A/c			4,00,00
			0
(Being asset to be received due to binding agreement recognized)			
Profit and Loss Account (Loss due to onerous contract)	Dr	4,00,00	
	.	0	
To Onerous Contract Provision Expense A/c			4,00,00
			0
(Being loss due to onerous contract recognized and asset derecognised)			

**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 be 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 be 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:**

$$(80\% \times \text{nil}) + (15\% \times \text{Rs.}20,00,000) + (5\% \times \text{Rs.}50,00,000) = 3,00,000 + 2,50,000 = 5,50,000$$

**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-imburement 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.

**Question 8 : Nov 2022 – RTP**

HVCL manufactures heavy equipment for construction industry. An order for supply of 90 equipment was received from ABIL. The unit price of the equipment was agreed at Rs. 190 lakhs each. 64 equipment was supplied during the year 20X1-20X2 and balance quantity remaining to be supplied as on 31.3.20X2. HVCL has 5 equipment in its inventory as on 31.3.20X2. HVCL considered that the contract was an onerous contract and therefore, the net realisable value of inventory has been taken as value of inventory as on 31.3.20X2.

The management of HVCL contends that costs incurred towards administrative overheads, finance charges, R & D expenses, sales overhead, head quarter expenditure etc., are considered as period cost and hence not considered for creation of provision. Hence, the same have not been included in the computation of unavoidable cost.

The management of HVCL has submitted the details of costs that have been considered for creation of provision towards onerous contract:

- Material cost - includes cost of material procured, cost of freight & insurance incurred for material procurement and handling, loading and unloading charges incurred.
- Labour cost/ Factory Overheads - includes salaries and other expenses of direct production department, and also expenses allocated from indirect departments to direct department.
- Material Overheads - Includes salaries and other expenses (including expenses allocated from other departments) booked under departments linked with materials like purchases, stores and quality control.

Accordingly, provision has been made considering the above costs only. The value of provision created for 21 remaining equipment to be produced is as per the working shown below:

Particulars	Value (Rs. in lakh)
-------------	---------------------

(i)	Cost of production (which includes material cost, labour cost/factory overhead and material overhead)	199.00
(ii)	Selling price	<u>(190.00)</u>
(iii)	Differential cost per equipment	<u>9.00</u>
(iv)	Differential cost of Rs. 9 Lakh per equipment for 21 equipment	189.00

Whether the company's accounting treatment of cost for creation of provision towards onerous contracts is in line with the provisions of Ind AS 37?

### Solution :

As per para 68 of Ind AS 37, onerous contract is a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable cost under a contract reflects the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation for penalties arising from failure to fulfilling it.

Ind AS 37 provides that the amount recognised shall be the best estimate of the expenditure required to settle the present obligation, which is the amount that an entity would rationally pay to settle the obligation at the end of the reporting period or to transfer it to a third party at that time. In case of onerous contracts, an amount that an entity would rationally pay to settle the obligation would be the lower of the compensation or penalties arising from failure to fulfil the contacts and excess of unavoidable cost of meeting the obligations under the contract from the economic benefits expected to be received under it.

As per para 68 of Ind AS 37, the cost of fulfilling a contract comprises the costs that relate directly to the contract. Costs that relate directly to a contract consist of both-

- (a) the incremental costs of fulfilling that contract—for example, direct labour and materials; and
- (b) an allocation of other costs that relate directly to fulfilling contracts— for example, an allocation of the depreciation charge for an item of property, plant and equipment used in fulfilling that contract among others.

The unavoidable costs of meeting the obligations under the contract are only costs that:

- "are directly variable with the contract and therefore incremental to the performance of the contract;"
- do not include allocated or shared costs that will be incurred regardless of whether the entity fulfils the contract or not; and
- cannot be avoided by the entity's future actions.

Accordingly, HVCL has correctly measured the cost for creation of provision for onerous contracts by considering material cost, labour cost (to the extent it relates directly to production) and material overheads (to the extent it relates directly to production).

Further, HVCL is correct that the period cost will not be considered for measurement of cost for the purpose of creation of provision on onerous contracts as they do not relate directly to fulfilling the contracts.

**Question 9 : Nov 2022 – Paper**

Orange Ltd. is going to prepared its annual financial statements for the year ending 31<sup>st</sup> March, 2022, in the process if discovered that a provision for construction obligation for payment of bonus to selected employees in the corporate office (material in amount) which was required to be recognized in the annual financial statements for the year ended 31<sup>st</sup> March, 2020 was not recognized due to oversight of facts. The bonus was paid during the financial year ended 31<sup>st</sup> March, 2021 and was recognized as an expense in the annual financial statements for the said year.

As finance manager of the company you are required to analyse whether the situation relating to constructive obligation for payment of bonus is an error requiring retrospective restatement of comparatives considering that the amount is material.

**Solution :**

As per paragraph 41 of Ind AS 8, 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.

As per paragraph 40A of Ind AS 1, an entity shall 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 retrospective restatement has a material effect on the information in the balance sheet at the beginning of the preceding period.

In the given case, expenses for the year ended 31<sup>st</sup> March, 2020 and liabilities as at 31<sup>st</sup> March, 2020 were understated because of non-recognition of bonus expense and related provision. Expenses for the year ended 31<sup>st</sup> March, 2021, on the other hand, were overstated to the same extent because of recognition of the aforesaid bonus as expense for the year. To correct the above errors in the annual financial statements for the year ended 31<sup>st</sup> March, 2022, the entity should:

- (a) restate the comparative amounts (i.e., those for the year ended 31<sup>st</sup> March, 2021) in the statement of profit and loss; and
- (b) present a third balance sheet as at the beginning of the preceding period (i.e., as at 1<sup>st</sup> April, 2020) wherein it should recognise the provision for bonus and restate the retained earnings.

**Question 9 : Nov 2022 – Paper**

TCO Limited is a telecom operator. Laying of cables across the world is a requirement to enable the entity to run its business. Cables are also laid under the sea and contracts are entered into for the same. By virtue of laws of the countries through which the cable passes, the entity is required

to restore the sea bed at the end of the contract period. Discuss the nature of obligation that TCO Limited has in such a case.

**Solution :**

Paragraph 14 of Ind AS 37 states that a provision shall be recognised when:

- (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, no provision shall be recognised.

Further, with regard to past event paragraph 17 of Ind AS 37 states that a past event that leads to a present obligation is called an obligating event. For an event to be an obligating event, it is necessary that the entity has no realistic alternative to settling the obligation created by the event. This is the case only:

- (a) where the settlement of the obligation can be enforced by law; or
- (b) in the case of a constructive obligation, where the event (which may be an action of the entity) creates valid expectations in other parties that the entity will discharge the obligation.

Applying the above guidance in the given scenario, provision should be recognised as soon as the obligating event takes place because the entity is under legal obligation to restore the seabed, provided the other recognition criteria stated in paragraph 14 reproduced above are met. Moreover, the amount of the provision would depend on the extent of the obligation arising from the obligating event. In the instant case, an obligating event is the laying of cables under the sea. To the extent the cables have been laid down under the sea, a legal obligation has arisen and to that extent provision for restoration of seabed should be recognised.

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Thanks ....



# IND AS – 108 OPERATING SEGMENTS

## CHAPTER - 23

### 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	<b>External sales (gross)</b>	1,00,000	35,000	1,35,000
	Tax	<u>(2,500)</u>	<u>(1,500)</u>	(4,000)
	External sales (net)	97,500	33,500	1,31,000
	Other operating income	<u>20,000</u>	<u>7,500</u>	27,500
	Total Revenue	<u>1,17,500</u>	<u>41,000</u>	1,58,500
2	<b>Results</b>			
	Segment results	5,000	2,000	7,000
	Unallocated income (net of unallocated expenses)			<u>1,500</u>

	Profit from operation before interest, taxation and exceptional items			8,500
	Interest and bank charges			<u>(1,000)</u>
	Profit before exceptional items			7,500
	Exceptional items			<u>Nil</u>
	Profit before taxation			7,500
	Less: Income Taxes			
	Current taxes			(975)
	Deferred taxes			<u>(25)</u>
	Profit after taxation			<u>6,500</u>
<b>3</b>	<b>Other Information</b>			
<b>(a)</b>	<b>Assets</b>			
	Segment Assets	25,000	15,000	40,000
	Investments			5,000
	Unallocated assets			<u>5,000</u>
	Total Assets			<u>50,000</u>
<b>(b)</b>	<b>Liabilities/Shareholder's funds</b>			
	Segment liabilities	15,000	5,000	20,000
	Unallocated liabilities			10,000
	Share capital			5,000
	Reserves and surplus			<u>15,000</u>
	Total liabilities / shareholder's funds			<u>50,000</u>
<b>(c)</b>	<b>Others</b>			
	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
<b>Total</b>	<b>1,480</b>

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
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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 ( $\text{Rs. } 12,80,000 \times 10\%$ ).

Segment A exceeds the quantitative threshold ( $\text{Rs. } 4,00,000 > \text{Rs. } 1,28,000$ ) and hence is a reportable segment.

Segment D exceeds the quantitative threshold ( $\text{Rs. } 6,90,000 > \text{Rs. } 1,28,000$ ) 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% ( $\text{Rs. } 4,70,000 / 6,40,000 \times 100$ ) 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% ( $\text{Rs. } 5,60,000 / 6,40,000 \times 100$ ) 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  $\text{Rs. } 4,00,000 + \text{Rs. } 80,000 + \text{Rs. } 70,000 = \text{Rs. } 5,50,000$

% 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
O	0	5,250	-750	10,500
P	500	5,500	900	10,500
Q	<u>1,200</u>	<u>1,050</u>	<u>600</u>	<u>5,250</u>
	<u>10,400</u>	<u>35,350</u>	<u>3,750</u>	<u>1,02,750</u>

Heavy Goods Ltd. needs to determine how many reportable segments it has. You are required to advise 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. Its business segments comprise paints (wall paints, 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	<u>(250)</u>	<u>(150)</u>	<u>(400)</u>
	Total Revenue (net)	9,750	3,350	13,100
	Other operating Income	<u>2,000</u>	<u>750</u>	<u>2,750</u>
	Total Revenue	<u>11,750</u>	<u>4,100</u>	<u>15,850</u>
2.	Results			
	Segment results	500	200	700
	Unallocated income (net of unallocated expenses)			<u>150</u>
	Profit from operation before interest, taxation and exceptional items			850
	Interest and bank charges			<u>(100)</u>
	Profit before exceptional items			750
	Exceptional items			<u>Nil</u>
	Profit before taxation			750
	Income Taxes			
	-Current taxes			(97.5)
	-Deferred taxes			<u>(2.5)</u>
	Profit after taxation			<u>650</u>
3.	Other Information			
(a)	Assets			
	Segment Assets	2,500	1,500	4,000
	Investments			500
	Unallocated assets			<u>500</u>
	Total Assets			<u>5,000</u>
(b)	Liabilities/Shareholder's funds			
	Segment liabilities	1,500	500	2,000
	Unallocated liabilities			1,000
	Share capital			500
	Reserves and surplus			<u>1,500</u>
	Total liabilities / shareholder's funds			<u>5,000</u>
(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	<u>100</u>	<u>60</u>	<u>30</u>	<u>5</u>	—	—	—	—
<b>Total</b>	<b><u>100</u></b>	<b><u>315</u></b>	<b><u>45</u></b>	<b><u>15</u></b>	<b><u>15</u></b>	<b><u>50</u></b>	<b><u>25</u></b>	<b><u>35</u></b>
Segment result	<b>5</b>	<b>(90)</b>	<b>15</b>	<b>(5)</b>	<b>8</b>	<b>(5)</b>	<b>5</b>	<b>7</b>
Profit/(Loss)								
Segment assets	<b>15</b>	<b>47</b>	<b>5</b>	<b>11</b>	<b>3</b>	<b>5</b>	<b>5</b>	<b>9</b>

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:

#### Criterion 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	
<b>Reportable segments</b>	<b>A</b>	<b>B</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	
<b>Reportable segments</b>	-	<b>B</b>	<b>C</b>	-	-	-	-	-	

**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)					<b>405</b>
<b>% of reportable segments external sales to entity's sales</b>					<b>69.14%</b>
<b>Required percentage</b>					<b>75%</b>

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.

**Question 8 : Nov 2022 – Paper**

Pharmaceuticals Limited has 5 operating segments namely K, L, M, N and O. The profit / loss of respective segments for the year ended 31<sup>st</sup> March, 2022 are as follows :

Segment	Profit / (Loss) (Rs. in crore)
K	1,560
L	3,000
M	(4,600)
N	(9,000)
O	12,000
<b>Total</b>	<b>2,980</b>

Based on the quantitative thresholds, you are required to determine that which of the above segments would be considered as reportable segments for the year ending March 31, 2022.

**Solution :**

With regard to quantitative thresholds to determine reportable segment relevant in context of instant case, paragraph 13(b) of Ind AS 108 'Operating Segments' 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., K, L and O – Total profit Rs. 16,560 crores.

(ii) All segments in loss, i.e., M and N – Total loss Rs. 13,600 crores.

Greater of the above – Rs. 16,560 crores.

Based on the above, reportable segments will be determined as follows:

Segment	Profit/(Loss) (Rs. in crore)	% age of Rs. 16,560 crore*	Reportable segment
K	1,560	9.42%	No
L	3,000	18.12%	Yes
M	(4,600)	27.78%	Yes
N	(9,000)	54.35%	Yes
O	<u>12,000</u>	72.46%	Yes
Total	<u>2,960</u>		

Hence, L, M, N, O are reportable segments.

### Question 9 : May 2023 – Paper

A Limited operates in coating industry. Its business segments comprise Coating (consisting of decorative, automotive, industrial paints and related activities) and Others (consisting of chemicals, polymers and related activities).

Certain information for Financial Year 2022-2023 is given below :

Segments	External Revenue (including GST)	GST	Other operating Income	Result	Assets	Liabilities
Coating	1,20,000	3,000	24,000	6,000	30,000	18,000
Others	42,000	1,800	9,000	2,400	18,000	6,000

#### Additional Information :

- Unallocated income net of expenses is Rs.18,00,00,000
- Interest and bank charges is Rs.12,00,00,000
- Income tax expenses is Rs.12,00,00,000 (current tax Rs.11,70,00,000 and deferred tax Rs.30,00,000)
- Unallocated Investments are Rs.60,00,00,000 and other assets are Rs.60,00,00,000.
- Unallocated liabilities, Reserve & Surplus and Share Capital are Rs.1,20,00,00,000, Rs.1,80,00,00,000 and Rs.60,00,00,000 respectively.
- Depreciation amounts for coating & others are Rs.6,00,00,000 and Rs.1,80,00,000 respectively.
- Capital expenditure for coating and others are Rs.30,00,00,000 and Rs.12,00,00,000 respectively.
- Revenue from outside India is Rs.3,72,00,00,000 and segment asset outside India Rs.60,00,00,000.

Based on the above information, how A Limited would disclose information about reportable segment, revenue, profit or loss, assets and liabilities for financial year 2022-2023. Ignore corresponding figures for the previous year. Give figures in T lakhs.

#### Solution :

**Segment information**

Information about operating segment

(1) **the company’s operating segments comprise:**

**Coatings:** consisting of decorative, automotive, industrial paints and related activities.

**Others:** consisting of chemicals, polymers and related activities.

(2) **Segment revenues, results and other information:** (Rs.in lakhs)

	<b>Revenue</b>	<b>Coating</b>	<b>Others</b>	<b>Total</b>
1	<b>External revenue (gross)</b>	1,20,000	42,000	1,62,000
	GST	<u>(3,000)</u>	<u>(1,800)</u>	<u>(4,800)</u>
	Total revenue (net)	1,17,000	40,200	1,57,200
	Other operating income	<u>24,000</u>	<u>9,000</u>	<u>33,000</u>
	Total Revenue	<u>1,41,000</u>	<u>49,200</u>	<u>1,90,200</u>
2	<b>Results</b>			
	Segment results	6,000	2,400	8,400
	Unallocated income (net of unallocated expenses)			<u>1,800</u>
	Profit from operation before interest, taxation and exceptional items			10,200
	Interest and bank charges			<u>(1,200)</u>
	Profit before exceptional items			9,000
	Exceptional items			<u>Nil</u>
	Profit before taxation			9,000
	Income taxes			
	Current taxes			(1,170)
	Deferred taxes			<u>(30)</u>
	Profit after taxation			<u>7,800</u>
3	<b>Other information</b>			
(a)	<b>Assets</b>			
	Segment assets	30,000	18,000	48,000
	Investments			6,000
	Unallocated assets			<u>6,000</u>
	Total assets			<u>60,000</u>
(b)	<b>Liabilities and Shareholder’s funds</b>			
	Segment liabilities	18,000	6,000	24,000
	Unallocated liabilities			12,000
	Share capital			6,000
	Reserves and surplus			<u>18,000</u>
	Total liabilities and shareholder’s funds			<u>60,000</u>
(c)	<b>Others</b>			

	Capital expenditure	(3,000)	(1,200)	(4,200)
	Depreciation	(600)	(180)	(780)
<b>Geographical Information</b>		<b>India</b>	<b>Outside India</b>	<b>Outside India</b>
	Revenue	1,53,000	37,200	1,90,200
	Segment assets	54,000	6,000	60,000
	Capital expenditure	4,200		4,200

**Notes:**

- (i) The operating segments have been identified in line with Ind AS 108, taking into account the nature of products, organisation structure, economic environment and internal reporting system.
- (ii) Segment revenue, results, assets and liabilities include the respective amounts identifiable to each of the segments. Unallocable assets include unallocable non-current assets and other current assets. Unallocable liabilities include unallocable current liabilities and net deferred tax liability.

**Question 10 : Nov 2023 – Paper**

Haymond Limited has three segments H, M & D. The following information is provided for the year ending 31st March, 2023:

All amounts are in Rs. Lakhs

Particulars	Segments			Head Office
	H	M	D	
Sales to M	500	-	-	
Sales to D	-	5	-	
Other Sales (Domestic)	10	-	-	
Sales (Export)	680	170	40	
Operating Profit /(Loss) before tax	30	5	(8)	
Reallocated cost from Head Office	4	2	2	
Interest cost	2	3	1	
Fixed Assets*	20	4	12	5
Net Current Assets	12	4	9	3
Long Term Liabilities	2	4	12	2

Other Information:

- (i) Share Capital amounts to Rs. 40,00,000
- (ii) Reserve & Surplus amounts to Rs. 12,00,000

Prepare segment information as per Ind AS 108.

**Solution :**

**(A)** Information about operating segment

- (1) The company's operating segment comprise: H, M & D
- (2) Segment revenue, results and other information

**Haymond Ltd.**  
**Segment Information / Report**

(All amounts are Rs. in lakhs)

Particulars	Reportable Segments			Head Office/ Unallocated items	Total
	H	M	D		
<b>1. Segment Revenue</b>					
Sales:					
Domestic	10	-	-	-	10
Export	<u>680</u>	<u>170</u>	<u>40</u>	-	<u>890</u>
External Sales	690	170	40	-	900
Inter-segment sales	<u>500</u>	<u>5</u>	-	-	<u>505</u>
Total Sales	1,190	175	40	-	1,405
Less: Inter-segment sales	<u>(500)</u>	<u>(5)</u>	-	-	<u>(505)</u>
Total Sales / Revenue	1,190	175	40	-	900
<b>2. Results</b>					
Segment result	30	5	-8		27
Reallocated cost	<u>(4)</u>	<u>(2)</u>	<u>(2)</u>		<u>(8)</u>
Profit from operation before interest, taxation and Exceptional items	26	3	-10		19
Finance cost (Interest expense)	<u>(2)</u>	<u>(3)</u>	<u>(1)</u>		
Profit before tax and exceptional items	<u>24</u>	<u>0</u>	<u>(11)</u>		<u>(6)</u>
<b>3. Information in relation to assets and liabilities</b>					
Reportable segment non- current assets	20	4	12	5	41
Reportable segment net current assets	<u>12</u>	<u>4</u>	<u>9</u>	<u>3</u>	<u>28</u>
Total Assets	<u>32</u>	<u>8</u>	<u>21</u>	<u>8</u>	<u>69</u>
Non-current liabilities	2	1	12	2	17

**(B) Geographical Information**

	Domestic Sales	Export Sales	Rs in lakhs Total
External sales	10	890	900

Thanks ....



# IND AS – 113

## FAIR VALUE

### MEASUREMENT

## CHAPTER - 24

### 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:

- The fair value of the asset, if market A is the principal market, and
- 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	<u>72</u>

#### (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	<u>(6)</u>	<u>(6)</u>
Fair value of the asset	<u>63</u>	<u>66</u>

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	<u>(6)</u>
Fair value of the asset	<u>69</u>

**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**

	<b>Rs.</b>
Price receivable	290
Less: Transportation cost	<u>(30)</u>
Fair value of the asset	<u>260</u>

(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:**

	<b>Rs.</b>	<b>Rs.</b>
	<b>Mumbai</b>	<b>Kolkata</b>
Price receivable	290	280
Less: Transaction cost	(40)	(20)
Less: Transportation cost	<u>(30)</u>	<u>(30)</u>
Fair value of the asset	<u>220</u>	<u>230</u>

Since Kolkata has maximum return fair value will be calculated using Kolkata.

**Fair value of the asset will be**

	<b>Rs.</b>
Price receivable	280
Less: Transportation cost	<u>(30)</u>
Fair value of the asset	<u>250</u>

(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%	<u>47.25</u>
<b>Total Expected Cash Flows before inflation</b>		<b><u>283.50</u></b>
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)	<u>20.98</u>
<b>Total Expected Cash Flows</b>	419.65+20.98)	440.63
Discount rate to be considered = risk-free rate entity's non-performance risk	5% + 3.5%	8.5%
<b>Expected present value at 8.5% for 10 years</b>	<b>440.63 / (1.085<sup>10</sup>)</b>	<b>194.88</b>

**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		<b>131.25 Cr</b>

**Question 5 : May 2022 – Paper**

Shravan Ltd. owns 6,800 ordinary shares in PQR Ltd, an unquoted company. PQR Ltd. has a total share capital of 2,00,000 shares with nominal value of Rs.10. PQR Ltd's after tax maintainable profit are estimated at Rs.28,00,000 per year. An appropriate price/earnings ratio determined from published industry date is 12 (before lack of marketability adjustment). Shravan Ltd's management estimates that the discount for the lack of marketability of PQR Ltd's share and restrictions on their transfer is 18%.

Shravan Ltd values its holding in PQR Ltd's shares based on earnings. Determine the fair value of Shravan Ltd's investment in PQR Ltd's shares.

**Solution :**

**Calculation of an earnings-based valuation of Shravan Ltd.'s holding of shares in PQR Ltd.:**

Particulars		Rs.
PQR Ltd.'s after-tax maintainable profits	(A)	Rs. 28,00,000
Price / Earnings ratio	(B)	12
Adjusted discount factor (1- 0.18)	(C)	0.82
Value of PQR Ltd.	(A) x (B) x (C)	Rs. 2,75,52,000

Value of a share of PQR Ltd. = Rs. 2,75,52,000 / 2,00,000 shares = Rs. 137.76

The fair value of Shravan Ltd.'s investment in PQR Ltd.'s shares is estimated at Rs. 9,36,768 (that is, 6,800 shares x Rs. 137.76 per share).

**Alternative way of presentation :**

Particulars		
PQR Ltd.'s after-tax maintainable profits in Rs.	(A)	28,00,000
PQR Ltd.'s number of outstanding shares	(B)	2,00,000
PQR Ltd.'s EPS in Rs.	(C = (A/B))	14
Industry PE ratio (given)	(D)	12
Market price of PQR Ltd. per share in Rs.	(E = (C x D))	168
Discount for lack of marketability @ 18% in Rs.	(F = E x 18%)	30.24
Adjusted price per share of PQR Ltd. in Rs.	(G = (E-F))	137.76
Shravan Ltd.'s holding	(H)	6,800 shares
Fair value of Shravan's investment in PQR Ltd.	(G x H)	9,36,768.00

**Question 6 : Nov 2022 – Paper**

Silver Ltd. is in the process of acquiring shares of Blue Ltd. as a part of business reorganization Plan. The projected free cash flow of Blue Ltd. for the next 5 years is as follows :

Particulars	Year 1	Year 2	Year 3	Year 4	Year 5
Cash flows	280.65	281.40	182.70	403.50	518.20
Terminal value					5,945

The weighted average cost of capital of blue Ltd. is 10%. The total debt as on measurement date is Rs.2,195 crores and the surplus cash and cash equivalent is Rs.159.21 crore.

The total number of shares of Blue Ltd. as on the measurement date is 12.80 crore.

You are required to determine the value per share of Blue Ltd. as per Income Approach of Ind AS 113.

(Present value factor of Rs.1 should be taken upto 4 decimals for the purpose of calculation)

**Solution :**

**Determination of Equity Value of Blue Ltd.**

(Rs. in crore)

Particulars	Year 1	Year 2	Year 3	Year 4	Year 5
Cash flows	280.65	281.40	182.70	403.50	518.20
Terminal value					5945
	280.65	281.40	182.70	403.50	6463.20
Discount rate @ 10%	0.9091	0.8264	0.7513	0.6830	0.6209
Free cashflow available to the firm	255.14	232.55	137.26	275.59	4013.00
Total of all years					4913.54
Less: Debt					(2,195.00)
Add: Cash & cash equivalent					159.21
Equity value of PT Ltd.					2,877.75
No. of shares (in crore)					12.80 Cr.
Per share value (Rs. 2,877.75 Cr. / 12.80 Cr)					Rs. 224.82

**Question 6 : May 2025 – Paper**

Investors Ltd. is in the process of acquisition of shares of Glue Ltd. as part of business reorganization plan. The projected free cash flows of Glue Ltd. for the next 5 years are as follows:

(Rs. in lakhs)

Particulars	Year 1	Year 2	Year 3	Year 4	Year 5
Cash flows	420	418	272	606	777
Terminal value					8,919

The weighted average cost of capital of Glue Ltd. is 12%. The total debt as on measurement date is Rs. 3,294 lakhs and the surplus cash and cash equivalents is Rs. 240 lakhs. The total number of shares of Glue Ltd. as on the measurement date is Rs. 20 lakhs\* .

You are required to determine the value per share of Glue Ltd. as per Income Approach as enunciated in Ind AS 113, Fair Value Measurement.

Compute value per share upto 2 decimal points.

Present value factor of Rs. 1 at 12% is as under:

Year 1	Year 2	Year 3	Year 4	Year 5
0.8929	0.7972	0.7118	0.6355	0.5674

**Solution :**

**Determination of equity value of Glue Ltd.**

(Rs. in lakhs)

Particulars	Year 1	Year 2	Year 3	Year 4	Year 5
Cash flows	420.0000	418.0000	272.0000	606.0000	777.0000
Terminal value	420.0000	418.0000	272.0000	606.0000	8,919.0000
	0.8929	0.7972	0.7118	0.6355	9,696.0000
Discount rate factor	375.0180	333.2296	193.6096	385.1130	0.5674
Free cash flow available to the firm	375.0180	333.2296	193.6096	385.1130	5,501.5104
Total of all years discounted cashflows					6,788.4806
Less: Debt					(3,294.0000)
Add: Cash & cash equivalents					<u>240.0000</u>
Equity value of Glue Ltd.				(A)	<u>3,734.4806</u>
Number of shares				(B)	20,00,000
Per share value				(A/B)	186.72403

Thanks ....



# IND AS – 101

## FIRST TIME ADOPTION

### CHAPTER - 25

#### 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 voluntarily 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
<b>Shareholder's Funds</b>		
Share Capital	7,953	7,953
Reserves & Surplus	16,547	16,597
<b>Non-Current Liabilities</b>		
Long Term Borrowings	1,000	1,000
Long Term Provisions	1,101	691
Other Long-Term Liabilities	5,202	5,904
<b>Current Liabilities</b>		
Trade Payables	9,905	8,455
Short Term Provisions	500	475
<b>Total</b>	<b>42,208</b>	<b>41,075</b>
<b>Non-Current Assets</b>		
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
<b>Current Assets</b>		
Trade Receivables	4,801	1,818
Investments	1,263	3,763
Other Current Assets	1,554	104
<b>Total</b>	<b>42,208</b>	<b>41,075</b>

**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	<u>50</u>
Total Assets	2054
Less: Trade Payables	75
Short Term Provisions	<u>35</u>
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	<u>104</u>
Total Assets	32,067

Less: Trade Payables	8,455
Short Term Provisions	<u>475</u>
	<u>23,137</u>

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
<b>Non-Current Assets</b>			
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
<b>Current Assets</b>			
Trade Receivables	1,818	(280)	1,538
Investments	3,763	-	3,763
Other Current Assets	104	(50)	54
<b>Total</b>	<b>41,075</b>	<b>(110)</b>	<b>40,965</b>
<b>Shareholder's Funds</b>			
Share Capital	7,953	-	7,953
Reserves & Surplus	16,597	-	16,597
<b>Non-Current Liabilities</b>			
Long Term Borrowings	1,000		1,000
Long Term Provisions	691		691
Other Long-Term Liabilities	5,904		5,904
<b>Current Liabilities</b>			
Trade Payables	8,455	(75)	8,380
Short Term Provisions	475	(35)	440
<b>Total</b>	<b>41,075</b>	<b>(110)</b>	<b>40,965</b>

### 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	<u>0.75</u>	<u>57.03</u>	102.03
<b>Balance total equity as on 1st April, 20X1 after transition to Ind AS</b>			<u>182.03</u>

**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		<u>25</u>
		105
Reserves and Surplus		<u>95</u>
Total Equity as per AS		200
<b>Adjustment due to reclassification</b>		

Preference share capital classified as financial liability		(25)
<b>Adjustment due to derecognition</b>		
Proposed Dividend not considered as liability as 1st April 20X1		0.78
<b>Adjustment due to remeasurement</b>		
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	<u>0.75</u>	<u>6.25</u>
<b>Equity as on 1st April, 20X1 after transition to Ind AS</b>		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	<u>6</u>
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)	<u>74.80</u>
Total liability component on each debenture (A)	93.82
Total equity component per debenture (Balancing figure) (B) = (C) – (A)	<u>6.18</u>
Face value per debenture (C)	<u>100.00</u>
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:**

- 3.17 is annuity factor of present value of Re. 1 at a discount rate of 10% for 4 years.
- 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.	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 dividend 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
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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.
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**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

### **Question 10 : May 2023 – RTP**

ABC Ltd., a public limited company, is in the business of exploration and production of oil and gas and other hydrocarbon related activities outside India. It operates overseas projects directly and/or through subsidiaries, by participation in various joint arrangements and investment in associates. The company was following Accounting Standards as notified under the Companies (Accounting Standards) Rules until 31st March, 20X1. However, it has adopted Indian Accounting Standards (Ind AS) with effect from 1st April, 20X1.

The goodwill recognised in accordance with AS 21 and AS 27 was due to corporate structure and the line-by-line consolidation of subsidiaries'/proportionate consolidation of jointly controlled entities' financial statements which was prepared on historical costs convention. ABC Ltd. has not taken into consideration the valuation of underlying oil and gas reserves for which excess amount (i.e. goodwill calculated as per the relevant AS requirements) has been paid by the company at the time of acquisition. The company further considered that in oil and gas companies, the goodwill generated on acquisition of mineral rights either through jointly controlled entities or subsidiaries, inherently derives its value from the underlying mineral rights and, accordingly, value of such goodwill depletes as the underlying mineral resources are extracted.

Therefore, taking a prudent approach and considering the above substance, the company amortised the goodwill in respect of its subsidiaries / jointly controlled assets over the life of the underlying mineral rights using Unit of Production method. This allowed the company to utilise

the value of goodwill over the life of mineral rights and completely charging off the goodwill over the life of the reserves.

For financial year 20X0-20X1, the company has availed transition exemption under Ind AS 101 and has not applied the principles of Ind AS 103.

ABC Ltd. considering the substance over form of the goodwill to be in the nature of 'acquisition costs' intends to continue amortisation of the goodwill recognised under AS in respect of its subsidiaries / joint ventures (jointly controlled entities under AS) over the life of the underlying mineral rights using Unit of Production method, under Ind AS also post transition date.

Comment on appropriateness of the accounting treatment, under Ind AS, for amortisation of the goodwill by the company and state whether the accounting treatment in respect of amortisation of goodwill is correct or not.

### **Solution :**

Point (g) of para C4 of Ind AS 101 states that the carrying amount of goodwill or capital reserve in the opening Ind AS Balance Sheet shall be its carrying amount in accordance with previous GAAP at the date of transition to Ind AS after the two adjustments. One of the adjustment states that the standard requires the first-time adopter to recognise an intangible asset that was subsumed in recognised goodwill or capital reserve in accordance with previous GAAP, the first-time adopter shall decrease the carrying amount of goodwill or increase the carrying amount of capital reserve accordingly (and, if applicable, adjust deferred tax and non-controlling interests)

As per the facts given, the entity paid excess amount to avail the rights to use the underlying oil and gas reserves. However, since the rights was not recorded in the books at that time, the value of goodwill subsumed the value of that intangible asset

which should be separately identified in the books. Hence, value of goodwill will be reduced accordingly and intangible asset for rights for using mine should be recognised

Further, regardless of whether there is any indication that the goodwill may be impaired, the first-time adopter shall apply Ind AS 36 in testing the goodwill for impairment at the date of transition to Ind AS and in recognising any resulting impairment loss in retained earnings (or, if so required by Ind AS 36, in revaluation surplus). The impairment test shall be based on conditions at the date of transition to Ind AS. No other adjustments (eg- previous amortisation of goodwill) shall be made to the carrying amount of goodwill / capital reserve at the date of transition to Ind AS.

However, once goodwill is recognised in the opening transition date balance sheet, the entity has to follow the provisions of Ind AS, which states that goodwill is not amortised but rather tested for impairment annually. Accordingly, the amortization of goodwill based on 'Unit of Production' method is not correct after implementation of Ind AS.

### **Question 11 : Nov 2023 – Paper**

Diamond Limited is transitioning to Ind AS. It has certain investments in Ruby Limited's Convertible Debt Instruments, which are currently (on the date of transition to Ind AS) exercisable and would provide Diamond Limited with a controlling stake over Ruby Limited on exercise of the conversion rights. Diamond Limited evaluated that Ruby Limited should be treated as its subsidiary under Ind AS. Hence it would require consolidation in its Ind AS Consolidated Financial

Statements. Ruby Limited was not considered as a Subsidiary, Associate or a Joint Venture under Previous GAAP.

How should Ruby Limited be consolidated on transition to Ind AS. Assume that Diamond Limited has opted to avail the exemption from retrospective re-statement of past business combinations as per applicable Ind AS?

**Solution :**

Ind AS 101 prescribes an optional exemption from retrospective restatement in relation to past business combinations. Ind AS 101 prescribes that when the past business combinations are not restated and a parent entity had not consolidated an entity as a subsidiary in accordance with its previous GAAP (either because it was not regarded as a subsidiary or no consolidated financial statements were required under previous GAAP), then the subsidiary's assets and liabilities would be included in the parent's opening consolidated financial statements at such values as would appear in the subsidiary's separate financial statements if the subsidiary were to adopt the Ind AS as at the parent's date of transition. For this purpose, the subsidiary's separate financial statements would be prepared as if it was a first-time adopter of Ind AS i.e. after applying the relevant first-time adoption mandatory exceptions and voluntary exemptions. In other words, the parent will adjust the carrying amount of the subsidiary's assets and liabilities to the amounts that Ind AS would require in the subsidiary's balance sheet.

The deemed cost of goodwill equals the difference at the date of transition between:

- (a) the parent's interest in those adjusted carrying amounts; and
- (b) the cost in the parent's separate financial statements of its investment in the subsidiary.

The measurement of non-controlling interest and deferred tax follows from the measurement of other assets and liabilities.

It may be noted here that the above exemption is available only under those circumstances where the parent, in accordance with the previous GAAP, has not presented consolidated financial statements for the previous year; or where the consolidated financial statements were prepared in accordance with the previous GAAP, but the entity was not treated as a subsidiary, associate or joint venture under the previous GAAP.

**Question 12 : May 2024 – Paper**

A Limited has chosen to elect the deemed cost exemption for carrying value of its property, plant and equipment as per previous GAAP in accordance with Ind AS 101. However, it does not wish to select the exemption available as per Ind AS 101 of capitalising exchange fluctuation on long-term foreign currency monetary items to property, plant and equipment and accordingly, it did not opt to avail the exemption available as per Ind AS 101 for previous GAAP policy of capitalizing exchange fluctuation to PPE.

In such a case, how would the company be required to treat the foreign exchange fluctuation already capitalised to the cost of property, plant and equipment under previous GAAP and also what will be the treatment of fluctuation on long-term foreign currency monetary items on transition date and after the transition date to Ind AS by the company in light of the above options exercised by the company?

**Solution :**

Ind AS 101 permits to continue with the carrying value for all of its property, plant and equipment as per the previous GAAP and use that as deemed cost for the purposes of first-time adoption of Ind AS. Accordingly, the carrying value of property, plant and equipment as per previous GAAP as at the date of transition need not be adjusted for the exchange fluctuations capitalized to property, plant and equipment.

Separately, it allows a company to continue with its existing policy for accounting for exchange differences arising from translation of long-term foreign currency monetary items recognised in the financial statements for the period ending immediately before the beginning of the first Ind AS financial reporting period as per the previous GAAP.

Accordingly, given that Ind AS 101 provides these two choices independent of each other, it may be possible for an entity to choose the deemed cost exemption for all of its property, plant and equipment and not elect the exemption of continuing the previous GAAP policy of capitalising exchange fluctuation to property, plant and equipment.

In such a case, a harmonious interpretation of the two exemptions would require the company to recognise the property, plant and equipment at the transition date at the previous GAAP carrying value (without any adjustment for the exchanges differences capitalized under previous GAAP)

But, for the purposes of the first (and all subsequent) Ind AS financial statements, foreign exchange fluctuation on all long-term foreign currency borrowings that arose after the transition date would be recognised in the statement of profit and loss.

**Question 13 : Nov 2024 – Paper**

Z Limited having net worth of Rs.25 crores has opted voluntarily to adopt Ind AS from 1st April, 2022 in accordance with the Companies (Indian Accounting Standard) Rules 2015.

Mr. A, the senior manager, of Z Limited 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:

- (i) 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 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.6,00,000.
- (ii) 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.2,80,000 as against the carrying amount of loan which at present equals rs.3,00,000.

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 Z 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 and its impact there upon for preparation of transition date balance sheet. Also pass journal entry for each of the issues mentioned above.

**Solution :**

**Assessment of Preliminary Impact Assessment on transition to Ind AS of Z Ltd.'s Financial Statements**

**(i) 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, the book value should be brought up to fair value. The resulting impact of fair valuation of land Rs. 1,00,000 should be adjusted in other equity.

**Journal Entry on the date of transition**

Particulars	Debit (Rs.)	Credit (Rs.)
Property, Plant and Equipment Dr. To Revaluation Surplus (OCI- Other Equity) (Being PPE recorded at fair value on the date of transition to Ind AS)	1,00,000	1,00,000

**(ii) 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	Fair value as on the date of transition is Rs. 2,80,000 as against its book value of Rs. 3,00,000. Accordingly, the difference of Rs. 20,000 is adjusted through retained earnings.

	amount of that financial asset or the new amortised cost of that financial liability.	
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**Journal Entry on the date of transition**

Particulars	Debit (Rs.)	Credit (Rs.)
Borrowings / Loan payable <span style="float: right;">Dr.</span>	20,000	
To Retained earnings		20,000
(Being Borrowings recorded at fair value on date of transition to Ind AS)		

**Question 14 : Sept 2025 – Paper**

Bee Kay Limited has voluntarily opted to adopt Indian Accounting Standards (Ind AS) from 1st April, 2025 in accordance with the Companies (Indian Accounting Standards) Rules, 2015.

The management has identified the following issues and has sought your guidance so that the Opening Ind AS Balance Sheet as on the date of transition can be prepared:

- (i) Property, Plant and Equipment (PPE) comprise land held for capital appreciation purposes costing Rs. 15,00,000 and qualifies to be treated as Investment Property as per Ind AS. Besides Exchange differences of Rs. 1,50,000 were capitalized to depreciable PPE on which accumulated depreciation of Rs. 37,500 was recognized. The management intends to avail deemed cost exemption for using the previous GAAP carrying values as deemed cost at the date of transition.
- (ii) Bee Kay Limited had acquired 70% shares of X Private Limited a few years ago thereby acquiring the control upon it at that time. It recognized a goodwill of Rs. 1,25,000 as per the erstwhile Accounting Standard by accounting the excess of consideration paid over the net assets acquired at the date of acquisition. Fair value exercise was not done at the time of acquisition.
- (iii) Company had given a loan of Rs. 10,00,000 at an interest rate of 7% per annum to an entity six years ago. Transaction costs were incurred separately for this loan. The loan is repayable in 10 equal instalments over the period of ten years along with accrued interest at the close of each year. The fair value of the loan as on the date of transition is Rs. 5,00,000 against the carrying amount of Rs. 4,00,000. The management says that it is a tedious task to compute the value of the loan by applying the effective interest rate method and has expressed its reluctance in doing so.

You are required to state necessary explanation for each of the items presented by the management of Bee Kay Limited in the form of notes, which may or may not require the adjustment on the date of transition.

**Solution :**

- (i) **Property, Plant & Equipment:** Since the land held for capital appreciation purposes qualifies as investment property, such investment property should be reclassified from

property, plant and equipment (PPE) to investment property and presented separately. As the Company has adopted the previous GAAP carrying values as deemed cost, all items of PPE and investment property should be carried at its previous GAAP carrying values of Rs. 15,00,000. As such, the past capitalised exchange differences require no adjustment in this case.

- (ii) **Goodwill:** Ind AS 103 mandatorily requires measuring the assets and liabilities of the acquiree at its fair value as on the date of acquisition. However, a first-time adopter may elect not to apply the provisions of Ind AS 103 with retrospective effect that occurred prior to the date of transition to Ind AS. Hence, company can continue to carry the goodwill in its books of account as per the previous GAAP.
- (iii) **Loan:** Para B8C of Ind AS 101 states that if it is impracticable (as defined in Ind AS 8) 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 at the date of transition to Ind AS. Accordingly, Rs. 5,00,000 would be the gross carrying amount of loan and difference of Rs. 1,00,000 (Rs. 5,00,000 – Rs. 4,00,000) would be adjusted to retained earnings.

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Thanks ....



# IND AS – 102

## SHARE BASED PAYMENTS

### CHAPTER - 26

#### 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. When vesting conditions are attached to the share based payment plans

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. When no vesting period / condition is attached or to be fulfilled

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
				<b>19,93,600</b>

**Journal Entries**

Date		Dr.(Rs.)	Cr.(Rs.)
1st April, 2015	Employee benefits expenses Dr. To Share based payment liability (Fair value of the SAR recognized initially)	19,00,000	19,00,000
31st March, 2016	Employee benefits expenses Dr. To Share based payment liability (Fair value of the SAR re-measured)	1,90,000	1,90,000
31st March, 2017	Share based payment liability Dr. To Employee benefits expenses (Fair value of the SAR re-measured & reversed)	1,21,200	1,21,200
31st March, 2018	Employee benefits expenses Dr. To Share based payment liability (Fair value of the SAR remeasured & recognized)	24,800	24,800
	Share based payment liability Dr. To Cash (Settlement of SARs in cash)	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	<u>(18)</u>	<u>(14)</u>	—

(d)	Year end – No of employees (a-b-c)	<u>360</u>	<u>348</u>	<u>353</u>
(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 <u>- 21,96,000</u> <u>6,34,400</u>	$\frac{360 \times 200 \times 61}{3} \times 3$ = 43,06,600 <u>- 28,30,400</u> <u>14,76,200</u>

### Journal Entries

		Rs.	Rs.
<b>31st March, 2016</b>			
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)			
<b>31st March, 2017</b>			
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)			
<b>31st March, 2018</b>			
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)			
<b>31st March, 2019</b>			
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 To Employee benefits expenses A/c (Employee benefits expenses transferred to Profit and Loss A/c)	Dr.	11,07,150	11,07,150
Share based payment reserve (equity) (353 x 200 x 61) To Share Capital (Share capital Issued)	Dr.	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 (200 × 100 employees × Rs.30 × 80% × ½) To Equity (Contribution from the parent)	Dr.	2,40,000	2,40,000
<b>Year 2</b>			
Remuneration expense [(200 x 81 employees x Rs.30) – 2,40,000] To Equity (Contribution from the parent)	Dr.	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**  

$$= \frac{1,850 \times 1,000 \times 1.2}{3} \times 1 = 7,40,000$$

b) **Year 12 – 13**  

$$= \frac{1,840 \times 1,000 \times 1.2}{3} \times 2 = 14,72,000 - 7,40,000$$

$$= 7,32,000$$

$$= \frac{1,840 \times 1,000 \times (1.05 - 0.9)}{1.5} \times 0.5 = \underline{92,000}$$

$$8,24,000$$

**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	Dr.	2,16,000	
To Share based payment liability (Fair value of the SAR recognized)			2,16,000
31 December 20X6			
Employee benefits expenses	Dr.	72,000	
To Share based payment liability (Fair value of the SAR re-measured)			72,000
31 December 20X7			
Employee benefits expenses	Dr.	1,62,000	
To Share based payment liability (Fair value of the SAR recognized)			1,62,000
Share based payment liability	Dr.	60,000	
To Cash (Settlement of SAR)			60,000
31 December 20X8			
Share based payment liability	Dr.	30,000	
To Employee benefits expenses (Fair value of the SAR recognized)			30,000
Share based payment liability	Dr.	3,60,000	
To Cash (Settlement of SAR)			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 2<sup>nd</sup> 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)		<u>(22,80,000)</u>
Balance transferred to Profit and Loss		<u>2,85,000</u>

**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

**Question 10 : Nov 2022 – RTP**

The following particulars in respect of stock options granted by a company are available:

No. of Employees covered	400	Nominal Value per share	Rs.100
No. of options per Employee	60	Exercise price per share	Rs.125

Shares offered were put in three groups. Group 1 was for 20% of shares offered with vesting period one-year. Group II was for 40% of shares offered with vesting period two-years. Group III was for 40% of shares offered with vesting period three-years. Fair value of option per share on grant date was Rs. 10 for Group I, Rs. 12.50 for Group II and Rs. 14 for Group III.

Position on 1st Year	Position on 2nd Year	Position on 3rd Year
No. of employees left = 40	Employees left = 35	Employees left = 28
Estimate of employees to leave in Year 2 = 36	Estimate of employees to leave in Year 3 = 30	Employees exercising Options in Group III = 295
Estimate of employees to leave in Year 3 = 34	Employees exercising Options in Group II = 319	
Employees exercising Options in Group I = 350		

Options not exercised immediately on vesting, were forfeited. Compute expenses to recognise in each year and show important accounts in the books of the company.

**Solution :**

**Total number of Options per employee = 60**

Group I - 20% vesting in Year <b>1</b>	Group II - 40% vesting in Year <b>2</b>	Group III - 40% vesting in Yr. <b>3</b>
= 12 options, Vesting period = 1 Yr.	= 24 options, Vesting period = 2 Yrs.	= 24 options, Vesting period = 3 Yrs.

**Computation of Expenses for all the years**

Group = No. of Options	Group I = 12 Options	Group II = 24 Options		Group III = 24 Options		
	Year 1	Year 1	Year 2	Year 1	Year 2	Year 3
(a) Employees at year end = [Opening No. of Employees - Forfeiture]	400 - 40 = 360	400 - 40 = 360	360 - 35 = 325	400 - 40 = 360	360 - 35 = 325	325 - 28 = 297
(b) Expected to leave in future	NA	36	NA	36 + 34 = 70	30	NA
(c) No. of employees eligible (a - b)	360	324	325	290	295	297
(d) Options expected to Vest = [(c) x No. of Shares]	(360 x 12 sh.) 4,320	(324 x 24 sh.) 7,776	(325 x 24 sh.) 7,800	(290 x 24 sh.) 6,960	(295 x 24 sh.) 7,080	(297 x 24 sh.) 7,128

(e) FV per option =	Rs.10	Rs.12.50	Rs.12.50	Rs.14	Rs.14	Rs.14
(f) Value of Total Options = [d x e]	Rs. 43,200	Rs. 97,200	Rs. 97,500	Rs. 97,440	Rs. 99,120	Rs. 99,792
(g) Total Cumulative Cost of Options = [(f) x Completed Yrs/ Total Yrs)	Rs. 43,200	[(f) x 1/2] Rs. 48,600	[(f) x 2/2] Rs. 97,500	[(f) x 1/3] Rs.32,480	[(f) x 2/3] Rs.66,080	[(f) x 3/3] Rs. 99,792
(h) Less: Recognized in last years	0	0	Rs. 48,600	0	Rs.32,480	Rs. 66,080
<b>(i) Expenses to be recognized</b>	<b>Rs. 43,200</b>	<b>Rs. 48,600</b>	<b>Rs. 48,900</b>	<b>Rs.32,480</b>	<b>Rs.33,600</b>	<b>Rs. 33,712</b>
<b>(j) Employees not exercising ESOP</b>	10 Employees	325 - 319 = 6 Employees		297 - 295 = 2 Employees		
(k) Total Expenses for-						
<b>Year 1</b>	Rs. 43,200 (Gr. 1) + Rs. 48,600 (Gr. 2) + Rs. 32,480 (Gr. 3) = Rs. 1,24,280					
<b>Year 2</b>	Rs. 48,900 (Gr. 2) + Rs. 33,600 (Gr. 3) = Rs. 82,500					
<b>Year 3</b>	Rs. 33,712 (Gr. 3 only)					

### Employees Benefit Expenses A/c

#### Year 1

	Rs.		Rs.
To Share-based Payment Reserve A/c	1,24,280	By Profit and Loss A/c	1,24,280
	<b>1,24,280</b>		<b>1,24,280</b>

#### Year 2

	Rs.		Rs.
To Share-based Payment Reserve A/c	82,500	By Profit and Loss A/c	82,500
	<b>1,24,280</b>		<b>1,24,280</b>

#### Year 3

	Rs.		Rs.
To Share-based Payment Reserve A/c	33,712	By Profit and Loss A/c	33,712
	<b>33,712</b>		<b>33,712</b>

### Share-based Payment Reserve A/c

#### Year 1

	Rs.		Rs.
To Retained Earnings [(360 - 350) Emp x 12 Options x Rs. 10]	1,200	By Employees Benefit Expenses A/c	1,24,280

To Share Capital (350 Emp x 12 Options x Rs. 100)	4,20,000	By Bank A/c (350 Emp x 12 Options x Rs. 125)	5,25,000
To Securities Premium (350 Emp x 12 Options x Rs. 35)	1,47,000		
To Balance c/d	81,080		
	<b>6,49,280</b>		<b>6,49,280</b>

**Year 2**

	Rs.		Rs.
To Retained Earnings [(325 - 319) Emp x 24 Options x Rs. 12.50]	1,800	By Balance b/d	81,080
To Share Capital (319 Emp x 24 Options x Rs. 100)	7,65,600	By Employees Benefit Expenses A/c	82,500
To Securities Premium (319 Emp x 24 Options x Rs. 37.50)	2,87,100	By Bank A/c (319 Emp 24 Options x Rs. 125)	9,57,000
To Balance c/d	66,080		
	<b>11,20,580</b>		<b>11,20,580</b>

**Year 3**

	Rs.		Rs.
To Retained Earnings [(297 - 295) Emp x 24 Options x Rs. 14]	672	By Balance b/d	66,080
To Share Capital (295 Emp x 24 Options x Rs. 100)	7,08,000	By Employees Benefit Expenses A/c	33,712
To Securities Premium (295 Emp x 24 Options x Rs. 39)	2,76,120	By Bank A/c (295 Emp x 24 Options x Rs. 125)	8,85,000
	<b>9,84,792</b>		<b>9,84,792</b>

**Working Note:**

	Group I Year 1	Group II Year 2	Group III Year 3
Exercise Price received per share	125.00	125.00	125.00
Value of service received per share, being the FV of the Options	<u>10.00</u>	<u>12.50</u>	<u>14.00</u>
Total Consideration received per share	135.00	137.50	139.00
Less: Nominal Value per share	<u>(100.00)</u>	<u>(100.00)</u>	<u>(100.00)</u>
Securities Premium per share	<u>35.00</u>	<u>37.50</u>	<u>39.00</u>

**Question 11 : Nov 2022 – Paper**

On 1<sup>st</sup> April, 2019 Sun Ltd. issued share-based option to one of its key managerial personnel (employee) which can be exercised either in cash or equity and it has following features :

**Option I**

No. of cash settled shares	70,000
Service condition	3 years

**Option II**

No. of equity settled shares of face value of Rs.100 each	80,000
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**Conditions :**

Service	3 years
Restriction to sell	2 years

**Fair Values :**

Share alternative fair value (with restriction)	Rs.125
Fair value at grant date	Rs.136
Fair value on 31 <sup>st</sup> March, 2020	Rs.141
Fair value on 31 <sup>st</sup> March, 2021	Rs.143
Fair value on 31 <sup>st</sup> March, 2022	Rs.146

You are required to pass the journal entries if the key managerial employees exercises cash option at the end of 31<sup>st</sup> March, 2022 and also if he exercises equity at the end of 31<sup>st</sup> March, 2022.

**Solution :**

	1st April 2019 (Rs.)	31st March 2020 (Rs.)	31st March 2021 (Rs.)	31st March 2022 (Rs.)
Equity alternative (80,000 x 125)	1,00,00,000			
Cash alternative (70,000 x 136)	95,20,000			
Equity option (1,00,00,000 – 95,20,000)	4,80,000			
Cash option (cumulative) (using period end fair value)		(70,000 x 141 x 1/3) 32,90,000	(70,000 x 143 x 2/3) 66,73,333	(70,000 x 146 x 3/3) 1,02,20,000
Equity option (cumulative)		(4,80,000 x 1/3) 1,60,000	(4,80,000 x 2/3) 3,20,000	(4,80,000 x 3/3) 4,80,000

Expense for the period			
Equity option	1,60,000	(3,20,000 – 1,60,000) 1,60,000	(4,80,000 – 3,20,000) 1,60,000
Cash Option	32,90,000	(66,73,333 – 32,90,000) <u>33,83,333</u>	(1,02,20,000 – 66,73,333) <u>35,46,667</u>
Total	<u>34,50,000</u>	<u>35,43,333</u>	<u>37,06,667</u>

**Journal Entries**

		Rs.	Rs.
<b>(i) If Cash alternative is chosen:</b>			
Share based payment liability	Dr.	1,02,20,000	
To Bank/ Cash			1,02,20,000
(Settlement in cash)			
Share based payment reserve (equity)*	Dr.	4,80,000	
To Retained earnings			4,80,000
(Being transfer of equity from one account to another one)			
<b>(ii) If Equity alternative is chosen:</b>			
Share based payment liability	Dr.	1,02,20,000	
To Share based payment reserve (equity)			1,02,20,000
(Being transfer of liability account to equity)			
Share based payment reserve (equity)	Dr.	1,02,20,000	
To Capital			80,00,000
To Securities Premium			27,00,000
(Being settlement made in equity)			
Alternative entries under equity settlement:			
<b>(ii) If Equity alternative is chosen:</b>			
Share based payment liability	Dr.	1,02,20,000	
To Share Capital			80,00,000
To Securities Premium			27,00,000
(Being settlement made in equity)			
Share based payment reserve (equity)*	Dr.	4,80,000	
To Retained earnings			4,80,000
(Being transfer of equity from one account to another one)			

\*The equity component recognized (Rs. 4,80,000) shall remain within equity.

**Question 12 : May 2023 – RTP**

Entity A runs a copper-mining business. Entity A has a year-end of 31st March. Dividends declared on the shares accrue to the employees during the three-year period. If the condition is met, the employees will receive the shares together with the dividends that have been declared on those shares during the three years upto 31st March, 20X3.

The entity estimates that on 1st April, 20X0 its shares are valued at Rs. 10 each. The grant date fair amount of each share is Rs. 10. Entity A prepares annual financial statements for the year ended 31st March and:

- on 1st April, 20X0 it estimates that 800 shares will vest;
- at the end of the first year (31st March, 20X1) it has revised this estimate to 780;
- at 31st March, 20X2 it has further revised this estimate to 750; and

- 750 shares vest on 31st March, 20X3 based on the number of employees still employed on that date.

On 1st April, 20X0 as part of a long-term incentive scheme, Entity A provisionally awards its sales employees 1,000 Entity A's shares receivable on 31st March, 20X3.

Explain the accounting treatment for the above share-based awards based on satisfaction of the condition that the sales employees must remain in employment until 31st March, 20X3. The requirement to remain in employment is a service condition and would not be reflected in the fair value of the share awards.

### Solution :

The grant date fair value amount would be recognised as an expense over the three-year service period adjusted by the number of shares expected to vest. Consequently, for each period, Entity A estimates how many eligible employees are expected to be employed on 31st March, 20X3 and this forms the basis for that adjustment. The journal entries would be:

#### Year 1 (Year ended 31st March, 20X1)

Employee benefit expenses A/c	Dr.	Rs. 2,600	
To Share-based payment reserve			Rs. 2,600

(To recognise the receipt of employee services in exchange for shares )

#### Year 2 (Year ended 31st March, 20X2)

Employee benefit expenses A/c	Dr.	Rs. 2,400	
To Share-based payment reserve			Rs. 2,400

(To recognise the receipt of employee services in exchange for shares )

#### Year 3 (Year ended 31st March, 20X3)

Employee benefit expenses A/c	Dr.	Rs. 2,500	
To Share-based payment reserve			Rs. 2,500

(To recognise the receipt of employee services in exchange for shares )

### Working Notes:

#### 1. Year 1

780 shares expected to vest x Rs. 10 grant date fair value of each share x 1/3 of vesting period elapsed = Rs. 2,600 recognised in Year 1.

#### 2. Year 2

(750 shares expected to vest x Rs. 10 grant date fair value of each share x 2/3 of vesting period elapsed) less Rs. 2,600 recognised in Year 1 = Rs. 2,400 recognised in Year 2.

#### 3. Year 3

(750 shares x Rs. 10 grant date fair value of each share) less Rs. 5,000 recognised in Years 1 and 2 = Rs. 2,500 recognised in Year 3.

### Question 13 : Nov 2023 – Paper

A Ltd. announced a stock appreciation right (SAR) on 1st April, 2020 for each of its employees. The scheme gives the employees the right to claim cash payment equivalent to an excess of market price of Company's shares on exercise date over the exercise price of Rs 250 per share in

respect of 100 shares, subject to a condition of continuous employment of 3 years. The SAR is exercisable after 31st March, 2023 but before 30th June, 2023. The fair value of SAR was:

- Rs. 42 in 2020-2021;
- Rs. 46 in 2021-2022; and
- Rs. 48 in 2022-2023.

In 2020-2021, the company estimates that 2% of its employees shall leave the Company annually. This was revised to 3% in 2021-2022. Actually:

- 15 employees left the company in 2020-2021;
- 10 employees left the company in 2021-2022; and
- 8 employees left the company in 2022-2023.

The SAR therefore actually vested in 492 employees on 30th June, 2023\* and when SAR was exercised, the intrinsic value was Rs. 50 per share.

Compute, by fair value method, the SAR expense for financial years;

- 2020-2021;
- 2021-2022;
- 2022-2023;
- 2023-2024.

Also provide SAR ledger from inception till closure. Discuss whether this account is in the nature of liability or equity?

### Solution :

Number of employees at the grant date to whom the SARs were granted = 492 + 15 + 10 + 8 = 525 employees

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
31st March, 2021	6,86,000	6,86,000	$[(525-15) \times 0.98 \times 0.98] \times 100 \times 42 \times 1/3]$
31st March, 2022	8,01,333	14,87,333	$[\{(525-15-10) \times 0.97 \times 100 \times 46 \times 2/3\} - 6,86,000]$
31st March, 2023	8,74,267	23,61,600	$[525-15-10-8] \times 48 \times 100 - 14,87,333$
30th June, 2023	(98,400)*	0	$[(492 \times 100 \times 50) - 23,61,600]$

\*Difference of opening liability Rs. 23,61,600 and actual liability paid Rs. 24,60,000  $[(492 \times 100 \times 50) - 23,61,600]$  is recognised to Profit and loss i.e. Rs. 98,400.

### SAR Ledger

Date	Particular	Amount	Date	Particular	Amount
31.3.2021	To Balance c/d	<u>6,86,000</u>	31.3.2021	By Employee benefits expenses	<u>6,86,000</u>
		<u>6,86,000</u>			<u>6,86,000</u>
31.3.2022	To Balance c/d	14,87,333	1.4.2021	By Balance b/d	6,86,000

		_____	31.3.2022	By Employee benefits expenses	<u>8,01,333</u>
		<u>14,87,333</u>			<u>14,87,333</u>
31.3.2022	To Balance c/d	23,61,600	1.4.2022	By Balance b/d	14,87,333
		_____	31.3.2023	By Employee benefits expenses	<u>8,74,267</u>
		<u>23,61,600</u>			<u>23,61,600</u>
30.6.2023	To Bank	24,60,000	1.4.2022	By Balance b/d	23,61,600
			30.6.2023	By Employee benefits expenses	98,400
		<u>24,60,000</u>			<u>24,60,000</u>

SAR Account is in the nature of liability because it is a cash settled share-based transaction which is summed up on payment of cash to the employees at the end of the exercise period.

#### Question 14 : May 2024 – RTP

Fashion India Ltd. (FIL) entered into an agreement with RFD Ltd. on 10th August, 20X2 for purchasing a machinery. The agreement has a clause that FIL will have to settle the consideration of machinery purchased by issuing its equity shares. FIL agreed to the clause and the order was confirmed. Machinery was supplied vide invoice dated 25th October, 20X2 and delivered on 1st November, 20X2. Agreed purchase consideration was Rs. 150 Lakhs and the fair value of the machinery supplied was estimated to be Rs. 160 Lakhs. As agreed, FIL issued 1,00,000 equity shares of face value Rs. 100 each to RFD Ltd.

As per Ind AS 102 'Share Based Payment', what should be the price and the date for recording the machinery purchased from RFD Ltd.?

#### Solution :

As per para 10 of Ind AS 102, for equity settled share-based payment transactions, the entity shall measure the goods or services received, and the corresponding increase in equity, directly, at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the entity shall measure their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted. Here, since the fair value of the asset received can be estimated reliably, the price for recording the machinery would be Rs. 160 lakhs.

Further the control is assumed to be transferred on the date the delivery is received which is 1st November, 20X2. Therefore, this will be the date for recognizing the machinery in the books.

#### Question 15 : Nov 2024 – Paper

Greater Ltd., in order to reward its employees launched a scheme effective from 1st April, 2021, in which employees will be granted equity shares of the company at a price less than the market price subject to satisfaction of certain conditions. Following details are provided to you:

- (a) According to scheme, each employee has an option to purchase 250 equity shares of the company at Rs.45 per share provided that the employee does not leave the company for 3 years from the date of launch of the scheme i.e. upto 31st March, 2024.
- (b) Once 3 years are completed by an employee, the employee can exercise the option within 1 year i.e. by 31st March, 2025.
- (c) The closing share price on stock exchange as at 1st April, 2021 is Rs.91 per share with face value of Rs.10 per share. A registered valuer has been appointed by the company who derived the price of option at Rs.75 using Black Scholes model of option pricing.
- (d) There are 750 employees eligible for the scheme. As at 31st March, 2022, 25 employees left the company and further 35 employees are expected to leave over the next 2 years. During the year 2022-23, a foreign based company entered into the market and started hiring experienced employees and therefore retention of existing employees has been problematic and a high attrition rate is observed in the market. 275 employees left the company during the year ended 31st March, 2023 and further 135 employees are expected to leave in the next one year. As at 31st March, 2024, only 400 employees remained with the company out of 750 employees.
- (e) Out of it only 375 employees exercised the option to purchase the equity shares during the year ended 31st March, 2024.

You are required to provide necessary accounting entries during the life of sharebased payment scheme to account the scheme implemented by the company.

**Solution :**

**Journal Entries**

		Rs.	Rs.
<b>31st March, 2022</b>			
Employee benefits expenses (W.N.1)	Dr.	43,12,500	
To Share-based payment reserve (equity)			43,12,500
(Being 1/3rd expenses on share-based payment recognised)			
Profit and Loss A/c	Dr.	43,12,500	
To Employee benefits expenses			43,12,500
(Being employee benefits expenses transferred to P/L)			
<b>31st March, 2023</b>			
Share-based payment reserve (equity) (W.N.1)	Dr.	3,75,000	
To Employee benefits expenses (transferred to P/L)			3,75,000
(Being reversal of excess expenses booked on computation of 2/3rd expenses on share-based payment)			
Employee benefits expenses	Dr.	3,75,000	
To Profit and Loss A/c			3,75,000
(Being employee benefits expenses transferred to P/L)			
<b>31st March, 2024</b>			
Employee benefits expenses (W.N.3)	Dr.	35,62,500	

To Share-based payment reserve (equity) (Being final recognition of expenses on vesting of share-based options)			35,62,500
Profit and Loss A/c	Dr.	35,62,500	
To Employee benefits expenses (Being employee benefits expenses transferred to P/L)			35,62,500
<b>31st March, 2025</b>			
Share-based payment reserve (equity) (W.N.4)	Dr.	75,00,000	
Bank A/c (W.N.4)	Dr.	42,18,750	
To Share Capital (W.N.4)			9,37,500
To Securities Premium (W.N.4)			1,03,12,500
To Retained Earnings (W.N.4)			4,68,750
(Being accounting on exercise of 375 options and lapse of 25 options)			

**Working Notes:**

**1. Calculation of Employee Benefit Expenses**

	31.3.2022	31.3.2023	31.3.2024
No of Employees	750	750	750
Less: Employees left	(25)	(3000)	(350)
Less: Employees expected	<u>(35)</u>	<u>(135)</u>	<u>-</u>
No of employees eligible	690	315	400
No of options per employee	250	250	250
Total options expected to vest	1,72,500	78,750	1,00,000
Fair value per option	75	75	75
Total FV	1,29,37,500	59,06,250	75,00,000
Cumulative expenses	1/3	2/3	3/3
	43,12,500	39,37,500	75,00,000
Expense already recognised	-	43,12,500	39,37,500
Expense to be recognised	43,12,500	3,75,000	35,62,500

**2. For the year ended 31st March, 2025**

Bank = 375 employees x 250 options x Rs. 45 = Rs. 42,18,750

Share capital = 375 employees x 250 options x Rs. 10 = Rs. 9,37,500

Securities Premium = 375 employees x 250 options x Rs. (75 + 35)  
= Rs. 1,03,12,500

Retained Earnings = (400-375) employees x 250 options x Rs. 75  
= Rs. 4,68,750

**Question 16 : May 2025 – RTP**

At 1st April, 20X1 an entity enters into a share-based payment arrangement with its employees. The terms of the award are as follows:

- Employees are required to work for the entity for five years; after that they will receive a cash payment equal to the value of the entity’s shares.
- If the entity achieves a successful IPO during the five -year period, the employees will receive free shares rather than a cash payment. So, employees might receive free shares at the time of IPO or a cash payment at the end of 5th year, but not both.
- No employees are expected to leave the entity over the next five years.
- At the date of the award and till the end of second year, it was not probable that a successful IPO would occur before year 5.
- At the end of year 3, a successful IPO becomes probable; and management expects it to occur in year 4.
- At the end of year 4, a successful IPO occurs; and employees receive free shares.
- The fair value of the equity-settled award alternative is Rs. 1,000 at the grant date. The fair value of the cash-settled alternative, ignoring the probability that an IPO will happen within the five years, is as follows:
  - o Rs. 50 at the end of year 1;
  - o Rs. 500 at the end of year 2;
  - o Rs. 100 at the end of year 3; and
  - o Rs. 50 at the end of year 4.

**Required:**

How the entity would account for this transaction?

**Solution :**

At the end of first and second year, the entity would not record a charge for the equity-settled award; this is because the vesting conditions are not expected to be met (that is, a successful IPO is not probable).

Hence, a liability is recognised, because cash settlement is probable until year 3. (Refer para 42 of Ind AS 102)

		Dr. (Rs.)	Cr. (Rs.)
<b>Year end 31st March, 20X2</b>			
Employee benefits expense (Rs. 50 / 5years)	Dr.	10	
To Share-based payment liability			10
Cash settled award recognised over the vesting period)			
<b>Year end 31st March, 20X3</b>			
Employee benefits expense{(Rs. 500 x 2/5)- Rs.10}	Dr.	190	
To Share-based payment liability			190
(Cash -settled award recognised over the vesting period)			

At the end of year 3, a successful IPO becomes probable; so the entity would record a charge for an equity-settled award.

There should also be a reversal of the SBP liability, because this award is now deemed not probable.

<b>Year end 31st March, 20X4</b>	<b>Dr.</b>	<b>Cr.</b>
Share-based payment Liability To Share-based Payment Reserve (Reversal of cash -settled share-based payment, because IPO deemed probable)	Dr. 200	200
Employee benefits expense {(Rs. 1,000 x $\frac{3}{4}$ ) - Rs. 200} To Share-based Payment Reserve (Equity -Settled award measured at grant date fair value of Rs. 550, because IPO is now deemed probable)	Dr. 550	550
<b>Year end 31st March, 20X5</b>		
Employee Benefits Expenses To Share-based Payment Reserve (Equity settled award recognised over the vesting period)	Dr. 250	250
Share-based Payment Reserve To Equity share capital (Settlement of share-based payment award through issuance of free shares)	Dr. 1,000	1,000

Equity -settled award measured at fair value of Rs. 1,000. All of the vesting conditions for this award have been met in year 4; so the award has vested, and the remaining charge of Rs. 250 (Rs. 1,000 – Rs. 750) is recognised in the Statement of profit and loss.

### Question 17 : May 2025 – Paper

National Ltd. granted 1,000 stock appreciation rights (SAR) each to its 160 employees on 1st April, 2021 with a fair value of Rs. 100 each. The terms of the award require the employees to provide service for four years to earn the award. The SARs are expected to be settled in cash and it is expected that 100% of the employees will exercise the options. The fair value of each SAR at each reporting date is as follows:

On 31st March, 2022	Rs. 120
On 31st March, 2023	Rs. 130
On 31st March, 2024	Rs. 135
On 31st March, 2025	Rs. 140

- (i) You are required to pass necessary journal entries across all the years for recognition of expenses.
- (ii) Would your answer be different, if at the end of the second year of service i.e. at 31st March, 2023, National Ltd. modifies the terms of the award to require only three years of total service instead of four years to earn the award. The SARs are expected to be settled in cash and it is expected that 100% of the employees will exercise the options. Pass revised journal entries.

### Solution :

(i) **Journal Entries in the books of National Ltd. (without modification of service period of stock appreciation rights)** (Rs. in lakhs)

Date	Particulars	Debit	Credit
31.3.2022	Employee Benefit Expenses <span style="float: right;">Dr.</span> To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	48.00	48.00
31.3.2023	Employee Benefit Expenses <span style="float: right;">Dr.</span> To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	56.00	56.00
31.3.2024	Employee Benefit Expenses <span style="float: right;">Dr.</span> To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	58.00	58.00
31.3.2025	Employee Benefit Expenses <span style="float: right;">Dr.</span> To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	62.00	62.00

**Working Note:**

Calculation of expenses for issue of stock appreciation rights without modification of service period

Period	Fair value (a)	To be Vested (b)	Cumulative (Rs..) a x 1000 awards x 160 employees x years of service	Expense (Rs.)
Start	100			
31st March 2022	120	100%	120 x 1000 x 160 x 1 years / 4 years of service = 48,00,000	48,00,000
31st March 2023	130	100%	130 x 1000 x 160 x 2 years / 4 years of service = 1,04,00,000	= 1,04,00,000 48,00,000 = 56,00,000
31st March 2024	135	100%	135 x 1000 x 160 x 3 years / 4 years of service = 1,62,00,000	= 1,62,00,000 – 1,04,00,000 = 58,00,000

31st March 2025	140	100%	140 x 1000 x 160 x 4 years / 4 years of service = 2,24,00,000	= 2,24,00,000 – 1,62,00,000 = 62,00,000
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(ii) **Journal Entries in the books of National Ltd. (with modification of service period of stock appreciation rights)** (Rs. in lakhs)

Date	Particulars	Debit	Credit
31.03.2023	Employee Benefit Expenses Dr. To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	90.67	90.67
31.03.2024	Employee Benefit Expenses Dr. To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	77.33	77.33

**Working Note:**

**Calculation of expenses for issue of stock appreciation rights with modification of service period**

Period	Fair value (a)	To be Vested (b)	Cumulative (Rs.) a x 1000 awards x 160 employees x years of service	Expense (Rs.)
1st April, 2021	100			
31st March, 2022	120	100%	120 x 1000 x 160 x 1 years / 4 years of service = 48,00,000	48,00,000
31st March, 2023	130	100%	130 x 1000 x 160 x 2 years / 3 years of service = 1,38,66,667	=1,38,66,667 – 48,00,000 = 90,66,667
31st March, 2024	135	100%	135 x 1000 x 160 x 3 years / 3 years of service = 2,16,00,000	=2,16,00,000 – 1,38,66,667 = 77,33,333

**Question 18 : Sept 2025 – RTP**

Max Ltd. enters into a share-based payment arrangement with its employees on the following terms:

- Each employee will receive 500 shares if they remain employed for a period of five years.
- It is expected that no employees are expected to leave during the five year period.
- The grant date fair value of the award is Rs. 4,000.

- If an employee leaves Max Ltd. after the five -year period, but before its shares are listed, the entity has an option to purchase the shares for fair value from the employee.
- On grant date, Max Ltd. expects to list in the list in the next 3-5 years. This is the first share-based plan and Max Ltd. has no past practice or stated policy of buying back shares from employees when the employees leave. Neither does Max Ltd. expect that it will settle the awards in cash.
- At the end of year 2, Max Ltd. on longer expects to list; and the employees are informed of this fact. Max Ltd. announces to employees that if it is not listed after the five years and employees leave, Max Ltd. will repurchase the shares. The fair value of the shares is Rs. 6,000 on this date.
- At the end of year 3, the fair value of the liability has increased to Rs. 9,000

**Required**

- Determine the accounting for years 1-3.
- What would be the treatment of the awards, if at the end of year 2, Max Ltd. does not inform employees that it will repurchase the shares after a five-year period, and a listing of the entity’s shares is still achievable. But at the end of year 6, Max Ltd. has not yet listed and two of the employees leave. Max Ltd. exercises its settlement choice and buys the leaving employee’s shares at fair value.

**Solution :**

- On the grant date, the employer accounts for the arrangement as an equity settled share-based payment because there is no present obligation to settle in cash.

**Journal Entries**

		Rs.	Rs.
Employee benefit expenses (4,000 x 1/5)	Dr.	800	
To Share-based payment reserve			800

At the end of year 2, Max Ltd. has created an obligation to settle in cash through a change in stated policy:

		Rs.	Rs.
Employee benefit expenses (4,000 x 1/5)	Dr.	800	
To Share-based payment reserve			800

The above entry is to record Rs. 4,000 vesting over a period of five years which was the expectation until year end.

		Rs.	Rs.
Share-based payment reserve	Dr.	2,400	
To Share-based payment liability (6,000 x 2/5)			2,400

In substance the reclassification represents the repurchase by Max Ltd. of its own shares, so no further expense is recognized. The subsequent measurement of the liability would follow the requirements for a cash settled share – based payment.

At the end of year 3, the award is accounted for on a cash – settled basis as follows:

		Rs.	Rs.

Employee benefit expenses	Dr.	3,000	
To Share-based payment liability (9,000 x 3/5 – 2,400)			3,000

- (ii) The settlement of the two employee's award may create a valid expectation in the minds of the remaining employees that they will also receive cash when they leave. However, judgement will be required to determine if an isolated transaction establishes past practice resulting in a cash settlement obligation for Max Ltd. Depending on any contrary facts, Max Ltd. should treat the remaining awards as cash settled, because it now revisit the classification of any similar grants that it has made and evaluate if it should reclassify them to cash -settled.

### Question 19 : Jan 2026 – RTP

H Ltd. is a parent company and has a subsidiary S Ltd. H Ltd. and S Ltd. are unlisted entities. Following arrangements with respect to ESOP scheme took place between them:

**1. Original ESOP scheme by H Ltd. (Parent ESOP scheme)**

At the beginning of year 1, H Ltd. granted 1,500 options in its own shares to its own employees as well as S Ltd.'s employees (i.e. 1,000 to H Ltd.'s employees and 500 to S Ltd.'s employees) with a fair value of Rs. 15 per options, conditional upon the completion of 3 years' service. H Ltd. will settle in its own equity shares. All the options are expected to vest. H Ltd. doesn't recharge to S Ltd. for ESOP expenses.

**2. New ESOP scheme by S Ltd. (Subsidiary ESOP scheme)**

H Ltd. and S Ltd. are unlisted entities. However, at the end of Year 1, S Ltd. gets listed. At the beginning of year 2, S Ltd. offers 1,500 options in its own shares to H Ltd.'s employees and its own employees (i.e. 1,000 to H Ltd.'s employees and 500 to S Ltd.'s employees), conditional upon H Ltd. and S Ltd.'s employees surrendering the right over parent ESOP scheme.

Remaining vesting period is same as H Ltd.'s ESOP scheme i.e. conditional upon the completion of remaining 2 years' service.

Incremental fair value of new ESOP scheme is Rs. 6. All the options are expected be vest. All H Ltd. and S Ltd.'s employees have opted for new ESOP scheme.

S Ltd. doesn't recharge to H Ltd. for ESOP expenses.

Required:

Analyze the above arrangements from the perspective of Consolidated Financial Statements and Individual Financial Statements of both parent and subsidiary. Also show the accounting treatment of the above arrangements in the Consolidated Financial Statements and Individual Financial Statements of both parent and subsidiary.

### Solution :

**Analysis of new ESOP scheme given on surrendering options under original ESOP scheme as replacement scheme**

The original ESOP scheme was issued by H Ltd. to its own employees as well as S Ltd.'s employees. S Ltd. has issued new ESOP scheme to its own and H Ltd.'s employees, conditional upon employees of S Ltd. and H Ltd. surrendering the right over original ESOP scheme.

Since obtaining the options under new ESOP scheme is conditional on surrendering the employee's entitlement under original ESOP scheme, the new scheme S Ltd. would be designated as replacement scheme for original scheme by S Ltd.

Accordingly, in the current fact pattern, the original ESOP scheme of H Ltd. has been replaced with the new ESOP scheme of S Ltd. Hence, according to para 28(c) of Ind AS 102, modification accounting would apply.

#### **Classification of new ESOP scheme**

**(i) Consolidated Financial Statements (CFS):**

The award is settled in equity shares of the group and therefore treated as an equity-settled share-based payment.

**(ii) Individual (Stand-alone) Financial Statements (SFS) of H Ltd.:**

From H Ltd.'s perspective, the award is treated as an equity-settled share-based payment. This is because H Ltd. does not have an obligation to settle the award.

**(iii) Individual (Stand-alone) Financial Statements (SFS) of S Ltd.**

ESOP will be settled against issue of S Ltd.'s own shares. Therefore, ESOP are classified as 'Equity settled'.

To the extent S Ltd. provides ESOP to H Ltd.'s employees, the same will be treated as dividend distribution to H Ltd.

#### **Accounting for change in settlor from H Ltd. (parent) to S Ltd. (subsidiary)**

**(i) Consolidated Financial Statements (CFS) of H Ltd.:**

- (a) As on the date of new ESOP scheme by S Ltd., there is ESOP reserve standing in CFS. This ESOP reserves is classified as 'Equity' in CFS considering that under original scheme, equity shares of H Ltd. are given.
- (b) ESOP reserve as per (a) above in CFS will continue even after new scheme. Since new scheme is accounted as modification of original scheme, grant date fair value as per original scheme plus incremental fair value as per new scheme is recognised as ESOP cost in CFS. Incremental fair value is accounted prospectively.
- (c) ESOP reserve as per (a) above in CFS is reclassified from 'Equity' to "Non-controlling interest' (NCI) due to change in settlor from H Ltd. (Parent) to S Ltd. (Subsidiary). This is because the definition of NCI refers to the equity in a subsidiary not attributable, directly or indirectly to a Parent.

**(ii) Stand-alone financial statements (SFS) of parent H Ltd. and subsidiary S Ltd.:**

- (a) Ind AS 102 doesn't contain any specific guidance on accounting for change in settlor.
- (b) Under original ESOP scheme, Parent H Ltd. was settlor. Therefore, on the date of new ESOP scheme, in the SFS of Parent H Ltd., there is 'ESOP reserves which would have been utilised in case Parent continued as settlor.
- (c) However, under the new ESOP scheme, Subsidiary S Ltd. is settlor. 'ESOP reserves' standing in SFS of Parent H Ltd. is no longer required as H Ltd. has passed on its responsibility of settling ESOP scheme to S Ltd. Therefore, 'ESOP reserves' in SFS of Parent H Ltd. is reversed.
- (d) Subsidiary S Ltd. under new ESOP scheme become settlor for an existing ESOP plan. However, in SFS of S Ltd. there is no 'ESOP reserves' standing. Therefore 'ESOP

reserves' relating to period already elapsed under original ESOP scheme is to be recognised in SFS of Subsidiary S Ltd.

### Journal Entries

Years	ESOP scheme references	Parent (H Ltd.) Standalone Financial Statement (P SFS)			Subsidiary (S Ltd.) Standalone Financial Statements (S SFS)		
		Particular	Debit	Credit	Particular	Debit	Credit
Year 1	Original ESOP scheme by Parent H Ltd.	Employees expenses* Dr.	5,000		Employees expenses# Dr.	2,500	
		Investment in Subsidiary**Dr.	2,500		To Equity (Capital Contribution from Parent)		2,500
		To Equity (ESOP reserves)		7,500			
		(Recognition of employees expenses/ investment in subsidiary under ESOP scheme by Parent for Year 1) [*Parent employees = 1,000 options x Rs. 15 x 1/3 = Rs. 5,000] [**Subsidiary employees = 500 options x Rs. 15 x 1/3 = Rs. 2,500]			(Recognition of employees expenses under ESOP scheme by Parent for Year 1) [#Subsidiary employees = 500 options x Rs. 2,500]		
Year 2- Beginning	Accounting for change in settlor from Parent to Subsidiary – at the beginning of Year 2	Equity (ESOP reserves) Dr.	7,500		Equity (Distribution to Parent) Dr.	5,000	
		To Investment in Subsidiary		2,500	Equity (capital contribution from Parent) Dr.	2,500	
		To Dividend Income (Deemed Distribution from Subsidiary)		5,000	To Equity (ESOP reserves)		7,500
		(Parent is no longer required to settle ESOP for its own employees as well as subsidiary employees under New ESOP scheme by Subsidiary)			(Accounting of obligations taken by Subsidiary under New ESOP scheme by Subsidiary for parent employees as well as its own employees. This entry is passed since subsidiary has taken obligation of existing scheme)		
Year 2- End	Modifications accounting – New ESOP scheme by Subsidiary	Employees expenses* Dr.	8,000		Equity (Distribution to Parent)# Dr.	8,000	
		To Dividend Income (Deemed Distribution from Subsidiary)		8,000	Employees expenses## Dr.	4,000	
					To Equity (ESOP reserves)		12,000
		(Recognition of employee expenses for parent employees under Old ESOP			(Recognition of employees' expenses for parent employees as well as		

		<p>scheme and incremental fair value under New ESOP scheme for Year 2)</p> <p>[*Parent employees =</p> <p>A                      Original      ESOP    scheme = (1000    options x Rs. 15 x    2/3 – 5,000) = Rs.    5,000</p> <p>B                      Incremental fair    value – New ESOP    scheme = (1000    options x Rs. 6 x    ½) = Rs. 3,000    Total = Rs. 8,000]</p>			<p>subsidiary employees under Old ESOP scheme and incremental fair value under New ESOP scheme for Year 2) [#Parent employees = Rs. 8,000 (i.e. computation same as parent) ##Subsidiary employees =</p> <p>A.                      Original      ESOP    scheme = (500    options x Rs. 15 x    2/3 – 2,500) = Rs.    2,500</p> <p>B                      Incremental fair    value – New ESOP    scheme = (500    options x Rs. 6 x ½)    = Rs. 4,000]</p>		
Year 3- End	Modifications accounting – New ESOP scheme by Subsidiary	<b>Particular</b>	<b>Debit</b>	<b>Credit</b>	<b>Particular</b>	<b>Debit</b>	<b>Credit</b>
		Employees expenses Dr.	8,000		Equity (Distribution to Parent) Dr.	8,000	
		To Dividend Income (Deemed Distribution from Subsidiary)		8,000	Employees expenses Dr.	4,000	
					To Equity (ESOP reserves)		12,000
		(Recognition of employee expenses for parent employees under New ESOP scheme for Year 2)			(Recognition of employees' expenses for parent employees as well as subsidiary employees under New ESOP scheme for Year 2)		

Thanks ....



# IND AS – 115

## REVENUE FROM CONTRACT WITH CUSTOMER

### CHAPTER - 27

#### 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	<u>(80)</u>
Profit	<u>20</u>

**Balance Sheet (Extracts)**

	Rs.Crores
Current assets	
Amount due from customers	
Contract cost to date	80
Profit recognized	<u>20</u>
	100
Progress billing to date	<u>(75)</u>
Billing to be done	<u>25</u>
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

- 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.
- 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)	<u>(48)</u>
Profit [(160/250) x (250-200)] - 20	<u>12</u>

**Statement of financial position (extracts) as on**

	<b>31 March 20X2</b>
	<b>Rs.Crores</b>
Current assets	
Amount due from customers	
Contract cost to date	145
Profit recognized (20+12)	<u>32</u>
	<b>177</b>
Progress billing	<u>(160)</u>
Billing to be done	<u>17</u>
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	<u>(Rs.87,300)</u>
Discount	<u>Rs.2,700</u>
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	<u>520</u>
Total estimated cost of construction	<u>1,300</u>
Degree of completion (780/1,300 x 100)	60%

	Rs.in lakh
Revenue recognized (1,250 x 60%)	<u>750</u>
Total foreseeable loss (1,300 – 1,250)	50
Less: Expense for the current year (780 – 750)	<u>(30)</u>
Loss to be provided for	<u>20</u>

**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
		<b>800</b>			<b>800</b>

**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
	<b>10,10,000</b>	<b>10,00,000</b>

(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
	<b>50,50,00,000</b>	<b>50,00,00,000</b>

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.

∴ Undiscounted points estimated to be recognized in next year = 18,00,000 × 80% = 14,40,000

∴ 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 × 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 because 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 31<sup>st</sup> March, 2019.

The first contract with A & Co. commences on 1<sup>st</sup> 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 31<sup>st</sup> 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 31<sup>st</sup> March, 2019 that the contract is 30% complete. Nivaan Limited has incurred costs up to 31<sup>st</sup> March, 2019 of Rs.16 lakhs and has received payments on account of Rs.13 lakhs.

The second contract with B & co. commenced on 1<sup>st</sup> Sept., 2018 and was for 18 months. The total sales value of contract was Rs.30 lakhs and 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 31<sup>st</sup> 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 31<sup>st</sup> 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 31<sup>st</sup> March, 2019.

Prepare financial statements extracts for Nivaan Limited in respect of the two construction contracts for the year ending 31<sup>st</sup> March, 2019.

**Solution :**

(a) Extracts of Balance Sheet of Nivaan Ltd. as on 31st March, 2019

	Rs. in lakh
Current Assets	
Contract Assets- Work-in-progress (Refer W.N. 3)	<u>9.0</u>
	—
Current Liabilities	
Contract Liabilities (Advance from customers) (Refer W.N. 2)	<u>4.5</u>

Extracts of Statement of Profit and Loss of Nivaan Ltd. as on 31st March, 2019

	Rs. in lakh
Revenue from contracts (Refer W.N. 1)	18
Cost of Revenue (Refer W.N. 1)	<u>(16.4)</u>
Net Profit on Contracts (Refer W.N. 1)	<u>1.6</u>

**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%) = <u>10.2</u>	(24 x 20%) = <u>4.8</u>	<u>15</u>
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	<u>(13)</u>	<u>(9.5)</u>	<u>(22.5)</u>

Advance received from the customers	<u>1</u>	<u>3.5</u>	<u>4.5</u>
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**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	<u>(10.2)</u>	<u>(4.8)</u>	<u>(15)</u>
Work-in-progress recognised at the end of the year	<u>5.8</u>	<u>3.2</u>	<u>9</u>

**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.

∴ Transaction price is equal to

1)	Fixed Contract Price	1,00,000
2)	Variable Contract Price	
	50,000 × 60%	= 30,000
	45,000 × 30%	= 13,500
	40,000 × 10%	= <u>4,000</u>
		<u>47,500</u>
		<u>1,47,500</u>

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%	<u>3,600</u>
		<u>25,950</u>

**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%	<u>2,52,000</u>
			<u>20,53,500</u>

$$\begin{aligned} \text{Average unit price} &= \text{Probability weighted sales value} / \text{Probability weighted sales volume} \\ &= 20,53,500 / 25,950 = \text{Rs.79.13 per unit} \end{aligned}$$

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 (Note 2)	–	–	–	3,25,000
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)		
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**(iv) Extract of Notes to the financial statements for the year ended 31st March, 2019 and 31st March, 2020**

**Note on Revenue**

	<b>2019-2020 Rs.</b>	<b>2018-2019 Rs.</b>
Sale of goods	–	2,51,927
Rendering of machine - maintenance services	75,000	45,000
Finance income	<u>–</u>	<u>28,073</u>
	<u>75,000</u>	<u>3,25,000</u>

**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.*
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\* 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-alone 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-alone 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
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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.

### Question 16 : May 2022 – Paper

ANANDAM Ltd. enter into a contract with a customer on 1<sup>st</sup> April, 20196 for the sale of a machine and spare parts. The manufacturing lead time for the machine and spare parts is 3 years.

On completion of manufacturing, ANANDAM Ltd. demonstrates that the machine and spare parts meet the agreed-upon specifications in the contract. The promises to transfer the machine and spare parts are distinct and results in two performance obligations each of which will be satisfied at a point in time.

On 31<sup>st</sup> March, 2022, the customer pays for the machine and spare parts, but only takes the physical possession of the machine. Although the customer inspects and accepts the spare parts, the customer requests that the space parts be stored at ANANDAM Ltd's warehouse because of its proximity to the customer's factors.

The customer has legal title to the spare parts and the parts can be identified as belonging to the customer. ANANDAM Ltd stored the spare parts in a separate section of its warehouse and the parts are ready for immediate shipment at the customer's request. ANANDAM Ltd. expects to

hold the spare parts for one to three years and does not have the authority to use the spare parts or direct them to another customer.

Determine how the revenue will be recognized by ANANDAM Ltd. for the different performance obligation as per Ind AS 115?

**Solution :**

**IDENTIFICATION OF OBLIGATIONS:**

ANANDAM Ltd. has made sale of two goods – machine and spare parts, whose control is transferred at a point in time. Additionally, company agrees to hold the spare parts for the customer for a period of 1-3 years, which is a separate performance obligation. Therefore, total transaction price shall be allocated amongst 3 performance obligations viz

- (i) Sale of machinery
- (ii) Sale of spare parts
- (iii) Custodial services for storing spare parts.

**RECOGNITION OF REVENUE:**

Recognition of revenue for each of the three performance obligations shall occur as follows:

- (i) **Sale of machinery:** Machine has been sold to the customer and physical possession as well as legal title passed to the customer on 31st March, 2022. Accordingly, revenue for sale of machinery shall be recognised on 31st March, 2022.
- (ii) **Sale of spare parts:** The customer has made payment for the spare parts and legal title has been passed to specifically identified goods, but such spares continue to be physically held by the entity. In this regard, the company shall evaluate if revenue can be recognized on bill-and-hold basis if **all** below criteria are met:

(a)	The reason for the bill-and-hold arrangement must be substantive (for example, the customer has requested the arrangement);	The customer has specifically requested the entity to store goods in their warehouse, owing to proximity to customer’s factory.
(b)	The product must be identified separately as belonging to the customer;	The spare parts have been specifically identified and inspected by the customer.
(c)	The product currently must be ready for physical transfer to the customer; and	The spares are identified and segregated, therefore, ready for delivery any time.
(d)	The entity cannot have the ability to use the product or to direct it to another customer	Spares have been segregated and cannot be redirected to any other customer.

Therefore, **all** the above conditions of bill-and-hold are met and hence, company can recognize revenue for sale of spare parts on 31st March, 2022.

- (iii) **Custodial services:** Such services shall be given for a period of 1 to 3 years from 31st March, 2022. Where services are given uniformly and customer receives & consumes benefits

simultaneously, revenue for such service shall be recognized on a straight-line basis over a period of time.

### Question 17 : May 2022 – Paper

Card Ltd. is engaged in the business of manufacturing of car locks and nut bolts.

**Car Locks :** Typically, a contract is entered into for sale of car locks and consideration is received in the event of delivery of goods to the customer place. The cost of each lock is Rs.1,500 and the selling price is Rs.1,800. The terms of the contract entitles the customer to return any unused car locks within 30 days and received a full refund. The Company estimates that the costs of recovering the car lock will be immaterial and expects that the returned car locks can be resold at a profit. The Company has sold a total of 20,000 car locks during the month ended 31<sup>st</sup> March, 2022. From past experience. Card Ltd. expects that 4% of the car locks will be returned in the financial year 2022-23.

**Nut Bolts :** On 1<sup>st</sup> April, 2021, Card Ltd. enters into an one year contract with a customer to deliver nut bolts. The contract stipulates that the price per piece will be adjusted retrospectively once the customer reaches certain sales volume, defined as follows :

Price per piece	Cumulative Sales Volume
Rs.200	1 – 50,000
Rs.190	50,001 – 1,00,000
Rs.180	100,001 and above

Volume is determined based on sales during the financial year. There are no minimum purchase requirements. Card Ltd. estimates that the total sales volume for the year will be 90,000 based on its experience with similar contracts and forecasted sales to the customer.

Card Ltd. sells 24,000 pieces to the customer during the first quarter of the financial year 2021-22 for a contract price of Rs.200 per piece.

You are required to :

- (i) Analyze the terms of the revenue contract with customers for sale of card locks as per Ind AS 115. Determine the amount of revenue, refund liability and the asset to be recognized by Card Ltd. for the said of car locks.
- (ii) Determine the transaction price, revenue and liability, if any for nut bolts as per Ind AS 115 at the end of first quarter of the financial year 2021-22.

### Solution :

#### Analysis:

- (i) (a) **Nature of consideration received:**

Card Ltd. applies the requirements in Ind AS 115 to the portfolio of 20,000 car locks because it reasonably expects that the effects on the financial statements from applying the requirements to the portfolio would not differ materially from applying the requirements to the individual contracts within the portfolio. Since the contract allows a customer to return the products, the consideration received from the customer is variable.

- (b) **Probability of significant reversal of cumulative revenue:**

Card Ltd. considers on constraining estimates of variable consideration to determine whether the estimated amount of variable consideration of Rs. 3,45,60,000 (Rs. 1,800 x 19,200 car locks not expected to be returned) can be included in the transaction price. Card Ltd. determines that although the returns are outside the entity's influence, it has significant experience in estimating returns for this product and customer class. In addition, the uncertainty will be resolved within a short time frame ie the 30-day return period. Thus, Card Ltd. concludes that it is highly probable that a significant reversal in the cumulative amount of revenue recognised (i.e. Rs. 3,45,60,000) will not occur as the uncertainty will be resolved (i.e. over the return period).

Card Ltd. estimates that the costs of recovering the products will be immaterial and expects that the returned products can be resold at a profit.

Upon transfer of control of the 20,000 car locks, Card Ltd. does not recognise revenue for 800 car locks that it expects to be returned. Consequently, it recognises the following:

- (1) revenue of Rs. 3,45,60,000 (Rs. 1,800 x 19,200 products not expected to be returned);
- (2) a refund liability of Rs. 14,40,000 (Rs. 1,800 refund x 800 products expected to be returned); and
- (3) an asset of Rs. 12,00,000 (Rs. 1,500 x 800 products for its right to recover products from customers on settling the refund liability).

- (ii) (a) **Transaction Price:** The transaction price will be based on Card Ltd.'s estimate of total sales volume for the year. Since Card Ltd. estimates cumulative sales volume of 90,000 nut bolts during the year, transaction price per nut bolt will be Rs. 190. Card Ltd. will update its estimate of the total sales volume at each reporting date until the uncertainty is resolved.
- (b) **Determination of Revenue:** Card Ltd. concludes that based on a transaction price of Rs. 190 per nut bolt, 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. 190 per nut bolt as each nut bolt is sold. Accordingly, for the first quarter of the financial year 2021-2022, Card Ltd. recognizes revenue of Rs. 45,60,000 (24,000 nut bolts x Rs. 190).
- (c) **Determination of Liability:** Card Ltd. will recognise a liability for cash received in excess of the transaction price for the first 50,000 nut bolts sold at Rs. 200 per nut bolt (that is, Rs. 10 per nut bolt) until the cumulative sales volume is reached for the next pricing tier and the price is retroactively reduced. Accordingly, for the first quarter of the financial year 2021-2022, Card Ltd. recognizes liability of Rs. 2,40,000 (24,000 nut bolts x (Rs. 200 – Rs. 190)).

#### Question 18 : Nov 2022 – RTP

A Ltd. owns 20 resorts across India. Every customer who stays in any of the resorts owned by A Ltd. is entitled to get points on the basis of total amount paid by him. Under this scheme, 1 point is granted for every Rs. 100 spent for stay in the resort. As per the past experience of A Ltd., the

likelihood of exercise of the points is 100% and the standalone price of each such point is Rs. 5. Customer X spends Rs. 10,000 in one of the resorts of A Ltd. What is the accounting treatment for the points granted by A Ltd.?

**Solution :**

Paragraph B40 of Ind AS 115, inter alia, states that, “if in a contract, an entity grants a customer the option to acquire additional goods or services, that option gives rise to a separate performance obligation only if the option provides a material right to the customer that it would not receive without entering into that contract”.

Further, paragraph B41 states that if a customer has the option to acquire an additional good or service at a price that would reflect the stand-alone selling price for that good or service, that option does not provide the customer with a material right even if the option can be exercised only by entering into a previous contract. In those cases, the entity has made a marketing offer that it shall account for in accordance with this Standard only when the customer exercises the option to purchase the additional goods or services.

In the given case, the customer does get a material right by way of a discount of Rs. 500 for every 100 points that he would not receive without the previous stay in that resort. Thus, the customer in effect pays the entity in advance for future goods and the entity recognises revenue when the goods are transferred.

According to paragraph B42, paragraph 74 requires an entity to allocate the transaction price to performance obligations on a relative stand-alone selling price basis. If the standalone selling price for a customer’s option to acquire additional goods or services is not directly observable, an entity shall estimate it on the basis of percentage discount the customer may obtain upon exercising the option and the likelihood of the option getting exercised.

In accordance with above, an entity shall account for award credit as a separate performance obligation of the sales transactions in which they are initially granted. The value of the consideration the entity expects to be entitled in respect of the initial sale shall be allocated between the award credits and the other components of the sale.

In the current case, the standalone selling price of the 100 points is Rs. 500. A Ltd. should allocate the fair value of the consideration (i.e. Rs. 10,000) between the points and the other components of the sale as Rs. 476 ( $500/10,500 \times 10,000$ ) and Rs. 9,524 ( $10,000/10,500 \times 10,000$ ) respectively in proportion of their standalone selling price. Since A Ltd. supplies the awards itself (i.e. it acts as a principal), it should recognise Rs. 476 as revenue when points are redeemed.

**Question 19 : Nov 2022 – Paper**

On 1<sup>st</sup> April, 2021 Mohan Ltd. has sold goods to Hari Ltd. at a consideration of Rs.7,50,000. The receipt of this is receivable in three equal instalments of Rs.2,50,000 each over a two year period (receipts on 1<sup>st</sup> April, 2021; 31<sup>st</sup> March 2022 and 31<sup>st</sup> March, 2023).

The company is offering a discount of 5% (i.e. Rs.37,500), if payment is made in full at the time of sale. The sale agreement reflects an implicit interest rate of 5.358% p.a.

The total consideration to be received from such sale is at Rs.7,50,000 and hence, the management has recognized the revenue from sale of goods for Rs.7,50,000.

You are required to analyse whether the above accounting treatment made by the accountant is in compliance of Ind AS. If not, advise the correct treatment alongwith journal entries and extracts of statement of Profit and Loss and Balance Sheet.

**Solution :**

The revenue from sale of goods shall be recognised at the fair value of the consideration received or receivable. The fair value of the consideration is determined by discounting all future receipts using an imputed rate of interest where the receipt is deferred beyond normal credit terms. The difference between the fair value and the nominal amount of the consideration is recognised as interest revenue. Hence, the accounting treatment of recognizing revenue of Rs. 7,50,000 by the accountant is not correct.

The fair value of consideration (cash price equivalent) of the sale of goods to be recognised on the date of sale should be calculated as follows:

Period	Consideration (Installment)	Present value factor	Present value of consideration
	Rs.		Rs.
Time of sale	2,50,000	-	2,50,000.00
End of 1st year	2,50,000	0.949	2,37,250.00
End of 2nd year	<u>2,50,000</u>	0.901	<u>2,25,250.00</u>
	<u>7,50,000</u>		<u>7,12,500.00</u>

Mohan Ltd. will recognise the revenue from sale of goods and finance income as follows:

Particulars		Rs.	Rs.
Initial recognition of sale of goods			
Cash / Bank A/c	Dr.	2,50,000	
Trade Receivable A/c	Dr.	4,62,500	
To Sale A/c			7,12,500
Recognition of interest expense and receipt of second installment			
Cash / Bank A/c	Dr.	2,50,000	
To Interest Income A/c (4,62,500 x 5.358%)			24,781
To Trade Receivable A/c			2,25,219
Recognition of interest expense and payment of final installment			
Cash / Bank A/c	Dr.	2,50,000	
To Interest Income A/c (Balancing figure)			12,719
To Trade Receivable A/c (4,62,500 – 2,25,319)			2,37,281

**Statement of Profit and Loss (Extracts)  
for the year ended 31st March, 2022 and 31st March, 2023**

	As at 31st March, 2022	As at 31st March, 2023
	Rs.	Rs.

Income		
Sale of Goods	7,12,500	-
Other Income (Finance income)	24,781	12,719

**Balance Sheet (extracts) as at 31st March, 2022 and 31st March, 2023**

	As at 31st March, 2022 Rs.	As at 31st March, 2023 Rs.
Assets		
Current Assets		
Financial Assets		
Trade Receivables	2,37,281	XXX

**Question 20 : Nov 2022 – Paper**

A Ltd. is in the business of infrastructure and has two divisions. The brief details of its business and underlying project details are as follows :

**Project 1 : Ludhiana – Chandigarh Expressway Toll Project :**

The company has commenced the construction of the project in the current year. The brief details of the Concession Agreement are given below :

- Total expenses incurred Rs.100 crore as on 31<sup>st</sup> March, 2022. Under IGAAP, the company has recorded such expenses as intangible assets in the books of account. Total expenses estimated to be incurred on the project are Rs.200 crore;
- Fair value of the construction service is Rs.220 crore;
- Total cash flow guaranteed by the government under the concession agreement is Rs.350 crore;
- Finance revenue over the period of operation phase is Rs.30 crore;
- Other income relates to the services provided during the operation phase.

**Project 2 : Bengaluru – Chennai Expressway Toll Project :**

The Company has also entered into another Concession Agreement with Government of Karnataka in the current year. The said concession agreement is Toll Based Project and the Company needs to collect the toll from the users of the expressway. The construction cost for the said project will be Rs.150 crore. The fair value of such construction cost is approximately Rs.200 crore. Under IGAAP, the company has recorded the expenses incurred on the said project as an intangible asset.

You are required to answer the following :

- What would be the classification of Ludhiana – Chandigarh Expressway Toll Project as per applicable Ind AS? Give brief reasoning.
- What would be the classification of Bengaluru – Chennai Expressway Toll Project as per applicable Ind As ? Give brief reasoning.
- What should be the accounting entries for the preparation of financial statements as per relevant Ind AS for the above 2 projects?

**Solution :**

**(i) Project 1 : Ludhiana -Chandigarh Expressway Toll Project**

Here the operator has a contractual right to receive cash from the grantor. The grantor has little, if any, discretion to avoid payment, usually because the agreement is enforceable by law. The operator has an unconditional right to receive cash if the grantor contractually guarantees to pay the operator. Hence, the operator recognizes a financial asset to the extent it has a contractual right to receive cash.

**(ii) Project 2 : Bengaluru -Chennai Expressway Toll Project**

Here the operator has a contractual right to charge users of the public services. A right to charge users of the public service is not an unconditional right to receive cash because the amounts are contingent on the extent that the public uses the service. Therefore, the operator shall recognise an intangible asset to the extent it receives a right (a license) to charge users of the public service.

**(iii) Accounting Entries for preparation of financial statements  
Ludhiana-Chandigarh Expressway Toll Project  
Journal Entries**

	Particulars		Dr. (Rs. in crore)	Cr. (Rs. in crore)
	<b>During construction:</b>			
1	Financial asset A/c <span style="float:right">Dr.</span> To Construction revenue (To recognise revenue relating to construction services, to be settled in cash)		220	220
2	Cost of construction (profit or loss) <span style="float:right">Dr.</span> To Bank A/c (As and when incurred) (To recognise costs relating to construction services)		200	200
	<b>During the operation phase:</b>			
3	Financial asset <span style="float:right">Dr.</span> To Finance revenue (As and when received or due to receive) (To recognise interest income under the financial asset model)		30	30
4	Financial asset <span style="float:right">Dr.</span> To Revenue [(350-220) – 30] (To recognise revenue relating to the operation phase)		100	100
5	Bank A/c <span style="float:right">Dr.</span>		350	

	To Financial asset (To recognise cash received from the grantor)		350
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**Bengaluru-Chennai Expressway Toll Project  
Journal Entries**

	Particulars		Dr. (Rs. in crore)	Cr. (Rs. in crore)
	<b>During construction:</b>			
1	Cost of construction (profit or loss) <span style="float: right;">Dr.</span> To Bank A/c (As and when incurred) (To recognise costs relating to construction services)		150	150
2	Intangible asset <span style="float: right;">Dr.</span> To Revenue (To recognise revenue relating to construction services provided for non-cash consideration)		200	200
	<b>During the operation phase:</b>			
3	Amortisation expense <span style="float: right;">Dr.</span> To Intangible asset (accumulated amortisation) (To recognise amortisation expense relating to the operation phase over the period of operation)		200	200
4	Bank A/c <span style="float: right;">Dr.</span> To Revenue (To recognise revenue relating to the operation phase)		?	?

**Note:** Amount in entry 4 is kept blank as no information in this regard is given in the question.

**Question 21 : Nov 2022 – Paper**

An entity enters into a contract for the sale of Product As for Rs.10,000. As part of the contract, the entity gives the customer a 40% discount voucher for any future purchases upto Rs.8,000 in the next 30 days. The entity intends to offer a 10% discount on all sales during the next 30 days as a part of seasonal promotion. The 10% discount cannot be used in addition to the 40% discount voucher.

The entity believes that there is 75% likelihood that a customer will redeem the voucher and on an average, a customer will purchase Rs.5,000 of additional products.

You are required to determine how many performance obligations does the entity have with their stand-alone selling price and allocated transaction price?

**Solution :**

Since all customers will receive a 10% discount on purchases during the next 30 days, the only additional discount that provides the customer with a material right is the incremental discount of 30% on the products purchased. The entity accounts for the promise to provide the incremental discount as a separate performance obligation in the contract for the sale of Product A.

The entity believes there is 75% likelihood that a customer will redeem the voucher and on an average a customer will purchase Rs. 5,000 of additional products. Consequently, the entity's estimated stand-alone selling price of the discount voucher is Rs. 1,125 (Rs. 5,000 average purchase price of additional products x 30% incremental discount x 75% likelihood of exercising the option). The stand-alone selling prices of Product A and the discount voucher and the resulting allocation of Rs. 10,000 transaction price are as follows:

Performance obligations	Stand-alone selling price
Product A	Rs. 10,000
Discount voucher	Rs. 1,125
Total	Rs. 11,125

Performance obligations		Allocated transaction price (to nearest Rs.)
Product A	$[(Rs. 10,000 \div Rs. 11,125) \times Rs. 10,000]$	Rs. 8,989
Discount voucher	$[(Rs. 1,125 \div Rs. 11,125) \times Rs. 10,000]$	<u>Rs. 1,011</u>
Total		<u>Rs. 10,000</u>

The entity allocates Rs. 8,989 to Product A and recognises revenue for Product A when control is transferred. The entity allocates Rs. 1,011 to the discount voucher and recognises revenue for the voucher when the customer redeems it for goods or services or when it expires.

### Question 22 : May 2023 – RTP

Company X enters into an agreement on 1st January, 20X1 with a customer for renovation of hospital and install new air-conditioners for total consideration of Rs. 50,00,000. The promised renovation service, including the installation of new air conditioners is a single performance obligation satisfied over time. Total expected costs are Rs. 40,00,000 including Rs. 10,00,000 for the air-conditioners. Company X determines that it acts as a principal in accordance with Ind AS 115 because it obtains control of the air conditioners before they are transferred to the customer. The customer obtains control of the air conditioners when they are delivered to the hospital premises.

Company X uses an input method based on costs incurred to measure its progress towards complete satisfaction of the performance obligation. As at 31st March, 20X1, other costs incurred excluding the air conditioners are Rs. 6,00,000.

Whether Company X should include cost of the air conditioners in measure of its progress of performance obligation? How should revenue be recognized for the year ended 31st March, 20X1?

**Solution :**

Paragraph B19 of Ind AS 115 inter alia, states that, “an entity shall exclude from an input method the effects of any inputs that, in accordance with the objective of measuring progress in paragraph 39, do not depict the entity’s performance in transferring control of goods or services to the customer”.

In accordance with the above, Company X assesses whether the costs incurred to procure the air conditioners are proportionate to the entity’s progress in satisfying the performance obligation. The costs incurred to procure the air conditioners i.e Rs. 10,00,000 are significantly relative to the total costs to completely satisfy the performance obligation i.e. Rs. 40,00,000. Also, Company X is not involved in manufacturing or designing of air conditioners.

Company X concludes that including the costs to procure the air conditioners in the measure of progress would overstate the extent of the entity’s performance. Consequently, in accordance with paragraph B19 of Ind AS 115, the entity adjusts its measure of progress to exclude the costs to procure the air conditioners from the measure of costs incurred and from the transaction price. The entity recognises revenue for the transfer of the air conditioners at an amount equal to the costs to procure the air conditioners (i.e., at a zero margin). Accordingly, the total revenue on account of renovation would be Rs. 50,00,000 – Rs. 10,00,000 = Rs. 40,00,000.

Company X assesses that as at 31st March, 20X1, the performance is 20% complete (i.e., Rs. 6,00,000 / Rs. 30,00,000).

Total revenue from renovation work would be  
= Rs. 50,00,000 – Rs. 10,00,000 = Rs. 40,00,000.

Consequently, as at 31st March, 20X1, Company X recognises the following:

		<b>Rs.</b>
Revenue	[(Rs. 40,00,000 x 20%) + Rs. 10,00,000]	18,00,000
Less: Cost of goods sold	(Rs. 6,00,000 of costs incurred + Rs. 10,00,000 costs of air conditioners)	<u>(16,00,000)</u>
Profit		<u>2,00,000</u>

**Question 23 : May 2023 – Paper**

On 1<sup>st</sup> April 2021, Z Limited enters into a contract to construct a manufacturing facility for Mint Limited at a fixed consideration of Rs.30.00 lakhs. Z Limited can earn an incentive of Rs.3.75 lakhs if the construction is completed within 24 months. Z limited expects the cost to be Rs.16.50 lakhs. At the inception of the contract, Z Limited determines that the contract contains single performance obligation satisfied over time. Z Limited also concludes that it is highly probable that a significant reversal in the amount of cumulative revenue recognized will occur as the completion of the manufacturing facility is highly susceptible to factors outside of the Company’s influence, due to exceptionally high rainfall in the region.

At 31st March, 2022, Z 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 due to uncertain weather conditions.

However, on 15th April 2022, the contract is modified. The fixed consideration is enhanced by Rs.2.25 lakhs and the expected costs increases by Rs.1.20 lakhs. The contract period is also

extended by 6 months. Z Limited now concludes that it is highly probable that the incentive award will be achieved. The contract remains a single performance obligation.

Compute, as per applicable Ind AS : (i) For Financial Year 2022-23, revenue from the contract, contract costs and resultant profit, (ii) Additional revenue (catch up adjustment) as on the date of modification of the contract i.e. 15<sup>th</sup> April, 2022.

**Solution :**

**Year 1 i.e. financial year 2021-2022**

In the given case, at contract inception, Z Ltd. will exclude the performance bonus of Rs. 3,75,000 from the transaction price because it is concluded that there is high probability that a significant reversal in the amount of cumulative revenue recognised will occur as the completion of the manufacturing facility is highly susceptible to factors outside the entity’s influence i.e. exceptionally high rainfall in the region.

Therefore, at the inception of the contract, for Z Ltd:

	Rs.
Transaction Price	30,00,000
Expected costs	<u>(16,50,000)</u>
Expected profit (45%)	<u>13,50,000</u>

As at the year end, 31st March, 2022, Z Ltd. reassessed the variable consideration (i.e. performance bonus) and has concluded that the amount is still uncertain in accordance with paragraphs 56–58 of Ind AS 115. Therefore, the cumulative revenue and costs recognised for the year ended March, 2022 will be as follows:

	Rs.
Revenue from the contract (65%)	19,50,000
Contract costs	<u>(10,72,500)</u>
Resultant profit	8,77,500

**Year 2 i.e. financial year 2022-2023**

On 15th April, 2022, Z Ltd. and Mint Ltd. agreed to modified the contract. As a result, the fixed consideration and expected costs increased by Rs. 2,25,000 and Rs. 1,20,000 respectively.

At the date of the modification, since Z Ltd. concluded that it is highly probable that incentive amount will be achieved, it has to include incentive amount of Rs. 3,75,000 in the transaction price. Therefore, the total potential consideration after the modification is Rs. 36,00,000 (Rs. 32,25,000 fixed consideration + Rs. 3,75,000 performance bonus) and total estimated cost is Rs. 17,70,000 (Rs. 16,50,000 + Rs. 1,20,000).

Further, since the modified contract remains a single performance obligation, Z Ltd. will account for the contract modification, as if it were part of the original contract in accordance with paragraph 21(b) of Ind AS 115.

Z Ltd. will update its measure of progress and estimates at the date of the modification as a cumulative catch-up adjustment as follows:

<b>Calculation of cumulative catch-up adjustment:</b>	<b>Rs.</b>
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Total potential consideration after the modification	A	36,00,000
Actual costs incurred	B	10,72,500
Total expected costs to complete	C	17,70,000
Percent completion of performance obligation (rounded off)	D = B/C	60.60%
Revenue recognised till date	E	19,50,000
Additional revenue to recognised	F = (A x D) - E	2,31,600

#### Question 24 : May 2023 – Paper

On 1<sup>st</sup> January, 2023, Z Limited enters into an agreement with a college for renovation of building including installation of new air conditioners at a transaction price of Rs.40.00 lakhs. The expected cost of air conditioners is Rs.12.00 lakhs. The other expected cost is Rs.20.00 lakhs. Z Limited purchases the air conditioners and they are delivered to the site before 31st March 2023. Z Limited uses an input method based on cost to measure progress towards completion of the contract. Z Limited has incurred actual other costs (excluding the air conditioners) of Rs.4.00 lakhs by 31st March, 2023.

Determine the revenue to be recognized as per applicable Ind AS for the year ended 31st March 2023 if performance obligation is met over a period of time.

#### Solution :

Costs to be incurred comprise two major components – air conditioners and cost of construction service.

- The air conditioners are part of the overall construction project and are not a distinct performance obligation.
- The cost of air conditioners is substantial to the overall project and are incurred well in advance.
- Upon delivery at site, customer acquires control of such air conditioners.
- And there is no modification done to the air conditioners, which the company only procures and delivers at site. Nevertheless, as part of materials used in overall construction project, the company is a principal in the transaction with the customer for such air conditioners also.

Therefore, applying the guidance on Input method –

- The measure of progress should be made based on the percentage of costs incurred relative to the total budgeted costs.
- The cost of air conditioners should be excluded when measuring such progress and revenue for such air conditioners should be recognized to the extent of costs incurred.

The revenue to be recognized is measured as follows:

Particulars	Amount (Rs.)
Transaction price	40,00,000
Costs incurred:	
(a) Cost of air conditioners	12,00,000
(b) Other costs	4,00,000

Measure of progress:	$4,00,000 / 20,00,000 = 20\%$
Revenue to be recognised:	
(a) For costs incurred (other than air conditioners)	Total attributable revenue = 28,00,000 % of work completed = 20%
(b) Revenue for air conditioners	Revenue to be recognised = 5,60,000 12,00,000 (equal to costs incurred)
Total revenue to be recognised	$12,00,000 + 5,60,000 = 17,60,000$

Therefore, for the year ended 31st March, 2023, the Company shall recognize revenue of Rs. 17,60,000 on the project.

### Question 25 : May 2023 – Paper

Summary Solutions Limited is engaged in the manufacturing of customized gifts for its corporate customers. On 1<sup>st</sup> December 2022, the company received an order from Rain Limited for the supply of 15,000 customized corporate gifts. On 4<sup>th</sup> December 2022, to meet the order, Summer Solutions Limited purchased 20,000 kg of certain material at Rs.110 per kg. The purchase price includes GST of Rs.10 per kg in respect of which full GST credit is admissible. Freight incurred amounted to Rs.1,00,000.

During January 2023 the company incurred the following expenses to design the corporate gift for Rain Limited :

- Fee to external designer Rs.20,000
- Labour Rs.8,000

After checking the sample of gift, the management of Rain Limited did not approve the design of gift and suggested some modifications. Consequently, the production team of Summer Solutions Limited made modifications to bring the inventories as per the conditions specified in the order. Following costs were incurred during testing phase :

- Materials Rs.45,000
- Labour Rs.20,000
- Depreciation of plant used during testing phase = Rs.7,000

Some of the materials used during testing phase was scrapped and sold for Rs.5,000.

During February 2023, Summer Solutions Limited incurred the following additional costs in the manufacturing of customized corporate gifts:

- Consumable stores Rs.1,25,000
- Labour Rs.1,42,000
- Depreciation of plant used in manufacturing of customized corporate gifts : Rs.38,000

On 15th March, 2023 the customized gifts were ready for delivery. There was no abnormal loss during the manufacturing process.

You are required to compute the cost of customized gifts. Your answer should be supported by appropriate reasons and calculations wherever necessary.

### Solution :

#### Statement showing computation of inventory cost

Particulars	Rs.	Reasons
-------------	-----	---------

Costs of purchase of raw material	21,00,000	Purchase price of raw material net of GST plus freight $[(20,000 \times (110-10)) + 1,00,000]$
Costs of purchase of consumable stores	1,25,000	Purchase price of consumable stores
Costs of conversion	1,42,000	Direct costs — labour
Production overheads	38,000	Fixed costs — depreciation
Production overheads	28,000	Product design costs and labour cost for specific customer
Other costs	<u>67,000</u>	Refer working note
Total cost of inventories	25,00,000	

**Working Note:****Costs of testing product designed for specific customer:**

Rs. 40,000 material (net of Rs. 5,000 recovered from the sale of scrapped output) + Rs. 20,000 labour + Rs. 7,000 depreciation = Rs. 67,000

**Question 26 : Nov 2023 – RTP**

On 1st April, 20X1, Entity X enters into a contract with Entity Y to sell mobile chargers for Rs. 100 per charger. As per the terms of the contract, if Entity Y purchases more than 1,000 chargers till March 20X2, the price per charger will be retrospectively reduced to Rs. 90 per unit. Till September 20X1, Entity X sold 95 chargers to Entity Y. Entity X estimates that Entity Y's purchases by March 20X2 will not exceed the required threshold of 1,000 chargers.

In October 20X1, Entity Y acquires another Entity C and from October 20X1 to December 20X1, Entity X sells an additional 600 chargers to Entity Y. Due to these developments, Entity X estimates that purchases of Entity Y will exceed the 1,000 chargers threshold for the period and therefore, it will be required to retrospectively reduce the price per charger to Rs. 90. Analyse the above scenario in light of Ind AS 115 and state how the revenue should be recognised in such a situation.

**Solution :**

Paragraph 56 of Ind AS 115 states that an entity shall include in the transaction price some or all of an amount of variable consideration estimated in accordance with paragraph 53 only to the extent that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty associated with the variable consideration is subsequently resolved.

Further, paragraph 57 of Ind AS 115 state that in assessing whether it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur once the uncertainty related to the variable consideration is subsequently resolved, an entity shall consider both the likelihood and the magnitude of the revenue reversal. Factors that could increase the likelihood or the magnitude of a revenue reversal include, but are not limited to, any of the following:

- (a) the amount of consideration is highly susceptible to factors outside the entity's influence. Those factors may include volatility in a market, the judgement or actions of third parties, weather conditions and a high risk of obsolescence of the promised good or service.

- (b) the uncertainty about the amount of consideration is not expected to be resolved for a long period of time.
- (c) the entity's experience (or other evidence) with similar types of contracts is limited, or that experience (or other evidence) has limited predictive value.
- (d) the entity has a practice of either offering a broad range of price concessions or changing the payment terms and conditions of similar contracts in similar circumstances.
- (e) the contract has a large number and broad range of possible consideration amounts.

Entity X estimates that the consideration in the above contract is variable. Therefore, in accordance with paragraphs 56 and 57 of Ind AS 115, Entity X is required to consider the constraints in estimating variable consideration. Entity X determines that it has significant experience with this product and with the purchasing pattern of the Entity Y. Thus, if Entity X concludes that it is highly probable that a significant reversal in the cumulative amount of revenue recognised (i.e. Rs. 100 per unit) will not occur when the uncertainty is resolved (i.e. when the total amount of purchases is known), then the Entity X will recognise revenue of Rs. 9,500 (95 chargers x Rs. 100 per charger) for the half year ended 30th September, 20X1.

Further, paragraphs 87 and 88 of Ind AS 115 that after contract inception, the transaction price can change for various reasons, including the resolution of uncertain events or other changes in circumstances that change the amount of consideration to which an entity expects to be entitled in exchange for the promised goods or services.

An entity shall allocate to the performance obligations in the contract any subsequent changes in the transaction price on the same basis as at contract inception. Consequently, an entity shall not reallocate the transaction price to reflect changes in stand-alone selling prices after contract inception. Amounts allocated to a satisfied performance obligation shall be recognised as revenue, or as a reduction of revenue, in the period in which the transaction price changes.”

In accordance with the above, in the month of October 20X1, due to change in circumstances on account of Entity Y acquiring Entity C and consequential increase in sale of chargers to Entity Y, Entity X estimates that Entity Y's purchases will exceed the 1,000 chargers threshold till March 20X2 for the period and therefore, it will be required to retrospectively reduce the price per charger to Rs. 90.

Consequently, the Entity X will recognise revenue of Rs. 53,050 for the quarter ended December 20X1 which is calculated as follows:

Particulars	Amount in Rs.
Sale of 600 chargers (600 chargers x Rs. 90 per charger)	54,000
Less: Change in transaction price (95 chargers x Rs. 10 price reduction) for the reduction of revenue relating to units sold till September 20X1.	<u>(950)</u>
Revenue recognised for the quarter ended December 20X1	53,050

### Question 27 : Nov 2023 – Paper

XYZ Limited is a sales and marketing company in amusement and entertainment domain. It negotiates and agrees in advance with four famous amusement parks to purchase their tickets for online sale through its payment gateway to general public. The negotiated rates are at a discount when compared with the price of tickets sold directly by amusement parks to the general

public. XYZ Limited is free to determine its sale price of the ticket. As part of the agreement, XYZ Limited will also assist the amusement parks/general public with respect to services provided by the amusement parks to the general public. However, each amusement park will continue to be responsible for fulfilling its / their obligation associated with the ticket, including solutions to dissatisfied customers. For XYZ Limited, there is no credit risk as payment is collected from customers beforehand. However, it carries an inventory risk as tickets have to be purchased in advance and unsold tickets are loss to XYZ Limited. Discuss whether XYZ Limited is a principal or an agent?

**Solution :**

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. The entity determines that its promise is to provide the customer with a ticket, which provides the right to enter the particular amusement park on a particular date. 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 enter the amusement park. However, the entity is not responsible for providing the services in amusement park, which will be provided by the amusement park owner.
- (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 i.e. XYZ Limited concludes that its promise is to provide a ticket (i.e. a right to enter the amusement park on a particular date) for 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 28 : Nov 2023 – Paper**

Whether the following expenses shall form part of 'costs incurred to obtain a contract'. Give reasons:

- (i) Commission paid only upon successful signing of the contract;
- (ii) Legal fees for drafting the terms of the arrangement/ agreement;
- (iii) Travel expenses of a sales person pitching for a new client contract;
- (iv) Salaries of sales people working exclusively on obtaining new clients;
- (v) Bonus based on quarterly sales;
- (vi) Commission paid to sales manager which is based on contracts obtained

**Solution :**

**Table showing expenses whether forming part of 'Cost to obtain a Contract'**

Sr.No.	Cost	Capitalize or expense / cost to obtain a contract	Reason
1.	Commission paid only upon successful signing of a contract	Capitalize/Yes	Assuming the entity expects to recover the cost, the commission is incremental since it would not have been paid if the parties decided not to enter into the arrangement just before signing.
2.	Legal fees for drafting terms of agreement	Expense/No  Capitalize/Yes	If the parties walk away during negotiations, the costs would still be incurred and therefore are not incremental costs of obtaining the contract. Alternatively, it can be 'Capitalised / Yes', due to the absence of words "to approve & sign" i.e. if the agreement is approved and signed, then is an incremental cost which needs to be capitalised.
3.	Travel expenses for a salesperson pitching a new client contract	Expense/No	Because the costs are incurred regardless of whether the new contract is won or lost, the entity expense out the costs, unless they are expressly reimbursable.
4.	Salaries for salespeople working exclusively on obtaining new clients	Expense/No	Salaries are incurred regardless of whether contracts are won or lost and therefore are not incremental costs to obtain the contract.
5.	Bonus based on quarterly sales	Capitalize/Yes	Bonuses based solely on sales are incremental costs to obtain a contract.
6.	Commission paid to sales manager based on contracts obtained	Capitalize/Yes	The commissions are incremental costs that would not have been incurred had the entity not obtained the contract.

**Question 29 : May 2024 – 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

Whether they could be considered as separate performance obligations as per the requirements of Ind AS 115?

**Solution :**

Paragraph 22 of 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 goods 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 goods 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 goods or service either on its own or together with other resources that are readily available to the customer (i.e. the goods or service is capable of being distinct); and
- (b) the entity’s promise to transfer the goods or service to the customer is separately identifiable from other promises in the contract (i.e. the promise to transfer the goods or service is distinct within the context of the contract).

Each performance obligation is required to be accounted for separately. The facts and circumstances of each contract should be carefully considered to determine the performance obligations.

However, based on the above guidance, the following table in general discusses whether the common goods and services in property sale contract should be considered as separate performance obligation or not:

<b>Goods/Service</b>	<b>Whether a separate performance obligation (PO) or not</b>	<b>Reason</b>
Common areas	Unlikely to be separate PO	Common areas are unlikely to be a separate PO 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 PO provided that it is distinct in the context of the contract.

Construction services and building materials	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 completed building.
Property management services and Golf membership	Likely to be separate PO	Property management services and golf membership are likely to be separate PO 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 a 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.

### Question 30 : May 2024 – Paper

Dark Limited is engaged in the construction and operation of thermal power plants in the country. It has entered into a purchase contract for USD 2,00,000 with Bright Limited, on 1st October, 2023 for purchase of power plant equipment on 31st March 2024. It is pertinent to note that the

functional currency of both companies is INR. Dark Limited and Bright Limited are listed companies in India and prepare their financial statements on a quarterly basis as per Ind AS.

Spot Rate as on 1st October, 2023 Rs./USD	75
Spot Rate as on 31st December ,2023 Rs./USD	82
Three month forward rate on 31st December, 2023 Rs./USD	70
Six month forward rate on 1st October, 2023 Rs./USD	80
Spot Rate on 31st March, 2024 Rs./ USD	85

Assume that this contract has an embedded derivative that is not closely related and requires separation. You are required to pass the necessary Journal Entries in the books of Bright Limited from the inception of the contract till the actual sale of equipment.

### Solution :

The contract should be separated using the 6-month USD / Rs. forward exchange rate, as at the date of the contract (1 USD = Rs. 80). The two components of the contract are therefore:

- A sale contract for USD 2,00,000
- A six-month currency forward to purchase USD 2,00,000 at Rs. 80
- This gives rise to a gain or loss on the derivative, and a corresponding derivative asset or liability.

### On delivery

1. Bright Ltd. records the sales at the amount of the host contract = Rs. 1,60,00,000
2. The embedded derivative is considered to expire.
3. The derivative asset or liability (i.e. the cumulative gain or loss) is settled by becoming part of the financial asset on delivery.
4. In this case, the carrying value of the currency forward at 31st March 2024 on maturity is = Rs. 2,00,000 (85 – 80) = Rs. 10,00,000 (profit/asset)

Below is the table summarising the computation of gain/ loss to be recorded at every period end

Date	Transaction	Sales	Debtors	Derivative Asset (Liability)	(Profit) Loss
		Rs.	Rs.	Rs.	Rs.
1st Oct. 2023	Embedded Derivative	Nil Value			
31st Dec. 2023	Change in Fair Value of Embedded Derivatives MTM (80 - 70) x 2,00,000			(20,00,000)	20,00,000
31st Mar. 2024	Change in Fair Value of Embedded Derivatives (85 - 70) x 2,00,000			30,00,000	(30,00,000)
31st Mar. 2024	Recording sales at forward rate	(1,60,00,000)	1,60,00,000		
31st Mar. 2024	Embedded derivative-settled against debtors		10,00,000	(10,00,000)	

### Journal Entries to be recorded at every period end

1st October, 2023 – No entry to be made

**31st December, 2023**

Particulars	Dr. Amount (Rs.)	Cr. Amount (Rs.)
Profit and loss A/c To Derivative financial liability A/c (Being loss on mark to market of embedded derivative booked)	Dr. 20,00,000	20,00,000

**31st March, 2024**

Particulars	Dr. Amount (Rs.)	Cr. Amount (Rs.)
Derivative financial asset A/c Derivative financial liability A/c To Profit and loss A/c (Being gain on embedded derivative based on spot rate at the date of settlement booked)	Dr. Dr. 10,00,000 20,00,000	30,00,000

**31st March, 2024**

Particulars	Dr. Amount (Rs.)	Cr. Amount (Rs.)
Trade Receivable A/c To Sales A/c (Being sale booked at forward rate on the date of transaction)	Dr. 1,60,00,000	1,60,00,000

**31st March, 2024**

Particulars	Dr. Amount (Rs.)	Cr. Amount (Rs.)
Trade Receivable A/c To Derivative financial asset A/c Being derivative asset re-classified as a part of trade receivables, bringing it to spot rate on the date of sale)	Dr. 10,00,000	10,00,000

**Question 31 : May 2024 – Paper**

Q Limited offers a new product X for sale to its customers at a price of Rs. 1,500. As a part of the Scheme, Q Limited gives the customers a discount voucher which entitles them a 30% discount on any future purchases up to Rs. 1,500 in the next 30 days. Q Limited intends to offer a 5%

discount on all sales during the next 30 days as a part of the seasonal promotion. The 5% discount cannot be used in addition to the 30% discount voucher. Q Limited believes that there is 80% likelihood that a customer will redeem the voucher and on an average, a customer will purchase Rs. 1,000 of additional products.

Find out is there any performance obligation on the part of Q Limited and if so calculate the stand alone and allocated transaction price.

**Solution :**

Since all customers will receive a 5% discount on purchases during the next 30 days, the only additional discount that provides the customer with a material right is the incremental discount of 25% on the products purchased. The entity accounts for the promise to provide the incremental discount as a separate performance obligation in the contract for the sale of Product X.

The entity believes there is 80% likelihood that a customer will redeem the voucher and, on an average, a customer will purchase Rs. 1,000 worth of additional products. Consequently, the entity's estimated stand-alone selling price of the discount voucher is Rs. 200 (Rs. 1,000 average purchase price of additional products x 25% incremental discount x 80% likelihood of exercising the option). The stand-alone selling prices of Product X and the discount voucher and the resulting allocation of the Rs. 1,500 transaction price are as follows:

Performance obligations	Stand-alone selling price Rs.
Product X	1,500
Discount voucher	200
Total	1,700

Performance obligations		Allocated transaction price Rs.
Product X	$(1,500 \div 1,700 \times 1,500)$	1,324
Discount voucher	$(200 \div 1,700 \times 1,500)$	<u>176</u>
Total		<u>1,500</u>

The entity allocates Rs. 1,324 to Product X and recognizes revenue for Product X when control transfers.

The entity allocates Rs. 176 to the discount voucher and recognizes revenue for the voucher when the customer redeems it for goods or services or when it expires.

**Question 33 : Nov 2024 – Paper**

Big Deal Ltd. is a marketing company having its departmental stores in 'A' class city of India. The company sells the diversified products. For the purpose of increasing sales and attract customers, the company during the financial year 2023-24, has adopted the following policy :

- (i) For every purchase of Rs.400 the customer is awarded with 6 points.
- (ii) Each point is redeemable on any future purchases of company's same departmental store situated in any of 'A' class city within 3 years i.e. upto 31st March, 2026

(iii) Value of each award point is Rs.0.60

During the financial year 2023-24, the Big Deal Ltd :

(i) Assessed that the sales of the company during the year 2023-24 is rs.150 lakhs.

(ii) Awarded 2,25,000 points to various customers during the year.

(iii) Estimated that out of the awarded points, 54,000 points will remain unredeemed as at 31st March' 2024 which shall be eligible for redemption till 31st March, 2026 and;

(iv) Expects only 75% points will be redeemed in the future.

As an accountant of the company, you are required to suggest the accounting treatment (Consolidated Journal Entries) in the following case :

How should the sales and redemption transactions be recognized and recorded as independent transactions in the FY 2023-24 as per Ind AS 115?

**Solution :**

Points earned on Rs. 1,50,00,000 @ 6 points on every Rs. 400

=  $[(1,50,00,000/400) \times 6] = 2,25,000$  points.

Out of 2,25,000 points, it is estimated that 54,000 points will remain unredeemed in the current year. Further, it is expected that 75% of the unredeemed points will be redeemed in the future.

Accordingly, value of points will be computed as follows:

Value of points redeemed in the current year

=  $(2,25,000-54,000)$  points x Rs. 0.6 each point = Rs. 1,02,600

Value of points estimated to be redeemed in future

=  $54,000$  points x 75% x Rs. 0.6 each point = Rs. 24,300

Total value of loyalty points = Rs. 1,02,600 + Rs. 24,300 = Rs. 1,26,900

Revenue recognized for sale of goods

= Rs. 1,48,74,165  $[1,50,00,000 \times (1,50,00,000 / 1,51,26,900)]$

Revenue for points = Rs. 1,25,835  $[1,26,900 \times (1,50,00,000 / 1,51,26,900)]$

**Journal Entry for the year 2023-2024**

		Rs.	Rs.
Bank A/c	Dr.	1,50,00,000	
To Sales A/c			1,48,74,165
To Liability under Customer Loyalty programme			1,25,835
(On sale of Goods)			
Liability under Customer Loyalty programme	Dr.	1,01,739	
To Sales A/c			1,01,739
(On redemption of (2,25,000 – 54,000) points)			

**Revenue for points to be recognized**

Undiscounted points estimated to be recognized next year

=  $54,000 \times 75\% = 40,500$  points

Total points to be redeemed within 3 years

=  $[(2,25,000 – 54,000) + 40,500] = 2,11,500$  points

Revenue to be recognised with respect to discounted points

= Rs. 1,25,835 x  $(1,71,000/2,11,500) = Rs. 1,01,739$

**Note:**

The above answer is based on the consideration that 75% likelihood of redemption of award points in future. **Alternatively**, the 75% likelihood of redemption of award points in future might not be considered. In such a case, the answer would be as follows:

Points earned on Rs. 1,50,00,000 @ 6 points on every Rs. 400.

$$= [(1,50,00,000/400) \times 6] = 2,25,000 \text{ points.}$$

Out of 2,25,000 points, it is estimated that 54,000 points will remain unredeemed in the current year.

Accordingly, value of points redeemed in the current year

$$= 2,25,000 \text{ points} \times \text{Rs. } 0.6 \text{ each point} = \text{Rs. } 1,35,000$$

Revenue recognized for sale of goods

$$= \text{Rs. } 1,48,66,204 [1,50,00,000 \times (1,50,00,000 / 1,51,35,000)]$$

Revenue for points = Rs. 1,33,796 [1,35,000 x (1,50,00,000 / 1,51,35,000)]

**Journal Entry for the year 2023-2024**

		Rs.	Rs.
Bank A/c	Dr	1,50,00,000	
To Sales A/c			1,48,66,204
To Liability under Customer Loyalty programme			1,33,796
(On sale of Goods)			
Liability under Customer Loyalty programme	Dr	1,08,175	
To Sales A/c			1,08,175
(On redemption of (2,25,000 – 54,000) points)			

**Revenue for points to be recognized**

Undiscounted points estimated to be recognized next year

$$= 54,000 \times 75\% = 40,500 \text{ points}$$

Total points to be redeemed within 3 years

$$= [(2,25,000 – 54,000) + 40,500] = 2,11,500 \text{ points}$$

Revenue to be recognised with respect to discounted points

$$= \text{Rs. } 1,33,796 \times (1,71,000 / 2,11,500) = \text{Rs. } 1,08,175$$

**Question 34 : Nov 2024 – Paper**

An entity provides broadband services to its customers along with voice call service. Customer buys modem from the entity. However, customer can also get the connection from the entity and modem from any other vendor. The installation activity requires limited effort and the cost involved is almost insignificant. It has various plans where it provides either broadband services or voice call services or both.

Comment on how to identify whether the performance obligations under the contract are distinct by using an automated process?

**Solution :**

To identify the performance obligations under the contract and determine if they are distinct, an automated process can be implemented using technology. The following steps can be taken:

- a. Analyze the clauses in the contract related to the services provided (broadband services, voice call services, modem sales).
- b. Each clause should be codified using appropriate parameters or tags to capture the relevant information.
- c. Assign Boolean values (0 or 1) to each parameter or tag in the codified clauses.
- d. Use "0" to represent "No" and "1" to represent "Yes" for each parameter.
- e. Define the criteria for evaluating the performance obligations based on the parameters and their Boolean values.
- f. Consider factors such as the type of service involved, benefits derived by the customer, and promises made in the contract regarding the transfer of goods or services.
- g. Develop an automated algorithm or script that evaluates the Boolean values of the parameters according to the defined criteria.
- h. Calculate scores or weights for each parameter based on their significance in determining performance obligations.
- i. Utilize the scores or weights assigned to the parameters to determine if the performance obligations are distinct.
- j. If the total score exceeds a certain threshold, consider it a separate performance obligation.

The automated process should flag and identify these distinct performance obligations based on the evaluation results.

Considering the above facts, the following conclusion arises:

There are three separate obligations

- Broadband Service
- Voice Call Services
- Modem

### Question 35 : May 2025 – Paper

HaSo Ltd. deals in manufacture of computer hardware and development of software applications. Discuss the revenue recognition of HaSo Ltd. as per Ind AS 115 in the following cases:

- (i) Mr. Grahak purchases a software application license from HaSo Ltd. for Rs. 2,00,000. Under the agreement, HaSo Ltd. will provide updates or upgrades on a when-and-if-available basis. Mr. Grahak can choose whether to install them or not. HaSo Ltd. will undertake no other activities that will change the functionality of the software application license.
- (ii) HaSo Ltd. licenses the right to operate its exclusive store in Madurai to Franchisee Ltd. The store will bear HaSo Ltd. trade name and brand logo. Franchisee Ltd. will have the right to sell HaSo Ltd.'s products for next 5 years from the date of agreement. Franchisee Ltd. pays an all-inclusive up-front fixed fee on signing of the agreement. The franchise agreement requires HaSo Ltd. to maintain the brand through product improvements, marketing campaigns etc.

### Solution :

- (i) Although the updates and upgrades will change the functionality of the software, they are not considered in determining the nature of the entity’s promise in granting the license. The activities of HaSo Ltd. to provide updates or upgrades are not considered because they transfer a promised goods or service to Mr. Grahak i.e. updates or upgrades are distinct from the licence. Therefore, the software application license Rs. 2,00,000 provides a right to use the IP that is satisfied at a point in time.  
Hence, Rs. 2,00,000 will be recognised immediately in the income statement by HaSo Ltd., on purchase of the software application license by Mr Grahak.
- (ii) The licence provides Franchisee Ltd. access to the IP as it exists at any point in time in the licence period. This is because:
- HaSo Ltd. is required to maintain the brand, which will significantly affect the IP by affecting Franchisee Ltd.’s ability to obtain benefit from the brand;
  - Any action by HaSo Ltd. may have a direct positive or negative effect on Franchisee Ltd.; and
  - These activities do not transfer goods or service to Franchisee Ltd.
- Therefore, HaSo Ltd. recognizes the up-front fee over the 5-year franchise period.

### Question 36 : Sept 2025 – Paper

On 1st April, 2023, Shivank Limited entered into a contract with Amey Limited to build an asset for consideration of Rs. 1,20,00,000 with a bonus of Rs. 35,00,000 if the asset is completed within 30 months. At the inception of the contract, Shivank Limited correctly accounted for the promised bundle of goods and services as a single performance obligation in accordance with Ind AS 115 and expected the costs to be Rs. 71,00,000. At the same time, it was concluded that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will occur. Completion of the asset was highly susceptible to factors outside of the Company's influence, mainly due to difficulties with the supply of components.

At 31st March, 2024, Shivank Limited had satisfied 60% of its performance obligation on the basis of costs incurred to date and concluded that the variable consideration was still constrained in accordance with Ind AS 115. However, on 30th April, 2024, the contract was modified with the result that the fixed consideration and expected costs increased by Rs. 15,50,000 and Rs. 7,60,000 respectively. The time allowable for achieving the bonus was extended by four months with the result that Shivank Limited concluded that it is highly probable that the bonus will be achieved and that the contract remained a single performance obligation.

You are required to give your opinion on the accounting treatment of contract for the years 2023-2024 and 2024-2025 with reference to the provisions of Ind AS 115.

### Solution :

#### For the year 2023-2024

Shivank 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, Shivank Limited expects the following:

Transaction price	–	Rs. 1,20,00,000
Expected costs	–	<u>(Rs. 71,00,000)</u>

Expected profit (40.83%) – Rs. 49,00,000

At contract inception, Shivank Limited excludes Rs. 35,00,000 bonus from the transaction price because it has been concluded that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will occur. Completion of the construction of asset is highly susceptible to factors outside the entity's influence.

By the end of the first year, the entity has satisfied 60% of its performance obligation on the basis of costs incurred to date. Costs incurred to date are therefore Rs. 42,60,000 and Shivank Limited reassesses the variable consideration and concludes that the amount is still constrained. Therefore at 31st March 2024, the following would be recognised:

Revenue (A)	–	Rs. 72,00,000 (Rs. 1,20,00,000 x 60%)
Costs (B)	–	<u>(Rs. 42,60,000)</u> (Rs. 71,00,000 x 60%)
Gross profit (C) i.e.(A-B)	–	<u>Rs. 29,40,000</u>

#### For the year 2024-2025

On 30th April 2024, the contract was modified. As a result, the fixed consideration and expected costs increase by Rs. 15,50,000 and Rs. 7,60,000, respectively.

The total potential consideration after the modification is Rs. 1,70,50,000 [which is Rs. 1,35,50,000 (i.e. 1,20,00,000 + 15,50,000) fixed consideration + Rs. 35,00,000 completion bonus]. In addition, the allowable time for achieving the bonus is extended by four months with the result that Shivank 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. 35,00,000 can be included in the transaction price.

Shivank Limited also concludes that the contract remains a single performance obligation. Thus, Shivank Limited accounts for the contract modification as if it were part of the original contract. Therefore, Shivank Limited updates its estimates of costs and revenue as follows:

Shivank Limited has satisfied 54.20% of its performance obligation (Rs. 42,60,000 actual costs incurred compared to Rs. 78,60,000 total expected costs). The entity recognises additional revenue of Rs. 20,41,100 [(54.20% of Rs. 1,70,50,000) – Rs. 72,00,000 revenue recognised to date] at the date of modification i.e. on 30th April 2024 as a cumulative catch-up adjustment.

#### Question 37 : Jan 2026 – RTP

A Ltd. enters into a contract with a customer for the exclusive supply of paint for a three-year period. A Ltd. makes a Rs. 50,000 upfront payment, which the customer will use to customize its paint sprayers for A Ltd.'s product. A Ltd. determines the upfront payment is not in respect of or for a distinct good or service.

A Ltd. estimates Rs. 10,00,000 in sales with the customer over the three-year period. Sales for Quarter 1 is Rs. 1,00,000 and for Quarter 2 is Rs. 1,25,000. However, A Ltd. updated its estimate of total sales over the contract to Rs. 15,00,000 during Quarter 2.

Required:

Determine the net revenue to be recognized in Quarter 1 and Quarter 2 by A Ltd.

#### Solution :

##### Treatment of upfront payment of Rs. 50,000

Upfront payment of Rs. 50,000 would be accounted for as a reduction of the transaction price. It would be deferred and recognised as a reduction of revenue (in proportion to estimated sales) over the contract term.

**Accounting for Quarter 1 and Quarter 2 is as follows:**

For the first quarter

- Quarter 1 sales = Rs. 1,00,000
- Entity estimates Rs. 10,00,000 sales over the three-year period
- Percentage of Quarter 1 sale to total estimated sale  
= (Rs. 1,00,000 / Rs. 10,00,000) x 100 = 10%
- Share of upfront payment to be recognised in Quarter 1  
= 10% x Rs. 50,000 = Rs. 5,000

Hence, in Quarter 1, A Ltd. recognizes revenue of Rs. 95,000 (Rs. 1,00,000 actual sales – Rs. 5,000 consideration paid to the customer)

For the second quarter

- Quarter 2 sales = Rs. 1,25,000
- A Ltd. updates its estimate of total sales over the contract to Rs. 15,00,000
- Total sales to date till Quarter 2  
= Rs. 1,00,000 +Rs. 1,25,000 = Rs. 2,25,000
- Percentage of sale till Quarter 2 to total estimated sale  
= (Rs. 2,25,000 / Rs. 15,00,000) x 100 = 15%
- Share of upfront payment to be recognised in Quarter 2  
= (15% x Rs. 50,000 upfront payment) – Upfront payment recognized in Quarter 1  
= Rs. 7,500 – Rs. 5,000 = Rs. 2,500

Hence, A Ltd. would recognize revenue of Rs. 1,22,500 for Quarter 2 (Rs. 1,25,000 actual sales – Rs. 2,500 upfront payment made to the customer).

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Thanks ....



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