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IND AS – 103

BUSINESS COMBINATION

CHAPTER - 28

Question 1 : May 2018 – RTP

On 1 April 20X1, Alpha Ltd. acquires 80 percent of the equity interest of Beta Pvt. Ltd. in exchange for cash of Rs 300. Due to legal compulsion, Beta Pvt. Ltd. had to dispose of their investments by a specified date. Therefore, they did not have sufficient time to market Beta Pvt. Ltd. to multiple potential buyers. The management of Alpha Ltd. initially measures the separately recognizable identifiable assets acquired and the liabilities assumed as of the acquisition date in accordance with the requirement of Ind AS 103. The identifiable assets are measured at Rs 500 and the liabilities assumed are measured at Rs 100. Alpha Ltd. engages an independent consultant, who determined that the fair value of 20 per cent non-controlling interest in Beta Pvt. Ltd. is Rs 84. Alpha Ltd. reviewed the procedures it used to identify and measure the assets acquired and liabilities assumed and to measure the fair value of both the non-controlling interest in Beta Pvt. Ltd. and the consideration transferred. After the review, it decided that the procedures and resulting measures were appropriate.

Calculate the gain or loss on acquisition of Beta Pvt. Ltd. and also show the journal entries for accounting of its acquisition. Also calculate the value of the non-controlling interest in Beta Pvt. Ltd. on the basis of proportionate interest method, if alternatively applied?

Solution :

1. Calculation of goodwill / gain on bargain purchase :

Consideration paid	300	
+ NCI at fair value	<u>84</u>	
	384	
– FV of net asset (500 – 100)		<u>400</u>
Gain from bargain purchase		16

2. Journal Entry :

		Dr.	Cr.
Assets A/c	Dr.	500	
To Liability			100
To Bank			300
To NCI			84
To Gain on bargain purchase (CR)			16

Question 2 : May 2018 – PAPER

Notorola Limited has two divisions A and B. Division A has been making constant profits while Division B has been invariably suffering losses.

On 31st March 2018, the division-wise draft extract of the Balance Sheet was as follows:

(Rs.in crore)

	A	B	Total
Fixed Assets Cost	500	1000	1500
Depreciation	(450)	(800)	(1250)
Net Fixed Assets (A)	50	200	250
Current Assets	400	1000	1400
Less: Current Liabilities	(50)	(800)	(850)
Net Current Assets (B)	350	200	550
Total (A) + (B)	400	400	800
Financed by :			
Loan Funds	-	600	60
Capital : Equity Rs.10 each	50	-	50
Surplus	350	-200	150
Total	400	400	800

Division B along with its assets and liabilities was sold for Rs.50 crore to Senovo Limited a new company, who allotted 2 crore equity shares of Rs.10 each at a premium of Rs.15 per share to the members of Notorola Limited in full settlement of the consideration, in proportion to their shareholding in the company. One of the members of the Notorola Limited was holding 52% shares of the company.

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

- (i) Pass journal entries in the books of Notorola Limited.
- (ii) Prepare the Balance Sheet of Notorola Limited after the entries in (i).
- (iii) Prepare the Balance Sheet of Senovo Limited.

Balance Sheet prepared for (ii) and (iii) above should comply with the relevant Ind AS and Schedule III of the Companies Act, 2013. Provide Notes to Accounts, for 'Other Equity' in case of (ii) and 'Share Capital' in case of (iii), only.

Solution :

(i) Journal of Notorola Ltd.

(Rs. In crore)

	Dr.	Cr.
Loan Funds	Dr. 600	
Current Liabilities	Dr. 800	
Provision for Depreciation	Dr. 800	
To Fixed Assets		1,000
To Current Assets		1,000
To Capital Reserve		200

(Being division B along with its assets and liabilities sold to Senovo Ltd. for Rs.50 crore)		
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(ii) **Notorola Ltd.**
Balance Sheet after demerger

		(Rs.in crore)	
ASSETS	Note No.	Amount	
Non-current assets			
Property, Plant and Equipment		50	
Current assets		400	
		<u>450</u>	
EQUITY AND LIABILITIES			
Equity			
Equity share capital (of face value of Rs.10 each)	1	50	
Other equity	2	350	
Liabilities			
Current liabilities			
Current liabilities		50	
		<u>450</u>	

Notes to Accounts

		Rs. in crore
1	Equity Share Capital 5 crore equity shares of face value of Rs.10 each Consequent to transfer of Division B to newly incorporated company Senovo Ltd., the members of the company have been allotted 2 crore equity shares of Rs.10 each at a premium of Rs.15 per share of Senovo Ltd., in full settlement of the consideration in proportion to their shareholding in the company	50
2	Other Equity Surplus (350 - 200) Add: Capital Reserve on reconstruction	<u>150</u> <u>200</u> 350

(iii) **Balance Sheet of Senovo Ltd.**

		(Rs.in crore)	
ASSETS	Note No.	Amount	
Non-current assets			
Property, Plant and Equipment		200	
Current assets		<u>1,000</u>	
		<u>1,200</u>	

EQUITY AND LIABILITIES		
Equity	1	20
Equity share capital (of face value of INR 10 each)	2	(220)
Other equity		
Liabilities		
Non-current liabilities		
Financial liabilities		
Borrowings		600
Current liabilities		
Current liabilities		<u>800</u>
		<u>1,200</u>

Notes to Accounts

		(Rs. In crore)
1. Share Capital		
Issued and Paid-up capital		
2 crore Equity shares of Rs.10 each fully paid up (All the above shares have been allotted to the members of Notorola Ltd. on takeover of Division B from Notorola Ltd. as fully paid-up pursuant to contract without payment being received in cash)		20
2. Other Equity (800 + 600 + 20) – (1,000 + 200)		220

Question 3 : Nov 2018 – RTP

ABC Ltd. prepares consolidated financial statements upto 31st March each year. On 1st July 2017, ABC Ltd. acquired 75% of the equity shares of JKL Ltd. and gained control of JKL Ltd. the issued shares of JKL Ltd. is 1,20,00,000 equity shares. Details of the purchase consideration are as follows:

- On 1st July, 2017, ABC Ltd. issued two shares for every three shares acquired in JKL Ltd. On 1st July, 2017, the market value of an equity share in ABC Ltd. was Rs.6.50 and the market value of an equity share in JKL Ltd. was Rs.6.
- On 30th June, 2018, ABC Ltd. will make a cash payment of Rs.71,50,000 to the former shareholders of JKL Ltd. who sold their shares to ABC Ltd. on 1st July, 2017. On 1st July, 2017, ABC Ltd. would have to pay interest at an annual rate of 10% on borrowings.
- On 30th June, 2019, ABC Ltd. may make a cash payment of Rs.3,00,00,000 to the former shareholders of JKL Ltd. who sold their shares to ABC Ltd. on 1st July, 2017. This payment is contingent upon the revenues of ABC Ltd. growing by 15% over the two-year period from 1st July, 2017 to 30th June, 2019. On 1st July, 2017, the fair value of this contingent consideration was Rs.2,50,00,000. On 31st March, 2018, the fair value of the contingent consideration was Rs.2,20,00,000.

On 1st July, 2017, the carrying values of the identifiable net assets of JKL Ltd. in the books of that company was Rs.6,00,00,000. On 1st July, 2017, the fair values of these net assets was Rs.7,00,00,000. The rate of deferred tax to apply to temporary differences is 20%.

During the nine months ended on 31st March, 2018, JKL Ltd. had a poorer than expected operating performance. Therefore, on 31st March, 2018 it was necessary for ABC Ltd. to recognise an impairment of the goodwill arising on acquisition of JKL Ltd., amounting to 10% of its total computed value.

Compute the impairment of goodwill in the consolidated financial statements of ABC Ltd. under both the methods permitted by Ind AS 103 for the initial computation of the non-controlling interest in JKL Ltd. at the acquisition date.

Solution :

Computation of goodwill impairment

	NCI at fair value	NCI at of net assets
	Rs. in '000	Rs. in '000
Cost of investment		
Share exchange (12,000 x 75% x 2/3 x Rs.6.50)	39,000	39,000
Deferred consideration (7,150 / 1.10)	6,500	6,500
Contingent consideration	25,000	25,000
Non-controlling interest at date of acquisition:		
Fair value – 3000 x Rs.6	18,000	
% of net assets – 68,000 (Refer W.N.) x 25%	–	17,000
Net assets on the acquisition date (Refer W.N.)	(68,000)	(68,000)
Goodwill on acquisition	20,500	19,500
Impairment @ 10%	2,050	1,950

Working Note:

Net assets on the acquisition date	Rs. '000
Fair value at acquisition date	70,000
Deferred tax on fair value adjustments [20% x (70,000 – 60,000)]	(2,000)
	68,000

Question 4 : Nov 2018 – RTP

Smart Technologies Inc. is a Company incorporated in India in 1998 having business in the field of development and installation of softwares, trading of computer peripherals and other IT related equipment and provision of cloud computing services along with other services incidental thereto. It is one of the leading brands in India.

After witnessing immense popularity and support in its niche market, Smart Technologies further grew by bringing its subsidiaries namely:

Company Name	Principle Activity
Cloudustries India Private Limited	Provision of cloud computing services.
Micro Fly India Private Limited	Trading of computer peripherals like mouse, keyboard, printer etc.

Smart Technologies started preparing its financial statements based on Ind AS from 1st April, 2015 on voluntary basis. The Microfly India Pvt. Ltd. is planning to merge the business of Cloudstries India Pvt. Ltd. with its own for which it presented before the members in the meeting the below extract of latest audited Balance Sheet of Cloudustries (prepared on the basis of Ind AS) for the year ended 31st March, 2017:

Balance Sheet as at March 31, 2017		(Rs. in Crores)
Assets		
Non-current assets		
Property, plant and Equipment		<u>15.00</u>
		<u>15.00</u>
Current Assets		
(a) Financial assets		
Trade Receivables		10.00
Cash and cash equivalents		10.00
Other current assets		8.00
		<u>28.00</u>
Total		<u>43.00</u>
Equity and Liabilities		
Equity		
Equity Share Capital		45.00
Other Equity		
Reserves and Surplus (Accumulated Losses)*		<u>(24.80)</u>
		<u>20.20</u>
Liabilities		
Non-current Liabilities		
Financial liabilities		
Borrowings		2.80
Current Liabilities		
		<u>20.00</u>
		<u>22.80</u>
Total		<u>43.00</u>

*The Tax Loss carried forward of the company is Rs.27.20 crores

On September 5, 2017, the merger got approved by the Directors. The purchase consideration payable by MicroFly to Cloudustries was fixed at Rs.18.00 crores payable in cash and that MicroFly take over all the assets and liabilities of Cloudustries.

Present the statement showing the calculation of assets/liabilities taken over as per Ind AS. Also mention the accounting of difference between consideration and assets/liabilities taken over.

Solution :

Before the merger, Cloudustries and MicroFly are the subsidiary of Smart Technologies Inc. As the control is not transitory, the proposed merger will fall under the category of Business combination of entities under common control, it will be accounted as per Appendix C of Ind AS 103 "Business Combination" and Pooling of Interest Method would be applied.

Statement showing the calculation of assets/liabilities taken over and treatment of difference between consideration and assets/liabilities taken over:

(a) **Net asset taken over:** (Rs.in crore)

Assets taken over:	
Property, Plant and Equipment	15.00
Cash and cash equivalents	10.00
Other current assets	8.00
Trade Receivables	<u>10.00</u>
Total - A	<u>43.00</u>
Less: Liabilities taken over:	
Borrowings	2.80
Current Liabilities	<u>20.00</u>
Total - B	<u>22.80</u>
Net Asset taken over (A-B)	20.20

(b) **Treatment of difference between consideration and assets/liabilities taken over:** (Rs.in crore)

Net Asset taken over - A	20.20
Less: Purchase Consideration - B	<u>18.00</u>
Difference (A – B)	1.80

The difference between consideration and assets/liabilities taken over of Rs.1.80 crore shall be transferred to capital reserve.

Question 5 : Nov 2018 – PAPER

Moon Ltd. acquires 75% of Star Limited on 1st April, 2017 for consideration transferred rs.60 lakh. Moon Limited intends to recognize the Non-Controlling Interest (NCI) at proportionate share of fair value of identifiable assets. With the assistance of a suitably qualified valuation professional, Moon Limited measures the identifiable net assets of Star Limited at Rs.90 lakh. Moon Limited performs a review and determines that the business combination did not include any transactions that should be accounted for separately from the business combination.

State whether the procedures followed by Moon Limited and the resulting measurements are appropriate or not. Also calculate the bargain purchase gain in the process.

Solution :

The amount of Star Ltd.'s identifiable net assets exceeds the fair value of the consideration transferred plus the fair value of the NCI in Star Ltd.'s, resulting in an initial indication of a gain on a bargain purchase. Accordingly, Moon Ltd. reviews the procedures it used to identify and measure the identifiable net assets acquired, to measure the fair value of both the NCI and the consideration transferred, and to identify transactions that were not part of the business combination.

Following that review, Moon Ltd. can conclude that the procedures followed and the resulting measurements were appropriate.

	Rs.
Identifiable net assets	90,00,000
Less: Consideration transferred	(60,00,000)
NCI (90,00,000 × 25%)	<u>(22,50,000)</u>
Gain on bargain purchase	<u>7,50,000</u>

Question 6 : May 2019 – RTP

How should contingent consideration payable in relation to a business combination be accounted for on initial recognition and at the subsequent measurement as per Ind AS in the following cases:

- (i) On 1 April 2016, A Ltd. acquires 100% interest in B Ltd. As per the terms of agreement the purchase consideration is payable in the following 2 tranches:
 - a. an immediate issuance of 10 lakhs shares of A Ltd. having face value of INR 10 per share;
 - b. a further issuance of 2 lakhs shares after one year if the profit before interest and tax of B Ltd. for the first year following acquisition exceeds INR 1 crore.
 - i. The fair value of the shares of A Ltd. on the date of acquisition is INR 20 per share. Further, the management has estimated that on the date of acquisition, the fair value of contingent consideration is Rs.25 lakhs.
 - ii. During the year ended 31 March 2017, the profit before interest and tax of B Ltd. exceeded Rs.1 crore. As on 31 March 2017, the fair value of shares of A Ltd. is Rs.25 per share.
- (ii) Continuing with the fact pattern in (a) above except for:
 - c. The number of shares to be issued after one year is not fixed.
 - d. Rather, A Ltd. agreed to issue variable number of shares having a fair value equal to Rs.40 lakhs after one year, if the profit before interest and tax for the first year following acquisition exceeds Rs.1 crore. A Ltd. issued shares with Rs.40 lakhs after a year.

Solution :

- (i) In the given case the amount of purchase consideration to be recognized **on initial recognition** shall be as follows:

Fair value of shares issued (10,00,000 x Rs.20)	Rs.2,00,00,000
Fair value of contingent consideration	Rs.25,00,000
Total purchase consideration	Rs.2,25,00,000

Subsequent measurement of contingent consideration payable for business combination

In general, an equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Ind AS 32 describes an equity instrument as one that meets both of the following conditions:

- (a) There is no contractual obligation to deliver cash or another financial asset to another party, or to exchange financial assets or financial liabilities with another party under potentially unfavorable conditions (for the issuer of the instrument).

- (b) If the instrument will or may be settled in the issuer's own equity instruments, then it is:
- (i) a non-derivative that comprises an obligation for the issuer to deliver a fixed number of its own equity instruments; or
 - (ii) a derivative that will be settled only by the issuer exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

In the given case, given that the acquirer has an obligation to issue fixed number of shares on fulfilment of the contingency, the contingent consideration will be classified as equity as per the requirements of Ind AS 32.

As per paragraph 58 of Ind AS 103, contingent consideration classified as equity should not be re-measured and its subsequent settlement should be accounted for within equity. Here, the obligation to pay contingent consideration amounting to Rs.25,00,000 is recognized as a part of equity and therefore not re-measured subsequently or on issuance of shares.

- (ii) The amount of purchase consideration to be recognized **on initial recognition** is shall be as follows:

Fair value shares issued (10,00,000 × Rs.20)	Rs.2,00,00,000
Fair value of contingent consideration	Rs.25,00,000
Total purchase consideration	Rs.2,25,00,000

Subsequent measurement of contingent consideration payable for business combination

The contingent consideration will be classified as liability as per Ind AS 32.

As per paragraph 58 of Ind AS 103, contingent consideration not classified as equity should be measured at fair value at each reporting date and changes in fair value should be recognized in profit or loss.

As at 31 March 2017, (being the date of settlement of contingent consideration), the liability would be measured at its fair value and the resulting loss of Rs.15,00,000 (Rs.40,00,000 – Rs.25,00,000) should be recognized in the profit or loss for the period. A Ltd. would recognize issuance of 160,000 (Rs.40,00,000/25) shares at a premium of Rs.15 per share.

Question 7 : Nov 2019 – RTP

H Ltd. acquired equity shares of S Ltd., a listed company, in two tranches as mentioned in the below table:

Date	Equity stake purchased	Remarks
1st November, 20X6	15%	The shares were purchased based on the quoted price on the stock exchange on the relevant dates.
1st January, 20X7	45%	

Both the above-mentioned companies have Rupees as their functional currency. Consequently, H Ltd. acquired control over S Ltd. on 1st January, 20X7. Following is the Balance Sheet of S Ltd. as on that date:

	(Rs.in crore)	(Rs.in crore)
ASSETS:		
<u>Non-current assets</u>		
(a) Property, plant and equipment	40.0	90.0
(b) Intangible assets	20.0	30.0
(c) Financial assets		
- Investments	100.0	350.0
<u>Current assets</u>		
(a) Inventories		
(b) Financial assets	20.0	20.0
- Trade receivables		
- Cash held in functional	20.0	20.0
Currency	4.0	4.5
(c) Other current assets		
Non-current asset held for sale	4.0	4.5
TOTAL ASSETS	208	
EQUITY AND LIABILITIES:		
<u>Equity</u>		
(a) Share capital (face value Rs.100)	12.0	50.4
(b) Other equity	141.0	Not applicable
<u>Non-current liabilities</u>		
(a) Financial liabilities		
- Borrowings	20.0	20.0
<u>Current liabilities</u>		
(a) Financial liabilities		
- Trade payables	28.0	28.0
(b) Provision for warranties	3.0	3.0
(c) Current tax liabilities	4.0	4.0
TOTAL EQUITY AND LIABILITIES	208.0	

Other information :

Property, plant and equipment in the above Balance Sheet include leasehold motor vehicles having carrying value of Rs.1 crore and fair value of Rs.1.2 crore. The date of inception of the lease was 1st April, 20X0. On the inception of the lease, S Ltd. had correctly classified the lease as a finance lease. However, if facts and circumstances as on 1st April, 20X7 are considered, the lease would be classified as an operating lease.

Following is the statement of contingent liabilities of S Ltd. as on 1st January, 20X7:

Particulars	Fair value (Rs. in crore)	Remarks
Law suit filed by a customer for a claim of Rs.2 crore	0.5	It is not probable that an outflow of resources embodying economic benefits will be

		required to settle the claim. Any amount which would be paid in respect of law suit will be tax deductible.
Income tax demand of Rs.7 crore raised by tax authorities; S Ltd. has challenged the demand in the court.	2.0	It is not probable that an outflow of resources embodying economic benefits will be required to settle the claim.

In relation to the above-mentioned contingent liabilities, S Ltd. has given an indemnification undertaking to H Ltd. up to a maximum of Rs.1 crore.

Rs.1 crore represents the acquisition date fair value of the indemnification undertaking.

Any amount which would be received in respect of the above undertaking shall not be taxable.

The tax bases of the assets and liabilities of S Ltd. is equal to their respective carrying values being recognised in its Balance Sheet.

Carrying value of non-current asset held for sale of Rs.4 crore represents its fair value less cost to sell in accordance with the relevant Ind AS.

In consideration of the additional stake purchased by H Ltd. on 1st January, 20X7, it has issued to the selling shareholders of S Ltd. 1 equity share of H Ltd. for every 2 shares held in S Ltd. Fair value of equity shares of H Ltd. as on 1st January, 20X7 is Rs.10,000 per share.

On 1st January, 20X7, H Ltd. has paid Rs.50 crore in cash to the selling shareholders of S Ltd. Additionally, on 31st March, 20X9, H Ltd. will pay Rs.30 crore to the selling shareholders of S Ltd. if return on equity of S Ltd. for the year ended 31st March, 20X9 is more than 25% per annum. H Ltd. has estimated the fair value of this obligation as on 1st January, 20X7 and 31st March, 20X7 as Rs.22 crore and Rs.23 crore respectively. The change in fair value of the obligation is attributable to the change in facts and circumstances after the acquisition date.

Quoted price of equity shares of S Ltd. as on various dates is as follows:

As on November, 20X6 Rs.350 per share

As on 1st January, 20X7 Rs.395 per share

As on 31st March, 20X7 Rs.420 per share

On 31st May, 20X7, H Ltd. learned that certain customer relationships existing as on 1st January, 20X7, which met the recognition criteria of an intangible asset as on that date, were not considered during the accounting of business combination for the year ended 31st March, 20X7. The fair value of such customer relationships as on 1st January, 20X7 was Rs.3.5 crore (assume that there are no temporary differences associated with customer relations; consequently, there is no impact of income taxes on customer relations).

On 31st May, 20X7 itself, H Ltd. further learned that due to additional customer relationships being developed during the period 1st January, 20X7 to 31st March, 20X7, the fair value of such customer relationships has increased to Rs.4 crore as on 31st March, 20X7.

On 31st December, 20X7, H Ltd. has established that it has obtained all the information necessary for the accounting of the business combination and that more information is not obtainable.

H Ltd. and S Ltd. are not related parties and follow Ind AS for financial reporting. Income tax rate applicable is 30%.

You are required to provide your detailed responses to the following, along with reasoning and computation notes:

- (a) What should be the goodwill or bargain purchase gain to be recognised by H Ltd. in its financial statements for the year ended 31st March, 20X7. For this purpose, measure non-controlling interest using proportionate share of the fair value of the identifiable net assets of S Ltd.
- (b) Will the amount of non-controlling interest, goodwill, or bargain purchase gain so recognised in (a) above change subsequent to 31st March, 20X7? If yes, provide relevant journal entries.
- (c) What should be the accounting treatment of the contingent consideration as on 31st March, 20X7?

Solution :

(i) As an only exception to the principle of classification or designation of assets as they exist at the acquisition date is that for lease contract and insurance contracts classification which will be based on the basis of the conditions existing at inception and not on acquisition date.

Therefore, H Ltd. would be required to retain the original lease classification of the lease arrangements and thereby recognise the lease arrangements as finance lease.

(ii) The requirements in Ind AS 37 'Provisions, Contingent Liabilities and Contingent Assets', do not apply in determining which contingent liabilities to recognise as of the acquisition date as per Ind AS 103 'Business Combination'. Instead, the acquirer shall recognise as of the acquisition date a contingent liability assumed in a business combination if it is a present obligation that arises from past events and its fair value can be measured reliably. Therefore, contrary to Ind AS 37, the acquirer recognises a contingent liability assumed in a business combination at the acquisition date even if it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation. Hence H Ltd. will recognize contingent liability of Rs.2.5 cr.

Since S Ltd. has indemnified for Rs.1 cr., H Ltd. shall recognise an indemnification asset at the same time for Rs.1 cr.

As per the information given in the question, this indemnified asset is not taxable. Hence, its tax base will be equal to its carrying amount. No deferred tax will arise on it.

(iii) As per Ind AS 103, non-current assets held for sale should be measured at fair value less cost to sell in accordance with Ind AS 105 'Non-current Assets Held for Sale and Discontinued Operations'. Therefore, its carrying value as per balance sheet has been considered in the calculation of net assets.

(iv) Any equity interest in S Ltd. held by H Ltd. immediately before obtaining control over S Ltd. is adjusted to acquisition-date fair value. Any resulting gain or loss is recognised in the profit or loss of H Ltd.

Calculation of purchase consideration as per Ind AS 103

Rs. in lakh

Investment in S Ltd.				
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On 1st Nov. 20X6	15%	$[(12/100) \times 395 \times 15\%]$	7.11
On 1st Jan. 20X7	45%		
Own equity given		$10,000 \times 12\% \times 45\% \times \frac{1}{2}$	270
Cash			50
Contingent consideration			<u>22</u>
			<u>349.11</u>

- (v) Calculation of deferred tax on assets and liabilities acquired as part of the business combination, including current tax and goodwill.

Item	Rs. in crore				
	Book value	Fair value	Tax base	Taxable (deductible) temporary difference	Deferred tax assets (liability) @ 30%
Property, plant and equipment	40	90	40	50	(15)
Intangible assets	20	30	20	10	(3)
Investments	100	350	100	250	(75)
Inventories	20	20	20	-	-
Trade receivables	20	20	20	-	-
Cash held in functional currency	4	4	4	-	-
Non-current asset held for sale	4	4	4	-	-
Indemnified asset	-	1	1	-	-
Borrowings	20	20	20	-	-
Trade payables	28	28	28	-	-
Provision for warranties	3	3	3	-	-
Current tax liabilities	4	4	4	-	-
Contingent liability		0.5	-	(0.5)	0.15
Deferred tax Liability					(92.85)

- (vi) Calculation of identifiable net assets acquired

	Rs.in crore	Rs.in crore
Property, plant and equipment	90	519
Intangible assets	30	-150.35
Investments	350	368.65
Inventories	20	
Trade receivables	20	
Cash held in functional currency	4	
Non-current asset held for sale	4	

Indemnified asset	<u>1</u>	
Total asset		519
Less: Borrowings	20	
Trade payables	28	
Provision for warranties	3	
Current tax liabilities	4	
Contingent liability (2 + 0.5)	2.50	
Deferred tax liability (W.N.2)	<u>92.85</u>	<u>(150.35)</u>
Net identifiable assets		<u>368.65</u>

(a) Calculation of NCI by proportionate share of net assets

Net identifiable assets of S Ltd. on 1.1.20X7 (Refer W.N.3) = 372.85 crore

NCI on 1.1.20X7 = 368.65 crore × 40% = 147.46 crore

Calculation of Goodwill as per Ind AS 103

Goodwill on 1.1.20X7 = Purchase consideration + NCI – Net assets
 = 349.11 + 147.46 – 368.65
 = 127.92 crore

(b) As per para 45 of Ind AS 103 'Business Combination', if the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the acquirer shall report in its financial statements provisional amounts for the items for which the accounting is incomplete.

During the measurement period, the acquirer shall retrospectively adjust the provisional amounts recognised at the acquisition date to reflect new information obtained about facts and circumstances that existed as of the acquisition date and, if known, would have affected the measurement of the amounts recognised as of that date.

During the measurement period, the acquirer shall also recognise additional assets or liabilities if new information is obtained about facts and circumstances that existed as of the acquisition date and, if known, would have resulted in the recognition of those assets and liabilities as of that date.

The measurement period ends as soon as the acquirer receives the information it was seeking about facts and circumstances that existed as of the acquisition date or learns that more information is not obtainable. However, the measurement period shall not exceed one year from the acquisition date.

Further, as per para 46 of Ind AS 103, the measurement period is the period after the acquisition date during which the acquirer may adjust the provisional amounts recognised for a business combination. The measurement period provides the acquirer with a reasonable time to obtain the information necessary to identify and measure the following as of the acquisition date in accordance with the requirements of this Ind AS:

(a) the identifiable assets acquired, liabilities assumed and any non-controlling interest in the acquiree;

- (b)
- (c); and
- (d) the resulting goodwill or gain on a bargain purchase.

Para 48 states that the acquirer recognises an increase (decrease) in the provisional amount recognised for an identifiable asset (liability) by means of a decrease (increase) in goodwill.

Para 49 states that during the measurement period, the acquirer shall recognise adjustments to the provisional amounts as if the accounting for the business combination had been completed at the acquisition date.

Para 50 states that after the measurement period ends, the acquirer shall revise the accounting for a business combination only to correct an error in accordance with Ind AS 8 'Accounting Policies, Changes in Accounting Estimates and Errors'.

On 31st December, 20X7, H Ltd. has established that it has obtained all the information necessary for the accounting of the business combination and the more information is not obtainable. Therefore, the measurement period for acquisition of S Ltd. ends on 31st December, 20X7.

On 31st May, 20X7 (i.e. within the measurement period), H Ltd. learned that certain customer relationships existing as on 1st January, 20X7 which met the recognition criteria of an intangible asset as on that date were not considered during the accounting of business combination for the year ended 31st March, 20X7. Therefore, H Ltd. shall account for the acquisition date fair value of customer relations existing on 1st January, 20X7 as an identifiable intangible asset. The corresponding adjustment shall be made in the amount of goodwill.

Accordingly, the amount of goodwill will be changed due to identification of new asset from retrospective date for changes in fair value of assets and liabilities earlier recognised on provisional amount (subject to meeting the condition above for measurement period). NCI changes would impact the consolidated retained earnings (parent's share). Also NCI will be increased or decreased based on the profit during the post-acquisition period.

Journal entry

Customer relationship	Dr.	3.5 crore
To NCI		1.4 crore
To Goodwill		2.1 crore

However, the increase in the value of customer relations after the acquisition date shall not be accounted by H Ltd., as the customer relations developed after 1st January, 20X7 represents internally generated intangible assets which are not eligible for recognition on the balance sheet.

- (c) Since the contingent considerations payable by H Ltd is not classified as equity and is within the scope of Ind AS 109 'Financial Instruments', the changes in the fair value shall be recognised in profit or loss. Change in Fair value of contingent consideration (23-22) Rs.1 crore will be recognized in the Statement of Profit and Loss.

Question 8 : Nov 2019 – PAPER

The Balance sheet of David Ltd. and Parker Ltd as on 31st march, 2019 is given below :

(Rs. in lakhs)		
Assets	David Ltd.	Parker Ltd.
Non-Current Assets :		
Property, plant and equipment	400	600
Investment	300	200
Current assets :		
Inventories	300	100
Financial Assets		
Traders receivables	400	200
Cash and cash equivalent	150	200
Others	300	300
Total	1,850	1,600
Equity and Liabilities		
Equity		
Share capital-Equity shares of Rs.100 each for Parker Ltd & Rs.10 each for David Limited	500	400
Other Equity	700	275
Non-Current liabilities :		
Long term borrowings	200	300
Long term provisions	100	80
Deferred Tax	20	55
Current Liabilities :		
Short term borrowings	130	170
Trade payables	200	320
Total	1,820	1,600

Other information :

- (i) David Ltd. acquired 70% shares of Parker Ltd. on 1st April, 2019 by issuing its own shares in the ratio of 1 share of David Ltd. for every 2 shares of Parker Ltd. The fair value of the shares of David Ltd. was Rs.50 per share.
- (ii) The fair value exercise resulted in the following :
 - (1) Fair value of property, plant and equipment (PPE) on 1st April, 2019 was Rs.450 lakhs.
 - (2) David Ltd. agreed to pay an additional payment as consideration that is higher of Rs.30 lakh and 25% of any excess profits in the first year after acquisition, over its profits in the preceding 12 months made by Parker Ltd. This additional amount will be due after 3 years. Parker Ltd. has earned Rs.20 lakh profit in the preceding year and expects to earn another Rs.10 Lakh.
 - (3) In addition to above, David Ltd. also has agreed to pay one of the founder shareholder-Director a payment of Rs.25 lakhs provided he says with the Company for two years after the acquisition.

- (4) Parker Ltd. had certain equity settled share-based payment award (original award) which got replaced by the new awards issued by David Ltd. As per the original term the vesting period was 4 years and as of the acquisition date the employees of Parker Ltd. have already served 2 years of service. As per the replaced awards, the vesting period has been reduced to one year (one year from the acquisition date). The fair value of the award on the acquisition date was as follows
- Original award – Rs.6 lakhs
Replacement award – Rs.9 lakhs
- (5) Parker Ltd. had a lawsuit pending with a customer who had made a claim of Rs.35 lakhs. Management reliably estimated the fair value of the liability to be Rs.10 lakhs
- (6) The applicable tax rate for both entities is 40%.

You are required to prepare opening consolidated balance sheet of David Ltd. as on 1st April, 2019 along with workings. Assume discount rate of 8%.

Solution :

1) Calculation of purchase consideration

- (a) Issue of shares

1 share for 2 shares held

No. of share of Parker	4 lakh
% Acquisition	70%
No. of share acquired	2.8 lakh
No. of share to be issued	1.4 lakh
Issue price	50
Consideration	70 lakhs

- (b) Contingent consideration = $\frac{30}{(1.08)^3} = 23.81$ lakhs

- (c) Replacement Award

Step1 : Fair value of original award = 6 lakh

Step 2 : Fair value replacement award = 9 lakh

Step 3 : Pre combination obligation = $\frac{6}{4} \times 2 = 3$ lakh

Step 4 : Post combination cost = 9 – 3 = 6 lakh

Note : Pre combination obligation = 3 lakh is paid off

Post combination cost = 6 lakh

Total : PC = A + B + C = 70 + 23.8 + 3 = 96.81 lakhs

2) Calculation of goodwill / gain from Bargain purchase

- (a) Calculation of Net Assets

Assets	: Property, Plant & Equipment	450
	Investments	200
	Inventories	100
	Trade Receivable	200

	Cash & Cash Equivalent	200	
	Other CA	<u>300</u>	1,450
Liabilities	: Long term Borrowings	300	
	Long term Provisions	80	
	Deferred tax	55	
	Short term Borrowings	170	
	Trade Payables	320	
	Contingent liability	<u>10</u>	<u>935</u>
			515
DTA	: Assets = 600 – 450 =	150	
	Liability = 10 – Nil =	10	
		160 × 40%	<u>64</u>
	Net Assets		<u>579</u>
(b)	Consideration paid	96.81	
	+ NCI (AT Prop. Share) (579 × 30%)	173.7	
		270.51	
	– Fair Value of Net Assets	579	
	Capital Reserve	308.49	
	Note : Amount payable to Director Should be booked as on Expense		

3) Consolidated balance sheet of David Ltd.

Assets

1)	Non Current Assets	
	Property, Plant & Equipment	850
	Investments	500
2)	Current Assets	
	Inventory	400
	FA	
	Trade Receivable	600
	Cash & Cash Equivalent	350
	Other CA	<u>600</u>
		<u>3,300</u>
	Equity & Liability	
1)	Equity	
	Share Capital	514
	Other Equity (700 + 308.49 + 56 3)	1067.49
	Non Controlling Interest	173.70
2)	Non Current Liability	
	Long term Borrowing	500
	Long term provisions (100 + 80 + 23.81)	203.81
	Deffered tax (20 + 55.64)	11

3) Current Liability	
Financial liability	
Short term Borrowings	300
Trade payable	520
Provisions for Law suit damage	<u>10</u>
	<u>3300</u>

Question 9 : Nov 2020 – RTP

Veera Limited and Zeera Limited are both in the business of manufacturing and selling of Lubricant. Veera Limited and Zeera Limited shareholders agree to join forces to benefit from lower delivery and distribution costs. The business combination is carried out by setting up a new entity called Meera Limited that issues 100 shares to Veera Limited's shareholders and 50 shares to Zeera Limited's shareholders in exchange for the transfer of the shares in those entities. The number of shares reflects the relative fair values of the entities before the combination. Also respective company's shareholders gets the voting rights in Meera Limited based on their respective shareholding.

Determine the acquirer by applying the principles of Ind AS 103 'Business Combinations'.

Solution :

As per IND AS 103 acquirer is

- Usually which issues equity
- Entity which gets longer voting rights
- Entity which has control over management
- Entity which is larger in size etc.

Based on information given in question entity Veera Ltd. is issued 100 shares of total of 150 shares i.e. $100/150 = 66.67\%$ which represents total voting right and \therefore Entity Veera is acquirer.

Question 10 : Nov 2020 – Paper

P Limited and S Limited are in business of manufacturing garments. P Limited holds 30% of equity shares of S Limited for last several years. P Limited obtains control of S Limited when it acquires further 65% stake of S Limited's shares, thereby resulting in a total holding of 95% on 31 December 2019. The acquisition had the following features:

- (i) P Limited transfers cash of Rs. 50,00,000 and issues 90,000 shares on 31 December 2019. The market price of P Limited's shares on the date of issue was Rs. 10 per share. The equity shares issued as per this transaction will comprise 5% of the post-acquisition capital of P Limited.
- (ii) P Limited agrees to pay additional consideration of Rs. 4,00,000, if the cumulative profits of S Limited exceeds Rs. 40,00,000 over the next two years. At the acquisition date, it is not considered probable that extra consideration will be paid. The fair value of contingent consideration is determined to be Rs. 2,00,000 at the acquisition date.
- (iii) P Limited spent acquisition-related costs of Rs. 2,00,000.

- (iv) The fair value of the NCI is determined to be Rs. 5,00,000 at the acquisition date based on market price. P Limited decided to measure non-controlling interest at fair value for this transaction.
- (v) P Limited has owned 30% of the shares in S Limited for several years. At 31 December 20.19, the investment is included in P Limited's consolidated balance sheet at Rs. 8,00,000. The fair value of previous holdings accounted for using the equity method is arrived at Rs. 18,00,000.

The fair value of S Limited's net identifiable assets at 31 December 2019 is Rs. 45,00,000, determined in accordance with Ind AS 103.

Analyze the transaction and determine the accounting under acquisition method for the business combination by P Limited.

Solution :

Identify the acquirer

In this case, P Limited has paid cash consideration to shareholders of S Limited. Further, the shares issued to S Limited pursuant to the acquisition do not transfer control of P Limited to erstwhile shareholders of S Limited. Therefore, P Limited is the acquirer and S Limited is the acquiree.

Determine acquisition date

As the control over the business of S Limited is transferred to P Limited on 31 December 2019, that date is considered as the acquisition date.

Determine the purchase consideration

The purchase consideration in this case will comprise of the following:

Cash consideration	Rs. 50,00,000
Equity shares issued (90,000 x 10 i.e., at fair value)	Rs. 9,00,000
Contingent consideration (at fair value)	Rs. 2,00,000
Fair value of previously held interest	Rs. 18,00,000
Total purchase consideration	Rs. 79,00,000

Acquisition cost incurred by and on behalf of P Limited for acquisition of S Limited should be recognised in the Statement of Profit and Loss. As such, an amount of Rs. 2,00,000 should be recognised in the Statement of Profit and Loss.

Fair value of identifiable assets and liabilities

The fair value of identifiable net assets (as given in the question) Rs. 45,00,000.

Non-Controlling Interest

The management has decided to recognise NCI at its fair value, which is given in the question as Rs. 5,00,000.

Re-measure previously held interests in case business combination is achieved in stages

In this case, the control has been acquired in stages i.e., before acquisition to control, P Limited exercised significant influence over S Limited. As such, the previously held interest should be measured at fair value and the difference between the fair value and the carrying amount as at the acquisition date should be recognised in the Statement of Profit and Loss. As such, an amount of Rs. 10,00,000 (i.e. 18,00,000 – 8,00,000) will be recognised in the Statement of Profit and Loss.

Determination of goodwill or gain on bargain purchase

Goodwill should be calculated as follows:

(Rs.)

Total consideration	79,00,000
Recognised amount of any non-controlling interest	5,00,000
Less: Fair value of net identifiable assets	(45,00,000)
Goodwill	39,00,000

Question 11 : Jan 2021 – Paper

On 1st April 2017, Kara Ltd. granted an award of 150 share options to each of its 1,000 employees, on condition of continuous employment with Kara Ltd. for three years and the benefits will then be settled in cash of an equivalent amount of share price. Fair value of each option on the grant date was Rs. 129.

Towards the end of 31st March 2018, Kara Ltd.'s share price dropped; so on 1st April 2018 management chose to reduce the exercise price of the options.

At the date of the re-pricing, the fair value of each of the original share options granted was Rs. 50 and the fair value of each re-priced option was Rs. 80. Thus, the incremental fair value of each modified option was Rs. 30.

At the date of the award, management estimated that 10% of employees would leave the entity before the end of three years (i.e., 900 awards would vest). During financial year 2018-2019, it became apparent that fewer employees than expected were leaving, so management revised its estimate of the number of leavers to only 5% (i.e. 950 awards would vest). At the end of 31st March 2020, awards to 930 employees actually vested.

Determine the expense for each year and pass appropriate journal entries as per the relevant Ind AS.

Solution :

Note: The first para of the question states that “benefits will then be settled in cash of an equivalent amount of share price.” This implies that the award is cash settled share-based payment. However, the second and third para talks about repricing of the option which arises in case of equity settled share-based payment.

Hence, two alternative solutions have been provided based on the information taking certain assumptions.

1st Alternative based on the assumption that the award is cash settled share-based payment.

In such a situation, the services received against share-based payment plan to be settled in cash are measured at fair value of the liability and the liability continues to be remeasured at every reporting date until it is actually paid off.

There is a vesting condition attached to the share-based payment plans i.e. to remain in service for next 3 years. The recognition of such share-based payment plans should be done by recognizing fair value of the liability at the time of services received and not at the date of grant. The liability so recognized will be fair valued at each reporting date and difference in fair value will be charged to profit or loss for the period.

Calculation of expenses:

For the year ended 31st March 2018

= Rs.50 x 150 awards x 900 employees x (1 year /3 years of service)
 = Rs.22,50,000

For the year ended 31st March 2019

Note: It is assumed that the fair value of Rs.80 each of repriced option continues at the end of the remaining reporting period ie 31st March, 2019 and 31st March, 2020

= [Rs.80 x 150 awards x 950 employees x (2 year / 3 years of service)] - Rs.22,50,000
 = Rs.7,60,00,000 – Rs.22,50,000 = Rs.53,50,000

For the year ended 31st March 2020

= [Rs.80 x 150 awards x 930 employees] - Rs.22,50,000 - Rs.53,50,000
 = Rs.1,11,60,000 – Rs.22,50,000 - Rs.53,50,000= Rs.35,60,000

Journal Entries

31st March, 2018			
Employee benefits expenses	Dr.	22,50,000	
To Share based payment liability (Fair value of the liability recognized)			22,50,000
31st March, 2019			
Employee benefits expenses	Dr.	53,50,000	
To Share based payment liability (Fair value of the liability re-measured)			53,50,000
31st March, 2020			
Employee benefits expenses	Dr.	35,60,000	
To Share based payment liability (Fair value of the liability recognized)			35,60,000
Share based payment liability	Dr.	1,11,60,000	
To Bank (Being liability for awards settled in cash)			1,11,60,000

2nd Alternative based on fair value at the grant date (ignoring the fact that the award has to be settled in cash).

Calculation of expenses:

For the year ended 31st March 2018

= [Rs.129 x 150 awards x 900 employees x (1 year /3 years of service)]
 = Rs.58,05,000

For the year ended 31st March 2019

Ind AS 102 requires the entity to recognise the effects of repricing that increase the total fair value of the share-based payment arrangement or are otherwise beneficial to the employee.

If the repricing increases the fair value of the equity instruments granted standard requires the entity to include the incremental fair value granted (ie the difference between the fair value of the repriced equity instrument and that of the original equity instrument, both estimated as at the date of the modification) in the measurement of the amount recognised for services received as consideration for the equity instruments granted.

If the repricing occurs during the vesting period, the incremental fair value granted is included in the measurement of the amount recognised for services received over the period from the repricing date until the date when the repriced equity instruments vest, in addition to the amount based on the grant date fair value of the original equity instruments, which is recognised over the remainder of the original vesting period. Accordingly, the amounts recognised are as follows:

Year ended	Calculation	Compensation expense for period Rs.	Cumulative compensation expense Rs.
31-Mar-18	[Rs.129 x 150 awards x 900 employees x (1 year /3 years of service)]	58,05,000	58,05,000
31-Mar-19	[Rs.129 x 150 awards x 950 employees x (2 year /3 years of service)] + (80-50) x 150 awards x 950 employees x (1 year / 2 years of service) - 58,05,000	85,87,500	1,43,92,500
31-Mar-20	[(Rs.129 + 30) x 150 awards x 930 employees] - 1,43,92,500	77,88,000	2,21,80,500

Journal Entries

31st March, 2018			
Employee benefits expenses To Outstanding Share based payment option (Fair value of the liability recognized)	Dr.	58,05,000	58,05,000
31st March, 2019			
Employee benefits expenses To Outstanding Share based payment option (Fair value of the liability re-measured)	Dr.	85,87,500	85,87,500
31st March, 2020			
Employee benefits expenses To Outstanding Share based payment option (Fair value of the liability recognized)	Dr.	77,88,000	77,88,000
Outstanding Share based payment option To Equity share capital (Being award settled)	Dr.	2,21,80,500	2,21,80,500

Question 12 : May 2021 – RTP

Bima Ltd. acquired 65% of shares on 1 June, 20X1 in Nafa Ltd. which is engaged in production of components of machinery. Nafa Ltd. has 1,00,000 equity shares of Rs. 10 each. The quoted market price of shares of Nafa Ltd. was Rs. 12 on the date of acquisition. The fair value of Nafa Ltd.'s identifiable net assets as on 1 June, 20X1 was Rs. 80,00,000.

Bima Ltd. wired Rs. 50,00,000 in cash and issued 50,000 equity shares as purchase consideration on the date of acquisition. The quoted market price of shares of Bima Ltd. on the date of issue was Rs. 25 per share.

Bima Ltd. also agrees to pay additional consideration of Rs. 15,00,000, if the cumulative profit earned by Nafa Ltd. exceeds Rs. 1 crore over the next three years. On the date of acquisition, Nafa Ltd. assessed and determined that it is considered probable that the extra consideration will be paid. The fair value of this consideration on the date of acquisition is Rs. 9,80,000. Nafa Ltd. incurred Rs. 1,50,000 in relation to the acquisition. It measures Non-controlling interest at fair value.

How will the acquisition of Nafa Ltd. be accounted by Bima Ltd., under Ind AS 103? Prepare detailed workings and pass the necessary journal entry.

Solution :

Computation of Goodwill / Capital reserve on consolidation as per Ind AS 103

Particulars	Rs.
Cost of investment:	
Share exchange (50,000 x 25)	12,50,000
Cash consideration	50,00,000
Contingent consideration	<u>9,80,000</u>
Consideration transferred at date of acquisition [A]	72,30,000
Fair value of non-controlling interest at date of acquisition [B] (1,00,000 x 35% x 12)	<u>4,20,000</u>
Total [C] = [A] + [B]	76,50,000
Net assets acquired at date of acquisition [D]	<u>(80,00,000)</u>
Capital Reserve [D] – [C]	<u>3,50,000</u>

In a business combination, acquisition-related costs (including stamp duty) are expensed in the period in which such costs are incurred and are not included as part of the consideration transferred. Therefore, Rs.1,50,000 incurred by Nafa Ltd. in relation to acquisition, will be ignored by Bima Ltd.

Journal entry at the date of acquisition by Bima Limited as per Ind AS 103:

	Rs.	Rs.
Identifiable net assets	Dr.	80,00,000
To Equity share capital (50,000 x 10)		5,00,000
To Securities Premium (50,000 x 15)		7,50,000
To Cash		50,00,000
To Provision for contingent consideration to Nafa Ltd.		9,80,000
To Non-controlling Interest		4,20,000
To Capital Reserve		3,50,000

Question 13 : July 2021 – Paper

As part of its business expansion strategy, UG Limited is in process of setting up a health care intermediates business. The process is at very initial stage. Towards this, UG Limited acquired on 1st April 2020, 100% ordinary shares of AG Limited. AG Limited manufactures health care intermediates. The purchase consideration of AG Limited was by way of a share exchange valued at Rs.1,750 lakhs. The fair value of AG Limited's net assets was Rs.750 lakhs, but this fair value does not include :

- A patent owned by AG Limited manufactures health care intermediate drug that has a remaining life of 10 years. A consultant has estimated the value of this patent at Rs.500 lakhs. However, the outcome of clinical trials for the same is awaited. If the trials are successful, the value of the drug would fetch estimated Rs.750 lakhs.
- AG Limited has developed and patented a new vaccine which has been approved for clinical use. The cost of developing the vaccine was Rs.600 lakhs. Based on an early assessment of its sales success; its market value has been estimated at Rs.1,000 lakhs by a valuer.

UG Limited has requested you to suggest the accounting treatment of the above transaction under applicable Ind As.

Solution :**Recognition Principle as per Ind AS:**

As per para 13 of Ind AS 103 'Business Combinations', the acquirer's application of the recognition principle and conditions may result in recognising some assets and liabilities that the acquiree had not previously recognised as assets and liabilities in its financial statements. This may be the case when the asset is developed by the entity internally and charged the related costs to expense.

Accounting Treatment:

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

- Patent owned by AG Limited:** The patent owned will be recognised at fair value by UG Limited even though it was not recognised by AG Limited in its financial statements. The patent will be amortised over the remaining useful life of the asset i.e. 10 years. Since the company is awaiting the outcome of the trials, the value of the patent cannot be estimated at Rs. 750 lakh and the extra Rs. 250 lakh should only be disclosed as a Contingent Asset and not recognised.
- Patent internally developed by AG Limited:** As per para 18 of Ind AS 103 'Business Combinations', the acquirer shall measure the identifiable assets acquired and the liabilities assumed at their acquisition date fair values. Since the patent developed has been approved for clinical use, it is an identifiable asset, hence the same will be measured at fair value i.e. Rs. 1,000 lakh on the acquisition date.

Hence the revised working would be as follows:

	Rs.
Fair value of net assets of AG Limited	750 lakh

Add: Patent (500 lakh + 1,000 lakh)	<u>1,500 lakh</u>
	2,250 lakh
Purchase consideration	<u>(1,750 lakh)</u>
Gain on bargain purchase	<u>500 lakh</u>

Question 14 : Nov 2021 – RTP

Company X is engaged in the business of exploration & development of Oil & Gas Blocks. Company X currently holds participating interest (PI) in below mentioned producing Block as follows :

Block Name	Company X	Company Y	Company Z	Total
AWM/01	30%	60%	10%	100%

For the above Block, Company X, Y & Z has entered into unincorporated Joint Venture.

Company Y is the Operator of the Block AWM/01. Company X & Company Z are the Joint Operators. Company Y incurs all the expenditure on behalf of Joint Venture and raise cash call to Company X & Company Z at each month end in respect of their share of expenditure incurred in Joint Venture. All the manpower and requisite facilities / machineries owned by the Joint venture and thereby owned by all the Joint Operators.

For past few months, due to liquidity issues, Company Z defaulted in payment of cash calls to operators. Therefore, company Y (Operator) has issued notice to company Z for withdrawal of their participating right from on 01.04.20X1. However, company Z has filed the appeal with arbitrator on 30.04.20X1.

Financial performance of company Z has not been improved in subsequent months and therefore company Z has decided to withdraw participating interest rights from Block AWM/01 and entered into sale agreement with Company X & Company Y. As per the terms of the agreement, dated 31.5.20X1, Company X will receive 33.33% share & Company Y will receive 66.67% share of PI rights owned by Company Z.

Company X is required to pay Rs.1 Lacs against 33.33% share of PI rights owned by Company Z. After signing of sale agreement, Operator (company Y) approach government of India for modification in PSC (Production Sharing Contract) i.e. removal of Company Z from PSC of AWM/01 and government has approved this transaction on 30.6.20X1. Government approval for the modification in PSC is essential given the industry in which the joint-operators operate.

Balance sheet of Company X & Company Z are as follows:

Particulars	Company X		Company Z	
	31.5.20X1 Rs.	30.6.20X1 Rs.	31.5.20X1 Rs.	30.6.20X1 Rs.
Assets				
Non-Current Assets				
Property, Plant & Equipment	5,00,000	10,00,000	1,50,000	3,00,000
Right of Use Asset	1,00,000	2,00,000	10,000	20,000
Development CWIP	50,000	1,00,000	50,000	1,00,000
Financial Assets				

Loan receivable	<u>25,000</u>	<u>50,000</u>	<u>25,000</u>	<u>50,000</u>
Total Non-Current Assets	<u>6,75,000</u>	<u>13,50,000</u>	<u>2,35,000</u>	<u>4,70,000</u>
Current assets				
Inventories	1,00,000	2,00,000	15,000	30,000
Financial Assets				
Trade receivables	1,50,000	3,00,000	50,000	1,00,000
Cash and cash equivalents	2,00,000	4,00,000	1,00,000	2,00,000
Other Current Assets	<u>2,25,000</u>	<u>50,000</u>	<u>25,000</u>	<u>50,000</u>
Total Current Assets	<u>6,75,000</u>	<u>9,50,000</u>	<u>1,90,000</u>	<u>3,80,000</u>
Total Assets	<u>13,50,000</u>	<u>23,00,000</u>	<u>4,25,000</u>	<u>8,50,000</u>
Equity and Liabilities				
Equity				
Equity share capital	3,00,000	3,00,000	1,00,000	1,00,000
Other equity	<u>2,00,000</u>	<u>3,00,000</u>	<u>75,000</u>	<u>2,50,000</u>
Total Equity	<u>5,00,000</u>	<u>6,00,000</u>	<u>1,75,000</u>	<u>3,50,000</u>
Liabilities				
Non-Current Liabilities				
Provisions	4,00,000	8,00,000	1,00,000	2,00,000
Other Liabilities	<u>1,50,000</u>	<u>3,00,000</u>	<u>50,000</u>	<u>1,00,000</u>
Total Non-Current Liabilities	<u>5,50,000</u>	<u>11,00,000</u>	<u>1,50,000</u>	<u>3,00,000</u>
Current Liabilities				
Financial Liabilities				
Trade Payables	<u>3,00,000</u>	<u>6,00,000</u>	<u>1,00,000</u>	<u>2,00,000</u>
Total Current Liabilities	<u>3,00,000</u>	<u>6,00,000</u>	<u>1,00,000</u>	<u>2,00,000</u>
Total Liabilities	<u>13,50,000</u>	<u>23,00,000</u>	<u>4,25,000</u>	<u>8,50,000</u>

Additional Information:

1. Fair Value of PPE & Development CWIP owned by Company Z as per Market participant approach is Rs. 5,00,000 & Rs. 2,00,000 respectively.
2. Fair Value of all the other assets and liabilities acquired are assumed to be at their carrying values (except cash & cash equivalents). Cash and cash equivalents of Company Z are not to be acquired by Company X as per the terms of agreement.
3. Tax rate is assumed to be 30%.
4. As per Ind AS 28, all the joint operators are joint ventures whereby each parties that have joint control of the arrangement have rights to the net assets of the arrangement and therefore every operator records their share of assets and liabilities in their books.

You need to determine the following:

1. Whether the above acquisition falls under business or asset acquisition as defined under business combination standard Ind AS 103?
2. Determine the acquisition date in the above transaction.
3. Prepare Journal entries for the above-mentioned transaction.

4. Draft the Balance Sheet for Company X based on your analysis in Part 1 above as at acquisition date.

Solution :

- (1) Ind AS 103 defines business as an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing goods or services to customers, generating investment income (such as dividends or interest) or generating other income from ordinary activities.

For a transaction to meet the definition of a business combination (and for the acquisition method of accounting to apply), the entity must gain control of an integrated set of assets and activities that is more than a collection of assets or a combination of assets and liabilities.

To be capable of being conducted and managed for the purpose identified in the definition of a business, an integrated set of activities and assets requires two essential elements— inputs and processes applied to those inputs.

Therefore, an integrated set of activities and assets must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output.

In the aforesaid transaction, Company X acquired share of participating rights owned by Company Z for the producing Block (AWM/01). The output exist in this transaction (Considering AWM/01) is a producing block. Also all the manpower and requisite facilities / machineries are owned by Joint venture and thereby all the Joint

Operators. Hence, acquiring participating rights tantamount to acquire inputs (Expertise Manpower & Machinery) and it is critical to the ability to continue producing outputs. Thus, the said acquisition will fall under the Business Acquisition and hence standard Ind AS 103 is to be applied for the same.

- (2) As per paragraph 8 of Ind AS 103, acquisition date is the date on which the acquirer obtains control of the acquiree. Further, paragraph 9 of Ind AS 103 clarifies that the date on which the acquirer obtains control of the acquiree is generally the date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree—the closing date. However, the acquirer might obtain control on a date that is either earlier or later than the closing date.

An acquirer shall consider all pertinent facts and circumstances in identifying the acquisition date. Since government of India (GOI) approval is a substantive approval for Company X to acquire control of Company Z’s operations, the date of acquisition cannot be earlier than the date on which approval is obtained from GOI. This is pertinent given that the approval from GOI is considered to be a substantive process and accordingly, the acquisition is considered to be completed only on receipt of such approval. Hence acquisition date in the above scenario is 30.6.20X1.

- (3) **Journal entry for acquisition**

Particulars	Amount (Rs.)	Amount (Rs.)

Property Plant & Equipment	Dr.	1,66,650	
Right-of-use Asset	Dr.	6,666	
Development CWIP	Dr.	66,660	
Financial Assets - Loan Receivables	Dr.	16,665	
Inventories	Dr.	9,999	
Trade Receivables	Dr.	33,330	
Other Current Assets	Dr.	16,665	
To Provisions			66,660
To Other Liabilities			33,330
To Trade Payables			66,660
To Deferred Tax Liability			29,997
To Cash & Cash Equivalent (Purchase consideration)			1,00,000
To Gain on bargain purchase (Other Comprehensive Income)			19,988
(Being assets acquired and liabilities assumed from Company Z recorded at fair value along gain on bargain purchase)			

(4)

**Balance Sheet of Company X as at 30.6.20X1
(Pre & Post Acquisition of PI rights pertaining to Company Z)**

Particulars	Pre-Acquisition	Adjustments	Post-Acquisition
	30.6.20X1		30.6.20X1
Assets			
Non - Current Assets			
Property Plant & Equipment	10,00,000	1,66,650	11,66,650
Right of Use Asset	2,00,000	6,666	2,06,666
Development CWIP	1,00,000	66,660	1,66,660
Financial Assets			
Loan receivable	<u>50,000</u>	16,665	<u>66,665</u>
Total Non-Current Assets	<u>13,50,000</u>		<u>16,06,641</u>
Current assets			
Inventories	2,00,000	9,999	2,09,999
Financial Assets			
Trade receivables	3,00,000	33,330	3,33,330
Cash and cash equivalents	4,00,000	(1,00,000)	3,00,000
Other Current Assets	50,000	16,665	66,665
Total Current Assets	<u>9,50,000</u>		<u>9,09,994</u>
Total Assets	<u>23,00,000</u>		<u>25,16,635</u>
Equity and Liabilities			
Equity			
Equity share capital	3,00,000	-	3,00,000
Other equity	3,00,000	-	3,00,000
Capital Reserve (OCI)	<u>-</u>	19,988	<u>19,988</u>

Total Equity	<u>6,00,000</u>		<u>6,19,988</u>
Liabilities			
Non-Current Liabilities			
Provisions	8,00,000	66,660	8,66,660
Other Liabilities	3,00,000	33,330	3,33,330
Deferred Tax Liability	-	29,997	<u>29,997</u>
Total Non-Current Liabilities	<u>11,00,000</u>		<u>12,29,987</u>
Current Liabilities			
Financial liabilities			
Trade Payables	<u>6,00,000</u>	66,660	<u>6,66,660</u>
Total Current Liabilities	<u>6,00,000</u>		<u>6,66,660</u>
Total Equity and Liabilities	<u>23,00,000</u>		<u>25,16,635</u>

Working Notes :

1. Determination of Company Z's balance acquired by Company X on 30.6.20X1 (Acquisition Date)

Particulars	As per	Carrying Value	Acquisition Date Value	Remarks
	Company Z			
	Books	33.33% Share	Rs.	
	30.6.20X1			
	Rs.	Rs.	Rs.	
Assets				
Non-Current Assets				
Property Plant & Equipment	3,00,000	99,990	1,66,650	Note 1
Right of Use Asset	20,000	6,666	6,666	
Development CWIP	1,00,000	33,330	66,660	Note 1
Financial Assets				
Loan receivable	<u>50,000</u>	<u>16,665</u>	<u>16,665</u>	
Total Non-Current Assets	<u>4,70,000</u>	<u>1,56,651</u>	<u>2,56,641</u>	
Current assets				
Inventories	30,000	9,999	9,999	
Financial Assets				
Trade receivables	1,00,000	33,330	33,330	
Cash and cash equivalents	2,00,000	66,660	66,660	
Other Current Assets	<u>50,000</u>	<u>16,665</u>	<u>16,665</u>	
Total Current Assets	<u>3,80,000</u>	<u>1,26,654</u>	<u>1,26,654</u>	
Liabilities				
Non-Current Liabilities				
Provisions	2,00,000	66,660	66,660	
Other Liabilities	<u>1,00,000</u>	<u>33,330</u>	<u>33,330</u>	
Total Non-Current Liabilities	<u>3,00,000</u>	<u>99,990</u>	<u>99,990</u>	
Current Liabilities				
Financial liabilities				

Trade Payables	<u>2,00,000</u>	<u>66,660</u>	<u>66,660</u>
Total Current Liabilities	<u>2,00,000</u>	<u>66,660</u>	<u>66,660</u>

Note 1: Fair Value of PPE:

Fair Value of PPE in Company Z Books	Rs. 5,00,000
33.33% Share acquired by Company X	Rs. 1,66,650

Note 2: Fair Value of Development CWIP:

Fair Value of PPE in Company Z Books	Rs. 2,00,000
33.33% Share acquired by Company X	Rs. 66,660

2. Computation Goodwill/Bargain Purchase Gain

Particulars	As at 30.6.20X1 (Rs.)
Total Non - Current Assets	2,56,641
Total Current Assets (Except Cash & Cash Equivalent of Rs. 66,660) (1,26,654 – 66,660)	59,994
Total Non-Current Liabilities	(99,990)
Total Current Liabilities	(66,660)
Total Deferred Tax Liability (Refer Working note 3)	<u>(29,997)</u>
Net Assets Acquired	1,19,988
Less: Consideration Paid	<u>(1,00,000)</u>
Gain on Bargain Purchase (To be transferred to OCI)	<u>19,988</u>

*In extremely rare circumstances, an acquirer will make a bargain purchase in a business combination in which the value of net assets acquired in a business combination exceeds the purchase consideration. The acquirer shall recognise the resulting gain in other comprehensive income on the acquisition date and accumulate the same in equity as capital reserve, if the reason for bargain purchase gain is clear and evidence exist. If there does not exist clear evidence of the underlying reasons for classifying the business combination as a bargain purchase, then the gain shall be recognised directly in equity as capital reserve. Since in above scenario it is clearly evident that due to liquidity issues, Company Z has to withdraw their participating right from AWM/01. The said bargain purchase gain should be transferred to other comprehensive income on the acquisition date.

3. Computation of Deferred Tax Liability arising on Business Combination

Particulars	Acquisition Date Value (Rs.)
Total Non - Current Assets	2,56,641

Total Current Assets (Except Cash & Cash Equivalent of Rs. 66,660)	59,994
Total Non-Current Liabilities	-99,990
Total Current Liabilities	-66,660
Net Assets Acquired at Fair Value	1,49,985
Book value of Net Assets Acquired	49,995
Temporary Difference	99,990
DTL @ 30% on Temporary Difference	29,997

Note: As per Ind AS 103, in case an entity acquires another entity step by step through series of purchase then the acquisition date will be the date on which the acquirer obtains control. Till the time the control is obtained the investment will be accounted as per the requirements of other Ind AS 109, if the investments are covered under that standard or as per Ind AS 28, if the investments are in Associates or Joint Ventures.

If a business combination is achieved in stages, the acquirer shall remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognise the resulting gain or loss, if any, in profit or loss or other comprehensive income, as appropriate.

Since in the above transaction, company X does not hold any prior interest in Company Z & company holds only 30% PI rights in Block AWM/01 through unincorporated joint venture, this is not a case of step acquisition.

Question 15 : May 2022 – RTP

Entity A acquires entity B. Entity A agrees with the former shareholders of entity B to pay Rs. 900, with an additional payment of Rs. 500 if the subsequent earnings of entity B reach a specified target in three years. The former shareholders also become employees. On the acquisition date, the fair value of the net assets of entity B amount to Rs. 850, and the fair value of additional payment is estimated at Rs. 200. At the acquisition date, the outflow of additional payment is not probable.

Over the next three years, the cumulative earnings of entity B (before considering the effects of the additional payments) amount to Rs. 1,050. At the end of year three, entity A pays Rs. 500 as the conditions were met.

State the impact on the financial position and results of classifying the payments as remuneration and contingent consideration.

Solution :

The impact on the financial position and results of classifying the payments as remuneration and contingent consideration is tabulated as follows:

	Additional Payment is classified as	
	Remuneration	Contingent consideration
Consideration	900	900

Fair value of additional payment	0	200
Total consideration	900	1,100
Fair value of net assets	(850)	(850)
Goodwill at acquisition date	50	250
Subsequent changes in additional payment	0	0
Total Goodwill	50	250
Cumulative earnings (before considering additional payment)	1,050	1,050
Impact of additional payment	(500)	(300)
Reported results across three years	550	750

Question 16 : May 2022 – Paper

The draft Balance Sheet of JAY Ltd. and KAY Ltd as 31st March 2021 is given below :

Particulars	JAY Limited (Rs. In lakhs)	KAY Limited (Rs. In lakhs)
ASSETS		
Non current Assets		
Property, Plant and Equipment	400	500
Investments	450	120
Current Assets		
Inventories	180	130
Financial Assets		
- Trade Receivables	520	270
- Cash and Cash Equivalents	260	145
- others	350	175
Total	2,160	1,340
Equity and Liabilities		
Equity		
Share Capital	600	450
- JAY Limited : Equity Shares of Rs.10 each		
- KAY Limited : Equity Share of Rs.100 each		
Other Equity	725	210
Non Current Liabilities		
Financial Liabilities		
- Long Term Borrowings	350	250
Long Term Provisions	70	80
Deferred Tax	40	20
Current Liabilities		
Financial Liabilities		
- Short Term Borrowings	125	145
- Trade Payables	250	185

Total	2,160	1,340
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Other Information :

- a. JAY Ltd. acquired 75% shares of KAY Ltd. on 1st April 2021 by issuing its own shares in the ratio of 2 shares of JAY Ltd. for every 3 shares of KAY Ltd. The fair value of the shares of JAY Ltd. was Rs.50 per share.
 - b. The fair value exercise resulted in the following :
 - i) Fair value of Property, Plant and Equipment of KAY Ltd. on 1st April, 2021 was Rs.425 Lakhs;
 - ii) JAY Ltd. also agreed to pay an additional payment as consideration that is higher of Rs.45 Lakhs and 30% of any excess profits in the first year, after acquisition, over its profits in the preceding 12 months made by KAY Ltd. This additional amount will be due after 3 years. Kay Ltd. has earned Rs.15 Lakhs profits in the preceding year and expected to earn another Rs.20 Lakhs;
 - iii) In addition to the above, JAY Ltd. also had agreed to pay one of the founder shareholder a payment of Rs.22 Lakhs provided he stays with the Company for 3 years after acquisition;
 - iv) KAY Ltd. had certain equity settled share based payment award (original award) which got replaced by the new awards issued by JAY Ltd. As per the original terms, the vesting period was 5 years and as of the acquisition date the employees of KAY Ltd. have already served 2 years of service. As per the replaced awards, the vesting period has been reduced to 1 year (1 year from the acquisition date). The fair value of the award on the acquisition date was as follows :
 - Original award – Rs.6 Lakhs
 - Replacement award – Rs.9 lakhs
 - v) KAY Ltd. had a lawsuit pending with a customer who made a claim of Rs.70 Lakh. Management reliably estimated the fair value of the liability to be Rs.75 Lakhs.
 - vi) The applicable tax rate for both entities is 30%.
- You are to prepare consolidated Balance sheet of JAY Ltd. as on 1st April, 2021. Assume 10% per annum discount rate. Management and working notes should form part of your answer.

Solution :

Consolidated Balance Sheet of JAY Ltd. as on 1st April, 2021 (Rs. in lakh)

	Amount
Assets	
Non-Current Assets:	
Property, plant and equipment	825.00
Financial assets	
Investment	570.00
Current assets:	
Inventories	310.00
Financial assets	

Trade receivables	790.00
Cash and cash equivalents	405.00
Others	525.00
Total	3425.00
Equity and Liabilities	
Equity	
Share capital - Equity shares of Rs. 10 each	622.50
Other Equity	1120.38
Non-controlling Interest	150.56
Non-Current liabilities:	
Financial Liabilities	
Long term borrowings	600.00
Long term provisions	183.81
Deferred tax	35.25
Current Liabilities:	
Financial Liabilities	
Short term borrowings	270.00
Trade payables	435.00
Provision for Lawsuit damages	7.50
Total	3425.00

Management Notes:

- a. As per Ind AS 103, the acquirer is required to record the assets and liabilities acquired at their respective fair value. Accordingly, the PPE of KAY Ltd. will be recorded at Rs. 425 lakh.
- b. The value of replacement award is allocated between consideration transferred and post combination expense. The portion attributable to purchase consideration is determined based on the fair value of the replacement award for the service rendered till the date of the acquisition. Accordingly, Rs. 2.4 lakh (6 x 2/5) is considered as a part of purchase consideration and is credited to JAY Ltd. equity as this will be settled in its own equity. The balance of Rs. 6.60 lakh (Rs. 9 lakh – Rs. 2.4 lakh) will be recorded as compensation expense in the post combination financial statements over the remaining life, which is 1 year in this scenario.
- c. There is a difference between contingent consideration and deferred consideration. In the given case Rs. 45 lakh is the minimum payment to be paid after 3 years and accordingly will be considered as deferred consideration. The other element is if company meet certain target, then they will get 30% of that or Rs. 45 lakh whichever is higher. In the given case, the minimum what is expected to be paid has been considered and the fair value of the contingent consideration has been considered as zero. The impact of time value on deferred consideration has been given @ 10%.
- d. The additional consideration of Rs. 22 lakh to be paid to the founder shareholder is contingent to him/her continuing in employment and hence this will be considered as

employee compensation and will be recorded as post combination expenses in the income statement of JAY Ltd.

Working Notes:

1. Computation for Purchase consideration

Particulars		Amount (Rs.)
Share capital of KAY Ltd.		<u>4,50,00,000</u>
Number of shares	4,50,000	
Shares to be issued 3:2	3,00,000	
Fair value Rs. per share		<u>50</u>
		Rs. in lakh
PC (3,00,000 x 75% x Rs. 50 per share) (A)		112.50
Deferred consideration after discounting Rs. 45 lakh for 3 years @ 10% (P.V. Factor 0.7513) (B)		33.81
Replacement award market-based measure of the acquiree award (6) x ratio of the portion of the vesting period completed (2) / greater of the total vesting period (3) or the original vesting period (5) of the acquiree award ie (6 x 2/5) (C)		<u>2.40</u>
PC in lakh (A+B+C)		<u>148.71</u>

2. Allocation of Purchase price

Particulars	Book value (A)	Fair value (B)	FV adjustment (A-B)
Property, plant and equipment	500.00	425.00	(75.00)
Investment	120.00	120.00	
Inventories	130.00	130.00	
Financial assets:			
Trade receivables	270.00	270.00	
Cash and cash equivalents	145.00	145.00	
Others	<u>175.00</u>	<u>175.00</u>	
	1,340.00	1,265.00	(75.00)
Less: Long term borrowings	(250.00)	(250.00)	
Long term provisions	(80.00)	(80.00)	
Deferred tax	(20.00)	(20.00)	
Short term borrowings	(145.00)	(145.00)	
Trade payables	(185.00)	(185.00)	
Contingent liability		<u>(7.50)</u>	<u>(7.50)</u>
Net assets (X)	<u>660.00</u>	577.50	(82.50)

Deferred tax asset on FV adjustment (82.50 x 30%) (Y)		<u>24.75</u>	
Net assets (X+Y)		602.25	
Non-controlling interest (602.50 x 25%) rounded off		150.56	
Purchase consideration (PC)		148.71	
Capital Reserve (Net assets – NCI – PC)		302.98	

3. Computation of consolidated amounts of consolidated financial statements

(Rs.in lakh)

	JAY Ltd.	KAY Ltd. (pre-acquisition)	PPA Allocation	Total
Assets				
Non-current assets:				
Property, plant and equipment	400.00	500.00	(75.00)	825.00
Investment	450.00	120.00		570.00
Current assets:				
Inventories	180.00	130.00		310.00
Financial assets:				
Trade receivables	520.00	270.00		790.00
Cash and cash equivalents	260.00	145.00		405.00
Others	350.00	175.00	-	525.00
Total	2160.00	1340.00	(75.00)	3425.00
Equity and Liabilities				
Equity				
Share capital - Equity shares of Rs. 10 each	600.00			
Shares allotted to KAY Ltd. (W.N.1) (3,00,000 x 75% x Rs. 10 per share)			22.50	622.50
Other Equity	725.00			1,120.38
Replacement award (W.N.1)			2.40	
Security Premium (W.N.1) (3,00,000 shares x 75% x Rs. 40)			90.00	
Capital Reserve (W.N.2)			302.98	
Non-controlling interest (W.N.2)			150.56	150.56
Non-current liabilities:				
Financial liabilities				

Long term borrowings	350.00	250.00		600.00
Long term provisions (W.N.1)	70.00	80.00	33.81	183.81
Deferred tax (W.N.2)	40.00	20.00	(24.75)	35.25
Current liabilities:				
Financial liabilities				
Short term borrowings	125.00	145.00		270.00
Trade payable	250.00	185.00		435.00
Liability for lawsuit damages	-	-	7.50	7.50
Total	2160.00	680.00	585.00	3425.00

Question 17 : Nov 2022 – RTP

How should contingent consideration payable in relation to a business combination be accounted for on initial recognition and at the subsequent measurement in the following cases:

- (a) On 1st April 20X1, A Ltd. acquires 100% interest in B Ltd. As per the terms of agreement the purchase consideration is payable in the following 2 tranches:
- an immediate issuance of 10 lakhs shares of A Ltd. having face value of Rs. 10 per share;
 - a further issuance of 2 lakhs shares after one year if the profit before interest and tax of B Ltd. for the first year following acquisition exceeds Rs. 1 crore.
- The fair value of the shares of A Ltd. on the date of acquisition is Rs. 20 per share. Further, the management has estimated that on the date of acquisition, the fair value of contingent consideration is Rs. 25 lakhs.
- During the year ended 31st March, 20X2, the profit before interest and tax of B Ltd. exceeded Rs. 1 crore. As on 31st March, 20X2, the fair value of shares of A Ltd. is Rs. 25 per share.
- (b) Continuing with the fact pattern in (a) above except for:
- The number of shares to be issued after one year is not fixed.
 - Rather, A Ltd. agreed to issue variable number of shares having a fair value equal to Rs. 40 lakhs after one year, if the profit before interest and tax for the first year following acquisition exceeds Rs. 1 crore.

Solution :

Paragraph 39 of Ind AS 103 provides that the consideration the acquirer transfers in exchange for the acquiree includes any asset or liability resulting from a contingent consideration arrangement. The acquirer shall recognise the acquisition-date fair value of contingent consideration as part of the consideration transferred in exchange for the acquiree.

With respect to contingent consideration, obligations of an acquirer under contingent consideration arrangements are classified as equity or a liability in accordance with Ind AS 32. Paragraph 58 of Ind AS 103 provides guidance on the subsequent accounting for contingent consideration.

- (a) (i) **In the given case, the amount of purchase consideration to be recognized on initial recognition shall as follows:**

Fair value shares issued (10,00,000 x Rs. 20)	Rs. 2,00,00,000
Fair value of contingent consideration	<u>Rs. 25,00,000</u>
Total purchase consideration	<u>Rs. 2,25,00,000</u>

(ii) Subsequent measurement of contingent consideration payable for business combination

In the given case, given that the acquirer has an obligation to issue fixed number of shares on fulfillment of the contingency, the contingent consideration will be classified as equity as per the requirements of Ind AS 32.

As per paragraph 58 of Ind AS 103, contingent consideration classified as equity should not be re-measured and its subsequent settlement should be accounted for within equity.

In the given case, the obligation to pay contingent consideration amounting to Rs. 25,00,000 is recognised as a part of equity and therefore not be re-measured subsequently or on issuance of shares.

(b) (i) In the given case, the amount of purchase consideration to be recognized on initial recognition is as follows:

Fair value shares issued (10,00,000 x Rs. 20)	Rs. 2,00,00,000
Fair value of contingent consideration	<u>Rs. 25,00,000</u>
Total purchase consideration	<u>Rs. 2,25,00,000</u>

(ii) Subsequent measurement of contingent consideration payable for business combination

In the given case, the contingent consideration will be classified as liability as per Ind AS 32.

As per paragraph 58 of Ind AS 103, contingent consideration not classified as equity should be measured at fair value at each reporting date and changes in fair value should be recognised in profit or loss.

As at 31st March, 20X2 (being the date of settlement of contingent consideration), the liability would be measured at its fair value and the resulting loss of Rs. 15,00,000 (Rs. 40,00,000 – Rs. 25,00,000) should be recognised in the profit or loss for the period. A Ltd. would recognize issuance of 1,60,000 (Rs. 40,00,000 / 25) shares at a premium of Rs. 15 per share.

Question 18 : May 2023 – RTP

In October 20X1, IHL acquired 75% of Very Relevant Limited by paying cash consideration of Rs.0.80 million. The fair value of non-controlling interest on the date of acquisition is Rs. 0.20 million. The value of Very Relevant Limited's identifiable net assets as per Ind AS 103 is Rs. 1.10 million.

With respect to acquisition of Very Relevant Limited, determine the value of gain on bargain purchases, when NCI is measured as per:

- Fair value method
- Proportionate share of net identifiable assets method.

Solution :

(a) When NCI is measured as per fair value method

	Rs. In million
Fair value of consideration transferred	0.80
Fair value of non-controlling interest	<u>0.20</u>
	1.00
Value of Very Relevant Limited's identifiable net assets as per Ind AS 103	<u>(1.10)</u>
Gain on bargain purchase	<u>0.10</u>

(b) When NCI is measured as per proportionate share method

	Rs. In million
Fair value of consideration transferred	0.80
Proportional share of non-controlling interest in the net identifiable assets of acquiree (1.10 x 25%)	<u>0.275</u>
	1.075
Value of Very Relevant Limited's identifiable net assets as per Ind AS 103	<u>(1.10)</u>
Gain on bargain purchase	<u>0.025</u>

Question 19 : May 2023 – Paper

The draft balance sheets of Swan Limited and Duck Limited as at 31st March, 2023 is as under :

Particulars	Amount in Rs. Lakhs	
	Swan Limited	Duck Limited
Assets		
Non – Current Assets		
Property, Plant and Equipment	800	1,000
Investments	900	240
Current Assets		
Inventories	360	260
Financial Assets		
– Trade Receivables	1,040	540
– Cash & Cash Equivalents	520	290
Other Current Assets	700	350
Total	4,320	2,680
Equity and Liabilities		
Equity		
Share Capital		
– Swan Limited : Equity Shares of Rs.10/- each	1,200	–
– Duck Limited : Equity Shares of Rs.100/- each	–	900
Other Equity	1,450	420

Non – Current Liabilities		
Financial Liabilities		
– Long Term Borrowings	700	500
Long Term Provisions	140	200
Deferred Tax	80	–
Current Liabilities		
Financial Liabilities		
– Short Term Borrowings	250	290
– Trade Payables	500	370
Total	4,320	2,680

On 1st April 2023, Swan Limited acquired 80% equity shares of Duck Limited. Swan Limited agreed to pay to each shareholder of Duck Limited, Rs.20/- per equity share in cash and to issue five equity shares of Rs.10/- each of Swan Limited in lieu of every six shares held by the shareholder Duck Limited. The fair value of the shares of Swan Limited was Rs.100/- per share as on the date of acquisition.

Swan Limited also agreed to pay an additional consideration being higher of Rs.90 lakhs and 30% of any excess profits in the first year, after acquisition, over Duck Limited’s profits in the preceding 12 months (financial year 2022 - 23) made by Duck Limited. The additional amount will be due in 3 years post the date of acquisition. Duck Limited had earned Rs.30 lakhs profit in the preceding year and expects to earn Rs.40 lakhs in financial year 2023 - 24.

The fair value exercise resulted in the following :

- i. Fair value of Property, Plant and Equipment and Investments of Duck Limited on 1st April 2023 was Rs.1200 lakhs and Rs.300 lakhs respectively.
- ii. Duck Limited owns a popular brand name that meets the recognition criteria for Intangible Assets under Ind AS 103 ‘Business Combinations’. Independent valuers have attributed a fair value of Rs.250 lakhs for the brand. However, the brand does not have any cost for tax purposes and no tax deductions are available for the same.
- iii. Following is the statement of Contingent Liabilities of Duck Limited as on 1st April 2023 :

Particulars	Fair Value (Rs./Lakhs)	Remarks
Law suit filed by a customer for a claim of Rs.20 lakhs	5	It is not probable that an outflow of resources embodying economic benefits will be required to settle the claim. Any amount which would be paid in respect of law suit will be tax deductible.

Income tax demand of Rs.70 lakhs raised by tax authorities. Duck Limited has challenged the demand in the High Court	20	It is not probable that an outflow of resources embodying economic benefits will be required to settle the claim.
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- iv. Duck Limited had certain equity settled share based payment awards (original award) which were replaced by the new issued by Swan Limited. As per the terms of original award, vesting period was 5 years and as of the acquisition date the employees of Duck Limited had already served 2 years of service. As per the new awards, the vesting period has been reduced to 1 year (1 year from the acquisition date). The fair value of the award on acquisition date was as follows :
Original Awards : Rs.12 lakhs
New Awards : Rs.18 lakhs.
- v. Further, Swan Limited has also agreed to pay one of the founder shareholder of Duck Limited a sum of Rs.15 lakhs provided he stays with the Company for two years after the acquisition.
- vi. The acquisition cost of Swan Limited for Duck Limited was Rs.26 lakhs.
- vii. The applicable tax rate for both the companies is 30 %.
- viii. Assume 10 % per annum discount rate.
- ix. Also, assume, unless stated otherwise, all items have a fair value and tax base equal to their carrying amounts at the acquisition date.

You are required to prepare opening Consolidated Balance Sheet of Swan Limited as on 1st April 2023. Working Notes should form part of your answer.

Solution :

Consolidated Balance Sheet of Swan Ltd as on 1st April, 2023

	Notes No.	Rs. in lakhs
Assets		
Non-current assets		
Property, plant and equipment	9	2,000.00
Intangible assets	10	250.00
Financial assets		
Investment	11	1,200.00
Current assets		
Inventories	12	620.00
Financial assets:		
Trade receivables	13	1,580.00
Cash and cash equivalents	14	640
Other current assets	15	1,050.00
Total		7,340.00
Equity and Liabilities		

Equity		
Share capital - Equity shares of Rs. 10 each	1	1,260.00
Other equity	2	2,475.18
Non-controlling interest (W.N.4)		330.70
Non-current liabilities		
Financial liabilities		
Long-term borrowings	3	1,200.00
Long-term provisions	4	407.62
Deferred tax liability	5	231.50
Current Liabilities		
Financial liabilities		
Short-term borrowings	6	540.00
Trade payables	7	870.00
Short-term provision	8	25.00
Total		7340.00

Notes to Accounts (All figures are Rs. in lakhs)

1. Equity Share capital

Equity shares of Rs. 10 each as per the balance sheet before acquisition of Duck Ltd.	1,200	
Shares allotted to Duck Ltd. (7,50,000 x 80% x Rs. 10)	<u>60</u>	1,260

2. Other Equity

As per the balance sheet before acquisition of Duck Ltd.	1,450		
Less: Acquisition cost	<u>(26)</u>	1,424	
Replacement award		4.80	
Security Premium (7,50,000 shares x 80% x Rs. 90)		540	
Capital Reserve (W.N.5)		<u>506.38</u>	2,475.18

3. Long-term borrowings

As per the balance sheet before acquisition of Duck Ltd.	700	
Duck Ltd.	<u>500</u>	1,200

4. Long-term provisions

As per the balance sheet before acquisition of Duck Ltd.	140	
Deferred consideration	67.62	
Duck Ltd.	<u>200</u>	407.62

5. Deferred tax liability

As per the balance sheet before acquisition of Duck Ltd.	80	
Deferred tax impact due to acquisition of Duck Ltd. (W.N.2)	<u>151.50</u>	231.50

6. Short term borrowings

As per the balance sheet before acquisition of Duck Ltd.	250	
Duck Ltd.	<u>290</u>	540

7. Trade payables

As per the balance sheet before acquisition of Duck Ltd.	500	
Duck Ltd.	<u>370</u>	870

8. Short-term provisions

Lawsuit damages	5	
Income-tax demand	<u>20</u>	25

9. Property, plant and equipment

As per the balance sheet before acquisition of Duck Ltd.	800	
Duck Ltd.	<u>1,200</u>	2,000

10. Intangible assets

Brand of Duck Ltd. acquired		250
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11. Investment

As per the balance sheet before acquisition of Duck Ltd.	900	
Duck Ltd.	<u>300</u>	1,200

12. Inventories

As per the balance sheet before acquisition of Duck Ltd.	360	
Duck Ltd.	<u>260</u>	620

13. Trade receivables

As per the balance sheet before acquisition of Duck Ltd.	1,040	
Duck Ltd.	<u>540</u>	1,580

14. Cash and cash equivalents

As per the balance sheet before acquisition of Duck Ltd.	520		
Less: Acquisition cost paid	(26)		
Less: Paid to Duck Ltd.	<u>(144)</u>	350	
Duck Ltd.		<u>290</u>	640

15. Other current assets

As per the balance sheet before acquisition of Duck Ltd.	700	
Duck Ltd.	<u>350</u>	1,050

Working Notes:

1. Computation of Purchase Consideration

Particulars	No. of shares	Rs. in lakhs
Share capital of Duck Ltd.		<u>900</u>
Number of shares	9,00,000	
Shares to be issued (5 shares against 6 shares of Duck Ltd.)	7,50,000	
Fair value of Swan Ltd.'s share is Rs. 100 per share		
Purchase consideration		
Shares issued (7,50,000x 80% x Rs. 100 per share) (A)		600
Cash payment (Rs. 20 x 9,00,000 x 80%) (B)		144
Deferred consideration (discounting Rs. 90 lakhs for 3 years @10%) ©		67.62
Replacement award [Market based measure of the acquiree award (12) x ratio of the portion of the vesting period completed (2) / greater of the total vesting period (3) or the original vesting period (5) of the acquiree award (i.e. 12 x 2/5)] (D)		<u>4.80</u>
Purchase consideration for 70% shares (A + B + C + D)		<u>816.42</u>

2. Computation of deferred tax impact due to change in fair value of asset and liabilities acquired

Particulars	Book value (A)	Fair value (B)	FV adjustment (A-B)
Property, plant and equipment	1,000	1,200	200
Intangible assets (Brand)	-	250	250
Investment	240	<u>300</u>	<u>60</u>
		1,750	510
Less: Contingent liability acquired Provision for lawsuit damages			<u>(5)</u>
Net difference in fair value			<u>505</u>
Deferred tax liability @ 30%			151.5

3. Computation of fair value of net identifiable assets acquired from Duck Ltd.

Particulars	Book value
Total assets as per the balance sheet	2,680
Add: Fair value adjustment in PPE and Investment (200+60)	260
Add: Intangible assets (Brand)	<u>250</u>

Fair value of total identifiable assets		3,190
Less: Total liabilities as per the balance sheet (500+200+290+370)		(1,360)
Less: Contingent liability acquired		
Lawsuit damages 5	5	
Income tax demand 20	<u>20</u>	(25)
Less: Defer tax liability (W.N.2)		<u>(151.50)</u>
Fair value of net identifiable assets (100%)		<u>1,653.50</u>

4. Computation of non-controlling interest in Duck Ltd. (Proportionate share basis)

Non-controlling interest (1,653.50 x 20%) = 330.70

5. Computation of capital reserve on acquisition of Duck Ltd.

Particulars	Book value
Fair value of net identifiable assets	1,653.50
Less: Purchase consideration	(816.42)
Less: NCI (W.N.4)	<u>(330.70)</u>
Capital reserve	<u>506.38</u>

Notes:

- The value of replacement award is allocated between consideration transferred and post combination expense. The portion attributable to purchase consideration is determined based on the fair value of the replacement award for the service rendered till the date of the acquisition. Accordingly, Rs. 4.8 lakh (12 x 2/5) is considered as a part of purchase consideration and is credited to Swan Ltd.'s equity as this will be settled in its own equity. Since the fair value of the award on the acquisition date is Rs. 18 lakh the balance of (18 - 4.8) Rs. 13.2 lakh will be recorded as employee expense in the books of Duck Ltd. over the remaining life, which is 1 year in this scenario.
- With respect to deferred consideration, Rs. 90 lakh is the minimum payment to be paid after 3 years. The other element is if company meet certain target then they will get 30% of that or Rs. 90 lakh whichever is higher. In the given case, since the minimum what is expected to be paid the fair value of the contingent consideration has been considered as zero. The impact of time value on deferred consideration has been given @ 10%.
- The additional consideration of Rs. 15 lakhs to be paid to the founder shareholder is contingent to him/her continuing in employment and hence this will be considered as employee compensation and will be recorded as post combination expenses in the statement of profit and loss of Duck Ltd.

Question 20 : Nov 2023 – RTP

Mini Limited is a manufacturing entity in textile industry. Mini Limited decided to reduce the cost of manufacturing by setting up its own power plant for their captive consumption. As per market research report, there was non-operational power plant in nearby area. Hence, it decided to acquire that power plant which was having capacity of 80MW along with all entire labour force.

This Power entity was owned by another entity Max Limited. Mini Limited approached Max Limited for acquisition of 80MW power plant at following terms:

- (i) Mini Limited will seek an independent valuation for determining fair value of 80MW power plant.
- (ii) Value of other Non-current assets acquired, and Non-current financial liabilities assumed is Rs. 11.10 million and Rs. 32 million respectively.
- (iii) Consideration agreed between both the parties is at Rs. 51 million.

Both the parties agreed to the terms and entered into agreement on 1st April, 20X1 with immediate effect.

Due to unavoidable circumstances, valuation could not be completed by the time Max Limited finalizes its financial statements for the year ending 31st March, 20X1. Max Limited's annual financial statements records the fair value of 80 MW Power Plant at Rs. 46.90 million with remaining useful life at 40 years.

Max Limited also has license to operate that power plant unrecorded in books. As on 31st March, 20X1, it has fair value of Rs. 5 million.

Six months after acquisition date, Mini Limited received the independent valuation, which estimated the fair value of 80MW Power Plant as Rs. 54.90 million.

CFO of Mini Limited, wants you to work upon following aspects of the transaction:

- (a) Determine whether transaction should be accounted as asset acquisition or business combination.
- (b) Calculate Goodwill / Bargain Purchase due to the above acquisition.
- (c) Pass necessary journal entries in the books of Mini Limited as per Ind AS 103 and prepare balance sheet as on date of acquisition.
- (d) Determine whether any adjustment is required in case of valuation received subsequent to acquisition. If yes, pass the necessary entries in the books of Mini Limited.

Balance Sheet of Mini Limited as at 31st March, 20X1

Particulars	(Rs. in Million)
ASSETS	
Non-current assets	
Property, plant and equipment	2,158
Capital work-in-progress	12
Deferred Tax Assets (Net)	324
Other non-current assets	<u>25</u>
Total non-current assets	2,519
Current assets	
Inventories	368
Financial assets	
(i) Investments	45
(ii) Trade Receivables	762
(iii) Cash and Cash Equivalent	110
(iv) Bank balances other than (iii) above	28

(v) Other financial assets	<u>267</u>
Total current assets	<u>1,580</u>
Total assets	<u>4,099</u>
EQUITY AND LIABILITIES	
Equity	
Equity Share Capital	295
Other equity	
Equity component of compound financial instruments	717
Reserves and surplus	<u>2,481</u>
Total equity	<u>3,493</u>
Liabilities	
Non-current liabilities	
Financial Liabilities	
Borrowings	<u>268</u>
Total non-current liabilities	<u>268</u>
Current liabilities	
Financial Liabilities	
(i) Trade payables	302
Other current liabilities	<u>36</u>
Total current liabilities	<u>338</u>
Total liabilities	<u>606</u>
Total equity and liabilities	<u>4,099</u>

Solution :

- (a) Ind AS 103 defines business as an integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing goods and services to customers, generating investment income (such as dividends or interest) or generating other income from ordinary activities.

In the given scenario, acquisition of power plant along with its labour force will be considered as integrated set of activity as it is capable of being generating power. Hence, transaction will be considered as business combination and not asset acquisition and acquisition method of accounting will be applied.

Thus, following will be the case:

- (i) Acquirer – Mini Ltd;
- (ii) Acquiree – Max Ltd;
- (iii) Acquisition date – 1st April, 20X1

- (b) **Calculation of Goodwill:**

Particulars	Rs. in Million
Purchase consideration (A)	<u>51</u>
Fair Value of Power Plant – PPE	46.90

Fair Value of other non-current assets		11.10
Fair Value of Intangible Asset (License) – Refer Note 1 below		5
Non-Current Liabilities assumed		<u>(32)</u>
Value of net assets acquired	(B)	<u>31</u>
Goodwill		20

Note 1: The licence to operate power plant is an intangible asset that meets the contractual-legal criterion for recognition separately from goodwill though acquirer cannot sell or transfer it separately from the acquired power plant. Intangible Assets needs to be recorded by the acquirer at the time of accounting for acquisition though not recorded by the acquiree in its book.

(c) **Journal Entries for acquiring power plant**

Particulars		Rs. in Million	Rs in Million
Fair Value of Power Plant	Dr.	46.90	
Fair Value of other assets	Dr.	11.10	
Fair Value of License acquired	Dr.	5	
Goodwill	Dr.	20	
	To Liabilities assumed		32
	To Bank (PC paid)		51

Balance Sheet of Mini Limited as at 1st April, 20X1

Particulars	Notes to Accounts	(Rs. in Million)
ASSETS		
Non-current assets		
Property, plant and equipment	1	2,204.90
Intangible Asset (License acquired in business combination)		5.00
Capital work-in-progress		12.00
Goodwill on acquisition		20.00
Deferred Tax Assets (Net)		324.00
Other non-current assets	2	<u>36.10</u>
Total non-current assets		<u>2,602.00</u>
Current assets		
Inventories		368.00
Financial assets		
I. Investments		45.00
II. Trade Receivables		762.00
III. Cash and Cash Equivalents	3	59.00
IV. Bank balances other than (iii) above		28.00
V. Other financial assets		<u>267.00</u>
Total current assets		<u>1,529.00</u>

Total assets		<u>4,131.00</u>
EQUITY AND LIABILITIES		
Equity		295.00
Equity Share Capital		
Other equity		717.00
Equity component of compound financial instruments		<u>2,481.00</u>
Reserves and surplus		<u>3,493.00</u>
Total equity		
Liabilities		
Non-current liabilities	4	<u>300.00</u>
Financial Liabilities		<u>300.00</u>
Borrowings		
Total Non-current liabilities		
Current liabilities		302.00
Financial Liabilities		36.00
I. Trade payables		<u>338.00</u>
Other current liabilities		<u>638.00</u>
Total Current liabilities		<u>4,131.00</u>
Total liabilities		
Total equity and liabilities		

Notes to Accounts

1. Property, Plant and Equipment

Particulars	Rs. in Million
PPE value as on 1st April, 20X1	2,158.00
Add: Fair Value of Power Plant acquired	<u>46.90</u>
Total	<u>2,204.90</u>

2. Other Non-current Assets

Particulars	Rs. in Million
Other non-current assets value as on 1st April, 20X1	25.00
	<u>11.10</u>
Add: Fair Value of Non-current assets acquired	<u>36.10</u>
Total	

3. Cash and Cash equivalents

Particulars	Rs. in Million
Cash and Cash equivalents as on 1st April, 20X1	110
Less: Payment of Purchase consideration transferred	<u>(51)</u>
Total	59

4. Non-current Liabilities

Particulars	Rs. in Million
Non-current Liabilities value as on 1st April, 20X1	268
Add: Non-current liabilities assumed in acquisition	<u>32</u>
Total	<u>300</u>

(d) Subsequent Accounting: Ind AS 103 provides a measurement period window, wherein if all the required information is not available on the acquisition date, then entity can do price allocation on provisional basis. During the measurement period, the acquirer shall retrospectively adjust the provisional amounts recognised at the acquisition date to reflect new information obtained about facts and circumstances that existed as on the acquisition date and, if known, would have affected the measurement of the amounts recognised as of that date. Any change i.e. increase or decrease in the net assets acquired due to new information available during the measurement period which existed on the acquisition date will be adjusted against goodwill.

Accordingly, in the financial statements for half year ending 30th September, 20X1, Mini Limited will retrospectively adjust the prior year information as follows:

- (i) the carrying amount of PPE (including power plant) as of 1st April, 20X1 is increased by Rs. 8 million (i.e. Rs. 54.90 million minus Rs. 46.90 million). The adjustment is measured as the fair value adjustment at the acquisition date less the additional depreciation that would have been recognised if the asset's fair value at the acquisition date had been recognised from that date $[(80,00,000/40) \times (6/12) = 0.1 \text{ million}]$
- (ii) the carrying amount of goodwill as of 1st April, 20X1 is decreased by Rs. 8 million; and
- (iii) depreciation expense for the period ending 30th September, 20X1 will increase by Rs. 0.1 million
- (iv) disclose in its financial statements of 1st April, 20X1, that the initial accounting for the business combination has not been completed because the valuation of property, plant and equipment has not yet been received;
- (v) disclose in its financial statements of 30th September, 20X1, the amounts and explanation of the adjustments to the provisional values recognised during the current reporting period. Therefore, Mini Limited discloses that comparative information is adjusted retrospectively to increase the fair value of the item of property, plant and equipment at the acquisition date by Rs. 8 million, offset by decrease in goodwill of Rs. 8 million.

Journal Entries

(1)	PPE (Power Plant)	Dr.	Rs. 8 Million	
	To Goodwill			Rs. 8 Million
(2)	Depreciation	Dr.	Rs. 0.1 Million	
	To Provision for Depreciation			Rs. 0.1 Million

Question 21 : May 2024 – RTP

On 1st April 20X1, Pride Limited acquired 30% of the ordinary shares of Famous Limited for Rs. 4,000 crores. Pride Limited accounts for its investment in Famous Limited using the equity method as prescribed under Ind AS 28. On 31st March 20X2, Pride Limited recognized its share of the net asset changes of Famous Limited using equity method accounting as follows:

Share of profit	Rs. 350 crore
Share of exchange difference in OCI	Rs. 50 crore
Share of revaluation reserve of PPE in OCI	Rs. 25 crore

The carrying amount of the investment in the associate on 31st March 20X2 is therefore Rs. 4,425 crore (4,000 + 350 + 50 + 25).

On 1st April 20X2, Pride Limited acquired the remaining 70% of Famous Limited for cash Rs. 12,500 crore.

The following additional information is relevant at that date:

Fair Value of 30% interest in Famous Limited as on 1st April 20X2	Rs. 4,500 crore
Fair Value of Net Identifiable Assets of Famous Limited as on 1st April 20X2	Rs. 15,000 crore

You are required to

- (i) Determine the acquisition date for Pride Ltd.
- (ii) Determine the gain on previously held interest in Pride Ltd. and suggest the accounting treatment on acquisition date as per Ind AS 103.
- (iii) Compute the amount of goodwill arising on the acquisition of Famous Ltd.
- (iv) Pass necessary journal entry on the acquisition date.

Solution :

(i) Acquisition date for accounting of business combination is

The date on which the acquirer obtains control of the acquiree is generally the date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree. In the given case, the acquisition date is 1st April, 20X2 i.e. when Pride Ltd. acquired 100% holding of Famous Ltd.

(ii) Computation of gain on previously held interest

An entity shall discontinue the use of the equity method from the date when its investment ceases to be an associate or a joint venture. If the investment in an associate becomes an investment in a subsidiary, the entity shall account for its investment in accordance with Ind AS 103 and Ind AS 110.

Ind AS 103 provides that in a business combination achieved in stages, the acquirer is required to remeasure the previously held equity interest at its acquisition date fair value and recognise any gain or loss in profit or loss or other comprehensive income, as appropriate. In prior reporting periods, the acquirer may have recognised changes in the value of its equity interest in the acquiree in other comprehensive income. If so, the amount that was recognised in the other comprehensive income shall be recognised on

the same basis as would be required if the acquirer had disposed directly of the previously held equity interest.

The gain on previously held equity interest in Famous Ltd. is calculated as follows:

Fair value of 30% interest as on 1st April, 20X2	Rs. 4,500 crore
Carrying value of 30% investment as on 31st March, 20X2	<u>(Rs. 4,425 crore)</u>
Gain on previously held interest	Rs. 75 crore
Unrealised gain previously recognised in OCI	<u>Rs. 50 crore</u>
Total gain recognised in Profit and loss	<u>Rs. 125 crore</u>

(iii) Computation of goodwill

For 70% share	Rs. 12,500 crore
For 30% share	<u>Rs. 4,500 crore</u>
Total amount of purchase consideration	Rs. 17,000 crore
Less: Fair value of net identifiable assets	<u>(Rs. 15,000 crore)</u>
Goodwill	Rs. 2,000 crore

(iv) Journal Entry on 1st April, 20X2

		Rs. in crore	
Net Identifiable Assets	Dr.	15,000	
Goodwill (W.N.1)	Dr.	2,000	
Foreign currency translation reserve	Dr.	50	
PPE revaluation reserve	Dr.	25	
To Cash			12,500
To Investment in Associate – Famous Ltd.			4,425
To Retained Earnings (W.N.)			25
To Gain on previously held interest recognised in profit and loss (Refer point (ii) above)			125

Working Note:

The credit to retained earnings represents the reversal of the unrealised gain of Rs. 25 crore in OCI related to the revaluation of PPE. In accordance with Ind AS 16, this amount is not reclassified to profit or loss.

Question 22 : May 2025 – RTP

On 1st April, 20X1, PQR Ltd. acquired 30% of the shares of XYZ Ltd. for Rs. 8,000 crores. At 31st March, 20X2, PQR Ltd. recognised its share of the net asset changes of XYZ Ltd. using equity accounting as follows:

(Amounts Rs. in crores)

Share of profit or loss	700
Share of exchange difference in OCI	100
Share of revaluation reserve of PPE in OCI	50

On 1st April, 20X2, PQR Ltd. acquired the remaining 70% of XYZ Ltd. for cash of Rs. 25,000 crores. The following additional information is relevant at that date.

(Amount Rs. in crores)

Fair value of the 30% interest already owned	9,000
Fair value of XYZ Ltd's identifiable net assets	30,000

Required

How should such business combination be accounted for?

Solution :

Paragraph 42 of Ind AS 103 provides that in a business combination achieved in stages, the acquirer shall remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognise the resulting gain or loss, if any, in profit or loss or other comprehensive income, as appropriate. In prior reporting periods, the acquirer may have recognised changes in the value of its equity interest in the acquiree in other comprehensive income. If so, the amount that was recognised in other comprehensive income shall be recognised on the same basis as would be required if the acquirer had disposed directly of the previously held equity interest.

Applying the above, PQR Ltd. records the following entry in its consolidated financial statements:

(Amounts Rs. in crores)

		Dr.	Cr.
Identifiable net assets of XYZ Ltd.	Dr.	30,000	
Goodwill (W.N.1)	Dr.	4,000	
Foreign currency translation reserve	Dr.	1,00	
PPE revaluation reserve	Dr.	50	
To Cash			25,000
To Investment in associate- XYZ Ltd. (W.N.3)			8,850
To Retained earnings (W.N.2)			50
To Gain on previously held interest in XYZ recognized in Profit or loss (W.N.4)			250
(To recognize acquisition of XYZ Ltd.)			

Working Notes :

1. Goodwill calculated as follows: (Rs. in crores)

Cash consideration	25,000
Fair value of previously held equity interest in XYZ	<u>9,000</u>
Total consideration	34,000
Fair value of identifiable net assets acquired	<u>(30,000)</u>
Goodwill	<u>4,000</u>

2. The credit to retained earnings represents the reversal of the unrealized gain of Rs. 50 crores in Other Comprehensive Income related to the revaluation of property, plant and equipment. In accordance with Ind AS 16, this amount is not reclassified to profit or loss.

3. The carrying amount of the investment in the associate on 31st March, 20X2 would be as follows: (Rs. in crores)

Investment in Associate	8,000
Share of profit or loss	700
Share of exchange difference in OCI	100
Share of revaluation reserve of PPE in OCI	50
	<u>8,850</u>

4. The gain on the previously held equity interest in XYZ Ltd. is calculated as follows:

(Rs. in crores)

Fair Value of 30% interest in XYZ Ltd. at 1st April, 20X2	9,000
Carrying amount of interest in XYZ Ltd. at 1st April, 20X2 (W.N.3)	<u>(8,850)</u>
	150
Unrealised gain previously recognized in OCI	<u>100</u>
Gain on previously held interest in XYZ Ltd. recognized in profit or loss	<u>250</u>

Thanks



IND AS – 110

CONSOLIDATION OF FINANCIAL STATEMENTS

CHAPTER - 29

Question 1 : May 2018 – PAPER

Hold Limited acquired 100% ordinary shares of Rs.100 each of Sub Limited on 1st October, 2017. On 31st March, 2018 the summarized Balance Sheets of the two companies were as given below:

Particulars		Hold Limited (Rs.)	Sub Limited (Rs.)
I.	Assets		
	(1) Non-current Assets		
	(i) Property, Plant & Equipment		
	(a) Land & Building	30,00,000	36,00,000
	(b) Plant & machinery	48,00,000	27,00,000
	(ii) Investment in Sub Limited	68,00,000	
	(2) Current Assets		
	(i) Inventory	24,00,000	7,28,000
	(ii) Financial Assets		
	(a) Trade Receivables	11,96,000	8,00,000
	(b) Cash & Cash Equivalentents	2,90,000	1,60,000
	Total	1,84,86,000	79,8,000
II.	Equity and Liabilities		
	(1) Equity		
	(i) Equity Share Capital (Shares of Rs.100 each fully paid)	1,00,00,000	40,00,000
	(ii) Other Equity		
	(a) Other Reserves	48,00,000	20,00,000
	(b) Retained Earnings	11,44,000	16,40,000
	(2) Current Liabilities		
	Financial Liabilities		
	(a) Bank Overdraft	16,00,000	-
	(b) Trade Payable	9,42,000	3,48,000
		1,84,86,000	79,88,000

The retained earnings of Sub Limited showed a credit balance of Rs.6,00,000 on 1st April, 2017 out of which a dividend of 10% was paid on 1st November 2017. Hold Limited has credited the dividend received to retained earnings account. There was no fresh addition to other reserves in

case of both companies during the current financial year. There was no opening balance in the retained earnings in the books of Hold Limited.

Following are the changes in fair value as per respective Ind AS from the book value as on 1st October, 2017 in the books of Sub Limited which is to be considered while consolidating the Balance Sheets.

- (i) Fair value of Plant and Machinery was Rs.40,00,000. (Rate of depreciation on Plant and Machinery is 10% p.a.)
- (ii) Land and Building appreciated by Rs.20,00,000.
- (iii) Inventories increased by Rs.3,00,000.
- (iv) Trade payable increased by Rs.2,00,000.

Prepare Consolidated Balance Sheet as on 31st March, 2018. The Balance Sheet should comply with the relevant Ind AS and Schedule III of the Companies Act, 2013.

Solution :

**Consolidated Balance Sheet of Hold Ltd. and its subsidiary, Sub Ltd.
As on 31st March, 2018**

Particulars	Rs.
Assets	
(1) Non-current assets	
Property, Plant & Equipment	1,72,00,000
Goodwill	
(2) Current Assets	
Inventories	34,28,000
Financial Assets	
Trade Receivables	19,96,000
Cash & Cash equivalents	<u>4,50,000</u>
Total	<u>2,30,74,000</u>
Equity and Liabilities	
Equity	
Share Capital	1,00,00,000
Other Equity	99,84,000
Liability	
(1) Non Current Liabilities	
(2) Current Liabilities	
Financial Liabilities	
Short term borrowings	16,00,000
Trade Payables	<u>14,90,000</u>
Total	<u>2,30,74,000</u>

Working Notes :

1. Calculation of goodwill

	Rs.
Consideration Paid	68,00,000
Fair value of Net Assets (40,00,000 + 4,00,000 + 61,70,000)	1,05,70,000
Goodwill gain from bargain purchase	<u>37,70,000</u>

2. Statement for changes in equity

	Sh.Cap	Other Equity	Total
OP.	1,00,00,000	59,44,000	1,59,44,000
-Div.	-	(4,00,000)	(2,00,000)
+ Gain	-	37,70,000	37,70,000
+ Reserves of Subsidiary	-	6,70,000	6,70,000
	1,00,00,000	99,84,000	1,99,84,000

3. Reserves of Subsidiary

Res.	20,00,000	Pre	RF	16,40,000		
		1/4	6,00,000		14,40,000	
		-Div.	<u>4,00,000</u>			
		Pre.	2,00,000	7,20,000	7,20,000	
				Pre	Post	
Pre	29,20,000			Post	7,20,000	
+ Plant	11,50,000			-Dep.	<u>50,000</u>	
+ L & B	20,00,000				6,70,000	
+ Inventory	3,00,000					
- TP	<u>(2,00,000)</u>					
	61,70,000					

4. PPE

L & B	Hold					
						30,00,000
		Sub.	(36,00,000 + 20,00,000)			56,00,000
P & M	Hold					48,00,000
		Sub.	(27,00,000 + 11,50,000 - 50,000)			<u>38,00,000</u>
						1,72,00,000

	CP	RP
1/4/17	30,00,000	
-Dep.	<u>1,50,000</u>	
30/9/17	28,50,000	40,00,000
-Dep.	<u>1,50,000</u>	<u>2,00,000</u>

31/3/18	27,00,000	38,00,000
5. Inventory		
Hold		24,00,000
Sub. (7,28,000 + 3,00,000)		<u>10,28,000</u>
		34,28,000
6. Trade Payable		
Hold		9,42,000
Sub. (3,48,000 + 2,00,000)		<u>5,48,000</u>
		14,90,000

Question 2 : May 2018 – PAPER

XYZ Limited acquired 70% of equity shares of TUV Limited on 1st April, 2010 at cost of Rs.20,00,000 when TUV Limited had an equity share capital of Rs.20,00,000 and reserve and surplus of Rs.1,60,000. In the four consecutive years, TUV Limited, fared badly and suffered losses of Rs.5,00,000, Rs.8,00,000, Rs.10,00,000 and Rs.2,40,000 respectively. Thereafter in 2014-15, TUV Limited, experienced turnaround and registered an annual profit of Rs.1,00,000. In the next two years i.e. 2015-16 and 2016-17, TUV Limited recorded annual profits of Rs.2,00,000 and Rs.3,00,000 respectively. Calculate the Non controlling interests and cost of control at the end of each year for the purpose of consolidation, as per Ind AS 110 "Consolidated Financial Statements".

Solution :

1) Date of Acquisition 1/4/2010

Acquirer – XYZ Ltd.

Acquiree – TUV Ltd.

% Acquired = 70%

NCI = 30%

2) Calculation of cost of control on 1/1/2010

Consideration paid (70%)	20,00,000
+ NCI (At Proportional share) (30%)	<u>6,48,000</u>
	26,48,000
– FV of NA (20,00,000 + 1,60,000) (100%)	<u>21,60,000</u>
Goodwill	4,88,000

3) NCI and Cost of Control at end of each year as per Ind AS 110.

Details	P/L	NCI	Holding	Goodwill
01/04/2010	-	6,48,000	-	4,88,000
2010-11	(5,00,000)	(1,50,000)	(3,50,000)	-
31/3/2011	-	4,98,000	-	4,88,000
2011-12	(8,00,000)	(2,40,000)	(5,60,000)	-

31/3/2012	-	2,58,000	-	4,88,000
2012-13	(10,00,000)	(3,00,000)	(7,00,000)	-
31/3/2013	-	(42,000)	-	4,88,000
2013-14	(2,40,000)	(72,000)	(1,68,000)	-
3/3/2014	-	(1,14,000)	-	4,88,000
2014-15	1,00,000	30,000	70,000	-
31/3/2015	-	(84,000)	-	4,88,000
2015-16	2,00,000	60,000	1,40,000	-
31/3/2016	-	(24,000)	-	4,88,000
2016-17	3,00,000	90,000	2,10,000	-
31/3/2017	-	66,000	-	4,88,000

Note :

- 1) P/L in subsequent yrs after acquisition does not have any impact on goodwill. Goodwill should be checked for impairment every year.
- 2) As per Ind AS 21 loss of subsidiary should be born by holding and minority interest will not be shown negative.

Question 3 : Nov 2018 – RTP

Sumati Ltd. acquired 100% (50,00,000) equity shares of Rs.10 each in Sheetal Ltd. on 1st April, 2014. Sheetal Ltd. was incorporated on 1st April, 2014.

Sumati Ltd. acquired 80% (24,00,000) equity shares in Dharam Ltd. for Rs.600 lakh on 1st April, 2014 when Dharam Ltd. had share capital of Rs.300 lakh and Reserves and Surplus of Rs.300 lakh. The company amortizes goodwill on consolidation on a SLM basis over a period of 5 years. A full year's amortization is considered if the goodwill exists for more than 6 months.

On 1st April, 2017, Sumati Ltd. sold 12,00,000 equity shares of Dharam Ltd. for cash consideration of Rs.360 lakh with recognition of profit arising out of this sale.

The net assets of Dharam Ltd. on 31st March, 2017 were Rs.700 lakh. The amount of Reserves and Surplus was Rs.880 lakh, Rs.720 lakh and Rs.480 lakh respectively of Sumati Ltd., Sheetal Ltd. and Dharam Ltd. on 31st March, 2017.

The Balance Sheet extracts of the companies as on 31st March, 2018 were as follows:

(Rs.in lakh)

	Sumati Ltd.	Sheetal Ltd.	Dharam Ltd.
Share Capital (Rs.10 each)	1000	500	300
Reserves and Surplus	1240	910	640
Current Liabilities	460	490	560
	2700	1900	1500
Fixed Assets	640	420	380
50,00,000 equity shares in Sheetal Ltd.	500		
12,00,000 equity shares in Dharam Ltd.	300		
Current Assets	1260	1480	1120
	2700	1900	1500

You are required to prepare for Sumati Ltd. Group Balance Sheet as on 31st March, 2018 following Ind AS 110 and Ind AS 111. Notes to Accounts and working notes should form part of your answer.

Solution :

Consolidated Balance Sheet as on 31.3.2018

Particulars	Note No.	(Rs. in lakh)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1,000
(b) Reserves and Surplus	2	2,206
(2) Current Liabilities	3	950
Total		4,156
II. Assets		
(1) Non-current assets		
Fixed Assets	4	1,060
Non-current investment (Investment in Associate Dharam Ltd.)	5	356
(2) Current assets	6	2,740
Total		4,156

Notes to Accounts

		Rs. In lakhs	
1	Share Capital		
	100 lakh Equity shares of Rs.10 each fully paid up		1,000
2	Consolidated Reserves and Surplus as on 31.3.2018		
	Balance of Reserves and surplus of Sumati Ltd. as on 31.3.2018	1,240	
	Add: Post-acquisition reserves and surplus of Sheetal Ltd. (subsidiary)	910	
	Profit accumulated over the years on investment of Sumati Ltd. (304-300)	4	
	Post-acquisition reserves and surplus of Dharam Ltd. (640-480) x 40%	64	
	Less: Goodwill amortised for the period (24/2)	<u>12</u>	2,206
3	Current Liabilities		
	Sumati Ltd.	460	
	Sheetal Ltd.	<u>490</u>	950
4	Fixed Assets		
	Sumati Ltd.	640	
	Sheetal Ltd.	<u>420</u>	1,060
5	Non-current investment (Investment in Associate Dharam Ltd.)		
	Carrying amount of Investment in Associate. [W.N.2]	304	

	(Identified goodwill included in the above Rs. 24 lakh) [W.N.3]		
	Add: Increase in reserves and surplus during the year (640-480) x 40%	64	
	Less: Goodwill written off in the fourth year (Rs. 24 lakh x ½)	<u>(12)</u>	356
6	Current assets		
	Sumati Ltd.	1,260	
	Sheetal Ltd.	<u>1,480</u>	2,740

Working Notes:

1. Cost of Control on acquisition of shares in Dharam Ltd. and amortization of goodwill

	Rs. In lakhs
Investment by Sumati Ltd.	600
Less: Share capital (300 x 80%)	(240)
Capital profit (pre-acquisition) (300 x 80%)	<u>(240)</u>
Goodwill	120
Less: Amortization for 3 years [(120/5) x3]	<u>(72)</u>
Carrying value of goodwill after 3 years	<u>48</u>

2. Ascertainment of carrying value of investment in Dharam Ltd. disposed off and retained

	Rs. In lakh
Net Assets of Dharam Ltd. on the date of disposal	700
Less: Minority's interest in Dharam Ltd. on the date of disposal (700 x 20%)	<u>(140)</u>
Share of Sumati Ltd. in Net Assets	560
Add: Carrying value of Goodwill (Refer W.N.1)	<u>48</u>
Total value of investment in Dharam Ltd. as on 1.4.2017	608
Less: Carrying Value of investment disposed off [Rs.608 lakh x (12 lakh /24 lakh)]	<u>(304)</u>
Carrying Value of investment retained by Sumati Ltd.	<u>304</u>

3. Goodwill arising on the Carrying Value of Unsold Portion of the Investment

	Rs. In lakh
Carrying value of retained 40% holdings in Dharam Ltd. as on 1st April, 2017	304
Less: Share in value of equity of Dharam Ltd., as at date of investment when its subsidiary relationship is transformed to an associate (700 x 40%)	<u>(280)</u>
Goodwill arising on such investment under Equity method as per AS 23	<u>(24)</u>

Question 4 : Nov 2018 – PAPER

Prepare the Consolidated Balance Sheet as on 31st March, 2018 of a group of companies comprising Usha Limited, Nisha Limited and Sandhya Limited. Their summarized balance sheets on that date are given below:

Amounts Rs.in lakh

	Usha Ltd.	Nisha Ltd.	Sandhya Ltd.
Equity and Liabilities			
<u>Shareholder's Equity</u>			
Share capital (Rs.10 per share)	300	200	160
Reserves	90	50	40
Retained earnings	80	25	30
<u>Current Liabilities</u>			
Trade Payables	235	115	90
Bills Payable			
Usha Ltd.	-	35	-
Sandhya Ltd.	15	-	-
	720	425	320
Assets			
<u>Non-Current Assets</u>			
Tangible assets	160	180	150
Investment:			
16 lakh shares in Nisha Ltd.	170	-	-
12 lakh shares in Sandhya Ltd.	-	140	-
<u>Current Assets</u>			
Cash in hand and at Bank	114	20	20
Bills Receivable	36	-	15
Trade Receivables	130	50	110
Inventories	110	35	25
	720	425	320

The following additional information is available:

- Usha Ltd. holds 80% shares in Nisha Ltd. and Nisha Ltd. holds 75% shares in Sandhya Ltd. Their holdings were acquired on 30th September, 2017.
- The business activities of all the companies are not seasonal in nature and therefore, it can be assumed that profits are earned evenly throughout the year.
- On 1st April, 2017, the following balances stood in the books of Nisha Limited and Sandhya Limited.

Rs.in lakh

	Nisha Ltd.	Sandhya Ltd.
Reserves	40	30
Retained Earnings	10	15

- Rs.5 Lakh included in the inventory figure of Nisha Limited, is inventory which has been purchased from Sandhya Limited at cost plus 25%.
- The parent company has adopted an accounting policy to measure Non-controlling interest at fair value (quoted market price) applying Ind AS 103. Assume market prices of Nisha Limited and Sandhya Limited are the same as respective face values.

(vi) The capital profit preferably is to be adjusted against cost of control.

Note: Analysis of profits and notes to accounts must be a part of your answer.

Solution :

- 1) Usha in Nisha = 80%
 Nisha in Sandhya = 75% NCI = 25%
 Usha in Sandhya = $80 \times 75\% = 60\%$ NCI = 40%
- 2) Consolidated Balance Sheet as on 31/3/2018.

Particulars	Rs.
Assets	
1) <u>NCA</u>	
PPE	490
Goodwill	
2) <u>CA</u>	
Inventory (170 – 1)	169
<u>FA</u>	
Trade Receivable (290 + 1)	291
Cash and Cash Equivalent	<u>154</u>
Total	1,104
Equity and Liabilities	
Equity	
Share Capital	300
Other Equity	280.9
NCI	83.1
Liabilities	
1) <u>NCC</u>	–
2) <u>CL</u>	
FL – Trade payable	<u>440</u>
Total	1,104

Working Notes :

- 1) **Calculation of goodwill**

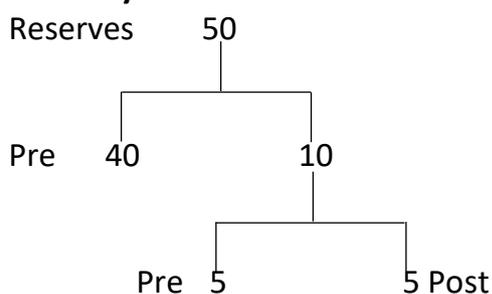
	Nisha	Sandhya
Consideration paid	170	112
+ NCI		
Nisha (200 × 20%)	<u>40</u>	<u>64</u>
Sandhya (160 × 40%)	210	176
Fair value of Net Assets		
Nisha (200 + 62.5)	262.5	–
Sandhya (160 + 57.5)	<u> </u>	<u>217.5</u>
Goodwill / Capital Reserve	52.5	41.5
Total	94	

2) State for Charge in Equity

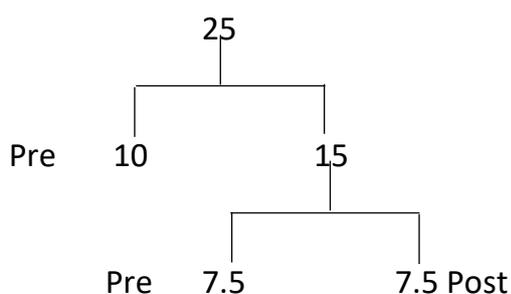
Detail	Share Capital	Other Equity	Total	NCI	NCI	Total
OP.	300	170	470	40	64	574
+ Capital Reserve	–	94	94	–	–	94
+ Reserve in Nisha	–	10	10	2.5	–	12.5
+ Reserve in Sandhya	–	6.9	6.9	–	4.6	11.5
– NCI	–	–	–	(28)	–	(28)
	300	280.9		14.5	68.6	

3) Reserves of subsidiary

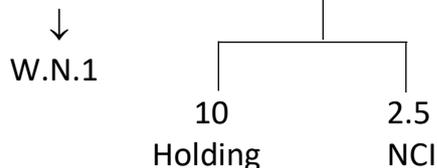
Nisha Ltd.



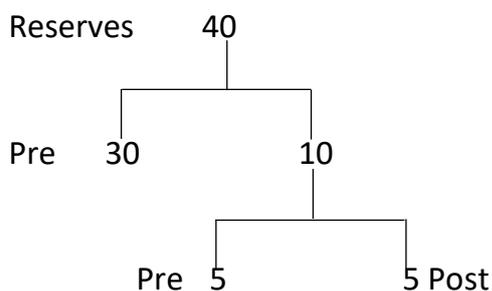
Retained Earnings

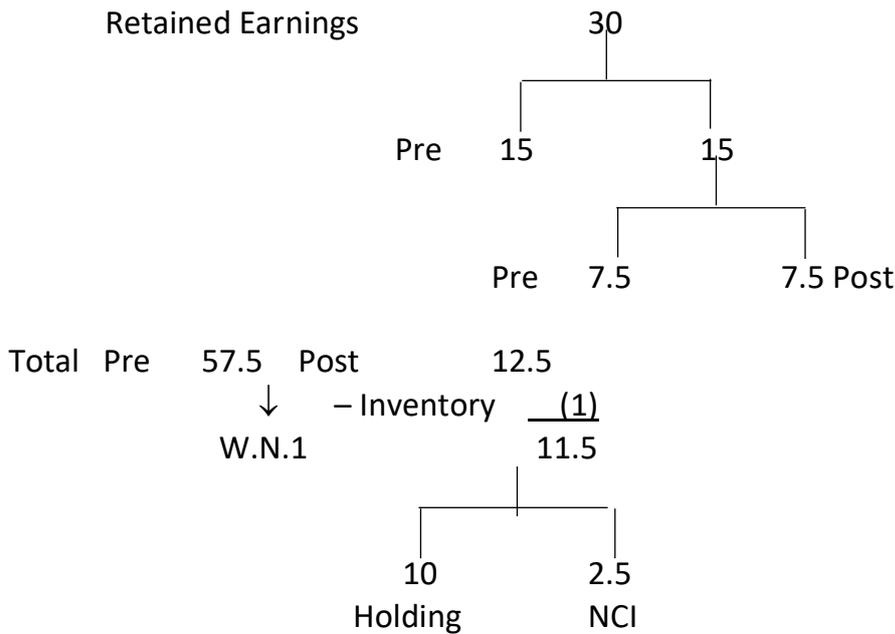


Total Pre 62.5 Post



Sandhya Ltd. Reserves





Question 5 : May 2019 – RTP

Angel Ltd. has adopted Ind AS with a transition date of 1st April, 2017. Prior to Ind AS adoption, it followed Accounting Standards notified under Companies (Accounting Standards) Rules, 2006 (hereinafter referred to as "IGAAP").

It has made investments in equity shares of Pharma Ltd., a listed company engaged in the business of pharmaceuticals. The shareholding pattern of Pharma Ltd. is given below:

Shareholders (refer Note 1)	Percentage shareholding as on 1st April, 2017
Angel Ltd.	21%
Little Angel Ltd. (refer Note 2)	24%
Wealth Master Mutual Fund (refer Note 3)	3%
Individual public shareholders (refer Note 4)	52%

Notes:

- (1) None of the shareholders have entered into any shareholders' agreement.
- (2) Little Angel Ltd. is a subsidiary of Angel Ltd. (under Ind AS) in which Angel Ltd. holds 51% voting power.
- (3) Wealth Master Mutual Fund is not related party of either Little Angel Ltd. or Pharma Ltd.
- (4) Individual public shareholders represent 17,455 individuals. None of the individual shareholders hold more than 1% of voting power in Pharma Ltd.

All commercial decisions of Pharma Ltd. are taken by its directors who are appointed by a simple majority vote of the shareholders in the annual general meetings ("AGM"). The following table shows the voting pattern of past AGMs of Pharma Ltd.:

Shareholders	AGM for the financial year		
	2013-14	2014-15	2015-16
Angel Ltd.	Attended and voted in favour of all the resolutions	Attended and voted in favour of all the resolutions	Attended and voted in favour of all the resolutions
Little Angel Ltd.	Attended and voted as per directions of Angel Ltd.	Attended and voted as per directions of Angel Ltd	Attended and voted as per directions of Angel Ltd
Wealth Master Mutual Fund	Attended and voted in favour of all the resolutions except for the reappointment of the retiring directors	Attended and voted in favour of all the resolutions except for the reappointment of the retiring directors	Attended and voted in favour of all the resolutions except for the reappointment of the retiring directors
Individuals	7% of the individual shareholders attended the AGM. All the individual shareholders voted in favour of all the resolutions, except that 50% of the individual Shareholders voted against the resolution to appoint the retiring directors.	8% of the individual shareholders attended the AGM. All the individual shareholders voted in favour of all the resolutions, except that 50% of the individual Shareholders voted against the resolution to appoint the retiring directors.	6% of the individual shareholders attended the AGM. All the individual shareholders voted in favour of all the resolutions, except that 50% of the individual Shareholders voted against the resolution to appoint the retiring directors.

Pharma Ltd. has obtained substantial long term borrowings from a bank. The loan is payable in 20 years from 1st April, 2017. As per the terms of the borrowing, following actions by Pharma Ltd. will require prior approval of the bank :

- Payment of dividends to the shareholders in cash or kind;
- Buyback of its own equity shares;
- Issue of bonus equity shares;
- Amalgamation of Pharma Ltd. with any other entity; and
- Obtaining additional loans from any entity.

Recently, the Board of Directors of Pharma Ltd. proposed a dividend of Rs. 5 per share. However, when the CFO of Pharma Ltd. approached the bank for obtaining their approval, the bank rejected the proposal citing concerns over the short-term cash liquidity of Pharma Ltd. Having learned about the developments, the Directors of Angel Ltd. along with the Directors of Little Angel Ltd. approached the bank with a request to re-consider its decision. The Directors of Angel Ltd. and Little Angel Ltd. urged the bank to approve a reduced dividend of at least Rs. 2 per share. However, the bank categorically refused to approve any payout of dividend.

Under IGAAP, Angel Ltd. has classified Pharma Ltd. as its associate. As the CFO of Angel Ltd., you are required to comment on the correct classification of Pharma Ltd. on transition to Ind AS.

Solution :

To determine whether Pharma Limited can be continued to be classified as an associate on transition to Ind AS, we will have to determine whether Angel Limited controls Pharma Limited as defined under Ind AS 110.

An investor controls an investee if and only if the investor has all the following:

- (a) Power over investee
- (b) Exposure, or rights, to variable returns from its involvement with the investee
- (c) Ability to use power over the investee to affect the amount of the investor's returns.

Since Angel Ltd. does not have majority voting rights in Pharma Ltd. we will have to determine whether the existing voting rights of Angel Ltd. are sufficient to provide it power over Pharma Ltd.

Analysis of each of the three elements of the definition of control:

Elements / conditions	Analysis
Power over investee	<p>Angel Limited along with its subsidiary Little Angel Limited (hereinafter referred to as "the Angel group") does not have majority voting rights in Pharma Limited. Therefore, in order to determine whether Angel group have power over Pharma Limited. we will need to analyse whether Angel group, by virtue of its non-majority voting power, have practical ability to <u>unilaterally direct the relevant activities</u> of Pharma Limited. In other words, we will need to analyse whether Angel group has de facto power over Pharma Limited. Following is the analysis of de facto power of Angel over Pharma Limited:</p> <ul style="list-style-type: none"> - The public shareholding of Pharma Limited (that is, 52% represents thousands of shareholders none individually holding material shareholding, - The actual participation of Individual public shareholders in the general meetings is minimal (that is, in the range of 6% to 8%). - Even the public shareholders who attend the meeting do not consult with each other to vote. - Therefore, as per guidance of Ind AS 110, the public shareholders will not be able to outvote Angel group (who is the largest shareholder group) in any general meeting. <p>Based on the above-mentioned analysis, we can conclude that Angel group has de facto power over Pharma Limited.</p>

Exposure, or rights, to variable returns from its involvement with the investee	Angel group has exposure to variable returns from its involvement with Pharma Limited by virtue of its equity stake.
Ability to use power over the investee to affect the amount of the investor's returns	<p>Angel group has ability to use its power (in the capacity of a principal and not an agent) to affect the amount of returns from Pharma Limited because it is in the position to appoint directors of Pharma Limited who would take all the decisions regarding relevant activities of Pharma Limited.</p> <p>Here, it is worthwhile to evaluate whether certain rights held by the bank would prevent Angel Limited's ability to use the power over Pharma Limited to affect its returns. It is to be noted that, all the rights held by the bank in relation to Pharma Limited are protective in nature as they do not relate to the relevant activities (that is, activities that significantly affect the Pharma Limited's returns) of Pharma Limited.</p> <p>As per Ind AS 110, protective rights are the rights designed to protect the interest of the party holding those rights without giving that party power over the <u>entity to which those rights relate</u>.</p> <p>Therefore, the protective rights held by the bank should not be considered while evaluating whether or not Angel Group has control over Pharma Limited.</p>
<p>Conclusion : Since all the three elements of definition of control is present, it can be concluded that Angel Limited has control over Pharma Limited.</p>	

Since it has been established that Angel Limited has control over Pharma Limited, upon transition to Ind AS, Angel Limited shall classify Pharma Limited as its subsidiary.

Question 6 : Nov 2019 – RTP

What will be the accounting treatment of dividend distribution tax in the consolidated financial statements in case of partly-owned subsidiary in the following scenarios:

Scenario 1: H Limited (holding company) holds 12,000 equity shares in S Limited (Subsidiary of H Limited) with 60% holding. Accordingly, S Limited is a partly-owned subsidiary of H Limited. During the year 20X1, S Limited paid a dividend @ Rs.10 per share and DDT @ 20% on it.

Should the share of H Limited in DDT paid by S Limited amounting to Rs.24,000 (60% x Rs.40,000) be charged as expense in the consolidated profit and loss of H Limited?

Scenario 2 (A): Extending the situation given in scenario 1, H Limited also pays dividend of Rs.300,000 to its shareholders and DDT liability @ 20% thereon amounts to Rs.60,000. As per the tax laws, DDT paid by S Ltd. of Rs.24,000 is allowed as set off against the DDT liability of H Ltd., resulting in H Ltd. paying Rs.36,000 (Rs.60,000 – Rs.24,000) as DDT to tax authorities.

Scenario 2(B)

If in (A) above, H Limited pays dividend amounting to Rs.100,000 with DDT liability @ 20% amounting to Rs.20,000.

Scenario (3):

Will the answer be different for the treatment of dividend distribution tax paid by associate in the consolidated financial statement of investor, if as per tax laws the DDT paid by associate is not allowed set-off against the DDT liability of the investor?

Solution :

Scenario 1: Since H Limited is holding 12,000 shares it has received Rs.1,20,000 as dividend from S Limited. In the consolidated financial statements of H Ltd., dividend income earned by H Ltd. and dividend recorded by S Ltd. in its equity will both get eliminated as a result of consolidation adjustments. Dividend paid by S Ltd. to the 40% non-controlling interest (NCI) shareholders will be recorded in the Statement of Changes in Equity as reduction of NCI balance (as shares are classified as equity as per Ind AS 32).

DDT of Rs.40,000 paid to tax authorities has two components- One Rs.24,000 (related to H Limited’s shareholding and other Rs.16,000 (40,000 × 40%) belong to non controlling interest (NCI) shareholders of S Limited). DDT of Rs.16,000 (pertaining to non-controlling interest (NCI) shareholders) will be recorded in the Statement of Changes in Equity along with dividend. DDT of Rs.24,000 paid outside the consolidated Group shall be charged as tax expense in the consolidated statement of profit and loss of H Ltd.

In accordance with the above, in the given case, CFS of H limited will be as under:

Transactions	H Ltd.	S Ltd.	Consol Adjustments	CFS H Ltd.
Dividend Income (P&L)	1,20,000	-	(1,20,000)	-
Dividend (in Statement of Changes in Equity by way of reduction of NCI)	-	(2,00,000)	1,20,000	(80,000)
DDT (in Statement of Changes in Equity by way of reduction of NCI)	-	(40,000)	24,000	(16,000)
DDT (in Statement of P&L)	-	-	(24,000)	(24,000)

Scenario 2 (A) : If DDT paid by the subsidiary S Ltd. is allowed as a set off against the DDT liability of its parent H Ltd. (as per the tax laws), then the amount of such DDT should be recognised in the consolidated statement of changes in equity of parent H Ltd.

In the given case, share of H Limited in DDT paid by S Limited is Rs.24,000 and entire Rs.24,000 was utilised by H Limited while paying dividend to its own shareholders.

Accordingly, DDT of Rs.76,000 (Rs.40,000 of DDT paid by S Ltd. (of which Rs.16,000 is attributable to NCI) and Rs.36,000 of DDT paid by H Ltd.) should be recognised in the consolidated statement of changes in equity of parent H Ltd. No amount will be charged to consolidated statement of profit and loss. The basis for such accounting would be that due to Parent H Ltd’s transaction of distributing dividend to its shareholders (a transaction recorded in Parent H Ltd’s equity) and the related DDT set-off, this DDT paid by the subsidiary is effectively a tax on distribution of dividend to the shareholders of the parent company.

In accordance with the above, in the given case, CFS of H limited will be as under:

Transactions	H Ltd.	S Ltd.	Consol Adjustments	CFS H Ltd.
Dividend Income (P&L)	1,20,000	-	(1,20,000)	-
Dividend (in Statement of Changes in Equity)	(3,00,000)	(2,00,000)	1,20,000	(3,80,000)*
DDT (in Statement of Changes in Equity)	(36,000)	(40,000)	-	(76,000)*

*Dividend of Rs.80,000 and DDT of Rs.16,000 will be reflected as reduction from non-controlling interest.

Scenario 2(B): In the given case, share of H Limited in DDT paid by S Limited is Rs.24,000 out of which only Rs.20,000 was utilised by H Limited while paying dividend by its own. Therefore, balance Rs.4,000 should be charged in the consolidated statement of profit and loss.

In accordance with the above, in the given case, CFS of H limited will be as under:

Transactions	H Ltd.	S Ltd.	Consol Adjustments	CFS H Ltd.
Dividend Income (P&L)	1,20,000	-	(1,20,000)	-
Dividend (in Statement of Changes in Equity)	(1,00,000)	(2,00,000)	1,20,000	(1,80,000)*
DDT (in Statement of Changes in Equity)	-	(40,000)	4,000	(36,000)*
DDT (in Statement of P&L)	-	-	(4,000)	(4,000)

*Dividend of Rs.80,000 and DDT of Rs.16,000 will be reflected as reduction from non- controlling interest.

Scenario (3): Considering that as per tax laws, DDT paid by associate is not allowed set off against the DDT liability of the investor, the investor's share of DDT would be accounted by the investor company by crediting its investment account in the associate and recording a corresponding debit adjustment towards its share of profit or loss of the associate.

Question 7 : May 2020 – RTP

Gamma Limited, a parent company, is engaged in manufacturing and retail activities. The group holds investments in different entities as follows:

- Gamma Limited holds 100% Investment in G Limited and D Limited;
- G Limited and D Limited hold 60% and 40% in GD Limited respectively;
- Delta Limited is a 100% subsidiary of GD Limited

Firstly, Gamma Limited wants you to suggest whether GD Limited can avail the exemption from the preparation and presentation of consolidated financial statements as per applicable Ind AS? Secondly, if all other facts remain the same as above except that G Limited and D Limited are both owned by an Individual (say, Mr. X) instead of Gamma Limited, then explain whether GD Limited can avail the exemption from the preparation and presentation of consolidated financial statements.

Solution :

As per paragraph 4(a) of Ind AS 110, an entity that is a parent shall present consolidated financial statements. This Ind AS applies to all entities, except as follows:

A parent need not present consolidated financial statements if it meets all the following conditions:

- (i) it is a wholly-owned subsidiary or is a partially-owned subsidiary of another entity and all its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting consolidated financial statements;
- (ii) its debt or equity instruments are not traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets);
- (iii) it did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; and
- (iv) its ultimate or any intermediate parent produces financial statements that are available for public use and comply with Ind ASs, in which subsidiaries are consolidated or are measured at fair value through profit or loss in accordance with this Ind AS.

In accordance with the above, it may be noted that as per paragraph 4(a)(i) above, a parent need not present consolidated financial statements if it is a:

- wholly-owned subsidiary; or
- is a partially-owned subsidiary of another entity and all its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting consolidated financial statements.

Although GD Limited is a partly-owned subsidiary of G Limited, it is the wholly-owned subsidiary of Gamma Limited (and therefore satisfies the condition 4(a)(i) of Ind AS 110 without regard to the relationship with its immediate owners, i.e. G Limited and D Limited). Thus, GD Limited being the wholly owned subsidiary fulfils the conditions as mentioned under paragraph 4(a)(i) and is not required to inform its other owner D Limited of its intention not to prepare the consolidated financial statements.

Thus, in accordance with the above, GD Limited may take the exemption given under paragraph 4(a) of Ind AS 110 from presentation of consolidated financial statements.

In Alternative Scenario, where both G Limited and D Limited are owned by an individual Mr. X, then GD Limited is ultimately wholly in control of Mr. X (i.e., an individual) and hence it cannot be considered as a wholly owned subsidiary of an entity.

This is because Ind AS 110 makes use of the term 'entity' and the word 'entity' includes a company as well as any other form of entity. Since, Mr. X is an 'individual' and not an 'entity', therefore, GD Limited cannot be considered as wholly owned subsidiary of an entity.

Therefore, in the given case, GD Limited is a partially-owned subsidiary of another entity. Accordingly, in order to avail the exemption under paragraph 4(a), its other owner, D Limited should be informed about and do not object to GD Limited not presenting consolidated financial statements. Further, for the purpose of consolidation of G Limited and D Limited, GD Limited will be required to provide relevant financial information as per Ind AS.

Parent Limited, prepares consolidated financial statements of the group on 31 March every year. During the year ended 31 March 2020, the following events affected the tax position of the group:

- (i) S Limited, a wholly owned subsidiary of Parent Limited, incurred a loss of Rs. 20,00,000 which is adjustable from future taxable profits of the company for tax purposes. S Limited is unable to utilize this loss against previous tax liabilities. Income Tax Act does not allow S Limited to transfer the tax loss to other group companies. However, it allows S Limited to carry forward the loss and utilize it against company's future taxable profits. The directors of Parent Limited estimate that S Limited will not make any taxable profits in the foreseeable future.
- (ii) On 1 April 2019, Parent Limited borrowed Rs. 50,00,000. The cost incurred by Parent Limited for arranging the borrowing was Rs. 1,00,000 on the said date and this expenditure is qualified for deduction under the Income Tax Act for the accounting year 2019-2020. The loan was given for a three-year period. As per agreement, no principal or interest was payable on the loan during the tenure of loan but the amount repayable on 31 March 2022 will be by way of a bullet payment of Rs. 65,21,900. As per Parent Limited, this equates to an effective annual interest rate of 10% on loan. As per the Income-tax Act, a further expense of Rs. 15,21,900 will be claimable from taxable income till the loan is repaid on 31 March 2022.

The rate of corporate income tax to be assumed @ 20%.

Explain and show how each of these events would affect the deferred tax assets/liabilities in the consolidated balance sheet of Parent Limited as at 31 March 2020 as per applicable Ind AS.

You are also required to examine whether the effective rate of interest arrived at by Parent Limited for the loan of Rs. 50,00,000 is in accordance with applicable Ind AS or not?

Solution :

- (i) The tax loss creates a potential deferred tax asset for the group since its carrying value is nil and its tax base is Rs. 20,00,000.

However, no deferred tax asset can be recognised because there is no prospect of being able to reduce tax liabilities in the foreseeable future as no taxable profits are anticipated.

- (ii) The carrying value of the loan at 31 March 2020 is Rs. 53,90,000 (Rs. 50,00,000 – Rs. 1,00,000 + (Rs. 49,00,000 x 10%)).

The tax base of the loan is Rs. 50,00,000.

This creates a deductible temporary difference of Rs. 3,90,000 (Rs. 53,90,000 – Rs. 50,00,000) and a potential deferred tax asset of Rs. 78,000 (Rs. 3,90,000 x 20%).

If there are prospects of availability of taxable profits in future, deferred tax asset can be recognised.

Amortisation Table for verification of effective rate of interest

Year	Opening balance (Rs.) (A)	Interest @ 10% (Rs.) (B)	Closing balance (Rs.) (A) + (B)
1	(50,00,000 – 1,00,000) 49,00,000	4,90,000	53,90,000
2	53,90,000	5,39,000	59,29,000

3	59,29,000	5,92,900	65,21,900
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Since the closing balance calculated as per the above table on the basis of 10% matches with the bullet payment of Rs. 65,21,900, it assures that 10% rate of interest taken as effective rate of interest is correct and is in accordance with Ind AS 109. It considers the impact of cost of borrowing adjusted from the loan amount at initial recognition.

Question 9 : Jan 2021 – Paper

On 1st April 2017, A Limited acquired 80% of the share capital of S Limited. On acquisition date the share capital and reserves of S Ltd. stood at Rs.5,00,000 and Rs.1,25,000 respectively. A Limited paid initial cash consideration of Rs.10,00,000. Additionally, A Limited issued 2,00,000 equity shares with a nominal value of Rs.1 per share at current market value of Rs.1.80 per share.

It was also agreed that A Limited would pay a further sum of Rs.5,00,000 after three years.

A Limited's cost of capital is 10%. The appropriate discount factor for Rs.1 @ 10% receivable at the end of

1st year: 0.91

2nd year: 0.83

3rd year: 0.75

The shares and deferred consideration have not yet been recorded by A limited.

Below are the Balance Sheet of A Limited and S Limited as at 31st March, 2019:

	A Limited (Rs.000)	S Limited (Rs.000)
Non-current assets:		
Property, plant & equipment	5,500	1,500
Investment in S Limited at cost	1,000	
Current assets:		
Inventory	550	100
Receivables	400	200
Cash	<u>200</u>	<u>50</u>
	<u>7,650</u>	<u>1,850</u>
Equity:		
Share capital	2,000	500
Retained earnings	1,400	300
	3,400	800
Non-current liabilities	3,000	400
Current liabilities	<u>1,250</u>	<u>650</u>
	<u>7,650</u>	<u>1,850</u>

Further information :

- (i) On the date of acquisition the fair values of S Limited's plant exceeded its book value by Rs.2,00,000. The plant had a remaining useful life of five years at this date;
- (ii) The consolidated goodwill has been impaired by Rs.2,58,000; and

(iii) The A Limited Group, values the non-controlling interest using the fair value method. At the date of acquisition, the fair value of the 20% non-controlling interest was Rs.3,80,000. You are required to prepare Consolidated Balance Sheet of A Limited as at 31st March, 2019. (Notes to Account on Consolidated Balance Sheet is not required).

Solution :

**Consolidated Balance Sheet of A Ltd. and its subsidiary, S Ltd.
as at 31st March, 2019**

Particulars		Rs. in 000s
I.	Assets	
(1)	Non-current assets	
(i)	Property Plant & Equipment (W.N.4)	7,120.00
(ii)	Intangible asset – Goodwill (W.N.3)	1,032.00
(2)	Current Assets	
(i)	Inventories (550 + 100)	650.00
(ii)	Financial Assets	
(a)	Trade Receivables (400 + 200)	600.00
(b)	Cash & Cash equivalents (200 + 50)	250.00
	Total Assets	9,652.00
II.	Equity and Liabilities	
(1)	Equity	
(i)	Equity Share Capital (2,000 + 200)	2,200.00
(ii)	Other Equity	
(a)	Retained Earnings (W.N.6)	1,190.85
(b)	Securities Premium	160.00
(2)	Non-Controlling Interest (W.N.5)	347.40
(3)	Non-Current Liabilities (3,000 + 400)	3,400.00
(4)	Current Liabilities (W.N.8)	2,353.75
	Total Equity & Liabilities	9,652.00

Notes:

- Since the question required not to prepare Notes to Account, the column of Note to Accounts had not been drawn.
- It is assumed that shares were issued during the year 2018-2019 and entries are yet to be made.

Working Notes:

1. Calculation of purchase consideration at the acquisition date i.e. 1st April, 2017

	Rs. in 000s
Payment made by A Ltd. to S Ltd.	
Cash	1,000.00
Equity shares (2,00,000 shares x Rs.1.80)	360.00
Present value of deferred consideration (Rs.5,00,000 x 0.75)	<u>375.00</u>

Total consideration	<u>1,735.00</u>
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2. Calculation of net assets i.e. net worth at the acquisition date i.e. 1st April, 2017

	Rs. in 000s
Share capital of S Ltd.	500.00
Reserves of S Ltd.	125.00
Fair value increase on Property, Plant and Equipment	<u>200.00</u>
Net worth on acquisition date	<u>825.00</u>

3. Calculation of Goodwill at the acquisition date i.e. 1st April, 2017 and 31st March, 2019

	Rs. in 000s
Purchase consideration (W.N.1)	1,735.00
Non-controlling interest at fair value (as given in the question)	<u>380.00</u>
	2,115.00
Less: Net worth (W.N.2)	<u>(825.00)</u>
Goodwill as on 1st April 2017	1,290.00
Less: Impairment (as given in the question)	<u>258.00</u>
Goodwill as on 31st March 2019	<u>1,032.00</u>

4. Calculation of Property, Plant and Equipment as on 31st March 2019

		Rs. in 000s
A Ltd.		5,500.00
S Ltd.	1,500.00	
Add: Net fair value gain not recorded yet	200.00	
Less: Depreciation $[(200/5) \times 2]$	<u>(80.00)</u>	<u>1620.00</u>
	<u>120.00</u>	<u>7120.00</u>

5. Calculation of Post-acquisition gain (after adjustment of impairment on goodwill) and value of NCI as on 31st March 2019

		Rs. in 000s NCI (20%)	Rs. in 000s A Ltd. (80%)
Acquisition date balance		380.00	Nil
Closing balance of Retained Earnings	300.00		
Less: Pre-acquisition balance	<u>(125.00)</u>		
Post-acquisition gain	175.00		
Less: Additional Depreciation on PPE $[(200/5) \times 2]$	<u>(80.00)</u>		
Share in post-acquisition gain	<u>95.00</u>	19.00	76.00
Less: Impairment on goodwill	258.00	<u>(51.60)</u>	<u>(206.40)</u>

	<u>347.40</u>	<u>(130.40)</u>
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6. Consolidated Retained Earnings as on 31st March 2019

	Rs. in 000s
A Ltd.	1,400.00
Add: Share of post-acquisition loss of S Ltd. (W.N.5)	(130.40)
Less: Finance cost on deferred consideration (37.5 + 41.25) (W.N.7)	<u>(78.75)</u>
Retained Earnings as on 31st March 2019	<u>1,190.85</u>

7. Calculation of value of deferred consideration as on 31st March 2019

	Rs. in 000s
Value of deferred consideration as on 1st April 2017 (W.N.1)	375.00
Add: Finance cost for the year 2017-2018 (375 x 10%)	<u>37.50</u>
	412.50
Add: Finance cost for the year 2018-2019 (412.50 x 10%)	<u>41.25</u>
Deferred consideration as on 31st March 2019	<u>453.75</u>

8. Calculation of current Liability as on 31st March 2019

	Rs. in 000s
A Ltd.	1,250.00
S Ltd.	650.00
Deferred consideration as on 31st March 2019 (W.N.7)	<u>453.75</u>
Current Liability as on 31st March 2019	<u>2,353.75</u>

Question 10 : July 2021 – Paper

Given below are the balance sheets of a group of companies comprising LX, MX Limited and NX Limited as on 31st march 2021 :

	Rs. In lakhs		
Particulars	LX Limited	MX Limited	NX Limited
Assets			
<u>Non-current Assets</u>			
Property, Plant and Equipment Investment	1,500	1,600	1,400
17.0 lakh shares in MX Limited	2,620	–	–
9.6 lakh shares in NX Limited	–	1,350	–
<u>Current Assets</u>			
Inventories	1,230	730	1,180
Financial Assets			
Trade Receivables	1,415	270	620
Bills Receivables	650	60	–
Cash in hand and at Bank	1,085	90	150
	8,500	4,100	3,350

Equity and Liabilities			
Shareholders' Equity			
Share Capital (Rs.100 per share)	3,400	2,000	1,600
Other Equity			
– Reserve	1,150	810	580
– Retained	1,030	600	310
Current Liabilities			
Financial Liabilities			
Trade Payables	2,920	690	805
Bills Payable	–	–	–
MX Limited	–	–	55
	8,500	4,100	3,350

LX Limited holds 85% shares in MX Limited, which were acquired on 1st April 2020 and MX Limited holds 60% shares in NX Limited, which were acquired on 30th September 2020. The following balance stood in the books of MX Limited and NX Limited as on 1st April 2020 :

Particulars	MX Limited Rs. In Lakhs	NX Limited Rs. In Lakhs
Reserves	760	520
Retained earnings	480	150

The business activities of NX Limited are not seasonal in nature.

The parent company has adopted an accounting policy to measure non-controlling interest at first value applying IND AS 103. The fair value is to be determined at quoted market price. The given market price of MX Limited is Rs.120 per share and NX Limited is Rs.125, per share.

Prepare the consolidated Balance Sheet as on 31st March 2021 of the group of companies LX Limited, Mx Limited and NX Limited.

Solution :

Consolidated Balance Sheet of the Group as at 31st March, 2021

Particulars	Note No.	Rs. in lakh
ASSETS		
Non-current assets		
Property, plant and equipment	1	4,500.00
Current assets		
(a) Inventories	2	3,140.00
(b) Financial assets		
Trade receivables	3	2,305.00
Bills receivables	4	655
Cash and cash equivalents	5	1,325.00
Total assets		11,925.00
EQUITY & LIABILITIES		
Equity attributable to owners of parent		

Share Capital		3,400.00
Other Equity	6	2,893.10
Non-controlling interests (W.N.4)		1,216.90
LIABILITIES		
Non-current liabilities		Nil
Current liabilities		
(a) Financial Liabilities		
Trade payables	7	4,415.00
Total equity and liabilities		11,925.00

Notes to Accounts

(Rs. in lakh)

1	Property Plant & Equipment		
	LX Ltd.	1,500	
	MX Ltd.	1,600	
	NX Ltd.	<u>1,400</u>	4,500
2	Inventories		
	LX Ltd.	1,230	
	MX Ltd.	730	
	NX Ltd.	<u>1,180</u>	3,140
3	Trade Receivables		
	LX Ltd.	1,415	
	MX Ltd.	270	
	NX Ltd.	<u>620</u>	2,305
4	Bills Receivables		
	LX Ltd.	650	
	MX Ltd. (60-55)	<u>5</u>	655
5	Cash & Cash equivalents		
	LX Ltd.	1,085	
	MX Ltd.	90	
	NX Ltd.	<u>150</u>	1,325
6	Other Equity		
	Reserve (W.N.5)	1,207.80	
	Retained earnings (W.N.5)	1,172.80	
	Capital Reserve (W.N.3)	<u>512.50</u>	2,893.10
7	Trade Payables		
	LX Ltd.	2,920	
	MX Ltd.	690	
	NX Ltd.	<u>805</u>	4,415

Working Notes:

1. Analysis of Reserves and Surplus (Rs. in lakh)

	MX Ltd.		NX Ltd.
Reserves as on 1.4.2020	760		520
Increase during the year 2020-2021 (580 - 520)		60	
Increase for the half year till 30.9.2020			<u>30</u>
Balance on acquisition date (A)	760		550
Total balance as on 31.3.2021	<u>810</u>		<u>580</u>
Post-acquisition balance	<u>50</u>		30
Retained Earnings as on 1.4.2020	480		<u>150</u>
Increase during the year 2020-2021 (310 - 150)		160	
Increase for the half year till 30.9.2020			<u>80</u>
Balance on acquisition date (B)	480		230
Total balance as on 31.3.2021	<u>600</u>		<u>310</u>
Post-acquisition balance	120		80
Total balance on the acquisition date (A+B)	<u>1,240</u>		<u>780</u>

2. Calculation of Effective Interest of LX Ltd. in NX Ltd.

Acquisition by LX Ltd. in MX Ltd.	= 85%
Acquisition by MX Ltd. in NX Ltd.	= 60%
Acquisition by Group in NX Ltd. (85% x 60%)	= 51%
Non-controlling Interest	= 49%

3. Calculation of Goodwill / Capital Reserve on the acquisition

	MX Ltd.	NX Ltd.
Investment or consideration	2,620.00	(1,350 x 85%) 1,147.50
Add: NCI at Fair value		
[(2,000 / 100) x 120 x 15%]	360.00	
[(1,600 / 100) x 125 x 49%]	<u>-</u>	<u>980.00</u>
	2,980.00	2,127.50
Less: Identifiable net assets (Share Capital + Increase in the Reserves and Surplus till acquisition date)	(2,000+760+480) <u>(3,240.00)</u>	(1,600+550+230) <u>(2,380.00)</u>
Capital Reserve	<u>260.00</u>	<u>252.50</u>
Total Capital Reserve (260 + 252.50)	512.50	

4. Calculation of Non-controlling Interest

	MX Ltd.	NX Ltd.
At Fair Value (See Note 3)	360.00	980.00
Add: Post Acquisition Reserves (W.N.1)	(50 x 15%) 7.50	(30 x 49%) 14.70
Add: Post Acquisition Retained Earnings (W.N.1)	(120 x 15%) 18.00	(80 x 49%) 39.20
Less: NCI share of investment in NX Ltd.	(1,350 x 15%) (202.50)*	-
	<u>183.00</u>	<u>1,033.90</u>
Total (183.00 + 1,033.90)		1,216.90

***Note:** The non-controlling interest in MX Ltd. will take its proportion in NX Ltd. Therefore, they have to bear their proportion in the investment by MX Ltd. (in NX Ltd.) also.

5. Calculation of Consolidated Other Equity

	Reserves	Retained Earnings
LX Ltd.	1,150.00	1,030.00
Add: Share in MX Ltd.	(50 x 85%) 42.50	(120 x 85%) 102.00
Add: Share in NX Ltd.	(30 x 51%) <u>15.30</u>	(80 x 51%) <u>40.80</u>
	1,207.80	1,172.80

Question 11 : Nov 2021 – RTP

PP Ltd., a non-investment entity, is the parent of Praja Ltd. within the meaning of Ind AS 110 'Consolidated Financial Statements'. The investment in Praja Ltd. was carried in the separate financial statements of PP Ltd. at fair value with changes in fair value recognised in the other comprehensive income. On 1st April, 20X2, PP Ltd. qualifies as one that is an investment entity. Carrying amount of the investment on 1st April, 20X2 was Rs. 8,00,000. The fair value of its investment in Praja Ltd was Rs. 10,00,000 on that date. PP Ltd had recognised in OCI an amount of Rs. 1,00,000 as a previous fair value increase related to the investment in Praja Ltd.

How would PP Ltd account for the investment in Praja Ltd on the date of change of its classification/status as an investment entity, in its separate financial statements?

Solution :

- (i) As per paragraph 11B(b) of Ind AS 27, on the date of change, ie, 1st April, 20X2, PP Ltd (the parent) becoming an investment entity, its investment in Praja Ltd (the subsidiary) shall be at fair value through profit and loss in accordance with Ind AS 109. Accordingly, the new carrying amount will be Rs. 10,00,000.
- (ii) The difference between the new carrying amount and the carrying amount of the investment on the date of change will be recognised in the profit and loss. Hence, PP Ltd will recognise an amount of Rs. 2,00,000 (Rs. 10,00,000 – Rs. 8,00,000) in profit and loss as gain.

(iii) Any fair value adjustments previously recognised in OCI in respect of subsidiary ie Praja Ltd. shall be treated as if the investment entity had disposed off the subsidiary at the date of change in status as per para 11B(b) of Ind AS 27.

Further, as per para B5.7.1 of Ind AS 109, amounts presented in other comprehensive income shall not be subsequently transferred to profit or loss. However, the entity may transfer the cumulative gain or loss within equity.

Therefore, the company shall not reclassify the fair value gains or losses to profit or loss on change in classification from FVTOCI to FVTPL. However, the company may transfer the fair value gains or losses from one component to the other within equity.

Moreover, Paragraph 11A(e) of Ind AS 107, requires disclosure of any transfers of the cumulative gain or loss within equity during the period and the reason for such transfers. Accordingly, PP Ltd. shall provide the disclosures if it transfers the cumulative gain or loss from one component to the other within equity.

Particulars	Rs.
Carrying amount of investment in Praja Ltd [as per (i) above]	10,00,000
Amounts recognised in profit and loss relating to investment in Praja Ltd [as per (ii) above]	2,00,000

Question 12 : Nov 2021 – RTP

Solar Limited has an 80% interest in its subsidiary, Mars Limited. Solar Limited holds a direct interest of 25% in Venus Limited. Mars Limited also holds a 30% interest in Venus Limited. The decisions concerning relevant activities of Venus Limited require a simple majority of votes. How should Solar Limited account for its investment in Venus Limited in its consolidated financial statements?

Solution :

In the present case, Solar Limited controls Mars Limited (since it holds 80% of its voting rights). Consequently, it also controls the voting rights associated with 30% equity interest held by Mars Limited in Venus Limited. Solar Limited also has 25% direct equity interest and related voting power in Venus Limited. Thus, Solar Limited controls 55% (30% + 25%) voting power of Venus Limited. As the decisions concerning relevant activities of Venus Limited require a simple majority of votes. Solar Limited controls Venus Limited and should therefore consolidate it in accordance with Ind AS 110.

Although, Solar Limited controls Venus Limited, its entitlement to the subsidiary's economic benefits is determined on the basis of its actual ownership interest. For the purposes of the consolidated financial statements, Solar Limited's share in Venus Limited is determined as 49% [25% + (80% × 30%)]. As a result, 51% of profit or loss, other comprehensive income and net assets of Venus Limited shall be attributed to the non-controlling interests in the consolidated financial statements (this comprises 6% attributable to holders of non-controlling interests in Mars Limited [reflecting 20% interest of non-controlling shareholders of Mars Limited in 30% of Venus Limited] and 45% to holders of non-controlling interests in Venus Limited).

Question 13 : May 2022 – Paper

RST Ltd. prepares consolidated financial statement as at 31st March each year. On 1st July 2021, RST acquired 75% of the equity shares of the DHF Ltd. and gained control of DHF Ltd. The issued shares of DHF Ltd. is 1,20,00,000 equity shares. Details of the purchase consideration are as follows :

- On 1st July 2021, RST Ltd. issued two shares for every three shares acquired in DHF Ltd. On 1st July 2021, the market value of an equity shares in RST Ltd. was Rs.6.50 and the market value of an equity shares in DHF Ltd. was Rs.5.50.
- On 30th June 2022, RST Ltd. will make cash payment of Rs.71,50,000 to the former share holders of DHF Ltd. who sold their shares to RST Ltd. on 1st July 2021. On 1st July, 2021 RST Ltd. would have to pay interest at an annual rate of 10% on borrowings.
- On 30th June 2023, RST Ltd. may make a cash payment of Rs.3,00,00,000 to the former share holders of DHF Ltd. who sold their shares to RST Ltd. on 1st July 2021. This payment is contingent upon the revenues of RST Ltd. growing by 15% over the two-year period from 1st July 2021 to 30th June, 2023. On 1st July, 2021, the fair value of this contingent consideration was Rs.2,20,00,000.

On 1st July 2021, the carrying values of the identifiable net assets of DHF Ltd. in the books of that company was Rs.6,00,00,000. On 1st July 2021, the fair values of these net assets was Rs.7,00,00,000. The rate of deferred tax to apply to temporary differences is 20%.

During the nine months ended on 31st March 2022, DHF Ltd. had a poorer than expected operating performance. Therefore, on 31st March 2022 it was necessary for RST Ltd. to recognize an impairment of the goodwill arising on acquisition of DHF Ltd. amounting to 12.50% of its total computed value.

Compute the impairment of goodwill in the consolidated financial statements of RST Ltd. under the methods permitted by Ind AS 103 for the initial computation of the non-controlling interest in DHF Ltd. at the acquisition date.

Solution :

	NCI at fair value Rs. in 000	NCI at proportionate share of net assets Rs. in 000
Cost of investment		
Share exchange (12,000 x 75% x 2/3 x Rs. 6.50)	39,000	39,000
Deferred consideration (7,150 / 1.10)	6,500	6,500
Contingent consideration	<u>25,000</u>	<u>25,000</u>
Total Purchase Consideration (a)	70,500	70,500
Non-controlling interest on the date of acquisition: (b)		
Fair value – 3,000 x Rs.5.50	16,500	
% of net assets – 68,000 (Refer W.N.) x 25%		17,000
Net assets on the acquisition date (Refer W.N.) (c)	<u>(68,000)</u>	<u>(68,000)</u>

Goodwill on acquisition	(a+b-c)	<u>19,000</u>	<u>19,500</u>
Impairment @ 12.50%		2,375.00	2,437.50

Working Note :

Net assets on the acquisition date	Rs. in 000
Fair value at the acquisition date	70,000
Deferred tax on fair value adjustments [20% x (70,000 – 60,000)]	<u>(2,000)</u>
	<u>68,000</u>

Question 14 : Nov 2022 – Paper

Given below are the balance sheet of a group of companies comprising X Ltd., Y Ltd. And Z Ltd. As on 31st March, 2022 :

	(Rs. In Lakhs)		
	X Ltd.	Y Ltd.	Z Ltd.
Assets			
Non-Current Assets			
Property, Plant & Equipment	1,120	1,260	1,050
Investment :			
112 lakh shares in Y Ltd.	1,190		
84 lakh shares in Z Ltd.		980	
Current Assets			
Inventories	770	245	175
Financial Assets :			
Trade Receivables	910	350	770
Bills Receivables	252	-	105
Cash in hand and at Bank	798	140	140
	5,040	2,975	2,240
Equity and Liabilities			
Shareholder's equity			
Share Capital (Rs.10 per share)	2,100	1,400	1,120
Other Equity :			
Reserves	630	350	280
Retained earnings	560	175	210
Current Liabilities			
Financial Liabilities :			
Trade Payables	1,645	805	630
Bills payable			
X Ltd.	-	245	-
Y Ltd.	105	-	-
	5,040	2,975	2,240

The following additional information is available :

- (i) X Ltd. Holds 80% shares in Y Ltd. And Y Ltd. Holds 75% shares in Z Ltd. Their holdings were acquired on 30th September, 2021.
- (ii) The business activities of all the companies are not seasonal in nature and therefore, it can be assumed that profits are earned evenly throughout the year.
- (iii) On 1st April, 2021 the following balances stood in the books of Y Ltd. And Z Ltd.

(Rs. in Lakhs)

	Y Limited	Z Limited
Reserve	280	210
Retained earnings	70	105

- (iv) Rs.35 lakhs included in the inventory figure of Y Ltd. Is inventory which has been purchased from Z Ltd. at cost plus 25%.
- (v) The parent company has adopted an accounting policy to measure non-controlling interest at fair value (quoted market price) applying Ind As 103. Assume that market price of the shares of Y Ltd. and Z Ltd. are the same as their respective face values.
- (vi) Y Ltd. purchased goods from Z Ltd. after acquiring the shares of Z Ltd.

You are required to prepare consolidated balance sheet as on 31st March 2022 of the group of companies X Limited, Y Limited

Solution :

Consolidated Balance Sheet of the Group as on 31st March, 2022

Particulars	Note No.	Rs. in lakh
ASSETS		
Non-current assets		
(a) Property, Plant and Equipment	1	3,430.00
Current Assets		
(a) Inventories	2	1,183.00
(b) Financial assets		
(i) Trade receivables	3	2,142.00
(ii) Cash and Cash equivalents	4	1,078.00
Total assets		7,833.00
EQUITY & LIABILITIES		
Equity attributable to owners of parent		
(a) Share Capital		2,100.00
(b) Other Equity	5	1,966.30
Non-controlling interests (W.N.4)		581.7
Total equity		4,648.00
LIABILITIES		
Non-current liabilities		Nil
Current liabilities		

(a) Financial Liabilities		
(i) Trade payables	6	3,185.00
Total liabilities		3,185.00
Total Equity and Liabilities		7,833.00

Notes to Accounts :

(Rs. in lakh)

1	Property, Plant & Equipment		
	X Ltd.	1,120.00	
	Y Ltd.	1,260.00	
	Z Ltd.	<u>1,050.00</u>	3,430.00
2	Inventories		
	X Ltd.	770.00	
	Y Ltd. (245 – 7)	238.00	
	Z Ltd.	<u>175.00</u>	1,183.00
3	Trade Receivables		
	X Ltd.	910.00	
	Y Ltd.	350.00	
	Z Ltd.	<u>770.00</u>	
		(A) <u>2,030.00</u>	
	Bills Receivables		
	X Ltd. (252 – 245)	7.00	
	Z Ltd.	<u>105.00</u>	
		(B) <u>112.00</u>	
	Total Trade Receivables (A+B)		2,142.00
4	Cash & Cash equivalents		
	X Ltd.	798.00	
	Y Ltd.	140.00	
	Z Ltd.	<u>140.00</u>	1,078.00
5	Other Equity		
	Reserve (W.N.5)	679.00	
	Retained Earnings (W.N.5)	629.30	
	Capital Reserve (W.N.3)	<u>658.00</u>	1,966.30
6	Trade Payables		
	X Ltd.	1,645.00	
	Y Ltd.	805.00	
	Z Ltd.	<u>630.00</u>	
		(A) <u>3,080.00</u>	
	Bills payable		
	X Ltd.	105.00	

Y Ltd. (245 - 245)		-	
	(B)	<u>105.00</u>	
Total Trade Payables (A+B)			3,185.00

***Note:** Bills Payable of X Ltd. is not reflecting as Bills Receivable of Y Ltd. This may happen since Y Ltd. may have discounted/endorsed the same to the bank/third party.

Working Notes:

1. Analysis of Reserves and Surplus

(Rs. in lakh)

		Y Ltd.		Z Ltd.
Reserves as on 31.3.2021		280.00		210.00
Increase during the year 2021-2022	70.00		70.00	
Increase for the half year till 30.9.2021		35.00		35.00
Balance as on 30.9.2021 (A)		315.00		245.00
Total balance as on 31.3.2022		350.00		280.00
Post-acquisition balance of Reserves		35.00		35.00
Retained Earnings as on 31.3.2021		70.00		105.00
Increase during the year 2021-2022	105.00		105.00	
Increase for the half year till 30.9.2021		52.50		52.50
Balance as on 30.09.2021 (B)		122.50		157.50
Total balance as on 31.3.2022		175.00		210.00
Post-acquisition balance of RE		52.50		52.50
Less: Unrealised Gain on inventories [(35 ÷ 125) x 25]		-		(7.00)
Post-acquisition balance of RE for CFS		52.50		45.50
Total balance on the acquisition date i.e. 30.9.2021 (A+B)		437.50		402.50

2. Calculation of Effective Interest of X Ltd. in Z Ltd.

Acquisition by X Ltd. in Y Ltd.	= 80%
Non-controlling Interest of Y Ltd.	= 20%
Acquisition by Y Ltd. in Z Ltd.	= 75%
Acquisition by Group in Z Ltd. (80% x 75)	= 60%
Non-controlling Interest of Z Ltd	= 40%

3. Calculation of Goodwill / Capital Reserve on acquisition of subsidiaries

Rs. in lakhs

	Y Ltd.	Z Ltd.
Investment or consideration	1190.00	(980 x 80%) 784.00
Add: NCI at Fair value (1,400 x 20%)	280.00	
(1,120 x 40%)	-	448.00

	1470.00	1232.00
Less: Identifiable net assets (Share Capital + Increase in the Reserves and Surplus till acquisition date)	(1,400+437.50) (1,837.50)	(1,120+402.50) (1,522.50)
Capital Reserve	367.50	290.50
Total Capital Reserve (367.50 + 290.50)	658.00	

4. Calculation of Non-controlling Interest

Rs. in lakhs

	Y Ltd.	Z Ltd.
At Fair Value (See Note 3)	280.00	448.00
Add: Post Acquisition Reserves (See Note 1)	(35 x 20%) 7.00	(35 x 40%) 14.00
Add: Post-acquisition retained earnings (See Note 1)	(52.50 x 20%) 10.50	(45.50 x 40%) 18.20
Less: NCI share of investment in Z Ltd.	(980 x 20%) (196.00)* 101.50	- 480.20
Total (101.50 + 480.20)	581.70	

*Note: The non-controlling interest in Y Ltd. will take its proportion in Z Ltd. So, they have to bear their proportion in the investment by Y Ltd. (in Z Ltd.) also.

5. Calculation of Consolidated Other Equity

Rs. in lakhs

	Reserves	Retained Earnings
X Ltd.	630.00	560.00
Add: Share in Y Ltd.	(35 x 80%) 28.00	(52.50 x 80%) 42.00
Add: Share in Z Ltd.	(35 x 60%) <u>21.00</u>	(45.50 x 60%) <u>27.30</u>
	679.00	629.30

In the above solution, it is assumed that profits of Z Ltd. has been earned evenly throughout the year irrespective of post-acquisition sale of goods to Y Ltd.

Alternatively, profit on sale of goods to Y Ltd. is deducted from total profit of Z Ltd. before distribution of total profit of Z Ltd. into pre-acquisition and post-acquisition. In such a case, the solution will be as follows:

Consolidated Balance Sheet of the Group as on 31st March, 2022

Particulars	Note No.	Rs. in lakh
ASSETS		
Non-current assets		
(a) Property, plant and equipment	1	3430.00
Current assets		
(c) Inventory	2	1183.00
(d) Financial assets		
(i) Trade receivable	3	2142.00
(ii) Cash and cash equivalents	4	1078.00

Total assets		7833.00
EQUITY & LIABILITIES		
Equity attributable to owners of parent		
Share Capital		2100.00
Other Equity	5	1964.90
Non-controlling interests (W.N.4)		583.10
Total equity		4648.00
LIABILITIES		
Non-current liabilities		Nil
Current liabilities		
(b) Financial Liabilities		
(i) Trade payables	6	<u>3185.00</u>
Total liabilities		<u>3185.00</u>
Total equity and liabilities		<u>7833.00</u>

Notes to Accounts

(Rs. in lakh)

1	Property, plant & equipment		
	X Ltd.	1120.00	
	Y Ltd.	1260.00	
	Z Ltd.	<u>1050.00</u>	3430.00
2	Inventories		
	X Ltd.	770.00	
	Y Ltd. (245 – 7)	238.00	
	Z Ltd.	<u>175.00</u>	1183.00
3	Trade receivable		
	X Ltd.	910.00	
	Y Ltd.	350.00	
	Z Ltd.	<u>770.00</u>	
		(A) <u>2030.00</u>	
	Bills receivable		
	X Ltd. (252 – 245)	7.00	
	Z Ltd.	<u>105.00</u>	
		(B) <u>112.00</u>	
	Total Trade Receivables (A+B)		2142.00
4	Cash & cash equivalents		
	X Ltd.	798.00	
	Y Ltd.	140.00	
	Z Ltd.	140.00	1078.00
5	Other equity		

	Reserve (W.N.5)		679.00	
	Retained Earnings (W.N.5)		631.40	
	Capital Reserve (W.N.3)		<u>654.50</u>	1964.90
6	Trade payable			
	X Ltd.		1645.00	
	Y Ltd.		805.00	
	Z Ltd.		<u>630.00</u>	
		(A)	<u>3080.00</u>	
	Bills payable			
	X Ltd.		105.00	
	Y Ltd. (245 - 245)		<u>-</u>	
		(B)	<u>105.00</u>	
	Total of Trade payable (A+B)			3185.00

*Note: Bills Payable of X Ltd. is not reflecting as Bills Receivable of Y Ltd. This may happen since Y Ltd. may have discounted / endorsed the same to the bank/third party.

Working Notes:

1. Analysis of Reserves and Surplus

(Rs. in lakh)

		Y Ltd.		Z Ltd.
Reserves as on 31.3.2021		280.00		210.00
Increase during the year 2021-2022	70.00		70.00	
Increase for the half year till 30.9.2021		<u>35.00</u>		<u>35.00</u>
Balance as on 30.9.2021 (A)		315.00		245.00
Total balance as on 31.3.2022		<u>350.00</u>		<u>280.00</u>
Post-acquisition balance of Reserves		<u>35.00</u>		<u>35.00</u>
		-		-
Retained Earnings as on 31.3.2021		70.00		105.00
Increase during the year 2021-2022 for Y Ltd.	105.00			
Increase during the year 2021-22 for Z Ltd.	105.00			
Less: Unrealised gain [(35/125)x25]	<u>(7.00)</u>			
Profit of the year earned evenly for Z Ltd.	<u>98.00</u>		98.00	
Increase for the half year till 30.9.2021		<u>52.50</u>		<u>49.00</u>
Balance as on 30.9.2021 (B)		122.50		154.00
Total balance as on 31.3.2022		<u>(175.00)</u>		<u>(210.00)</u>
Post-acquisition balance		52.50		56.00
Less: Unrealised gain on inventories [(35/125)x25]		<u>-</u>		<u>-7.00</u>
Post-acquisition balance for CFS		<u>52.50</u>		<u>49.00</u>
Total balance on the acquisition date i.e. 30.9.2021 (A+B)		437.50		399.00

2. Calculation of Effective Interest of X Ltd. in Z Ltd.

Acquisition by X Ltd. in Y Ltd.	= 80%
Non-controlling Interest of Y Ltd.	= 20%
Acquisition by Y Ltd. in Z Ltd.	= 75%
Acquisition by Group in Z Ltd. (80% x 75%)	= 60%
Non-controlling Interest of Z Ltd	= 40%

3. Calculation of Goodwill / Capital Reserve on the acquisition (Rs. in lakhs)

	Y Ltd.	Z Ltd.
Investment or consideration	1,190	(980 x 80%) 784
Add: NCI at Fair value (1,400 x 20%) (1,120 x 40%)	280 —	448
	1,470	1232
Less: Identifiable net assets (Share Capital + Increase in the Reserves and Surplus till acquisition date)	(1,400+437.50) <u>(1,837.50)</u>	(1,120+399) <u>(1,519.00)</u>
Capital Reserve	<u>367.50</u>	<u>287.00</u>
Total Capital Reserve (367.50 + 287.00)	654.5	

4. Calculation of Non-controlling Interest (Rs. in lakhs)

	Y Ltd.	Z Ltd.
At Fair Value (See Note 3)	280.00	448.00
Add: Post-acquisition Reserves (See Note 1)	(35 x 20%) 7.00	(35 x 40%) 14.00
Add: Post-acquisition Retained Earnings (See Note 1)	(52.50 x 20%) 10.50	49.00 x 40%) 19.60
Less: NCI share of investment in Z Ltd.	(980 x 20%) <u>(196.00)*</u>	—
	101.5	481.60
Total (101.50 + 481.60)	583.1	

*Note: The non-controlling interest in Y Ltd. will take its proportion in Z Ltd. So, they have to bear their proportion in the investment by Y Ltd. (in Z Ltd.) also.

5. Calculation of Consolidated Other Equity (Rs. in lakhs)

	Reserves	Retained Earnings
X Ltd.	630.00	560.00
Add: Share in Y Ltd.	(35 x 80%) 28.00	(52.50 x 80%) 42.00
Add: Share in Z Ltd.	(35 x 60%) <u>21.00</u>	(49.00 x 60%) <u>29.40</u>
	<u>679.00</u>	<u>631.40</u>

Question 15 : May 2023 – RTP

'High Speed Limited' manufactures and sells cars. The Company wants to foray into the two-wheeler business and therefore it acquires 30% interest in Quick Bikes Limited for Rs. 5,00,000 as at 1st November, 20X1 and an additional 25% stake as at 1st January, 20X2 for Rs. 5,00,000 at its fair value.

Following is the Balance Sheet of Quick Bikes Limited as at 1st January, 20X2:

Liabilities	Carrying value	Fair value	Assets	Carrying value	Fair value
Share capital	1,00,000		Plant and equipment	3,50,000	7,50,000
Reserves	5,50,000		Investment in bonds	4,00,000	5,00,000
Trade payables	<u>1,50,000</u>	<u>1,50,000</u>	Trade Receivables	<u>50,000</u>	<u>50,000</u>
Total	8,00,000		Total	8,00,000	

Quick Bikes Limited sells the motorcycles under the brand name 'Super Start' which has a fair value of Rs. 3,50,000 as at 1st January, 20X2. This is a self-generated brand therefore Quick Bikes Limited has not recognized the brand in its books of accounts.

Following is the separate balance sheet of High Speed Limited as at 1st January, 20X2:

Liabilities	Amount	Assets	Amount
Share capital	5,00,000	Plant and equipment	13,50,000
Reserves	15,00,000	Investment in Quick Bike	10,00,000
Short term loans	4,00,000	Trade Receivables	80,000
Trade payables	3,00,000	Cash and bank balances	5,20,000
Other liabilities	<u>2,50,000</u>		
Total	29,50,000	Total	29,50,000

In relation to the acquisition of Quick Bikes Limited, you are required to:

- (i) Pass the necessary journal entries to give effect of business combination in accordance with Ind AS 103 as at acquisition date 1st January, 20X2. NCI is measured by the entity at fair value. Provide working notes, ignore deferred tax implication; and
- (ii) Prepare a consolidated balance sheet of High Speed Limited as at 1st January, 20X2.

Solution :

(i)

Journal Entry

		Rs.	Rs.
Plant and Equipment	Dr	7,50,000	
Investment in bonds	Dr	5,00,000	
Trade Receivables	Dr	50,000	
Brand	Dr	3,50,000	
Goodwill (balancing figure)	Dr	5,00,000	
	To Investment in Quick Bikes		10,00,000
	To Profit or loss A/c (W.N.1)		1,00,000
	To Trade Payables		1,50,000
	To NCI (W.N.3)		9,00,000

(Being assets and liabilities acquired at fair value and previous investment considered at fair value on the acquisition date)		
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Working Notes:

1. Calculation of fair value of shares on the acquisition date 1st January, 20X2

25% Shares purchase on 1st January, 20X2 (fair value)	Rs. 5,00,000
30% Shares purchase on 1st November, 20X1 at Rs. 5,00,000	
Fair value = [(5,00,000 / 25%) x 30%]	<u>Rs. 6,00,000</u>
Total consideration at fair value on acquisition date	Rs. 11,00,000
Less: Cost of investment (5,00,000 + 5,00,000)	<u>(Rs. 10,00,000)</u>
Gain recognised to Profit or Loss/OCI (as appropriate)	<u>Rs. 1,00,000</u>

2. Computation of Net Identifiable Assets at fair value

	Rs.
Plant and Equipment	7,50,000
Investment in bonds	5,00,000
Trade Receivables	50,000
Self-generated Brand	<u>3,50,000</u>
	<u>16,50,000</u>
Less: Trade Payables	<u>(1,50,000)</u>
Net Identifiable Assets at fair value	<u>15,00,000</u>

3. Measurement of Non-controlling Interest (on fair value basis)

Share of NCI (100- 30-25)	45%
Taking fair value of shares on 1st January, 20X2 as a base	Rs.9,00,000
[(11,00,000/ 55%) x 45%]	

(ii) Consolidated Balance Sheet of High Speed Limited as at 1st January, 20X2

	Note No.	Rs.
Assets		
Non-current assets		
(a) Property, plant and equipment	1	21,00,000
(b) Intangible asset	2	8,50,000
(c) Investment in bonds		5,00,000
Current Assets		
(a) Financial assets		
(i) Trade receivables	3	1,30,000
(ii) Cash and cash equivalents	4	<u>5,20,000</u>
		<u>41,00,000</u>
Equity and Liabilities		
Equity		

(a) Equity share capital		5,00,000
(b) Other Equity	5	16,00,000
Non-controlling Interest (W.N.3)		9,00,000
Current Liabilities		
(a) Financial liabilities		
(i) Borrowings	6	4,00,000
(ii) Trade Payables	7	4,50,000
(b) Other Current Liabilities	8	<u>2,50,000</u>
		41,00,000

Notes to Accounts

Sr. No.		Rs.	Rs.
1.	Property, plant and equipment High Speed Ltd. Quick Bikes Ltd.	13,50,000 <u>7,50,000</u>	21,00,000
2.	Intangible asset Goodwill Brand value of Quick Bikes Ltd.	5,00,000 <u>3,50,000</u>	8,50,000
3.	Trade Receivables High Speed Ltd. Quick Bikes Ltd.	80,000 <u>50,000</u>	1,30,000
4.	Cash and cash equivalents Quick Bikes Ltd		5,20,000
5.	Other Equity - Reserves High Speed Ltd. Add: Gain on investment in Quick Bikes Ltd	15,00,000 <u>1,00,000</u>	16,00,000
6.	Borrowings Short term loans of High Speed Ltd		4,00,000
7.	Trade Payables High Speed Ltd. Quick Bikes Ltd.	3,00,000 <u>1,50,000</u>	4,50,000
8.	Other Current Liabilities High Speed Ltd.		2,50,000

Question 16 : May 2023 – Paper

On 1st April 2021, P Limited acquired 100 % interest in S Limited for Rs.75.00 lakhs when the fair value of the net assets of S Limited was Rs.60.00 lakhs. Goodwill of Rs.15.00 lakhs arose on consolidation. On 31st March, 2023, P Limited disposed off 80% interest in S Limited for Rs.114.00 lakhs. As on the date of disposal, the carrying value of the net assets of the S Limited excluding goodwill was Rs.1,20,00,000/-. The fair value of the remaining interest is Rs.28,50,000/-.

You are required to :

- i. calculate the gain or loss on sale of disposal and
- ii. pass necessary journal entries on disposal of 80% interest in S Limited in P Limited's separate and consolidated financial statements as on 31st March, 2023.

Solution :

(a) In P Ltd.'s Separate Financial Statements

(i) Calculation of Gain or Loss on disposal in P Ltd.'s separate financial statements

	Rs. in lakhs
Sales proceeds	114.0
Less: Cost of investment in subsidiary (75 x 80%)	<u>(60.0)</u>
Gain on sale in parent's account	<u>54.0</u>

(ii) Journal Entry in P Limited's separate financial statements Rs. in lakhs

Date	Particulars	Dr.	Cr.
31.3.2023	Bank A/c Dr.	114.00	
	Investment in Associates Dr.	15.00	
	To Investment in subsidiary A/c		75.00
	To Gain on sale of subsidiary A/c		54.00
31.3.2023	Gain on sale of subsidiary A/c Dr.	54	
	To Statement of Profit and Loss		54

Note: In case of partial disposal of investment leading to significant influence because of loss of control, the above solution has been provided by applying proportionate approach. However, cost of retained investment on the date of loss of control has not been defined in Ind AS 27 'Separate Financial Statements'. Therefore, paragraphs 10 and 11(a) of Ind AS 8 (i.e. in the absence of accounting policy that specifically applies to a transaction, management shall refer to, and consider the applicability of the requirements in Ind AS dealing with similar and related issues) have been applied. Further, para 25(b) of Ind AS 110 *inter alia* states that recognition of investment retained in the former subsidiary **to be the fair value** which shall be regarded as the fair value on initial recognition of a financial asset in accordance with Ind AS 109 or, when appropriate, the cost on initial recognition of an investment in an associate or joint venture.

Accordingly, following **ALTERNATE** solution may also be considered:

(i) Calculation of Gain or Loss on disposal in P Ltd.'s separate financial statements:

	Rs. in lakhs
Sales proceeds	114.0
Fair value of 20% interest retained	<u>28.50</u>
	142.50
Less: Cost of investment in subsidiary	<u>(75.0)</u>
Gain on sale in parent's account	<u>67.5</u>

(ii) Journal Entry in P Limited's separate financial statements Rs. in lakhs

Date	Particulars	Dr.	Cr.
31.3.2023	Bank A/c Dr.	114.00	
	Investment in Associate at cost (as per para 25 Ind AS 110) Dr.	28.50	
	To Investment in subsidiary A/c		75.00
	To Gain on sale of subsidiary A/c		67.50
31.3.2023	Gain on sale of subsidiary A/c Dr.	67.50	
	To Statement of Profit and Loss		67.50

(b) In P Ltd.'s Consolidated Financial Statements

(i) Calculation of Gain or Loss on disposal in P Ltd.'s consolidated financial statements

	Rs. in lakhs
Sales proceeds	114.00
Fair value of 20% interest retained	<u>28.50</u>
	142.50
Less: Net assets disposed, including goodwill (1,20,00,000 + 15,00,000)	<u>(135.00)</u>
Gain on sale in the group's financial statements	7.50

(ii) Journal Entry in P Limited's consolidated financial statements Rs. in lakhs

Date	Particulars	Dr.	Cr.
31.3.2023	Bank A/c Dr.	114.00	
	Fair value of Net identifiable assets Dr.	28.50	
	To Net asset of subsidiary A/c		120.00
	To Goodwill		15.00
	To Gain on sale of subsidiary A/c		7.50
31.3.2023	Gain on sale of subsidiary A/c Dr.	7.50	
	To Statement of Profit or Loss		7.50

Note:

The above solution has been drawn on the assumption that the retained investment had led to significant influence. Accordingly, investment in an associate has been accounted for on partial disposal of investment by P Ltd.

However, it may **alternatively** be assumed that the retained investment, after loss of control due to partial disposal of investment, does not lead to significant influence on S Ltd. In such a situation, retained interest will be measured at fair value in P Ltd.'s Separate Financial Statements as given in the alternate solution and main solution will not be applicable in such a case.

Ishwar Ltd. holds investments in Vinayak Ltd. The draft balance sheets of two entities at 31st March, 20X4 were as follows:

Particulars	Ishwar Ltd. Rs. in '000s	Vinayak Ltd. Rs. in '000s
Assets		
Non-current Assets		
Property, Plant and Equipment	26,20,000	18,50,000
Investment	<u>21,15,000</u>	<u>NIL</u>
Total non-current assets	<u>47,35,000</u>	<u>18,50,000</u>
Current Assets		
Inventories	6,00,000	3,75,000
Trade Receivables	4,50,000	3,30,000
Cash and Cash Equivalents	<u>75,000</u>	<u>60,000</u>
Total current assets	<u>11,25,000</u>	<u>7,65,000</u>
TOTAL ASSETS	<u>58,60,000</u>	<u>26,15,000</u>
Equity and Liabilities		
Equity		
Share Capital (Rs. 1 shares)	7,00,000	5,00,000
Retained Earnings	28,65,000	10,50,000
Other Components of Equity	<u>12,50,000</u>	<u>50,000</u>
Total Equity	<u>48,15,000</u>	<u>16,00,000</u>
Non-current Liabilities		
Provisions	6,250	NIL
Long-term Borrowings	4,13,750	4,50,000
Deferred Tax	<u>2,25,000</u>	<u>1,40,000</u>
Total Non-current Liabilities	<u>6,45,000</u>	<u>5,90,000</u>
Current Liabilities		
Trade and Other Payables	3,00,000	2,50,000
Short-term Borrowings	<u>1,00,000</u>	<u>1,75,000</u>
Total Current Liabilities	<u>4,00,000</u>	<u>4,25,000</u>
TOTAL EQUITY AND LIABILITIES	<u>58,60,000</u>	<u>26,15,000</u>

Additional Information:

Ishwar Ltd.'s investment in Vinayak Ltd. On 1st April, 20X1, Ishwar Ltd. acquired 400 million shares in Vinayak Ltd. by means of a share exchange of one share in Ishwar Ltd. for every two shares acquired in Vinayak Ltd. On 1st April, 20X1, the market value of one share of Ishwar Ltd. was Rs.7. Ishwar Ltd. appointed a professional firm for conducting due diligence for acquisition of Vinayak Ltd., the cost of which amounted to Rs. 15 million. Ishwar Ltd. included these acquisition costs in the carrying amount of the investment in Vinayak Ltd. in the draft balance sheet of Ishwar Ltd.

There has been no change to the carrying amount of this investment in Ishwar Ltd.'s own balance sheet since 1st April, 20X1.

On 1st April, 20X1, the individual financial statements of Vinayak Ltd. showed the following balances:

- Retained earnings Rs. 750 million
- Other components of equity Rs. 25 million

The directors of Ishwar Ltd. carried out a fair value exercise to measure the identifiable assets and liabilities of Vinayak Ltd. at 1st April, 20X1. The following matters emerged:

- Property having a carrying amount of Rs. 800 million (land component Rs. 350 million, buildings component Rs. 450 million) had an estimated fair value of Rs. 1,000 million (land component Rs. 400 million, buildings component Rs. 600 million). The buildings component of the property had an estimated useful life of 30 years at 1st April, 20X1.
- Plant and equipment having a carrying amount of Rs. 600 million had an estimated fair value of Rs. 700 million. The estimated remaining useful life of this plant at 1st April, 20X1 was four years. None of this plant and equipment had been disposed of between 1st April, 20X1 and 31st March, 20X4.
- On 1st April, 20X1, the notes to the financial statements of Vinayak Ltd. disclosed contingent liability. On 1st April, 20X1, the fair value of this contingent liability was reliably measured at Rs. 30 million. The contingency was resolved in the year ended 31st March, 20X2 and no payments were required to be made by Vinayak Ltd. in respect of this contingent liability.
- The fair value adjustments have not been reflected in the individual financial statements of Vinayak Ltd. In the consolidated financial statements, the fair value adjustments will be regarded as temporary differences for the purposes of computing deferred tax. The rate of deferred tax to apply to temporary differences is 20%.

The directors of Ishwar Ltd. used the proportion of net assets method when measuring the non-controlling interest in Vinayak Ltd. in the consolidated balance sheet.

Impairment review of goodwill on acquisition of Vinayak Ltd.

No impairment of the goodwill on acquisition of Vinayak Ltd. was evident when the reviews were carried out on 31st March, 20X2 and 20X3. On 31st March, 20X4, the directors of Ishwar Ltd. carried out a further review and concluded that the recoverable amount of the net assets of Vinayak Ltd. at that date was Rs. 2,000 million. Vinayak Ltd. is regarded as a single cash generating unit for the purpose of measuring goodwill impairment.

Provision

On 1st April, 20X3, Ishwar Ltd. completed the construction of a non-current asset with an estimated useful life of 20 years. The costs of construction were recognised in property, plant and equipment and depreciated appropriately. Ishwar Ltd. has a legal obligation to restore the site on which the non-current asset is located on 31st March, 2X43. The estimated cost of this restoration work, at 31st March, 2X43 prices, is Rs. 125 million. The directors of Ishwar Ltd. have made a provision of Rs. 6.25 million ($1/20 \times \text{Rs. } 125 \text{ million}$) in the draft balance sheet at 31st March, 20X4.

An appropriate annual discount rate to use in any relevant calculations is 6% and at this rate the present value of Rs. 1 payable in 20 years is 31.2 paise.

Prepare the consolidated balance sheet of Ishwar Ltd. at 31st March, 20X4. Consider deferred tax implications.

Solution :

Consolidated Balance Sheet of Ishwar Ltd. at 31st March, 20X4

Particulars	Rs. in '000s
Assets	
Non-current Assets:	
Property, Plant and Equipment [(26,20,000 + 18,50,000) + {(2,00,000 (W.N.1) – 15,000 (W.N.1)) + (1,00,000 (W.N.1) – 75,000 (W.N.1)) + (39,000 – 1,950) (WN 7)}]	47,17,050
Investment (21,15,000 – 14,00,000 – 15,000)	7,00,000
Goodwill (W.N.2)	<u>1,85,600</u>
Total non-current assets	<u>56,02,650</u>
Current Assets:	
Inventories (6,00,000 + 3,75,000)	9,75,000
Trade Receivables (4,50,000 + 3,30,000)	7,80,000
Cash and Cash Equivalents (75,000 + 60,000)	<u>1,35,000</u>
Total current assets	<u>18,90,000</u>
TOTAL ASSETS	74,92,650
Equity and Liabilities	
Equity attributable to equity holders of the parent	
Share Capital	7,00,000
Retained Earnings (W.N.5)	30,31,960
Other Components of Equity (W.N.6)	<u>12,70,000</u>
	50,01,960
Non-controlling Interest (W.N.4)	<u>3,53,600</u>
Total equity	<u>53,55,560</u>
Non-current Liabilities	
Provisions (39,000 + 2,340 (W.N.7))	41,340
Long-term Borrowings (4,13,750 + 4,50,000)	8,63,750
Deferred Tax (W.N.8)	<u>4,07,000</u>
Total non-current liabilities	<u>13,12,090</u>
Current Liabilities	
Trade and Other Payables (3,00,000 + 2,50,000)	5,50,000
Short-term Borrowings (1,00,000 + 1,75,000)	<u>2,75,000</u>
Total Current Liabilities	<u>8,25,000</u>
TOTAL EQUITY AND LIABILITIES	<u>74,92,650</u>

Working Notes:

1. Computation of Net Assets of Vinayak Ltd.

	1st April, 20X1 (Date of	31st March, 20X4 (Date of

	acquisition) Rs. in '000s	consolidation) Rs. in '000s
Share Capital	5,00,000	5,00,000
<u>Retained Earnings:</u>		
Per accounts of Vinayak Ltd.	7,50,000	7,50,000
<u>Fair Value Adjustments:</u>		
Property (10,00,000 – 8,00,000)*	# 2,00,000	\$ 2,00,000
Extra depreciation due to Buildings appreciation*		\$ (15,000)
((6,00,000 – 4,50,000) x 3/30)	# 1,00,000	\$ 1,00,000
Plant and Equipment (7,00,000 – 6,00,000)*		\$ (75,000)
Extra depreciation due to Plant and Equipment appreciation*	# (30,000)	\$ NIL
(1,00,000 x ¾)	25,000	50,000
Contingent Liability*	(54,000)	
Other Components of Equity		<u>(42,000)</u>
<u>Deferred Tax on Fair Value Adjustments*:</u>		
Date of acquisition (20% x #2,70,000 (from above))	14,91,000	<u>17,68,000</u>
Date of Consolidation (20% x \$2,10,000 (from above))		
Net Assets for Consolidation		
The post-acquisition increase in Net Assets is Rs. 2,77,000 (Rs. 17,68,000 – Rs. 14,91,000). Rs. 25,000 of this increase is due to changes in Other Components of Equity and the remaining Rs. 2,52,000 due to changes in retained earnings		

2. Computation of Goodwill on Consolidation

	Vinayak Ltd. Rs. in '000s
<u>Cost of Investment:</u>	
Shares issued to acquire Vinayak Ltd. (4,00,000 x ½ x Rs. 7)	14,00,000
Non-controlling Interests at the date of acquisition:	<u>2,98,200</u>
Vinayak Ltd. – 20% x Rs. 1,491,000 (from W.N.1)	16,98,200
<u>Net Assets at the date of acquisition:</u>	<u>(14,91,000)</u>
Vinayak Ltd. (W.N.1)	2,07,200

Goodwill before Impairment	<u>(21,600)</u>
Less: Impairment of Goodwill (refer W.N.3)	<u>1,85,600</u>
Goodwill reported in Consolidated Balance Sheet	

3. Impairment of Goodwill on acquisition of Vinayak Ltd.

	Vinayak Ltd. Rs. in '000s
Net Assets of Vinayak Ltd. at 31st March, 20X4 (W.N.1)	17,68,000
Grossed up Goodwill on acquisition (100/80 x Rs. 2,07,200) (Refer Note 1 below)	<u>2,59,000</u>
	<u>20,27,000</u>
Recoverable amount of Vinayak Ltd. as a CGU	<u>(20,00,000)</u>
Therefore, gross impairment will be	27,000
Impairment attributed to Parent (refer Note 2 below)	21,600

Note 1: Grossing up of Goodwill

As per **Para C4 of Appendix C to Ind AS 36 Impairment of Assets** – If an entity measures non-controlling interests at its proportionate interest in the net identifiable assets of a subsidiary at the acquisition date, rather than at fair value, goodwill attributable to non-controlling interests is included in the recoverable amount of the related Cash Generating Unit but is not recognised in the parent's consolidated financial statements. As a consequence, **an entity shall gross up the carrying amount of goodwill allocated to the unit** to include the goodwill attributable to the non-controlling interest. This adjusted carrying amount is then compared with the recoverable amount of the unit to determine whether the cash-generating unit is impaired.

Note 2: Allocation of Impairment of Goodwill

Since the non-controlling interests of Vinayak Ltd. are measured at proportionate share of identifiable net assets of Vinayak Ltd., the goodwill computed is entirely attributable only to the parent of Vinayak Ltd. Accordingly, the impairment also would be attributed entirely to the parent of Vinayak Ltd., and not to the non-controlling interest.

4. Computation of Non-controlling Interest (NCI)

	Vinayak Ltd. Rs. in '000s
NCI at the date of acquisition (W.N.2)	2,98,200
Share of post-acquisition increase in net assets (20% x Rs. 2,77,000 (from W.N.1))	<u>55,400</u>
	<u>3,53,600</u>

5. Computation of consolidated Retained Earnings

	Rs. in '000s
Balance as per accounts of Ishwar Ltd.	28,65,000
<u>Adjustments:</u>	
Acquisition costs	(15,000)

Restoration Provision (W.N.7)	1,960
Share of Vinayak Ltd.'s post-acquisition profits (80% x Rs. 2,52,000 (W.N.1))	2,01,600
Impairment of Goodwill (W.N.3)	<u>(21,600)</u>
	<u>30,31,960</u>

6. Other Components of Equity

	Rs. in '000s
Balance as per accounts of Ishwar Ltd.	12,50,000
Share of Vinayak Ltd.'s post-acquisition balance (80% x Rs. 25,000 (W.N.1))	<u>20,000</u>
	12,70,000

7. Computation of Restoration Provision

	Rs. in '000s
Provision for Restoration originally required (Rs. 1,25,000 x 0.312)	39,000
One year's unwinding of discount (Rs. 39,000 x 6%) A	(2,340)
One year's depreciation of capitalized cost (Rs 39,000 x 1/20) B	(1,950)
Original provision incorrectly made C	6,250
So retained earnings adjustment equals [C -A - B]	1,960

8. Computation of Deferred Tax

	Rs. in '000s
Ishwar Ltd. + Vinayak Ltd.	3,65,000
Fair value adjustments in Vinayak Ltd. (from W.N.1)	<u>42,000</u>
	<u>4,07,000</u>

Question 18 : Nov 2023 – Paper

The extracts of the Balance Sheets of Hammer Ltd. and its subsidiary Sleek Ltd. as on 31st March, 2023 are given below:

Particulars	Note No.	Hammer Ltd. (Rs.)	Sleek Ltd. (Rs.)
I. ASSETS			
A. Non-Current Assets			
Property, Plant and Equipment	1	6,00,000	3,25,000
Intangible Assets	2	1,25,000	75,000
Investments		6,25,000	1,25,000
B. Current Assets			
Inventories		1,25,000	1,60,000
Financial Assets			
Trade receivables		3,25,000	2,90,000

	Cash and Cash equivalents		1,50,000	3,50,000
Total Assets			19,50,000	13,25,000
II.	EQUITY AND LIABILITIES			
A.	Equity			
	Equity Share Capital (Rs. 10 each)		10,00,000	5,00,000
	Other Equity	3	5,50,000	3,75,000
B.	Non- Current Liabilities			
	Financial Liabilities			
	Borrowings	4	-	1,00,000
C.	Current Liabilities			
	Financial Liabilities			
	Short term borrowings			
	Bank Overdraft		1,00,000	50,000
	Trade Payables		3,00,000	3,00,000
Total Equity and Liabilities			19,50,000	13,25,000

Notes to Accounts

Note No	Particulars	Hammer Ltd. (Rs.)	Sleek Ltd. (Rs.)
1	Property, Plant and Equipment		
	(a) Plant and Machinery	2,00,000	1,25,000
	(b) Furniture and Fittings	<u>4,00,000</u>	<u>2,00,000</u>
		<u>6,00,000</u>	3,25,000
2	Intangible Assets		
	Goodwill	1,25,000	75,000
3	Other Equity		
	(a) General Reserve	2,00,000	1,25,000
	(b) Retained Earnings	<u>3,50,000</u>	<u>2,50,000</u>
		<u>5,50,000</u>	<u>3,75,000</u>
4	Borrowings		
	8% Debentures of Rs. 100 each	-	1,00,000

Additional information:

Hammer Ltd. acquired 20,000 equity shares of Sleek Ltd. on 1st April, 2022 at a cost of Rs. 2,40,000 and further acquired 17,500 equity shares on 1st October, 2022 at a cost of Rs. 1,92,500; The 8% debentures of Sleek Ltd. includes debentures held by Hammer Ltd. of nominal value of Rs. 35,000. These were acquired by Hammer Ltd. on 1st January, 2022 at a cost of Rs. 84,000; The retained earnings of Sleek Ltd. had a credit balance of Rs. 75,000 as on 1st April, 2022. On that date the balance of General Reserve was Rs. 50,000;

- Sleek Ltd. had paid dividend @ 10% on its paid-up equity share capital out of the balance of retained earnings as on 1st April, 2022 for the financial year 2021-2022. The entire dividend received by Hammer Ltd. was credited in its statement of profit and loss;
- As per the resolution dated 28th February 2023, Sleek Ltd. had allotted bonus shares @ 1 equity share for every 10 shares held out of its general reserve. The accounting effect has not been given;
- Trade receivables of Hammer Ltd. includes bills receivables of Rs. 2,00,000 drawn upon Sleek Ltd. Out of this, bills of Rs. 50,000 have been discounted with bank;
- During the financial year 2022-2023, Hammer Ltd. purchased goods from Sleek Ltd., of Rs. 25,000 at a sales price of Rs. 30,000, 40% of these goods remained unsold on 31st March, 2023;
- On 1st October, 2022, machinery of Sleek Ltd. was overvalued by 20,000 for which necessary adjustments are to be made. Depreciation is charged @ 10% per annum;
- The parent company i.e., Hammer Ltd. has adopted an accounting policy to measure non-controlling interest at fair value (quoted market price) applying Ind AS 103. Assume the fair value per equity share of Sleek Ltd. at Rs. 11 on the date when control of Sleek Ltd. was acquired by Hammer Ltd.

You are required to prepare a consolidated balance sheet, as per Ind AS, of Hammer Ltd. and its subsidiary Sleek Ltd. as at 31st March, 2023.

Solution :

Consolidated Balance Sheet of Hammer Ltd. as at 31st March, 2023

	Notes No.	Rs. in lakhs
Assets		
Non-current assets		
Property, plant and equipment	1	9,06,000
Intangible assets	1	2,00,000
Financial assets		
Investment	1	2,33,500
Current assets		
Inventories	1	2,83,000
Financial assets		
Trade receivables	1	4,65,000
Cash and cash equivalents	1	5,00,000
Total		25,87,500
Equity and Liabilities		
Equity		
Share capital - Equity shares of Rs. 10 each	2	10,00,000
Other equity	3	7,47,750

Non-controlling interest (W.N.)		1,74,750
Non-current liabilities:		
Financial liabilities		
Borrowings	1	65,000
Current Liabilities:		
Financial liabilities		
Bank Overdraft	1	1,50,000
Trade payables	1	4,50,000
Total		25,87,500

Notes to Accounts

Note 1: Assets and Liabilities

Particulars	Hammer Ltd.	Sleek Ltd.	Adjustments	Total
Property, Plant and Equipment	6,00,000	3,25,000	-20,000 + 1,000	9,06,000
Intangible Assets	1,25,000	75,000		2,00,000
Investments	1,92,500*	1,25,000	-84,000	2,33,500
Inventories	1,25,000	1,60,000	-2,000	2,83,000
Trade Receivables	3,25,000	2,90,000	-1,50,000	4,65,000
Cash and Cash Equivalents	1,50,000	3,50,000		5,00,000
Borrowings	0	1,00,000	-35,000	65,000
Bank Overdraft	1,00,000	50,000		1,50,000
Trade Payables	3,00,000	3,00,000	-1,50,000	4,50,000

*6,25,000 – 2,40,000-1,92,500

Note 2: Equity Share Capital

1,00,000 equity shares of Rs. 10 each, fully paid	<u>10,00,000</u>
	<u>10,00,000</u>

Note 3: Consolidated Other Equity

General Reserve	W.N.1	2,28,125
Retained Earnings	W.N.1	3,64,625
Capital Reserve	W.N.2	<u>1,55,000</u>
		<u>7,47,750</u>

Working Notes:

1. Consolidated Other Equity

Particulars	General Reserve	Retained Earnings
Standalone - Hammer Ltd.	2,00,000	3,50,000
Less: Fair Value Loss of existing stake [2,40,000 - (20,000 x 11)]		(20,000)

Less: Loss on cancellation of debentures		(49,000)
Add: Share in Post-acquisition Profits	<u>28,125</u>	<u>83,625</u>
	<u>2,28,125</u>	<u>3,64,625</u>

2. Computation of Goodwill or Bargain Purchase for (75% stake)

(i) Computation of net worth (net identifiable assets) as on 1st October, 2022

Share Capital	5,00,000
Pre-acquisition Retained Earnings (after adjusting downward revaluation of machinery)	1,17,500
Pre-acquisition General Reserve	37,500
Bonus issue*	<u>50,000</u>
Net Identifiable assets	<u>7,05,000</u>

***Note :** Bonus shares issued in 1:10 ratio i.e. Rs. 50,000 and bonus issue has not been accounted for yet. The opening balance of the general reserve is Rs. 50,000 while the closing balance is Rs. 1,25,000 which implies that Rs. 75,000 have been transferred during the year and this amount should be allocated between pre and post-acquisition based on time proportion. Therefore, the general reserve on the date of acquisition will be Rs. 50,000 + 50% of Rs. 75,000 i.e. Rs. 37,500 = Rs. 87,500. Here, it should be noted that the date of bonus issue is 28th February, 2023 and bonus amount is Rs. 50,000. Since the balance of post-acquisition general reserve (50% of Rs. 75,000 i.e. Rs. 37,500) is insufficient, it is assumed that bonus shares are issued from pre-acquisition general reserve i.e. balance on the date of acquisition assuming that transfer to general reserve, in general, is an appropriation of profit which is done at the end of the year. This implies that outstanding balance in general reserve at the time of bonus issue is the opening balance.

However, one may assume otherwise like insufficient post-acquisition balance of Rs. 12,500 (50,000 – 37,500) has only been adjusted through pre-acquisition share of Rs. 87,500 or first adjustment of bonus issue has been done and later bifurcation of remaining balance has been done into pre and post-acquisition. In such a case balance of consolidated general reserve (post-acquisition), net worth, bargain purchase and NCI will undergo a change.

(ii) Computation of bargain purchase i.e capital reserve

Net worth or Net identifiable assets		7,05,000
Purchase consideration (1,92,500 + 2,20,000)	4,12,500	
NCI [12,500 shares x Rs. 11 (i.e. Rs.1,92,500 / 17,500 shares)]	<u>1,37,500</u>	<u>5,50,000</u>
Bargain purchase (capital reserve)		<u>1,55,000</u>

3. Non-Controlling Interest A/c (at Fair Value)

NCI at fair value as on 1st October, 2023	1,37,500
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Post-acquisition General Reserve	9,375
Post-acquisition Retained Earnings	<u>27,875</u>
NCI at fair value as on 31st March, 2023	<u>1,74,750</u>

4. Analysis of Other Equity

(i) General Reserve

Closing balance as on 31st March, 2023		1,25,000
Less: Opening Balance	Pre	<u>(50,000)</u>
Net Profit transferred during the year		<u>75,000</u>
For 6 months till 30th September, 2022	Pre	37,500
For 6 months from 1st October, 2022 to 31st March, 2023	Post	<u>37,500</u>
Total pre-acquisition reserve (50,000 + 37,500)	Pre	87,500
Less: Bonus issue	Pre	<u>(50,000)</u>
Balance General Reserve	Pre	<u>37,500</u>
Share of Hammer Ltd. in pre-acquisition reserve (75%)	Pre	28,125
Share of NCI in pre-acquisition reserve (25%)	Pre	9,375
Share of Hammer Ltd. in post-acquisition reserve (75%)	Post	28,125
Share of NCI in post-acquisition reserve (25%)	Post	9,375

(ii) Retained Earnings (RE)

Closing balance as on 31st March, 2023		2,50,000
Less: Opening balance	75,000	
Less: Dividend @10%	<u>(50,000)</u>	Pre
		<u>(25,000)</u>
During the year		<u>2,25,000</u>
For 6 months till 30th September, 2022		
	Pre	<u>1,12,500</u>
For 6 months from 1st October 2022 to 31st March, 2023		
	Post	1,12,500
Add: Saving in Depreciation (W.N.5)		1,000
Less: Unrealised Gain [(30,000-25,000) x 40%]		<u>(2,000)</u>
Net post-acquisition RE	Post	<u>1,11,500</u>
Total pre-acquisition RE (25,000 + 1,12,500)	Pre	1,37,500
Less: Downward revaluation of machinery		<u>(20,000)</u>
	Pre	<u>1,17,500</u>
Share of Hammer Ltd. in pre-acquisition RE (75%)	Pre	88,125
Share of NCI in pre-acquisition RE (25%)	Pre	29,375
Share of Hammer Ltd. in post-acquisition RE (75%)	Post	83,625
Share of NCI in post-acquisition RE (25%)	Post	27,875

5. Plant and Machinery balance as on 31st March 2023

	Rs.
Balance as on 31.3.2023 as given in question (after depreciation)	1,25,000
Less: Downward revaluation less depreciation saving	<u>(19,000)*</u>
	<u>1,06,000</u>

Question 19 : May 2024 – RTP

At the beginning of its current financial year, AB Limited holds 90% equity interest in BC Limited. During the financial year, AB Limited sells 70% of its equity interest in BC Limited to PQR Limited for a total consideration of Rs. 56 crore and consequently loses control of BC Limited.

At the date of disposal, fair value of the 20% interest retained by AB Limited is Rs. 16 crore and the net assets of BC Limited are fair valued at Rs. 60 crore.

These net assets include the following:

- Debt investments classified as fair value through other comprehensive income (FVOCI) of Rs. 12 crore and related FVOCI reserve of Rs. 6 crore.
- Net defined benefit liability of Rs. 6 crore that has resulted in a reserve relating to net measurement losses of Rs. 3 crore.
- Equity investments (considered not held for trading) of Rs. 10 crore for which irrevocable option of recognising the changes in fair value in FVOCI has been availed and related FVOCI reserve of Rs. 4 crore.
- Net assets of a foreign operation of Rs. 20 crore and related foreign currency translation reserve of Rs. 8 crore.

In consolidated financial statements of AB Limited, 90% of the above reserves were included in equivalent equity reserve balances, with the 10% attributable to the non-controlling interest included as part of the carrying amount of the non-controlling interest.

What would be the accounting treatment on loss of control in the consolidated financial statements of AB Limited?

Solution :

Paragraph 25 of Ind AS 110 states that, "if a parent loses control of a subsidiary, the parent:

- derecognises** the assets and liabilities of the former subsidiary from the consolidated balance sheet.
- recognises** any investment retained in the former subsidiary at its fair value when control is lost and subsequently accounts for it and for any amounts owed by or to the former subsidiary in accordance with relevant Ind AS. That fair value shall be regarded as the fair value on initial recognition of a financial asset in accordance with Ind AS 109 or, when appropriate, the cost on initial recognition of an investment in an associate or joint venture.
- recognises** the gain or loss associated with the loss of control attributable to the former controlling interest."

Paragraph B98(c) of Ind AS 110 states that, on loss of control over a subsidiary, a parent shall reclassify to profit or loss, or transfer directly to retained earnings if required by other Ind AS, the

amounts recognised in other comprehensive income in relation to the subsidiary on the basis specified in paragraph B99.

As per paragraph B99, if a parent loses control of a subsidiary, the parent shall account for all amounts previously recognised in other comprehensive income in relation to that subsidiary on the same basis as would be required if the parent had directly disposed of the related assets or liabilities. Therefore, if a gain or loss previously recognised in other comprehensive income would be reclassified to profit or loss on the disposal of the related assets or liabilities, the parent shall reclassify the gain or loss from equity to profit or loss (as a reclassification adjustment) when it loses control of the subsidiary. If a revaluation surplus previously recognised in other comprehensive income would be transferred directly to retained earnings on the disposal of the asset, the parent shall transfer the revaluation surplus directly to retained earnings when it loses control of the subsidiary.

In view of the basis in its consolidated financial statements, AB Limited shall:

- (a) re-classify the FVOCI reserve in respect of the debt investments of Rs. 5.4 crore (90% of Rs. 6 crore) attributable to the owners of the parent to the statement of profit or loss in accordance with paragraph B5.7.1A of Ind AS 109, Financial Instruments which requires that the cumulative gains or losses previously recognised in OCI shall be recycled to profit and loss upon derecognition of the related financial asset. This is reflected in the gain on disposal. Remaining 10% (i.e., Rs. 0.6 crore) relating to non-controlling interest (NCI) is included as part of the carrying amount of the non-controlling interest that is derecognised in calculating the gain or loss on loss of control of the subsidiary.
- (b) transfer the reserve relating to the net measurement losses on the defined benefit liability of Rs. 2.7 crore (90% of Rs. 3 crore) attributable to the owners of the parent within equity to retained earnings. It is not reclassified to profit or loss. The remaining 10% (i.e., Rs. 0.3 crore) attributable to the NCI is included as part of the carrying amount of NCI that is derecognised in calculating the gain or loss on loss of control over the subsidiary. No amount is reclassified to profit or loss, nor is it transferred within equity, in respect of the 10% attributable to the non-controlling interest.
- (c) reclassify the cumulative gain on fair valuation of equity investment of Rs. 3.6 crore (90% of Rs. 4 crore) attributable to the owners of the same parent from OCI to retained earnings under equity as per paragraph B5.7.1 of Ind AS 109, Financial Instruments, which provides that in case an entity has made an irrevocable election to recognise the changes in the fair value of an investment in an equity instrument not held for trading in OCI, it may subsequently transfer the cumulative amount of gains or loss within equity. The remaining 10% (i.e., Rs. 0.4 crore) related to the NCI are derecognised along with the balance of NCI and not reclassified to profit and loss.
- (d) reclassify the foreign currency translation reserve of Rs. 7.2 crore (90% × Rs. 8 crore) attributable to the owners of the parent to statement of profit or loss as per paragraph 48 of Ind AS 21 'The Effects of Changes in Foreign Exchange Rates', which specifies that the cumulative amount of exchange differences relating to the foreign operation, recognised in OCI, shall be reclassified from equity to profit or loss on the disposal of foreign operation. This is reflected in the gain on disposal. Remaining 10% (i.e., Rs. 0.8 crore) relating to the NCI is included as part of the carrying amount of the NCI that is derecognised in calculating

the gain or loss on the loss of control of subsidiary, but is not reclassified to profit or loss in pursuance of paragraph 48B of Ind AS 21, which provides that the cumulative exchange differences relating to that foreign operation attributed to NCI shall be derecognised on disposal of the foreign operation, but shall not be reclassified to profit or loss.

The impact of loss of control over BC Limited on the consolidated financial statements of AB Limited is summarised below:

(Rs. in crore)

Particular	Amount (Dr)	Amount (Cr)	P&L Impact	RE Impact
Gain / Loss on Disposal on Investments				
Bank	56			
Non-controlling interest (Derecognised)	6			
Investment at FV (20% Retained)	16			
Gain on Disposal (P&L) balancing figure		18	18	
De-recognition of total net assets of subsidiary	60			
Reclassification of FVTOCI reserve on debt instruments to profit or loss				
FVTOCI reserve on debt instruments (6 cr. x 90%) To Profit and loss	5.4	5.4	5.4	
Reclassification of net measurement loss reserve to profit or loss				
Reserve and Surplus To Net measurement loss reserve (FVTOCI) [(3 cr. x 90%)]	2.7	2.7		-2.7
Reclassification of FVTOCI reserve on equity instruments to retained earnings				
FVTOCI reserve on equity instruments (4 cr. x 90%) To Reserve and Surplus	3.6	3.6	3.6	
Foreign currency translation reserve reclassified to profit or loss				
Foreign currency translation reserve (FVOCI) [8 cr. x 90%] To Profit and loss	7.2	7.2	7.2	-
Total			30.6	0.9

Question 20 : May 2024 – Paper

The Accountant Mr. Ramesh Kanna of ‘H’ Limited submitted to you the following Standalone Balance Sheet extracts as at 31st March 2024:

Amount in Rs.

	H Ltd.	S Ltd.	A Ltd.
Assets			

Non-current assets						
(a) Property, Plant and Equipment	5,50,000		4,80,000		2,50,000	
(b) Financial Assets Investments:				4,80,000		2,50,000
14,000 shares in S Ltd.	5,60,000					
4,000 shares in A Ltd.	<u>1,00,000</u>	12,10,000				
Current assets						
(a) Inventory	4,85,000		3,82,500		2,45,500	
(b) Financial Assets						
Cash and cash equivalents	89,000		98,000		1,77,000	
Trade receivables	<u>3,95,000</u>	<u>9,69,000</u>	<u>3,05,000</u>	<u>7,85,500</u>	<u>1,78,500</u>	<u>6,01,000</u>
Total Assets		21,79,000		12,65,500		8,51,000
Equity & Liabilities						
Shareholder's Equity						
(a) Equity Share Capital (Rs. 10 per share)	5,00,000		2,00,000		1,00,000	
(b) Other Equity	<u>9,00,000</u>	14,00,000	<u>7,50,000</u>	9,50,000	<u>4,24,000</u>	5,24,000
Retained earnings						
Non-current liabilities						
(a) Financial Liabilities						
Borrowing–Term Loans		4,00,000		1,50,000		1,00,000
Current liabilities						
(a) Financial Liabilities						
Trade payables		3,79,000		1,65,500		2,27,000
Total Equity and Liabilities		21,79,000		12,65,500		8,51,000

The following additional information is made available in respect of these companies:

- (i) H Limited purchased the shares in S Limited on 31st October 2023 when retained earnings of S Limited was Rs. 500,000 and the shares in A Limited were acquired on 30th June 2023 when its retained earnings stood at Rs. 1,75,000.
- (ii) Inventory of A Limited as on 31st March, 2024 include inventory valued at Rs. 60,000 which had been purchased from H Limited, on 1st January, 2024 at cost plus 20%.
- (iii) Trade payable of H Limited includes Rs. 25,000 payable to A Limited, the amount receivable being recorded in the receivables of A Limited.
- (iv) Goodwill in respect of the acquisition of S Limited has been fully impaired. The recoverable amount of the investment in A Limited exceeds its' carrying value at 31st March 2024. Non-controlling interest is valued at the proportionate share of the identifiable net assets.
- (v) 10% dividends were declared by both H Limited and S Limited whereas A Limited declared 15% dividend for the year 2023-24.
- (vi) On 31st March, 2024, S Limited made a bonus issue of one equity share for every two shares held by the shareholders of S Limited.
- (vii) Dividends were declared but were not accounted for by all these companies in the books before the year end. Similarly, the bonus issued by S Limited was not reflected in the balance sheet as on 31st March, 2024.

You are required to take note of the above available information and draw the consolidated Balance Sheet of H Limited as at 31st March 2024. Notes to accounts are not required.

Solution :

Note: Since adjustments (v) and (vii) of the question state that dividend has been declared by all the entities but no information is provided whether it has been paid or due. In this regard, it may be noted that since dividend is paid for the entire year 2023-2024, it is assumed as final dividend which is approved in the Annual General Meeting conducted at later point time from the reporting date.

Accordingly, following assumptions are possible based on which alternative solutions have been provided:

- A. Ignored the adjustment for dividend completely as dividend has to be approved in the Annual General Meeting.
- B. Considered dividend as declared but not paid.
- C. Considered dividend as declared and paid.

Alternative A: Ignored the adjustment for dividend completely as it has to be approved in the AGM.

**Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd.
and Associate A Ltd. as at 31st March, 2024**

	Rs.
Assets	
Non-current assets	
Property, plant and equipment (Rs. 5,50,000 + Rs. 4,80,000)	10,30,000
Goodwill (Rs. 70,000- Impaired Rs. 70,000)	Nil
Financial assets	
Investment in A Ltd. (W.N.1 (iii))	2,05,600
Current assets	
Inventory (Rs. 4,85,000+ Rs. 3,82,500)	8,67,500
Financial assets	
Cash and cash equivalents (Rs. 89,000 + Rs. 98,000)	1,87,000
Trade receivables (Rs. 3,95,000+Rs. 3,05,000)	<u>7,00,000</u>
Total	<u>29,90,100</u>
Equity and Liabilities	
Equity	
Share capital - Equity shares of Rs. 10 each	5,00,000
Other equity (W.N.4+ W.N.1(i))	11,10,600
Non-controlling interest (W.N.3)	2,85,000
Non-current liabilities	
Financial liabilities	
Borrowings-term loans (Rs. 4,00,000 + Rs. 1,50,000)	5,50,000
Current Liabilities	
Financial liabilities	
Trade payables (Rs.3,79,000+Rs. 1,65,500)	<u>5,44,500</u>
Total	<u>29,90,100</u>

Working Notes:

1. Computation of Investment in Associate A Ltd. as per Equity method

(i) Capital reserve on the date of acquisition

The cost of the investment is lower than the net fair value of the investee's identifiable assets and liabilities. Hence there is capital reserve calculated as follows:

	Rs.
Cost of acquisition of investment	1,00,000
H Ltd.'s share in fair value of net assets of A Ltd. on the date of acquisition $[(1,00,000 + 1,75,000) \times 40\%]$	<u>(1,10,000)</u>
Capital Reserve	<u>10,000</u>

Capital reserve is recorded directly in equity.

(ii) Share in profit of A Ltd.

	Rs.
Share in post-acquisition profit of A Ltd. $[(4,24,000 - 1,75,000) \times 40\%]$	99,600

(iii) Closing balance of investment of Associate A Ltd. at the end of the year

	Rs.
Cost of acquisition of investment	1,00,000
Add: Capital reserve	10,000
Share in post-acquisition profit	99,600
Less: Unrealised gain on inventory $[(60,000 \times 20/120) \times 40\%]$	<u>(4,000)</u>
Closing balance of investment	<u>2,05,600</u>

2. Analysis of Retained Earnings of S Ltd.

(i) Retained Earnings (RE) of S Ltd.

	Rs.
Closing balance as on 31st March, 2024	7,50,000
Less: Pre-acquisition as on 31st October, 2023	<u>(5,00,000)</u>
Post-acquisition Profit	<u>2,50,000</u>

(ii) Computation of net worth (net identifiable assets) as on 31st October, 2023

	Rs.
Share Capital of S Ltd.	2,00,000
Pre-acquisition Retained Earnings	<u>5,00,000</u>
Net Identifiable assets	<u>7,00,000</u>

(iii) Computation of Goodwill on acquisition date of S Ltd.

		Rs.
Purchase consideration	5,60,000	
NCI as per proportionate share method $(7,00,000 \times 30\%)$	<u>2,10,000</u>	7,70,000

Less: Net worth or Net Identifiable Assets	(7,00,000)
Goodwill	<u>70,000</u>

3. Non-Controlling Interest as on 31st March, 2024

	Rs.
NCI (by proportionate share method) as on 31st October, 2023	2,10,000
Post-acquisition Retained Earnings (W.N.4)	<u>75,000</u>
NCI as on 31st March, 2024	<u>2,85,000</u>

4. Consolidated Retained Earnings

Particulars	H Ltd Rs.	S Ltd Rs.
Opening Balance of Retained Earnings	9,00,000	
Post-acquisition Retained Earnings (W.N.2(i))		2,50,000
Less: Unrealised gain on downstream transaction with Associate A Ltd.	(4,000)	
Less: Impairment of Goodwill on acquisition of S Ltd.	(70,000)	
Add: Share of profit and loss in Associate A Ltd.	99,600	
Less: Share of NCI in post-acquisition Retained Earnings [2,50,000 x 30%]		<u>(75,000)</u>
	<u>9,25,600</u>	<u>1,75,000</u>
Total Consolidated Retained Earnings		<u>11,00,600</u>

Note: Bonus issue by a subsidiary is a transaction with owner in their capacity as owner. Therefore, bonus issue is only a transfer from one component of equity to the other thereby not changing the equity. Accordingly, though bonus issue shall be accounted in the individual financial statements of subsidiary, the same shall not have any effect in consolidated financial statements of the Group.

Alternative B: Considered dividend as declared but not paid

Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. and Associate A Ltd. as at 31st March, 2024

	Rs.
Assets	
Non-current assets	
Property, plant and equipment (Rs. 5,50,000 + Rs. 4,80,000)	10,30,000
Goodwill (Rs. 70,000- Impaired Rs. 70,000)	Nil
Financial assets	
Investment in A Ltd. (Refer W.N.1 (iii))	1,99,600
Current assets	

Inventory (Rs. 4,85,000 + Rs. 3,82,500)	8,67,500
Financial assets	
Cash and cash equivalents (Rs. 89,000+ Rs. 98,000)	1,87,000
Trade receivables (Rs. 3,95,000+Rs. 3,05,000)	7,00,000
Other Receivables	
(Dividend receivable from A Ltd. (Rs. 15,000 x 40%))	6,000
Total	29,90,100
Equity and Liabilities	
Equity	
Share capital - Equity shares of Rs. 10 each	5,00,000
Other equity (W.N.4+W.N.1(i))	10,60,600
Non-controlling interest (W.N.3)	2,79,000
Non-current liabilities	
Financial liabilities	
Borrowings- term loans (Rs. 4,00,000 + Rs. 1,50,000)	5,50,000
Current Liabilities	
Financial liabilities	
Trade payables (Rs. 3,79,000+Rs. 1,65,500)	5,44,500
Other payables	56,000
[Dividend payable to NCI by S Ltd. (Rs. 20,000 x 30%) Rs. 6,000+ Dividend payable by H Ltd. to its shareholders Rs. 50,000]	
Total	29,90,100

Working Notes:

1. Computation of Investment in Associate A Ltd. as per Equity method

(i) Capital reserve on the date of acquisition

The cost of the investment is lower than the net fair value of the investee's identifiable assets and liabilities. Hence there is capital reserve calculated as follows:

	Rs.
Cost of acquisition of investment	1,00,000
Less : H Ltd.'s share in fair value of net assets of A Ltd. on the date of acquisition [(1,00,000 + 1,75,000) x 40%]	<u>(1,10,000)</u>
Capital Reserve	<u>10,000</u>

Capital reserve is recorded directly in equity.

(ii) Share in profit of A Ltd.

	Rs.
Share in post-acquisition profit of A Ltd. [(4,24,000 - 1,75,000) x 40%]	99,600
Less: Dividend (1,00,000 x 15% x 40%)	<u>(6,000)</u>

Share in profit of A Ltd.	<u>93,600</u>
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(iii) **Closing balance of investment of Associate A Ltd. at the end of the year**

	Rs.
Cost of acquisition of investment	1,00,000
Add: Capital reserve	10,000
Share in post-acquisition profit	93,600
Less: Unrealised gain on inventory [(60,000 x 20/120) x 40%]	<u>(4,000)</u>
Closing balance of investment	<u>1,99,600</u>

2. **Analysis of Retained Earnings of S Ltd.**

(i) **Retained Earnings (RE) of S Ltd.**

	Rs.
Closing balance as on 31st March, 2024	7,50,000
Less: Pre-acquisition as on 31st October, 2023	<u>(5,00,000)</u>
Post-acquisition Profit	<u>2,50,000</u>

(ii) **Computation of net worth (net identifiable assets) as on 31st October, 2023**

	Rs.
Share Capital of S Ltd.	2,00,000
Add : Pre-acquisition Retained Earnings	<u>5,00,000</u>
Net Identifiable assets	<u>7,00,000</u>

(iii) **Computation of Goodwill on acquisition date of S Ltd.**

		Rs.
Purchase consideration	5,60,000	
NCI as per proportionate share method (7,00,000 x 30%)	<u>2,10,000</u>	7,70,000
Less: Net worth or Net Identifiable Assets		<u>(7,00,000)</u>
Goodwill		<u>70,000</u>

3. **Non-Controlling Interest as on 31st March, 2024**

	Rs.
NCI (by proportionate share method) as on 31st October, 2023	2,10,000
Post-acquisition Retained Earnings (W.N.4)	<u>69,000</u>
NCI as on 31st March, 2024	<u>2,79,000</u>

4. **Consolidated Retained Earnings**

Particulars	H Ltd Rs.	S Ltd Rs.
Opening Balance of Retained Earnings	9,00,000	

Post-acquisition Retained Earnings (W.N.2(i))		2,50,000
Less: Unrealised gain on downstream transaction with Associate A Ltd.	(4,000)	
Less: Impairment of Goodwill on acquisition of S Ltd.	(70,000)	
Add: Share of profit and loss in Associate A Ltd.	93,600	
Less: Dividend payable by H Ltd.	(50,000)	(20,000)
Add: Dividend Income receivable from S Ltd.	14,000	
Add: Dividend income receivable from A Ltd.	6,000	
Less: Share of NCI in post-acquisition Retained Earnings [(2,50,000 – 20,000) x 30%]		<u>(69,000)</u>
	<u>8,89,600</u>	<u>1,61,000</u>
Total Consolidated Retained Earnings		<u>10,50,600</u>

Note: Bonus issue by a subsidiary is a transaction with owner in their capacity as owner. Therefore, bonus issue is only a transfer from one component of equity to the other thereby not changing the equity. Accordingly, though bonus issue shall be accounted in the individual financial statements of subsidiary, the same shall not have any effect in consolidated financial statements of the Group.

Alternative C: Considered dividend as declared and paid
Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. and Associate A Ltd. as at 31st March, 2024

	Rs.
Assets	
Non-current assets	
Property, plant and equipment (Rs. 5,50,000 + Rs. 4,80,000)	10,30,000
Goodwill (Rs. 70,000- Impaired Rs. 70,000)	Nil
Financial assets	
Investment in A Ltd. (Refer W.N.1 (iii))	1,99,600
Current assets	
Inventory (Rs. 4,85,000+ Rs. 3,82,500)	8,67,500
Financial assets	
Cash and cash equivalents [(Rs. 89,000 - Rs. 50,000 + Rs. 14,000 + Rs. 6,000) + (Rs. 98,000 - Rs. 20,000)]	1,37,000
Trade receivables (Rs. 3,95,000+Rs. 3,05,000)	<u>7,00,000</u>
Total	<u>29,34,100</u>
Equity and Liabilities	
Equity	
Share capital - Equity shares of Rs. 10 each	5,00,000
Other equity (W.N.4+W.N.1(i))	10,60,600
Non-controlling interest (W.N.3)	2,79,000

Non-current liabilities	
Financial liabilities	
Borrowings- term loans (Rs. 4,00,000 + Rs. 1,50,000)	5,50,000
Current Liabilities	
Financial liabilities	
Trade payables (Rs. 3,79,000+Rs. 1,65,500)	<u>5,44,500</u>
Total	<u>29,34,100</u>

Working Notes:

1. Computation of Investment in Associate A Ltd. as per Equity method

(i) Capital reserve on the date of acquisition

The cost of the investment is lower than the net fair value of the investee's identifiable assets and liabilities. Hence there is capital reserve calculated as follows:

	Rs.
Cost of acquisition of investment	1,00,000
Less : H Ltd.'s share in fair value of net assets of A Ltd. on the date of acquisition [(1,00,000 + 1,75,000) x 40%]	<u>(1,10,000)</u>
Capital Reserve	<u>10,000</u>

Capital reserve is recorded directly in equity.

(ii) Share in profit of A Ltd.

	Rs.
Share in post-acquisition profit of A Ltd. [(4,24,000 - 1,75,000) x 40%]	99,600
Less: Dividend (1,00,000 x 15% x 40%)	<u>(6,000)</u>
Share in profit of A Ltd.	<u>93,600</u>

(iii) Closing balance of investment of Associate A Ltd. at the end of the year

	Rs.
Cost of acquisition of investment	1,00,000
Add: Capital reserve	10,000
Share in post-acquisition profit	93,600
Less: Unrealised gain on inventory [(60,000 x 20/120) x 40%]	<u>(4,000)</u>
Closing balance of investment	<u>1,99,600</u>

2. Analysis of Retained Earnings of S Ltd.

(i) Retained Earnings (RE) of S Ltd.

	Rs.
Closing balance as on 31st March, 2024	7,50,000
Less: Pre-acquisition as on 31st October, 2023	<u>(5,00,000)</u>
Post-acquisition Profit	<u>2,50,000</u>

(ii) **Computation of net worth (net identifiable assets) as on 31st October, 2023**

	Rs.
Share Capital of S Ltd.	2,00,000
Add : Pre-acquisition Retained Earnings	<u>5,00,000</u>
Net Identifiable assets	<u>7,00,000</u>

(iii) **Computation of Goodwill on acquisition date of S Ltd.**

		Rs.
Purchase consideration	5,60,000	
NCI as per proportionate share method (7,00,000 x 30%)	<u>2,10,000</u>	7,70,000
Less: Net worth or Net Identifiable Assets		<u>(7,00,000)</u>
Goodwill		<u>70,000</u>

3. **Non-Controlling Interest as on 31st March, 2024**

	Rs.
NCI (by proportionate share method) as on 31st October, 2023	2,10,000
Post-acquisition Retained Earnings (W.N.4)	<u>69,000</u>
NCI as on 31st March, 2024	<u>2,79,000</u>

4. **Consolidated Retained Earnings**

Particulars	H Ltd Rs.	S Ltd Rs.
Opening Balance of Retained Earnings	9,00,000	
Post-acquisition Retained Earnings (W.N.2(i))		2,50,000
Less: Unrealised gain on downstream transaction with Associate A Ltd.	(4,000)	
Less: Impairment of Goodwill on acquisition of S Ltd.	(70,000)	
Add: Share of profit and loss in Associate A Ltd.	93,600	
Less: Dividend payable by H Ltd.	(50,000)	(20,000)
Add: Dividend Income receivable from S Ltd.	14,000	
Add: Dividend income receivable from A Ltd.	6,000	
Less: Share of NCI in post-acquisition Retained Earnings [(2,50,000 – 20,000) x 30%]		<u>(69,000)</u>
	<u>8,89,600</u>	<u>1,61,000</u>
Total Consolidated Retained Earnings		<u>10,50,600</u>

Note: Bonus issue by a subsidiary is a transaction with owner in their capacity as owner. Therefore, bonus issue is only a transfer from one component of equity to the other thereby not changing the equity. Accordingly, though bonus issue shall be accounted in the individual financial

statements of subsidiary, the same shall not have any effect in consolidated financial statements of the Group.

Question 21 : Nov 2024 – RTP

On 1st April 20X1, A Limited acquired 80% of the share capital of S Limited. On the acquisition date the share capital and reserves of S Ltd. stood at Rs. 5,00,000 and Rs. 1,25,000 respectively. A Limited paid initial cash consideration of Rs. 10,00,000. Additionally, A Limited issued 2,00,000 equity shares with a nominal value of Rs. 1 per share at current market value of Rs. 1.80 per share. It was also agreed that A Limited would pay a further sum of Rs. 5,00,000 after three years. A Limited's cost of capital is 10%. The appropriate discount factor for Rs. 1 @ 10% receivable at the end of

1st year: 0.91

2nd year: 0.83

3rd year: 0.75

The shares and deferred consideration have not yet been recorded by A limited.

Below are the Balance Sheet of A Limited and S Limited as at 31st March, 20X3:

	A Limited (Rs. 000)	S Limited (Rs. 000)
Non-current assets:		
Property, plant & equipment	5,500	1,500
Investment in S Limited at cost	1,000	
Current assets:		
Inventory	550	100
Receivables	400	200
Cash	<u>200</u>	<u>50</u>
	<u>7,650</u>	<u>1,850</u>
Equity:		
Share capital	2,000	500
Retained earnings	<u>1,400</u>	<u>300</u>
	3,400	800
Non-current liabilities	3,000	400
Current liabilities	<u>1,250</u>	<u>650</u>
	<u>7,650</u>	<u>1,850</u>

Further information:

- (i) On the date of acquisition, the fair values of S Limited's plant exceeded its book value by Rs. 2,00,000. The plant had a remaining useful life of five years at this date;
- (ii) The consolidated goodwill has been impaired by Rs. 2,58,000; and
- (iii) The A Limited Group, values the non-controlling interest using the fair value method. At the date of acquisition, the fair value of the 20% non-controlling interest was Rs. 3,80,000.

You are required to prepare Consolidated Balance Sheet of A Limited as at 31st March, 20X3. (Notes to Account on Consolidated Balance Sheet is not required).

Solution :

**Consolidated Balance Sheet of A Ltd. and its subsidiary, S Ltd.
as at 31st March, 20X3**

Particulars	Rs. in 000s
I. Assets	
(1) Non-current assets	
(i) Property Plant & Equipment (W.N.4)	7,120.00
(ii) Intangible asset – Goodwill (W.N.3)	1,032.00
(2) Current Assets	
(i) Inventories (550 + 100)	650.00
(ii) Financial Assets	
(a) Trade Receivables (400 + 200)	600.00
(b) Cash & Cash equivalents (200 + 50)	250.00
Total Assets	9,652.00
II. Equity and Liabilities	
(1) Equity	
(i) Equity Share Capital (2,000 + 200)	2,200.00
(ii) Other Equity	
(a) Retained Earnings (W.N.6)	1190.85
(b) Securities Premium	160.00
(2) Non-Controlling Interest (W.N.5)	347.40
(3) Non-Current Liabilities (3,000 + 400)	3,400.00
(4) Current Liabilities (W.N.8)	2,353.75
Total Equity & Liabilities	9,652.00

Notes:

- Since the question required not to prepare Notes to Account, the column of Note to Accounts had not been drawn.
- It is assumed that shares were issued during the year 20X2-20X3 and entries are yet to be made.

Working Notes:**1. Calculation of purchase consideration at the acquisition date i.e. 1st April, 20X1**

	Rs. in 000s
Payment made by A Ltd. to S Ltd.	
Cash	1,000.00
Equity shares (2,00,000 shares x Rs.1.80)	360.00
Present value of deferred consideration (Rs.5,00,000 x 0.75)	<u>375.00</u>
Total consideration	<u>1735.00</u>

2. Calculation of net assets i.e. net worth at the acquisition date i.e. 1st April, 20X1

	Rs. in 000s
Share capital of S Ltd.	500.00
Reserves of S Ltd.	125.00
Fair value increase on Property, Plant and Equipment	<u>200.00</u>
Net worth on acquisition date	<u>825.00</u>

3. Calculation of Goodwill at the acquisition date i.e. 1st April, 20X1 and 31st March, 20X3

	Rs.in 000s
Purchase consideration (W.N.1)	1,735.00
Non-controlling interest at fair value (as given in the question)	<u>380.00</u>
	2,115.00
Less: Net worth (W.N.2)	<u>(825.00)</u>
Goodwill as on 1st April 20X1	1,290.00
Less: Impairment (as given in the question)	<u>(258.00)</u>
Goodwill as on 31st March 20X3	<u>1,032.00</u>

4. Calculation of Property, Plant and Equipment as on 31st March 20X3

		Rs.in 000s
A Ltd.		5,500.00
S Ltd.	1,500.00	
Add: Net fair value gain not recorded yet	200.00	
Less: Depreciation $[(200/5) \times 2]$	<u>(80.00)</u>	<u>1,620.00</u>
		<u>7,120.00</u>

5. Calculation of post-acquisition gain (after adjustment of impairment on goodwill) and value of NCI as on 31st March 20X3

		Rs. in 000s NCI (20%)	Rs. in 000s A Ltd. (80%)
Acquisition date balance		380.00	Nil
Closing balance of Retained Earnings	300.00		
Less: Pre-acquisition balance	<u>(125.00)</u>		
Post-acquisition gain	175.00		
Less: Additional Depreciation on PPE $[(200/5) \times 2]$	<u>(80.00)</u>		
Share in post-acquisition gain	<u>95.00</u>	19.00	76.00
Less: Impairment on goodwill	258.00	<u>(51.60)</u>	<u>(206.40)</u>
		<u>347.40</u>	<u>(130.40)</u>

6. Consolidated Retained Earnings as on 31st March 20X3

	Rs.in 000s
A Ltd.	1,400.00
Add: Share of post-acquisition loss of S Ltd. (W.N.5)	(130.40)
Less: Finance cost on deferred consideration (37.5 + 41.25) (W.N.7)	<u>(78.75)</u>
Retained Earnings as on 31st March 20X3	<u>1,190.85</u>

7. Calculation of value of deferred consideration as on 31st March 20X3

	Rs.in 000s
Value of deferred consideration as on 1st April 20X1 (W.N.1)	375.00
Add: Finance cost for the year 20X1-20X2 (375 x 10%)	<u>37.50</u>
	412.50
Add: Finance cost for the year 20X2-20X3 (412.50 x 10%)	<u>41.25</u>
Deferred consideration as on 31st March 20X3	453.75

8. Calculation of current Liability as on 31st March 20X3

	`in 000s
A Ltd.	1,250.00
S Ltd.	650.00
Deferred consideration as on 31st March 20X3 (W.N.7)	<u>453.75</u>
Current Liability as on 31st March 20X3	<u>2,353.75</u>

Question 22 : Nov 2024 – Paper

The balance sheets pf H Ltd. and S Ltd. as on 31.03.2024 were as follows :

Particulars	H LTD	S LTD
	Rs. in Lakhs	
Assets :		
Non-Current Assets		
Property, Plant and Equipment	14,800	6,000
Financial Assets : Investment		
Investment in S Ltd	5,800	
1000 Debenture in S Ltd	1,500	
Current Assets		
Inventories	2,600	2,000
Financial Assets		
Trade Receivables (due from S Ltd. Rs.160 lakh)	4,000	3,000
Dividend Receivable	320	—
Cash and Cash Equivalent	500	2,000

Total	29,520	13,000
Equity and Liabilities		
Equity		
Equity Share Capital (Rs.10 per share)	10,000	4,000
Other Equity (Retained Earnings)	16,320	5,000
Non-current Liabilities		
13% Debenture of Rs.100 each		3,000
Current Liabilities		
Financial Liabilities :		
Trade Payables (due to H Ltd. Rs.120 lakh)	1,700	600
Dividend Payable		400
Other Liabilities	1,500	
Total	29,520	13,000

Additional Information:

- (i) On 01st April’ 2023, S Ltd. had 400 lakh shares of Rs.10 each and Rs.3,000 lakh in its Retained Earnings in Other Equity. H Ltd. acquired 80% share of S Ltd. on 01st April’ 2023 at a consideration of Rs.5,800 lakh in cash.
- (ii) The following changes in book value of identifiable net assets of S Ltd. as on 01st April’ 2023 are to be considered for arriving the fair value of identifiable net assets and to record the changes in their fair value on the said date. These change in the fair values are to be considered while drawing consolidated Financial Statements of the Group.

Assets	Book value	Fair value
PPE	Rs.2500 lakhs	Rs.2800 lakhs
Inventory	Rs.500 lakhs	Rs.200 lakhs

The rate of depreciation on PPE is 10% p.a.
- (iii) NCI was to be measured at fair value based on the purchase consideration.
- (iv) Goodwill was impaired by Rs.100 lakh.
- (v) H Ltd. sold goods worth Rs.200 lakh to S Ltd. on credit at a profit of 20% on sales. 50% of the goods were still laying unsold.
- (vi) S Ltd. issued a cheque of Rs.40 lakh in favour of H Ltd. as a part payment of the goods purchased from it in March, 2024. The cheque is yet to be received by H Ltd.
- (vii) Dividend payable represents the dividend declared out of pre-acquisition profit. H Ltd. credited its share of dividend from S Ltd. to its profits.

Prepare the Consolidated Balance Sheet of the Group as at 31st March’ 2024.

Solution :

**Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd.
as at 31st March, 2024**

	Notes No.	Rs. in lakhs
Assets		
Non-current assets		

Property, plant and equipment	1	21,070
Goodwill	2	150
Current assets		
Inventory	3	4,275
Financial assets		
Cash and cash equivalents	4	2,540
Trade receivables	5	6,840
Dividend receivable	6	Nil
Total		34,875
Equity and Liabilities		
Equity		
Share capital - Equity shares of Rs. 10 each		10,000
Other equity	7	16,292
Non-controlling interest (W.N.4)		1,824
Non-current liabilities		
Financial liabilities		
Borrowings- 13% Debentures	8	2,999
Current Liabilities		
Financial liabilities		
Trade payables	9	2,180
Dividend payable	10	80
Other liabilities		1,500
Total		34,875

Notes to Accounts

1. Property, Plant and Equipment

Rs. in lakhs

Particulars		Rs.	Rs.
H Ltd.		14,800	
S Ltd.	6,000		
Add: Fair value gain	300		
Less: Additional depreciation due to fair value gain	(30)	<u>6,270</u>	21,070

2. Goodwill

Rs. in lakhs

Particulars		Rs.	Rs.
Goodwill on acquisition of S Ltd. (Refer W.N.3)		250	
Less: Impairment		<u>(100)</u>	150

3. Inventory

Rs. in lakhs

Particulars		Rs.	Rs.
H Ltd.		2,600	

S Ltd.	2,000		
Less: Fair value loss	(300)		
Less: Unrealised gain (200/80% x 20% x 50%)	<u>(25)</u>	<u>1,675</u>	4,275

4. Cash and cash equivalent Rs. in lakhs

Particulars	Rs.	Rs.	Rs.
H Ltd.	500		
Add: Cheque in Transit	<u>40</u>	540	
S Ltd.		<u>2,000</u>	2,540

5. Trade Receivable Rs. in lakhs

Particulars		Rs.	Rs.
H Ltd.	4,000		
Less: Mutual transaction	<u>(160)</u>	3,840	
S Ltd.		<u>3,000</u>	6,840

6. Dividend Receivable Rs. in lakhs

Particulars		Rs.	Rs.
H Ltd.		320	
Less: Mutual transaction		<u>(320)</u>	Nil

7. Other Equity (Retained Earnings) Rs. in lakhs

Particulars		Rs.	Rs.
H Ltd.		16,320	
Less: Share of pre-acquisition dividend (400 x 80%)		<u>(320)</u>	16,000
Post acquisition RE of S Ltd. (W.N.1)		2,370	
Less: Share of NCI in post-acquisition RE of S Ltd. (2,370 x 20%)		<u>(474)</u>	1,896
Less: Impairment of goodwill (100 x 80%)			(80)
Less: Loss on cancellation of debentures (mutual holding) (W.N.5)			(1,499)
Less: Unrealised gain (W.N.6)			<u>(25)</u>
			<u>16,292</u>

8. Borrowings (13% Debentures) Rs. in lakhs

Particulars		Rs.	Rs.
S Ltd.		3,000	
Less: Mutual holding by H Ltd. (1,000 Debentures x 100)		<u>(1)</u>	2,999

9. Trade Payables Rs. in lakhs

Particulars		Rs.	Rs.
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H Ltd.		1,700	
S Ltd.	600		
Less: Mutual transaction	<u>(120)</u>	<u>480</u>	2,180

10. Dividend Payables Rs. in lakhs

Particulars	Rs.	Rs.
S Ltd.	400	
Less: Mutual transaction	<u>(320)</u>	80

Working Notes:

1. Analysis of Retained Earnings of S Ltd. Rs. in lakhs

Closing balance as on 31st March, 2024	5,000
Less: Pre-acquisition Retained Earnings as on 1st April, 2023 (3,000 – 400)	<u>(2,600)</u>
	2,400
Less: Additional depreciation	<u>(30)</u>
Post-acquisition Retained Earnings	<u>2,370</u>

2. Computation of net worth (net identifiable assets) as on 1st April, 2023 Rs. in lakhs

Share Capital of S Ltd.	4,000
Pre-acquisition Retained Earnings	3,000
Fair value gain on PPE (2,800 – 2,500)	300
Fair value loss on inventory (500 - 200)	<u>(300)</u>
Net Worth or Net Identifiable Assets	<u>7,000</u>

3. Computation of Goodwill on acquisition date of S Ltd. Rs. in lakhs

Purchase consideration	5,800
NCI (by fair value method) as on 1st April, 2023 [(5,800/80%) x 20%]	<u>1,450</u>
	7,250
Less: Net worth or Net Identifiable Assets (W.N.2)	<u>(7,000)</u>
Goodwill as on 1st April, 2023	<u>250</u>

4. Non-Controlling Interest as on 31st March, 2024 Rs. in lakhs

NCI (by fair value method) as on 1st April, 2023	1,450
Less: Share of pre-acquisition dividend (400 x 20%)	(80)
Post-acquisition Retained Earnings (2,370 x 20%)	474
Less: Share of impairment of Goodwill (100 x 20%)	<u>(20)</u>
NCI as on 31st March, 2024	<u>1,824</u>

5. Loss on settlement of Debentures held by H Ltd. Rs. in lakhs

Investment in Debentures by H Ltd.	1,500
Less: Nominal value of debentures held by H Ltd. (1,000 x Rs. 100)	<u>(1)</u>

Loss on settlement of investment in Debentures	<u>1,499</u>
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6. Computation of unrealised gain by H Ltd. on sale of goods to S Ltd. Rs. in lakhs

Cost price of the goods sold	200
Sales price of the goods sold (200/80%)	250
Profit on sale of such goods	50
Unrealized gain on 50% unsold goods (50 x 50%)	25

Note: In the above solution, it is assumed that in additional information (v), Rs. 200 lakh is the cost price of the goods for H Ltd. which is sold to S Ltd. at Rs. 250 lakhs i.e. after 20% profit on sales. However, alternatively it may be assumed that Rs. 200 lakhs is the sales price of the goods for H Ltd. profit will be Rs. 200 lakhs x 20% i.e. Rs. 40 lakhs. In such a situation, the answer will be as follows:

**Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd.
as at 31st March, 2024**

	Notes No.	Rs. in lakhs
Assets		
Non-current assets		
Property, plant and equipment	1	21,070
Goodwill	2	150
Current assets		
Inventory	3	4,280
Financial assets		
Cash and cash equivalents	4	2,540
Trade receivables	5	6,840
Dividend receivable	6	<u>Nil</u>
Total		<u>34,880</u>
Equity and Liabilities		
Equity		
Share capital - Equity shares of Rs. 10 each		10,000
Other equity	7	16,297
Non-controlling interest (W.N.4)		1,824
Non-current liabilities		
Financial liabilities		
Borrowings - 13% Debentures	8	2,999
Current Liabilities		
Financial liabilities		
Trade payables	9	2,180
Dividend payable	10	80
Other liabilities		<u>1,500</u>

Total			<u>34,880</u>
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Notes to Accounts

1. Property, Plant and Equipment in lakhs

Particulars		Rs.	Rs.
H Ltd.		14,800	
S Ltd.	6,000		
Add: Fair value gain	300		
Less: Additional depreciation due to fair value gain	<u>(30)</u>	<u>6,270</u>	21,070

2. Goodwill **Rs. in lakhs**

Particulars		Rs.	Rs.
Goodwill on acquisition of S Ltd. (Refer W.N.3)		250	
Less: Impairment		<u>(100)</u>	150

3. Inventory **Rs. in lakhs**

Particulars		Rs.	Rs.
H Ltd.		2,600	
S Ltd.	2,000		
Less: Fair value loss	(300)		
Less: Unrealised gain (W.N.6)	<u>(20)</u>	<u>1,680</u>	4,280

4. Cash and cash equivalent **Rs. in lakhs**

Particulars		Rs.	Rs.	Rs.
H Ltd.		500		
Add: Cheque in Transit	<u>40</u>		540	
S Ltd.			<u>2,000</u>	2,540

5. Trade Receivable **Rs. in lakhs**

Particulars		Rs.	Rs.
H Ltd.	4,000		
Less: Mutual transaction	<u>(160)</u>	3,840	
S Ltd.		<u>3,000</u>	6,840

6. Dividend Receivable **Rs. in lakhs**

Particulars		Rs.	Rs.
H Ltd.		320	
Less: Mutual transaction	<u>(320)</u>		Nil

7. Other Equity (Retained Earnings) **Rs. in lakhs**

Particulars	Rs.	Rs.
H Ltd.	16,320	
Less: Share of pre-acquisition dividend (400 x 80%)	<u>(320)</u>	16,000
Post acquisition RE of S Ltd. (W.N.1)	2,370	
Less: Share of NCI in post-acquisition RE of S Ltd. (2,370 x 20%)	<u>(474)</u>	1,896
Less: Impairment of goodwill (100 x 80%)		(80)
Less: Loss on cancellation of debentures (mutual holding) (W.N.5)		(1,499)
Less: Unrealised gain (W.N.6)		<u>(20)</u>
		<u>16,297</u>

8. Borrowings (13% Debentures) Rs. in lakhs

Particulars	Rs.	Rs.
S Ltd.	3,000	
Less: Mutual holding by H Ltd. (1,000 Debentures x 100)	<u>(1)</u>	2,999

9. Trade Payables Rs. in lakhs

Particulars	Rs.	Rs.
H Ltd.	1,700	
S Ltd. 600		
Less: Mutual transaction <u>(120)</u>	<u>480</u>	2,180

10. Dividend Payables Rs. in lakhs

Particulars	Rs.	Rs.
S Ltd.	400	
Less: Mutual transaction	<u>(320)</u>	80

Working Notes:

1. Analysis of Retained Earnings of S Ltd. Rs. in lakhs

Closing balance as on 31st March, 2024	5,000
Less: Pre-acquisition Retained Earnings as on 1st April, 2023 (3,000 – 400)	<u>(2,600)</u>
	2,400
Less: Additional depreciation	<u>(30)</u>
Post-acquisition Retained Earnings	<u>2,370</u>

2. Computation of net worth (net identifiable assets) as on 1st April, 2023 Rs. in lakhs

Share Capital of S Ltd.	4,000
Pre-acquisition Retained Earnings	3,000
Fair value gain on PPE (2,800 – 2,500)	300
Fair value loss on inventory (500 - 200)	<u>(300)</u>
Net Worth or Net Identifiable Assets	<u>7,000</u>

3. Computation of Goodwill on acquisition date of S Ltd.	Rs. in lakhs
Purchase consideration	5,800
NCI (by fair value method) as on 1st April, 2023 [(5,800/80%) x 20%]	<u>1,450</u>
	7,250
Less: Net worth or Net Identifiable Assets (W.N.2)	<u>(7,000)</u>
Goodwill as on 1st April, 2023	<u>250</u>

4. Non-Controlling Interest as on 31st March, 2024	Rs. in lakhs
NCI (by fair value method) as on 1st April, 2023	1,450
Less: Share of pre-acquisition dividend (400 x 20%)	(80)
Post-acquisition Retained Earnings (2,370 x 20%)	474
Less: Share of impairment of Goodwill (100 x 20%)	<u>(20)</u>
NCI as on 31st March, 2024	<u>1,824</u>

5. Loss on settlement of Debentures held by H Ltd.	Rs. in lakhs
Investment in Debentures by H Ltd.	1,500
Less: Nominal value of debentures held by H Ltd. (1,000 x Rs. 100)	<u>(1)</u>
Loss on settlement of investment in Debentures	<u>1,499</u>

6. Computation of unrealised gain by H Ltd. on sale of goods to S Ltd.	Rs. in lakhs
Sales price of the goods sold	200
Profit on sale of such goods (200/20%)	40
Unrealized gain on 50% unsold goods (40 x 50%)	20

Question 23 : May 2025 – Paper

A Limited and B Limited are engaged in the manufacture of pharmaceuticals. On 1st June, 2024, A Limited acquired 15% of equity shares of B Limited. On 1st October, 2024, A Limited obtains control of B Limited when it acquires a further 55% of B Limited's shares, thereby resulting into a total holding of 70%. The fair value of the shares of B Limited was Rs. 40 per share as on that date. Prior to the acquisition of additional 55% stake by A Limited on 1st October, 2024, the Balance Sheets of the two companies stood as under:

Particulars	(Rs. in lakhs)	
	A Ltd.	B Ltd.
Assets		
Non-Current Assets		
Property, Plant and Equipment	600	400
Investments (6,00,000 Shares of B Ltd. acquired on 1st June, 2024)	210	-
Current Assets		
Inventories	500	150

Financial Assets		
Trade receivables	450	300
Cash and cash equivalents	400	100
Other Current Assets	200	230
Non-current assets held for sale	-	250
Total	2,360	1,430
Equity and Liabilities		
Equity		
Share Capital – Equity Shares of Rs. 100 each	500	-
Share Capital – Equity Shares of 10 each	-	400
Other Equity	810	225
Non-Current Liabilities		
Financial Liabilities		
Long-term Borrowings	250	200
Long-term Provisions	50	70
Deferred Tax Liability	40	-
Current Liabilities		
Financial Liabilities		
Short-term Borrowings	400	285
Trade Payables	310	250
Total	2,360	1,430

In consideration of the additional stake acquired by A Limited on 1st October, 2024, it agreed to pay to each selling shareholder of B Limited a sum of Rs. 15 per share in cash and issue 1 Equity Share of Rs. 100 each of A Limited in lieu of 8 Equity Shares of Rs. 10 each held by the selling shareholder in B Limited. The fair value of the shares of A Limited as on 1st October, 2024 is Rs. 160 per share.

In addition to the above:

- A Limited agreed to pay an additional payment as consideration that is higher of Rs. 35 lakhs and 25% of any excess profit in the first year, after acquisition over its profits in the preceding one year made by B Limited. This additional amount would be due after 2 years. B Limited has earned Rs. 10 lakhs profit in the preceding year and expects to earn another Rs. 20 lakhs.
- A Limited also agreed to pay one of the promoter shareholders of B Limited a payment of Rs. 15 lakhs provided he stays with the company for two years after acquisition.
- A Limited* had a certain equity settled share-based payment award (Original award) which was replaced by the new award issued by B Limited. As per the original terms, the vesting period was 4 years and as of the acquisition date, the employees of B Limited have already served 2 years of service. As per the replaced award, the vesting period is reduced to one year (one year from the acquisition date). The fair value of the award on the acquisition date was as under:

- (i) Original Award: Rs. 5 lakhs
- (ii) Replacement Award: Rs. 8 lakhs
- (d) The fair value exercise resulted in the following:
 - (i) The fair value of Property, Plant and Equipment and Inventory of B Limited as on 1st October, 2024 was Rs. 480 lakhs and Rs. 170 lakhs respectively.
 - (ii) The carrying value of Non-Current Asset held for sale of Rs. 250 lakhs of B Limited represents its fair value less cost to sell in accordance with the relevant Ind AS.
 - (iii) B Limited has developed and patented a new drug for Parkinson disease which has been approved for clinical use. The cost of developing the drug was Rs. 140 lakhs. Based on early assessment of its sales success, the valuer has estimated its market value at Rs. 200 lakhs.
 - (iv) B Limited had a lawsuit for infringement of Trademark pending with a competitor who had made a claim of Rs. 50 lakhs. B Limited has disclosed the same as a contingent liability as it is not probable that the amount would be payable. Management reliably estimated the fair value of the liability to be 10 lakhs. Any sum which would be paid in respect of the lawsuit would be tax deductible.
- (e) The cost of capital of A Limited is 10%. The appropriate discount factor for Rs. 1 @ 10% payable at the end of 1st year is 0.91 and 2nd year is 0.83.
- (f) The applicable tax rate for both the entities is 30%.

Unless stated otherwise, all items have a fair value and tax base equal to their carrying amounts at the acquisition date. A Limited chooses to measure the Non-Controlling Interest in B Limited as per Proportionate Share of identifiable net assets method.

You are required to prepare the opening Consolidated Balance Sheet of A Limited as on 1st October, 2024 as per the applicable Ind AS. Working Notes should form part of your answer.

Solution :

Consolidated Balance Sheet of A Ltd. and its subsidiary B Ltd. as at 1st October, 2024

	Notes No.	Rs. in lakhs
Assets		
Non-current assets		
Property, plant and equipment	1	1,080.00
Goodwill	2	461.95
Intangible assets (patents)		200.00
Current assets		
Inventories	3	670.00
Financial assets		
Cash and cash equivalents	4	170.00
Trade receivables	5	750.00
Other current assets	6	430.00
Assets held for sale		250.00
Total		4,011.95

Equity and Liabilities		
Equity		
Other equity	7	775.00
Non-controlling interest (W.N.4)	8	1,007.50
Non-current liabilities		248.40
Financial liabilities		
Long-term borrowings	9	450.00
Long-term provisions	10	149.05
Deferred tax liabilities	11	127.00
Current Liabilities		
Financial liabilities		
Short-term borrowings	12	685.00
Trade payables	13	560.00
Provision for lawsuit damages		10.00
Total		4,011.95

Notes to Accounts

1. Property, Plant and Equipment

Rs. in lakhs

Particulars			
A Ltd.		600.00	
B Ltd.	400.00		
Add: Fair value gain	80.00	480.00	1,080.00

2. Goodwill

Rs. in lakhs

Particulars	
Goodwill on acquisition of B Ltd. (Refer W.N.5)	461.95

3. Inventories

Rs. in lakhs

Particulars			
A Ltd.		500.00	
B Ltd.	150.00		
Add: Fair value given	20.00	170.00	670.00

4. Cash and cash equivalents

Rs. in lakhs

Particulars			
A Ltd.	400.00		
Less: Paid to B Ltd.'s Shareholders	<u>(330.00)</u>	70.00	
B Ltd.		<u>100.00</u>	170.00

Note: The additional consideration paid to promoter shareholder is contingent to him/her continuing in employment and hence this will be considered as employee compensation and will be recorded as post combination expense in the income statement by A Ltd.

5. Trade receivables **Rs. in lakhs**

Particulars		
A Ltd.	450.00	
B Ltd.	<u>300.00</u>	750.00

6. Other current assets **Rs. in lakhs**

Particulars		
A Ltd.	200.00	
B Ltd.	<u>230.00</u>	430.00

7. Equity **Rs. in lakhs**

Particulars	
Equity Share Capital 7,75,000 Equity shares of Rs. 100 each (Out of the above, 2,75,000 Equity shares of Rs. 100 each allotted to shareholders of B Ltd for consideration other than cash)	775.00

8. Other equity **Rs. in lakhs**

Particulars			
A. Retained earnings of A Ltd.	810.00		
Add: Gain on previously acquired shares of A Ltd.	<u>30.00</u>	840.00	
B. Replacement award		2.50	
C. Security premium (2,75,000 shares x Rs. 60)		<u>165.00</u>	1007.50

9. Long-term borrowings **Rs. in lakhs**

Particulars		
A Ltd.	250.00	
B Ltd.	<u>200.00</u>	450.00

10. Long term provisions **Rs. in lakhs**

Particulars		
A Ltd.	50.00	
Add: Deferred consideration	<u>29.05</u>	79.05

B Ltd.		<u>70.00</u>	149.05
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11. Deferred tax liabilities **Rs. in lakhs**

Particulars		
Deferred tax liability of A Ltd	40.00	
Deferred tax liability (W.N. 2)	<u>87.00</u>	127.00

12. Short term borrowings **Rs. in lakhs**

Particulars		
A Ltd.	400.00	
B Ltd.	285.00	685.00

13. Trade payables **Rs. in lakhs**

Particulars		
A Ltd.	310.00	
B Ltd.	<u>250.00</u>	560.00

Working Notes:

1. Calculation of purchase consideration **Rs. in lakhs**

Investment in B Ltd.			
Shares acquired			
On 1st June, 2024	15%	[(400/10) x 15% x Rs. 40]	240.00
On 1st October, 2024	55%		
Own equity given		(40 x 55%) x 1/8 x Rs.160	440.00
Cash		(40 x 55%) x Rs. 15	330.00
Contingent consideration		(35 x 0.83)	29.05
Replacement award		(5 x 2/4)	<u>2.50</u>
			<u>1041.55</u>

2. Calculation of deferred tax on assets and liabilities acquired as part of the business combination

Item	Rs. in lakhs				
	Book value	Fair value	Tax base	Taxable (deductible) temporary difference	Deferred tax assets (liability) @ 30%
Property, plant and equipment	400.00	480.00	400.00	80.00	-24.00
Intangible assets		200.00	0.00	200.00	-60.00
Inventories	150.00	170.00	150.00	20.00	-6.00
Trade receivables	300.00	300.00	300.00	-	-

Cash and cash equivalents	100.00	100.00	100.00	-	-
Other current assets	230.00	230.00	230.00	-	-
Non-current asset held for sale	250.00	250.00	250.00	-	-
(A)	1430.00	1730.00	1430.00	300.00	(90.00)
Trade payables	250.00	250.00	250.00	-	-
Long-term provisions	70.00	70.00	70.00	-	-
Short-term borrowings	285.00	285.00	285.00	-	-
Contingent liability	-	10.00	-	(10.00)	3.00
(B)	605.00	615.00	605.00	(10.00)	3.00
Deferred tax liabilities (A-B)					-87.00

3. Calculation of fair value of identifiable net assets acquired

	Rs. in lakhs	Rs. in lakhs
Property, plant and equipment	480.00	
Intangible assets	200.00	
Inventories	170.00	
Trade receivables	300.00	
Cash and cash equivalents	100.00	
Non-current asset held for sale	250.00	
Other current assets	<u>230.00</u>	
Total assets		1730.00
Less: Long-term borrowings	200.00	
Trade payables	250.00	
Long-term provisions	70.00	
Short-term borrowings	285.00	
Contingent liabilities	10.00	
Deferred tax liabilities	<u>87.00</u>	
Total liabilities		<u>(902.00)</u>
Net identifiable assets		<u>828.00</u>

4. Calculation of NCI by proportionate share of identifiable net assets

Identifiable net assets of S Ltd. on 1st October, 2024 (Refer W.N.3) = Rs. 828.00 lakhs
 NCI on 1st October, 2024 = 828.00 lakhs x 30% = 248.40 lakhs

5. Calculation of Goodwill

Particulars	Rs. in Lakhs
Fair Value of Net Identifiable Assets	828.00
Less: NCI	<u>(248.40)</u>
	579.60

Less: Purchase Consideration	<u>(1041.55)</u>
Goodwill on 1st October, 2024	<u>461.95</u>

Question 24 : Sept 2025 – RTP

A Ltd. owns 100% of a subsidiary B Ltd. It disposes of 60% of its interest in the subsidiary for Rs. 360 million and loses control of the subsidiary. It will de-consolidate the subsidiary and account for the remaining 40% interest as an associate using the equity method of accounting. At the disposal date, the fair value of the retained investment in B Ltd. is determined to be Rs. 240 million. The carrying value of the identifiable net assets of the subsidiary is Rs. 440 million, excluding goodwill. There is Rs. 60 million of goodwill recorded related to the previously acquired interests in the subsidiary. A Ltd. tested the subsidiary's goodwill and long-lived assets prior to disposal and there was no impairment. There is Rs. 4 million credit in the available-for-sale reserve and Rs. 10 million credit in the revaluation reserve relating to the subsidiary B Ltd. The tax consequences of the gain have been ignored.

Required:

- (i) Pass Journal Entries for sale of 60% stake of B Ltd. on disposal date
- (ii) Compute gain on 40% retained investment

Solution :

- (i) The accounting entry on the disposal date for the 60% interest sold, the gain recognised on the 40% retained investment and the de-recognition of the subsidiary is as follows:

		Rs. in million	
Cash / Bank A/c	Dr.	360	
Investment in associate	Dr.	240	
Available -for-sale reserve	Dr.	4	
Revaluation reserve	Dr.	10	
To Net assets (including goodwill)			500
To Retained earnings			10
To Gain on disposal of controlling interest			104

The Rs. 104 million gain on the interest sold and the retained investment is recognised in the income statement and is disclosed in the consolidated financial statements.

- (ii) Computation of remeasurement of the retained non-controlling investment to fair value:

	Rs. in million
Fair value of retained investment	240
Percentage retained of carrying value of subsidiary [(440+ 60) x 40%]	<u>(200)</u>
Gain on retained investment	<u>40</u>

The gain or loss on the interest sold and on the retained investment recognised in the income statement, is calculated as follows:

	Rs. in million
Fair value of the consideration	360

Fair value of retained investment	<u>240</u>
	600
Less: Carrying value of former subsidiary's assets (440 + 60)	(500)
Available for sale reserve transferred to income	<u>4</u>
Gain on interest sold and on retained investment	<u>104</u>

Question 25 : Sept 2025 – Paper

R Limited is a subsidiary of Z Limited. Their respective balance sheet as at 31st March, 2025 is as under:

	Note No.	Z Ltd. (Rs. in lakhs)	R Ltd. (Rs. in lakhs)
I. Assets			
Non-current assets			
(i) Property, plant and equipment	4	450	248
(ii) Intangible assets	5	75	45
(iii) Investments		375	68
Current assets			
(i) Inventories		75	75
(ii) Financial assets			
a. Trade receivables	6	110	120
b. Cash and cash equivalents		85	135
Total Assets		1,170	691
II. Equity and Liabilities			
Equity			
(i) Share Capital	1	720	360
(ii) Other Equity	2	315	225
Liabilities			
Current Liabilities			
(i) Financial liabilities			
a. Bank overdraft		45	30
b. Trade payables	3	90	76
Total Equity and Liabilities		1,170	691

Notes to the Balance Sheet :

Note No.		Z Ltd. (Rs. in Lakhs)	R Ltd. (Rs. in Lakhs)
1	Share capital:		
	(i) Equity shares of Rs. 10 each	600	300
	(ii) 10% Preference shares of Rs. 10 each	<u>120</u>	<u>60</u>

		<u>720</u>	<u>360</u>
2	Other equity:		
	(i) General reserve	120	75
	(ii) Retained earnings	<u>195</u>	<u>150</u>
		<u>315</u>	<u>225</u>
3	Trade payables:		
	(i) Sundry creditors	90	69
	(ii) Bills payable	<u>Nil</u>	<u>7</u>
		<u>90</u>	<u>76</u>
4	Property, plant and equipment:		
	(i) Machinery	210	135
	(ii) Furniture and fixture	<u>240</u>	<u>113</u>
		<u>450</u>	<u>248</u>
5	Intangible asset:		
	Goodwill	75	45
6	Trade receivables:		
	(i) Sundry debtors	106	120
	(ii) Bills receivable	<u>4</u>	<u>Nil</u>
		<u>110</u>	<u>120</u>

Additional Information

- (a) Z Ltd. acquired 12,00,000 equity shares of R Ltd. on 1st April, 2024 and further acquired 13,50,000 equity shares of R Ltd. on 1st January, 2025 at a cost of Rs. 1,44,00,000 and Rs. 1,55,25,000 respectively.
- (b) The Preference share capital of R Ltd. includes nominal value of Rs. 22,50,000 held by Z Ltd. acquired on 1st April, 2024 at a cost of Rs. 54,00,000.
- (c) The retained earnings of R Ltd. had a credit balance of Rs. 45,00,000 as on 1st April, 2024 and that of General Reserve on that date was Rs. 30,00,000.
- (d) R Ltd. had paid dividend @ 12% on its paid-up equity share capital out of its retained earnings' balance on 1st April, 2024 for the year 2023-2024. The entire dividend received by Z Ltd. in August 2024 has been credited to its retained earnings.
- (e) On 1st October, 2024, machinery of R Ltd. was overvalued by Rs. 15,00,000 for which necessary adjustments are to be made. The Company charges depreciation @ 10% on W.D.V. basis.
- (f) Bills receivables of Z Ltd. were drawn upon R Ltd. out of which bills amounting to Rs. 3,00,000 have been discounted with bank.

You are required to prepare consolidated balance sheet (In Rs. without rounding off) of Z Ltd. and its subsidiary R Ltd. as on 31st March, 2025 with the assumption that the group has adopted fair value method to measure NCI and the fair value of each equity share of R Ltd. is Rs. 14 per share as on the date of acquisition of control by Z Ltd. and also on 31st March 2025. Ignore taxation and adjustment, if any, of preference dividend.

Solution :

Consolidated Balance Sheet of Z Ltd. as at 31st March 2025

	Notes No.	Rs.
Assets		
Non-current assets		
(i) Property, plant and equipment	1	6,83,75,000
(ii) Intangible assets	1	75,00,000
(iii) Financial assets		
a. Investments	1	89,75,000
Current assets		
(i) Inventories	1	1,50,00,000
(ii) Financial assets		
a. Trade receivables	1	2,26,00,000
b. Cash and cash equivalents	1	<u>2,20,00,000</u>
Total		<u>14,44,50,000</u>
Equity and Liabilities		
Equity		
(i) Share capital	2	7,20,00,000
(ii) Other equity	3	3,79,96,875
(iii) Non-controlling interest (W.N.3)		1,07,53,125
Current Liabilities		
(i) Financial liabilities		
a. Bank overdraft	1	75,00,000
b. Trade payables	1	<u>1,62,00,000</u>
Total		<u>14,44,50,000</u>

Notes to Accounts

Note 1: Assets and Liabilities

Particulars	Z Ltd.	R Ltd.	Adjustments	Rs.
Property, Plant and Equipment	4,50,00,000	2,48,00,000	-15,00,000 + 75,000	6,83,75,000
Intangible Assets	75,00,000	45,00,000	-45,00,000	75,00,000
Investments	3,75,00,000	68,00,000	1,44,00,000 -1,55,25,000 -54,00,000	89,75,000
Inventories	75,00,000	75,00,000		1,50,00,000
Trade Receivables	1,10,00,000	1,20,00,000	-4,00,000	2,26,00,000
Cash and Cash Equivalents	85,00,000	1,35,00,000		2,20,00,000
Bank Overdraft	45,00,000	30,00,000		75,00,000
Trade Payables	90,00,000	76,00,000	-4,00,000	1,62,00,000

Note 2: Share Capital

	Rs.
60 lakhs Equity shares of Rs. 10 each, fully paid	6,00,00,000
10%, 12 lakhs Preference Share of Rs. 10 each fully paid	<u>1,20,00,000</u>
	<u>7,20,00,000</u>

Note 3: Consolidated Other Equity

		Rs.
General Reserve	W.N.1	1,29,56,250
Retained Earnings	W.N.1	2,17,78,125
Capital Reserve	W.N.2	<u>32,62,500</u>
		<u>3,79,96,875</u>

Working Notes:

1. Consolidated Other Equity

Particulars	General Reserve	Retained Earnings
Standalone - Z Ltd.	1,20,00,000	1,95,00,000
Add: Fair Value gain of existing stake [(12 lakh x 14) – 144 lakhs]		24,00,000
Less: Fair Value loss of existing stake [(12 lakh x Rs. 11.50) – 144 lakhs]		
Less: Loss on cancellation of preference shares (54 lakhs - 22.5 lakhs)		(31,50,000)
Add: Share in post-acquisition Profits (W.N.4(i))	9,56,250	
(W.N.4(ii))		30,28,125
	1,29,56,250	2,17,78,125

2. Computation of bargain purchase i.e. capital reserve

(i) Computation of net worth (net identifiable assets) as on 1st January 2025

	Rs.
Share Capital	3,00,00,000
Pre-acquisition Retained Earnings (after adjusting downward revaluation of machinery)	1,00,12,500
Pre-acquisition General Reserve	63,75,000
Adjustment for Goodwill since it has no fair value	<u>-45,00,000</u>
Net worth or Net Identifiable assets	<u>4,18,87,500</u>

(ii) **Computation of bargain purchase i.e. capital reserve**

		Rs.
Net worth or Net identifiable assets		4,18,87,500
Purchase consideration (155.25 lakhs + 168 lakhs)	3,23,25,000	
NCI [30 lakhs shares x 15% x Rs. 14]	<u>63,00,000</u>	<u>(3,86,25,000)</u>
Bargain purchase (capital reserve)		<u>32,62,500</u>

3. **Non-Controlling Interest A/c (at Fair Value)**

	Rs.
NCI at fair value as on 1st January 2025	63,00,000
Post-acquisition General Reserve (W.N.4(i))	1,68,750
Post-acquisition Retained Earnings (W.N.4(ii))	5,34,375
Preference share capital (60 lakh – 22.50 lakh)	<u>37,50,000</u>
NCI at fair value as on 31st March 2025	<u>1,07,53,125</u>

4. **Analysis of Other Equity**

(i) **General Reserve**

		Rs.
Closing balance as on 31st March 2025		75,00,000
Less: Opening Balance (45.00 - 36.00)	pre	<u>(30,00,000)</u>
Net Profit transferred during the year		<u>45,00,000</u>
For 9 months till 31st December 2024	pre	33,75,000
For 3 months from 1st Jan. 2025 to 31st Mar. 2025	post	11,25,000
Total pre-acquisition reserve (30.00 lakh+33.75 lakh)	pre	63,75,000
Share of Z Ltd. in post-acquisition reserve (85%)	post	9,56,250
Share of NCI in post-acquisition reserve (15%)	post	1,68,750

(ii) **Retained Earnings (RE)**

		Rs.
Closing balance as on 31st March, 2025		1,50,00,000
Less: Opening balance 45,00,000		
Less: Dividend @12% (300 lakhx12%) (36,00,000)	Pre	<u>(9,00,000)</u>
During the year		<u>1,41,00,000</u>
For 9 months till 31st December, 2024	Pre	<u>1,05,75,000</u>
For 3 months from 1st Jan. 2025 to 31st Mar. 2025	Post	35,25,000
Add: Saving in Depreciation for 3 months (from 1st January 2025 to March 2025)		<u>37,500</u>

Net post-acquisition RE	Post	<u>35,62,500</u>
Total pre-acquisition RE (9.00 + 105.75)	Pre	1,14,75,000
Less: Downward revaluation of machinery		(15,00,000)
Add: Saving in depreciation for 3 months (from 1st October 2024 to 31st December 2024)		<u>37,500</u>
	Pre	<u>1,00,12,500</u>
Share of Z Ltd. in post-acquisition RE (85%)	Post	30,28,125
Share of NCI in post-acquisition RE (15%)	Post	5,34,375

Note:

- At page 4 of the Question Paper under additional information (a) the second acquisition of 13,50,000 equity shares on 1st January 2025 has been done at Rs. 1,55,25,000. This implies that fair value per share is Rs. 11.50 (1,55,25,000/13,50,000). However, in the last para of the question at the same page, the fair value of R Ltd.'s share is mentioned as Rs. 14 per share on the date of acquisition.
The above solution has been drawn considering fair value of R Ltd.'s share as Rs. **14 per share** for the purpose of computation of gain or loss on existing stake and bargain purchase.
However, alternatively one can draw a solution considering fair value of R Ltd.'s share as Rs. **11.5 per share** for the purpose of computation of gain or loss on existing stake and bargain purchase only. In such a case, the amount of consolidated retained earnings and bargain purchase i.e. capital reserve will be Rs. 1,87,78,125 and Rs. 62,62,500 respectively.
- Furthermore, the above solution has been drawn considering goodwill being residuary in nature, has no fair value. However, one may draw a solution considering goodwill as an identifiable asset.

Thanks



IND AS – 28

INVESTMENTS IN JOINT VENTURE & ASSOCIATES

CHAPTER - 30

Question 1 : Nov 2018 – RTP

As provided in Ind- AS 111 - Joint Arrangements - this is a joint arrangement because two or more parties have joint control of the property under a contractual arrangement. The arrangement will be regarded as a joint operation because Alpha Ltd. and Gama Ltd. have rights to the assets and obligations for the liabilities of this joint arrangement. This means that the company and the other investor will each recognise 50% of the cost of constructing the asset in property, plant and equipment.

The borrowing cost incurred on constructing the property should under the principles of Ind AS 23 'Borrowing Costs', be included as part of the cost of the asset for the period of construction. In this case, the relevant borrowing cost to be included is Rs.50,00,000 ($\text{Rs.10,00,00,000} \times 10\% \times 6/12$).

The total cost of the asset is Rs.40,50,00,000 ($\text{Rs.40,00,00,000} + \text{Rs.50,00,000}$) Rs.20,25,00,000 crores is included in the property, plant and equipment of Alpha Ltd. and the same amount in the property, plant and equipment of Gama Ltd.

The depreciation charge for the year ended 31 March 2018 will therefore be Rs.1,01,25,000 ($\text{Rs.40,50,00,000} \times 1/20 \times 6/12$) Rs.50,62,500 will be charged in the statement of profit or loss of the company and the same amount in the statement of profit or loss of Gama Ltd.

The other costs relating to the arrangement in the current year totalling Rs.54,00,000 (finance cost for the second half year of Rs.50,00,000 plus maintenance costs of Rs.4,00,000) will be charged to the statement of profit or loss of Alpha Ltd. and Gama Ltd. in equal proportions- Rs.27,00,000 each.

Solution :

As provided in Ind- AS 111 - Joint Arrangements - this is a joint arrangement because two or more parties have joint control of the property under a contractual arrangement. The arrangement will be regarded as a joint operation because Alpha Ltd. and Gama Ltd. have rights to the assets and obligations for the liabilities of this joint arrangement. This means that the company and the other investor will each recognise 50% of the cost of constructing the asset in property, plant and equipment.

The borrowing cost incurred on constructing the property should under the principles of Ind AS 23 'Borrowing Costs', be included as part of the cost of the asset for the period of construction. In this case, the relevant borrowing cost to be included is Rs.50,00,000 ($\text{Rs.10,00,00,000} \times 10\% \times 6/12$).

The total cost of the asset is Rs.40,50,00,000 (Rs.40,00,00,000 + Rs.50,00,000) Rs.20,25,00,000 crores is included in the property, plant and equipment of Alpha Ltd. and the same amount in the property, plant and equipment of Gama Ltd.

The depreciation charge for the year ended 31 March 2018 will therefore be Rs.1,01,25,000 (Rs.40,50,00,000 x 1/20 x 6/12) Rs.50,62,500 will be charged in the statement of profit or loss of the company and the same amount in the statement of profit or loss of Gama Ltd.

The other costs relating to the arrangement in the current year totalling Rs.54,00,000 (finance cost for the second half year of Rs.50,00,000 plus maintenance costs of Rs.4,00,000) will be charged to the statement of profit or loss of Alpha Ltd. and Gama Ltd. in equal proportions- Rs.27,00,000 each.

Question 2 : May 2020 – RTP

An entity P (parent) has two wholly-owned subsidiaries - X and Y, each of which has an ownership interest in an 'associate', entity Z. Subsidiary X is a venture capital organisation. Neither of the investments held in associate Z by subsidiaries X and Y is held for trading. Subsidiary X and Y account for their investment in associate Z at fair value through profit or loss in accordance with Ind AS 109 and using the equity method in accordance with Ind AS 28 respectively.

How should P account for the investment in associate Z in the following scenarios:

Scenario 1: Where both investments in the associate result in significant influence on a stand-alone basis - Subsidiary X and Y ownership interest in associate Z is 25% and 20% respectively.

Scenario 2: When neither of the investments in the associate results in significant influence on a stand-alone basis, but do provide the parent with significant influence on a combined basis - Subsidiary X and Y ownership interest in associate Z is 10% each.

Scenario 3: When one of the investments in the associate results in significant influence on a stand-alone basis and the other investment in the associate does not result in significant influence on a stand-alone basis - Subsidiary X and Y ownership interest in associate Z is 30% and 10% respectively.

Assume there is significant influence if the entity has 20% or more voting rights.

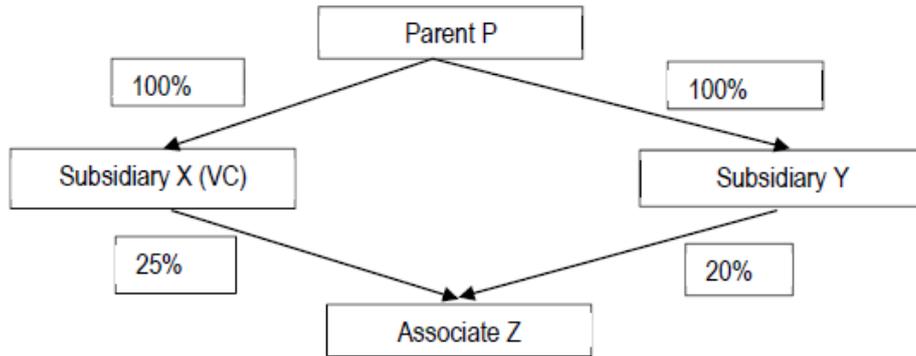
Solution :

Paragraph 18 of Ind AS 28 states that, “when an investment in an associate or a joint venture is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure investments in those associates and joint ventures at fair value through profit or loss in accordance with Ind AS 109. An entity shall make this election separately for each associate or joint venture, at initial recognition of the associate or joint venture.”

Paragraph 19 of Ind AS 28 provides that, “when an entity has an investment in an associate, a portion of which is held indirectly through a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure that portion of the investment in the associate at fair value through profit or loss in accordance with Ind AS 109 regardless of whether the venture capital organisation has significant influence over that portion of the investment. If the entity makes that election, the entity shall apply the equity method to any remaining portion of its investment in an associate that is not

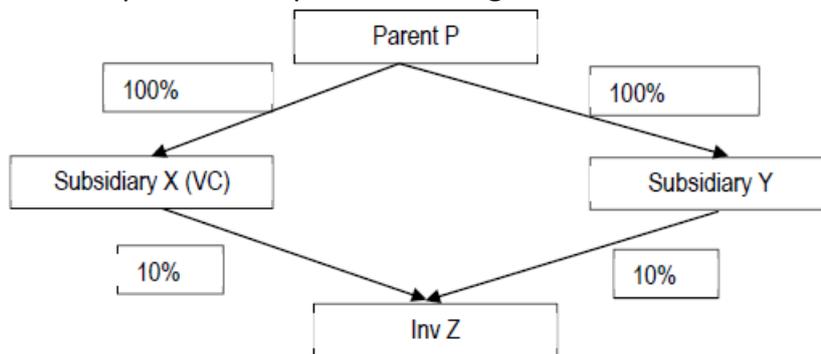
held through a venture capital organisation”. Therefore, fair value exemption can be applied partially in such cases.

Scenario 1: Where both investments in the associate result in significant influence on a stand-alone basis.



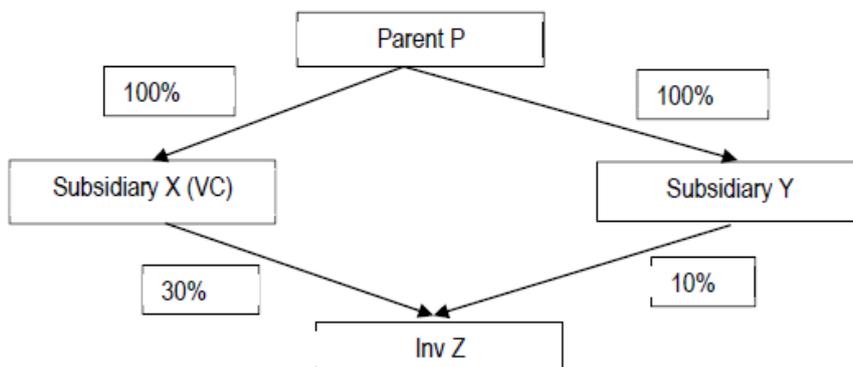
In the present case, in accordance with paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 20% interest held by Y. Under the partial use of fair value exemption, P may elect to measure the 25% interest held by X at fair value through profit or loss.

Scenario 2: When neither of the investments in the associate results in significant influence on a stand-alone basis, but do provide the parent with significant influence on a combined basis.



In the present case in accordance with the paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 10% interest held by Y, even though Y would not have significant influence on a stand-alone basis. Under the partial use of fair value exemption, P may elect to measure the 10% interest held by X at fair value through profit or loss.

Scenario 3: When one of the investments in the associate results in significant influence on a stand-alone basis and the other investment in the associate does not result in significant influence on a stand-alone basis



In the present case, in accordance with paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 10% interest held by Y, even though Y would not have significant influence on a stand-alone basis. Under the partial use of fair value exemption, the P may elect to measure the 30% interest held by X at fair value through profit or loss.

Question 3 : Nov 2020 – RTP

On 1st April 2019, Investor Ltd. acquires 35% interest in another entity, XYZ Ltd. Investor Ltd. determines that it is able to exercise significant influence over XYZ Ltd. Investor Ltd. has paid total consideration of Rs.47,50,000 for acquisition of its interest in XYZ Ltd. At the date of acquisition, the book value of XYZ Ltd.’s net assets was

Rs.90,00,000 and their fair value was Rs.1,10,00,000. Investor Ltd. has determined that the difference of Rs.20,00,000 pertains to an item of property, plant and equipment (PPE) which has remaining useful life of 10 years.

During the year, XYZ Ltd. made a profit of Rs.8,00,000. XYZ Ltd. paid a dividend of Rs.12,00,000 on 31st March, 2020. XYZ Ltd. also holds a long-term investment in equity securities. Under Ind AS, investment is classified as at FVTOCI in accordance with Ind AS 109 and XYZ Ltd. recognized an increase in value of investment by Rs.2,00,000 in OCI during the year. Ignore deferred tax implications, if any.

Calculate the closing balance of Investor Ltd.’s investment in XYZ Ltd. as at 31st March, 2020 as per the relevant Ind AS.

Solution :

Calculation of Investor Ltd.’s investment in XYZ Ltd. under equity method:

	Rs.	Rs.
Acquisition of investment in XYZ Ltd.		
Share in book value of XYZ Ltd.’s net assets (35% of Rs.90,00,000)	31,50,000	
Share in fair valuation of XYZ Ltd.’s net assets [35% of (Rs.1,10,00,000 – Rs.90,00,000)]	7,00,000	
Goodwill on investment in XYZ Ltd. (balancing figure)	<u>9,00,000</u>	
Cost of investment		47,50,000
Profit during the year		
Share in the profit reported by XYZ Ltd. (35% of Rs.8,00,000)	2,80,000	
Adjustment to reflect effect of fair valuation [35% of (Rs.20,00,000/10 years)]	<u>-70,000</u>	
Share of profit in XYZ Ltd. recognised in income by Investor Ltd.		2,10,000
Long term equity investment		
FVTOCI gain recognised in OCI (35% of Rs.2,00,000)		70,000
Dividend received by Investor Ltd. during the year [35% of Rs.12,00,000]		<u>(4,20,000)</u>
Closing balance of Investor Ltd.’s investment in XYZ Ltd.		<u>46,10,000</u>

Question 4 : Nov 2020 – Paper

Entity K is owned by three institutional investors - M Limited, N Limited and C Limited - holding 40%, 40% and 20% equity interest respectively. A contractual arrangement between M Limited and N Limited gives them joint control over the relevant activities of Entity K. It is determined that Entity K is a joint operation (and not a joint venture). C Limited is not a party to the arrangement between M Limited and N Limited. However, like M Limited and N Limited, C Limited also has rights to the assets, and obligations for the liabilities, relating to the joint operation in proportion of its equity interest in Entity K.

Would the manner of accounting to be followed by M Limited and N Limited on the one hand and C Limited on the other in respect of their respective interests in Entity K be the same or different? You are required to explain in light of the relevant provisions in the relevant standard in this regard.

OR

An entity negotiates with major airlines to purchase tickets at reduced rates compared with the price of tickets sold directly by the airlines to the public. The entity agrees to buy a specific number of tickets and will pay for those tickets even if it is not able to resell them. The reduced rate paid by the entity for each ticket purchased is negotiated and agreed in advance. The entity determines the prices at which the airline tickets will be sold to its customers. The entity sells the tickets and collects the consideration from customers when the tickets are sold; therefore, there is no credit risk to the entity.

The entity also assists the customers in resolving complaints with the service provided by airlines. However, each airline is responsible for fulfilling obligations associated with the ticket, including remedies to a customer for dissatisfaction with the service.

Determine whether the entity is a principal or an agent with suitable explanation in light with the provisions given in the relevant standard.

Solution :

Ind AS 111 states that a joint operator shall recognise in relation to its interest in a joint operation:

- (a) its assets, including its share of any assets held jointly;
- (b) its liabilities, including its share of any liabilities incurred jointly;
- (c) its revenue from the sale of its share of the output arising from the joint operation;
- (d) its share of the revenue from the sale of the output by the joint operation; and
- (e) its expenses, including its share of any expenses incurred jointly.

A joint operator shall account for the assets, liabilities, revenues and expenses relating to its interest in a joint operation in accordance with the Ind AS applicable to the particular assets, liabilities, revenues and expenses.

Further, Ind AS 111 states that a party that participates in, but does not have joint control of a joint operation shall also account for its interest in the arrangement in accordance with above provisions of the standard, if that party has rights to the assets, and obligations for the liabilities, relating to the joint operation.

In the given case, all three investors (M Limited, N Limited and C Limited) share in the assets and liabilities of the joint operation in proportion of their respective equity interest. Accordingly, both M Limited and N Limited (which have joint control) and C Limited (which does not have joint

control but participates) shall recognise their interest in joint operation as per above guidance while accounting for their respective interests in Entity K in their respective separate financial statements as well as in the consolidated financial statements.

OR

To determine whether the entity's performance obligation is to provide the specified goods or services itself (i.e. the entity is a principal) or to arrange for another party to provide those goods or services (i.e. the entity is an agent), the entity considers the nature of its promise as per Ind AS 115.

The entity determines that its promise is to provide the customer with a ticket, which provides the right to fly on the specified flight or another flight if the specified flight is changed or cancelled. The entity considers the following indicators for assessment as principal or agent under the contract with the customers:

- (a) the entity is primarily responsible for fulfilling the contract, which is providing the right to fly. However, the entity is not responsible for providing the flight itself, which will be provided by the airline.
- (b) the entity has inventory risk for the tickets because they are purchased before they are sold to the entity's customers and the entity is exposed to any loss as a result of not being able to sell the tickets for more than the entity's cost.
- (c) the entity has discretion in setting the sales prices for tickets to its customers.

The entity concludes that its promise is to provide a ticket (i.e. a right to fly) to the customer. On the basis of the indicators, the entity concludes that it controls the ticket before it is transferred to the customer. Thus, the entity concludes that it is a principal in the transaction and recognises revenue in the gross amount of consideration to which it is entitled in exchange for the tickets transferred.

Question 5 : Jan 2021 – Paper

On 1st April 2019, Big Limited acquired a 35 interest in Dig Limited and achieved a significant influence. The cost of the investment was Rs.3,00,000. Dig Limited has net assets of Rs.5,50,000 as on 1st April 2019. The fair value of those net assets is Rs.6,50,000, since the fair value of property, plant and equipment is Rs.1,00,000 higher than its book value. This property, plant and equipment have a remaining useful life of 8 years. For the financial year 2019-2020, Dig Limited earned a profit (after tax) of Rs.1,00,000 and paid a dividend of Rs.11,000 out of these profits. Dig Ltd. has also recognized the loss of Rs.15,000, that arose from re-measurement of defined benefit directly in 'Other Comprehensive Income'.

Calculate Big Ltd.'s interest in Dig Ltd. as at the year ended 31st March 2020 under the relevant method.

Solution :

Calculation of Big Ltd.'s interest in Dig Ltd at the year ended 31st March, 2020 as per Equity method:

	Amount (Rs.)
Cost of investment (35%)	3,00,000

Share in profit after adjustment (Refer Working Note)	30,625
Dividend received by Big Ltd from Dig Ltd (35% x Rs.11,000)	(3,850)
Big Ltd.'s share of loss in OCI w.r.t Dig Ltd .'s loss from remeasurement of defined benefit liability (35% x Rs.15,000)	<u>(5,250)</u>
Big Ltd.'s interest in Dig Ltd at the end of the year	<u>3,21,525</u>

Working Note:

Computation of Share in profit after adjustment

	Amount (Rs.)
Big Ltd.'s share of Dig Ltd.'s after tax profit (35% x Rs.1,00,000)	35,000
Less: Big Ltd.'s share of depreciation based on fair value (35% x Rs.12,500)	<u>(4,375)</u>
Share in profit after adjustment	<u>30,625</u>

Question 6 : May 2025 – RTP

X Ltd. acquired a 10% interest in V Ltd. for Rs. 50,000 on 1st June, 20X6. The investment in V Ltd. was accounted for as equity investment (not held for trading) for which irrevocable option has been availed for subsequent measurement of financial assets at FVTOCI. X Ltd. recognized an increase in fair value of Rs. 30,000 in other comprehensive income for the year ended 31st March, 20X7.

X Ltd. acquired an additional 25% interest in V Ltd. for Rs. 2,00,000 on 1st April, 20X7 and achieved significant influence. The fair value of V Ltd.'s net assets was Rs. 2,50,000 at June, 20X6 and had increased to Rs. 4,00,000 on 1st April, 20X7. V Ltd. recorded profits after dividends of Rs. 1,00,000 between 1st June, 20X6 and 1st April, 20X7.

How should X Ltd. account for an investment in V Ltd. on account of piecemeal acquisition when such investment provides X Ltd. significant influence over V Ltd.? Pass necessary journal entries for the same.

Solution :

While applying equity method, paragraph 10 of Ind AS 28 requires, the investment in an associate to be initially recognized at cost. However, it doesn't include any specific guidance on how to account for existing investment, which is accounted for under Ind AS 109, that subsequently becomes an associate or a joint venture. One may apply the fair value approach, by drawing an analogy from paragraph 42 of Ind AS 103.

Paragraph 42 of Ind AS 103, 'Business Combinations', deals with the situation where control over an acquiree is achieved in stages. In such a case, the acquirer shall remeasure its previously held equity interest in the acquiree at its acquisitions- date fair value and recognize the resulting gain or loss, if any, in profit or loss or OCI, as appropriate. In prior reporting periods, the acquirer may have recognized changes in the value of its equity interest in the acquiree on OCI. If so, the amount that was recognized in OCI shall be recognized on the same basis as would be required if the acquirer had disposed directly of the previously held equity interest.

On application of the above guidance, following accounting will be done:

Computation of goodwill on gaining significant influence on V Ltd.

Particulars	Rs.
Fair value of previously held 10% interest [2,00,000/25% x10%]	80,000
Fair value of additional 25% (amount paid)	<u>2,00,000</u>
Cost of investment in associate V Ltd.	2,80,000
Less: Fair value of identifiable net assets acquired (4,00,000 x 35%)	<u>(1,40,000)</u>
Goodwill	<u>1,40,000</u>

Journal Entries

Particulars		Amount (Rs.)	Amount (Rs.)
Investment A/c (10%)	Dr.	30,000	
To OCI (Equity)			30,000
Investment in Associates A/c (35%)	Dr.	2,80,000	
To Bank A/c			2,00,000
To Investment (FVTOCI) (10%)			80,000
OCI (Equity)	Dr.	30,000	
To Retained Earning			30,000

Question 7 : Sept 2025 – RTP

H Ltd. purchased a 100% subsidiary S Ltd. for Rs. 500,000 at the end of March, 20X3, when the fair value of the S Ltd.'s net assets was Rs. 400,000. H Ltd. sold 60% of its investment in the S Ltd. in March, 20X5 for Rs. 675,000, leaving H Ltd. with 40% investment and significant influence. At the date of disposal, the carrying value of the net assets of S Ltd., excluding goodwill, is Rs. 800,000. The fair value of the investment in S Ltd. retained is proportionate to the fair value of the 60% investment sold.

Required:

Compute gain or loss for H Ltd. on sale of 60% stake in S Ltd. for the purpose of separate financial statements and consolidated financial statements.

Solution :

(i) Computation of gain on the sale of 60% investment in Separate Financial Statements of H Ltd.'s for the year ended 31st March, 20X5

	Rs.
Sale proceeds	6,75,000
Less: Cost of investment in S Ltd. (5,00,000 x 60%)	<u>(3,00,000)</u>
Gain on sale in the parent's financial statements	<u>3,75,000</u>

(ii) Computation of gain on the sale of 60% investment in Consolidated Financial Statements of H Ltd.'s for the year ended 31st March, 20X5

In the consolidated financial statements, the group will calculate the gain or loss on disposal differently. The carrying amounts of all of the assets, including goodwill and the full amount of any cumulative exchange differences and any FVOCI-reserve previously recognised in equity, are de-recognised. when control is lost. This is compared to the proceeds received and the fair value of the investment retained.

The gain on disposal will be calculated as follows:

	Rs.
Sale proceeds	6,75,000
Add: Fair value of 40% interest retained	<u>4,50,000</u>
	11,25,000
Less: Net assets disposed, including goodwill (8,00,000 + 1,00,000)	<u>(9,00,000)</u>
Gain on sale in the group's financial statements	2,25,000

This gain on loss of control would be recorded in profit or loss. The gain or loss includes the gain of Rs. 1,35,000 (Rs. 6,75,000 - (Rs. 9,00,000 x 60%)) on the portion sold. However, it also includes a gain on remeasurement of the 40% retained interest of Rs. 90,000 (Rs. 4,50,000 - Rs. 3,60,000). The entity will need to disclose the portion of the gain that is attributable to remeasuring any remaining interest to fair value that is Rs. 90,000).

Question 8 : Sept 2025 – RTP

Beta Limited (investee) has issued 2,000 equity shares which are outstanding at the reporting date. On this date, Beta issues 1,000 share options to its employees, which can be converted into 1,000 equity shares of Beta. The grant-date fair value of each option issued is Rs. 1. The options will vest over five years and all 1,000 options are expected to vest.

Beta recognises share-based remuneration expense of Rs. 200 in its profit or loss and an offsetting credit to equity in the current year. Alpha Limited (investor) holds 600 shares of Beta. Alpha has significant influence over Beta. Alpha recognises its share of the remuneration expense in its profit or loss as part of income from the equity-accounted investees. It records the offsetting credit as a reduction of its investment in Beta.

At the end of the vesting period, all options vest and are exercised. The exercise price is Rs. 3 per option. The face value per share is Rs. 1.

Required

- (i) Pass journal entries in the books of Beta Limited and Alpha Limited for recording share-based payment expenses for the first year.
- (ii) Pas Journal entries for exercising of option in the 5th year, in the books of Beta Limited.
- (iii) In the books of Alpha Limited, compute the loss on dilution of shares of Beta Limited and pass journal entries for the same. Beta has net assets totalling Rs. 11,000, immediately before the shares are issued.

Solution :

(i) **Journal Entries to be recorded over the five-year vesting period:**

		Rs.	Rs.
In Beta's books			
Share based payments remuneration (profit or loss)	Dr.	200	
To Shareholders' equity (ESOP reserve)			200
(To recognise share based payment at associate level)			
In Alpha's books			
Share based payment remuneration (profit or loss)	Dr.	60	
Investment in associate			60
(To recognise share based payment at investor level)			

(ii) **Journal Entries in the books of Beta to recognise share issue:**

		Rs.	Rs.
Cash	Dr.	3,000	
Shareholders' equity (ESOP reserve)	Dr.	1,000	
To Share capital			1,000
To Share premium			3,000
(To recognise exercise of options at the associate level)			

(iii) **Accounting in the Financial Statements of Alpha**

The issue of new share options results in a dilution of Alpha's interest in Beta by 10% [$30\% - \{(600/(2,000 + 1000) \times 100)\}$]. However, Alpha maintains significant influence over Beta. Alpha calculates loss on dilution as below.

Alpha's share of net assets before exercise (11,000 x 30%)	3,300
Alpha's share of net assets after exercise ((11,000+3,000) x 20%)	<u>(2,800)</u>
Cumulative adjustment required	500
Less: Adjustment previously recognized for share based payment expense (60 x 5 years)	<u>(300)</u>
Loss on dilution	<u>200</u>

Alpha passes the following entry to recognise dilution

		Rs.	Rs.
Loss on dilution (profit or loss)	Dr.	200	
To Investment in associate			200
(To recognize dilution of investment in associate)			

Thanks



IND AS – 111

JOINT ARRANGEMENTS

CHAPTER - 31

Question 1 : May 2020 – RTP

AB Limited and BC Limited establish a joint arrangement through a separate vehicle PQR, but the legal form of the separate vehicle does not confer separation between the parties and the separate vehicle itself. Thus, both the parties have rights to the assets and obligations for the liabilities of PQR. As neither the contractual terms nor the other facts and circumstances indicate otherwise, it is concluded that the arrangement is a joint operation and not a joint venture.

Both the parties own 50% each of the equity interest in PQR. However, the contractual terms of the joint arrangement state that AB Limited has the rights to all of Building No. 1 owned by PQR and the obligation to pay all of the debt owed by PQR to a lender XYZ. AB Limited and BC Limited have rights to all other assets in PQR, and obligations for all other liabilities of PQR in proportion of their equity interests (i.e. 50% each).

PQR's summarized balance sheet is as follows:

	(Rs. in crore)
	Amount
Building 1	240
Building 2	200
Cash	40
Total Assets	480
Equity	140
Debt owed to XYZ	240
Employee benefit plan obligation	100
Total Liabilities	480

How would AB Limited present its interest in PQR in its financial statements?

Solution :

Ind AS 111 states that “a joint operator shall recognise in relation to its interest in a joint operation:

- its assets, including its share of any assets held jointly;
- its liabilities, including its share of any liabilities incurred jointly;
- its revenue from the sale of its share of the output arising from the joint operation;
- its share of the revenue from the sale of the output by the joint operation; and
- its expenses, including its share of any expenses incurred jointly.”

The rights and obligations, as specified in the contractual arrangement, that an entity has with respect to the assets, liabilities, revenue and expenses relating to a joint operation might differ

from its ownership interest in the joint operation. Thus a joint operator needs to recognise its interest in the assets, liabilities, revenue and expenses of the joint operation on the basis (bases) specified in the contractual arrangement, rather than in proportion of its ownership interest in the joint operation.

Thus, AB Limited would record the following in its financial statements, to account for its rights to the assets of PQR and its obligations for the liabilities of PQR.

	Rs. in crore
Assets	
Cash	20
Building 1*	240
Building 2	100
Liabilities	
Debt owned to XYZ (third party)**	240
Employees benefit plan obligation	50

* Since AB Limited has the rights to all of Building No. 1, it records the amount in its entirety.

** AB Limited has obligation for the debt owed by PQR to XYZ in its entirety.

Question 2 : May 2022 – RTP

Identify the type of joint arrangements in each of the following scenarios:

- (i) X Ltd and Y Ltd, manufacturing similar type of mobile phones, form a joint arrangement to manufacture and sell mobile phones. Under the terms of the arrangement, both X Ltd and Y Ltd are to use their own assets to manufacture the mobile phones and both are responsible for liabilities related to their respective manufacture. The arrangement also lays down the distribution revenues from the sale of the mobile phones and expenses incurred thereof. X Ltd however has exclusive control over the marketing and distribution functions and does not require the consent of Y Ltd in this aspect. No separate entity is created for the arrangement.
- (ii) Continuing with (i) above, what would be the classification of the joint arrangement if X Ltd and Y Ltd both jointly control all the relevant activities of the Joint arrangement including the marketing and the distribution functions?
- (iii) What would be the classification of the joint arrangement if under the terms of the arrangement, a separate entity is created to manufacture the mobile phones.
- (iv) Continuing with (iii) above, the joint arrangement is a means of manufacturing mobile phones on a common platform but the output of the joint arrangement is purchased by both X Ltd and Y Ltd in the ratio of 50:50. The joint arrangement cannot sell output to third parties. The price of the output sold to X Ltd and Y Ltd is set by both the parties to the arrangement to cover the production costs and other administrative costs of the joint arrangement entity.
- (v) Would your answer in (iv) above be different if X Ltd and Y Ltd sold their respective share of output to third parties?

- (vi) Assume that in (iv) above, the contractual terms of the arrangement were modified so that the joint arrangement entity is not obliged to sell the output to X Ltd and Y Ltd but was able to sell the output to third parties.

Solution :

For a joint arrangement to be either a *joint operation* or *joint venture*, it depends on whether the parties to the joint arrangement have rights to the assets and obligations for liabilities (will be a joint operation) OR whether the parties to the joint arrangement have rights to the net assets of the arrangement (will be joint venture).

- (i) In order to fit into the definition of a joint arrangement, the parties to the joint arrangement should have joint control over the arrangement. In the given case, decisions relating to relevant activities, ie, marketing and distribution, are solely controlled by X Ltd and such decisions do not require the consent of Y Ltd. Hence, the joint control test is not satisfied in this arrangement and the arrangement does not fit into the definition of a joint arrangement in accordance with the Standard.
- (ii) Where X Ltd and Y Ltd both jointly control all the relevant activities of the arrangement and since no separate entity is formed for the arrangement, the joint arrangement is in the nature of a *joint operation*.
- (iii) Where under a joint arrangement, a separate vehicle is formed to give effect to the joint arrangement, then the joint arrangement can either be a *joint operation* or a *joint venture*. Hence in the given case, if:
- (a) The contractual terms of the joint arrangement, give both X Ltd and Y Ltd rights to the assets and obligations for the liabilities relating to the arrangement, and the rights to the corresponding revenues and obligations for the corresponding expenses, *then the joint arrangement will be in the nature of a joint operation*.
- (b) The contractual terms of the joint arrangement, give both X Ltd and Y Ltd. rights to the net assets of the arrangement, *then the joint arrangement will be in the nature of a joint venture*.
- (iv) Where the rights to assets and liabilities to obligations are not clear from the contractual arrangement, then other facts and circumstances also need to be considered to determine whether the joint arrangement is a joint operation or a joint venture.

When the provision of the activities of the joint venture is primarily to produce output and the output is available / distributed only to the parties to the joint arrangement in some pre-determined ratio, then this indicates that the parties have substantially all the economic benefits of the assets of the arrangement. The only source of cash flows to the joint arrangement is receipts from parties through their purchases of the output and the parties also have a liability to fund the settlement of liabilities of the separate entity. Such an arrangement indicates that the joint arrangement is in the nature of a *joint operation*. In the given case, the output of the joint arrangement is exclusively used by X Ltd. and Y Ltd. and the joint arrangement is not allowed to sell the output to outside parties. Hence, the joint arrangement between X Ltd. and Y Ltd. is in the nature of a *joint operation*.

- (v) It makes no difference whether the output of the joint arrangement is exclusively for use by the parties to the joint arrangement or the parties to the arrangement sold their share of the output to third parties.
Hence, even if X Ltd. and Y Ltd. sold their respective share of output to third parties, the fact still remains that the joint arrangement cannot sell output directly to third parties. Hence, the joint arrangement will still be deemed to be in the nature of *a joint operation*.
- (vi) Where the terms of the contractual arrangement enable the separate entity to sell the output to third parties, this would result in the separate entity assuming demand, inventory and credit risks. Such facts and circumstances would indicate that the arrangement is a joint venture.

Question 3 : Nov 2023 – RTP

Entities A and B establish a 50:50 joint operation in the form of a separate legal entity, Entity J, whereby each operator has a 50% ownership interest and takes 50% of the output.

On formation of the joint operation, Entity A contributes a property with fair value of Rs. 110 lakhs and intangible asset with fair value of Rs. 10 lakhs whereas Entity B contributes equipment with a fair value of Rs. 120 lakhs.

The carrying amounts of the assets contributed by Entities A and B are Rs. 100 lakhs and Rs. 80 lakhs, respectively.

What will be the amount of any gain or loss to be recognised by Entity A and Entity B in its separate financial statements as well as consolidated financial statements?

Solution :

Paragraph B34 of Ind AS 111 states that when an entity enters into a transaction with a joint operation in which it is a joint operator, such as a sale or contribution of assets, it is conducting the transaction with the other parties to the joint operation and, as such, the joint operator shall recognise gains and losses resulting from such a transaction only to the extent of the other parties' interests in the joint operation.

The amount of gain or loss to be recognised by Entity A in its separate financial statements as well as consolidated financial statements will be computed as below

(All amounts are Rs. in lakhs)

A's share of fair value of asset contributed by Entity B (50% x Rs. 120 lakhs)	60
Less: Asset contributed by Entity A to the joint operation – carrying amount of proportion ceded to Entity B (50% x Rs. 100 lakhs)	<u>(50)</u>
Gain to be recognised by Entity A	<u>10</u>

The gain can alternatively be calculated as:

Share acquired in fair value of net assets of joint operation (50% x Rs. 120 lakhs)	120
Less: Carrying amount of asset contributed	(100)
Less: Unrealised portion of gain on asset contributed	(10)

(50% × (Rs. 120 lakhs – Rs. 100 lakhs))	_____
Gain to be recognised by Entity A	<u>10</u>

The amount of gain or loss to be recognised by Entity B in its separate financial statements as well as consolidated financial statements will be computed as below:

(All amounts are Rs. in lakhs)

B's share of fair value of asset contributed by Entity A (50% x Rs. 120 lakhs)	60
Less: Asset contributed by Entity A to the joint operation – carrying amount of proportion ceded to Entity B (50% x Rs. 100 lakhs)	<u>(40)</u>
Gain to be recognised by Entity B	<u>20</u>

The gain can alternatively be calculated as:

Share acquired in fair value of net assets of joint operation (50% x Rs. 240 lakhs)	120
Less: Carrying amount of asset contributed	(80)
Less: Unrealised portion of gain on asset contributed (50% × (Rs. 120 lakhs – Rs. 80 lakhs))	<u>(20)</u>
Gain to be recognised by Entity B	<u>20</u>

Question 4 : Nov 2024 – RTP

P Limited and Q Limited enter into a contractual arrangement to buy a building that has 12 floors, which they will lease to other parties. P Limited and Q Limited are authorised to lease five floors each. P Limited and Q Limited can unilaterally make all decisions related to their respective floors and are entitled to all of the income from those floors. The remaining two floors will be jointly managed – all decisions concerning these two floors must be unanimously agreed to between P Limited and Q Limited who will share net profits or net losses in respect of these two floors equally, i.e. they both have the rights to the net assets of the arrangement. The leasing of property is determined to be the relevant activity.

Whether this arrangement is a joint operation or a joint venture?

Solution :

Paragraphs 15-17 of Ind AS 111 state that a joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets and obligations for the liabilities, relating to the arrangement. Those parties are called joint operators.

Further, a joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. Those parties are called joint venturers.

Furthermore, an entity applies judgement when assessing whether a joint arrangement is a joint operation or a joint venture. An entity shall determine the type of joint arrangement in which it is involved by considering its rights and obligations arising from the arrangement. An entity assesses its rights and obligations by considering the structure and legal form of the arrangement,

the terms agreed by the parties in the contractual arrangement and, when relevant, other facts and circumstances.

In the given case, accounting by P Limited and Q Limited would be as follows:

(i) Five floors that P Limited controls

Five floors that are controlled by P Limited shall be accounted for by P Limited as investment property under Ind AS 40, Investment Property, which defines the term 'investment property' as property (land or a building—or part of a building—or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both, rather than for:

- (a) use in the production or supply of goods or services or for administrative purposes; or
- (b) sale in the ordinary course of business.

(ii) Five floors that Q Limited controls

Five floors that are controlled by Q Limited shall be accounted for by Q Limited as investment property under Ind AS 40.

(iii) Two floors that P Limited and Q Limited jointly control

For the two floors that are jointly controlled by P Limited and Q Limited, as per the contractual arrangement, both P Limited and Q Limited will share net profits or net losses equally i.e. they both have the rights to the net assets of the arrangement. Thus, the arrangement in respect of these two floors is a joint venture and shall be accounted for accordingly by P Limited and Q Limited.

Thanks



IND AS – 27

SEPARATE FINANCIAL STATEMENTS

CHAPTER - 32

Question 1 : Nov 2020 – RTP

A company, AB Ltd. holds investments in subsidiaries and associates. In its separate financial statements, AB Ltd. wants to elect to account its investments in subsidiaries at cost and the investments in associates as financial assets at fair value through profit or loss (FVTPL) in accordance with Ind AS 109, Financial Instruments. Whether AB Limited can carry investments in subsidiaries at cost and investments in associates in accordance with Ind AS 109 in its separate financial statements?

Solution :

Ind AS 27, Separate Financial Statements inter-alia provides that, when an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109, Financial Instruments in its separate financial statements. Further, the entity shall apply the same accounting for each category of investments.

It may be noted that although the 'category' is used in number of Standards, it is not defined in any of the Ind AS. It seems that subsidiaries, associates and joint ventures would qualify as separate categories. Thus, the same accounting policies are applied for each category of investments - i.e. each of subsidiaries, associates and joint ventures. However, paragraph 10 of Ind AS 27 should not be read to mean that, in all circumstances, all investments in associates are one 'category' of investment and all investments in joint ventures or an associate are one 'category' of investment. These categories can be further divided into sub-categories provided the sub-category can be defined clearly and objectively and results in information that is relevant and reliable. For example, an investment entity parent can have investment entity subsidiary (at fair value through profit or loss) and non-investment entity subsidiary (whose main purpose is to provide services that relate to the investment entity's investment activities) as separate categories in its separate financial statements. In the present case, investment in subsidiaries and associates are considered to be different categories of investments. Further, Ind AS 27 requires to account for the investment in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109 for each category of Investment. Thus, AB Limited can carry its investments in subsidiaries at cost and its investments in associates as financial assets in accordance with Ind AS 109 in its separate financial statements.

Question 2 : Nov 2020 – Paper

Entity H holds a 20% equity interest in Entity S (an associate) that in turn has a 100% equity interest in Entity T. Entity S recognised net assets relating to Entity T of Rs. 10,000 in its consolidated financial statements. Entity S sells 20% of its interest in Entity T to a third party (a non-controlling shareholder) for Rs. 3,000 and recognises this transaction as an equity transaction in accordance with the provisions of Ind AS 110, resulting in a credit in Entity S's equity of Rs.1,000.

The financial statements of Entity H and Entity S are summarised as follows before and after the transaction:

Before

H's consolidated financial statements

Assets	(Rs.)	Liabilities	(Rs.)
Investment in S	<u>2,000</u>	Equity	<u>2,000</u>
Total	<u>2,000</u>	Total	<u>2,000</u>

S's consolidated financial statements

Assets	(Rs.)	Liabilities	(Rs.)
Assets (from T)	<u>10,000</u>	Equity	<u>10,000</u>
Total	<u>10,000</u>	Total	<u>10,000</u>

The financial statements of S after the transaction are summarised below:

After

S's consolidated financial statements

Assets	(Rs.)	Liabilities	(Rs.)
Assets (from T)	10,000	Equity	10,000
Cash	3,000	Equity transaction Impact with non- controlling interest	<u>1,000</u>
		Equity attributable to owners	11,000
		Non-controlling interest	2,000
Total	13,000	Total	13,000

Although Entity H did not participate in the transaction, Entity H's share of net assets in Entity S increased as a result of the sale of S's 20% interest in T. Effectively, H's share in S's net assets is now Rs. 2,200 (20% of Rs. 11,000) i.e., Rs. 200 in addition to its previous share.

How this equity transaction that is recognised in the financial statements of Entity S reflected in the consolidated financial statements of Entity H that uses the equity method to account for its investment in Entity S?

Solution :

Ind AS 28 defines the equity method as “a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition change in the investor’s share of the investee’s net assets. The investor’s profit or loss includes its share of the

investee's profit or loss and the investor's other comprehensive income includes its share of the investee's other comprehensive income."

Ind AS 28, states, inter alia, that when an associate or joint venture has subsidiaries, associates or joint ventures, the profit or loss, other comprehensive income, and net assets taken into account in applying the equity method are those recognised in the associate's or joint venture's financial statements (including the associate's or joint venture's share of the profit or loss, other comprehensive income and net assets of its associates and joint ventures), after any adjustments necessary to give effect to uniform accounting policies.

The change of interest in the net assets / equity of the associate as a result of the investee's equity transaction is reflected in the investor's financial statements as 'share of other changes in equity of investee' (in the statement of changes in equity) instead of gain in Statement of profit and loss, since it reflects the post-acquisition change in the net assets of the investee as per the provisions of Ind AS 28 and also faithfully reflects the investor's share of the associate's transaction as presented in the associate's consolidated financial statements.

Thus, in the given case, Entity H recognises Rs. 200 as change in other equity instead of in statement of profit and loss and maintains the same classification as of its associate, Entity S, i.e., a direct credit to equity as in its consolidated financial statements.

Question 3 : Nov 2021 – RTP

A company, AB Ltd. holds investments in subsidiaries and associates. In its separate financial statements, AB Ltd. wants to elect to account its investments in subsidiaries at cost and the investments in associates as financial assets at fair value through profit or loss (FVTPL) in accordance with Ind AS 109, Financial Instruments.

Whether AB Limited can carry investments in subsidiaries at cost and investments in associates in accordance with Ind AS 109 in its separate financial statements?

Solution :

Paragraph 10 of Ind AS 27 'Separate Financial Statements' *inter-alia* provides that, when an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109 'Financial Instruments' in its separate financial statements. Further, the entity shall apply the same accounting for each category of investments.

It may be noted that although the 'category' is used in number of Standards, it is not defined in any of the Ind AS. It seems that subsidiaries, associates and joint ventures would qualify as separate categories. Thus, the same accounting policies are applied for each category of investments - i.e. each of subsidiaries, associates and joint ventures. However, paragraph 10 of Ind AS 27 should not be read to mean that, in all circumstances, all investments in associates are one 'category' of investment and all investments in joint ventures or an associate are one 'category' of investment. These categories can be further divided into sub-categories provided the sub-category can be defined clearly and objectively and results in information that is relevant and reliable. For example, an investment entity parent can have investment entity subsidiary (at fair value through profit or loss) and non-investment entity subsidiary (whose main purpose is to

provide services that relate to the investment entity's investment activities) as separate categories in its separate financial statements.

In the present case, investment in subsidiaries and associates are considered to be different categories of investments. Further, Ind AS 27 requires to account for the investment in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109 for each category of Investment. Thus, AB Limited can carry its investment in subsidiaries at cost and its investments in associates as financial assets in accordance with Ind AS 109 in its separate financial statements.

Thanks



IND AS – 32, 107, 109

FINANCIAL INSTRUMENTS

CHAPTER - 33

Question 1 : May 2018 – RTP

On 1st April, 20X4, Shelter Ltd. issued 5,000, 8% convertible debentures with a face value of Rs.100 each maturing on 31st March, 20X9. The debentures are convertible into equity shares of Shelter Ltd. at a conversion price of Rs.105 per share. Interest is payable annually in cash. At the date of issue, Shelter Ltd. could have issued non-convertible debt with a 5 year term bearing a coupon interest rate of 12%. On 1st April, 20X7, the convertible debentures have a fair value of Rs.5,25,000. Shelter Ltd. makes a tender offer to debenture holders to repurchase the debentures for Rs.5,25,000, which the holders accepted. At the date of repurchase, Shelter Ltd. could have issued non-convertible debt with a 2 year term bearing a coupon interest rate of 9%. Show accounting entries in the books of Shelter Ltd. for recording of equity and liability component:

- At the time of initial recognition and
- At the time of repurchase of the convertible debentures.

The following present values of Rs. 1 at 8%, 9% & 12% are supplied to you:

Interest Rate	Year 1	Year 2	Year 3	Year 4	Year 5
8%	0.926	0.857	0.794	0.735	0.681
9%	0.917	0.842	0.772	0.708	0.65
10%	0.893	0.797	0.712	0.636	0.567

Solution :

- At the time of initial recognition

	Rs.
Liability component	
Present value of 5 yearly interest payments of Rs.40,000, discounted at 12% annuity (40,000 x 3.605)	1,44,200
Present value of Rs.5,00,000 due at the end of 5 years, discounted at 12%, compounded yearly (5,00,000 x 0.567)	2,83,500
	4,27,700
Equity component	
(Rs.5,00,000 – Rs.4,27,700)	72,300
Total proceeds	5,00,000

Note:

- Since rs.105 is the conversion price of debentures into equity shares and not the redemption price, the liability component is calculated @ Rs.100 each only.

Journal Entry

		Rs.	Rs.
Bank	Dr.	5,00,000	
To 8% Debentures (Liability component)			4,27,700
To 8% Debentures (Equity component)			72,300
(Being Debentures are initially recorded a fair value)			

2) Conversion is assumed at option of investor.

(ii) **At the time of repurchase of convertible debentures**

The repurchase price is allocated as follows:

	Carrying Value @ 12%	Fair Value @ 9%	Difference
	Rs.	Rs.	Rs.
Liability component			
Present value of 2 remaining yearly interest payments of Rs.40,000, discounted at 12% and 9%, respectively	67,600	70,360	
Present value of Rs.5,00,000 due in 2 years, discounted at 12% and 9%, compounded yearly, respectively	<u>3,98,500</u>	<u>4,21,000</u>	
Liability component	4,66,100	4,91,360	(25,260)
Equity component			
(5,25,000 - 4,91,360)	<u>72,300</u>	<u>33,640*</u>	<u>38,660</u>
Total	<u>5,38,400</u>	<u>5,25,000</u>	<u>13,400</u>

*(5,25,000 – 4,91,360) = 33,640

Journal Entries

		Rs.	Rs.
8% Debentures (Liability component)	Dr.	4,66,100	
Profit and loss A/c (Debt settlement expense)	Dr.	25,260	
To Bank A/c			4,91,360
(Being the repurchase of the liability component recognised)			
8% Debentures (Equity component)	Dr.	72,300	
To Bank A/c		33,640	
To Reserves and Surplus A/c			38,660
(Being the cash paid for the equity component recognised)			

Question 2 : May 2018 – PAPER

S Limited issued redeemable preference shares to its Holding Company -H Limited. The terms of the instrument have been summarized below. Analyse the given situation, applying the guidance in Ind AS 109 'Financial Instruments', and account for this in the books of H Limited.

Nature	Non-cumulative redeemable preference shares
Repayment	Redeemable after 3 years
Date of Allotment	1st April 2015
Date of Repayment	31st March 2018
Total Period	3 Years
Value of Preference Shares issued	5,00,00,000
Dividend Rate	0.0001% Per Annum
Market rate of interest	12% Per Annum
Present value factor	0.7118

Solution :

Applying Ind AS 109 a financial asset shall be recorded a fair value upon initial recognition. According fair value of investment in S Ltd. shall be.

$$50,00,000 \times 0.7118 = 3,55,90,000$$

Note : Dividend is ignored as the amount is small making it insignificant.

∴ Balance 5,00,000 = 3,55,90,000 = 1,44,10,000 shall be treated as equity

1.4.2015	Preference shares (FA)	3,55,90,000	
	Investment (Equity)	1,44,10,000	
	To Bank		5,00,00,000

Subsequently preference shares shall be carried over at amortised cost.

Year	Opening Balance	Interest (12%)	CF	C/O.
1	3,55,90,000	42,70,800	-	3,98,60,800
2	3,98,60,800	47,83,296	-	4,46,44,096
3	4,46,44,096	53,55,904	5,00,00,000	-

31.3.16	Preference shares (FA)	42,70,800	
	To Interest		42,70,800
31.3.17	Preference shares (FA)	47,83,296	
	To Interest		47,83,296
31.3.18	Preference shares (FA)	53,55,904	
	To Interest		53,55,904
31.3.18	Bank	5,00,00,000	
	To Preference shares		5,00,00,000

Question 3 : May 2018 – PAPER

On 1st January 2017, Expo Limited agreed to purchase USD (\$) 40,000 from E&I Bank in future on 31st December 2017 for a rate equal to Rs. 65 per USD. Expo Limited did not pay any amount upon entering into the contract. Expo Limited is a listed company in India and prepares its financial statements on a quarterly basis.

Using the definition of derivative included in Ind AS 109 and following the principles of recognition and measurement as laid down in Ind AS 109, you are required to record the entries for each quarter ended till the date of actual purchases of USD.

For the purpose of accounting, use the following information representing marked to market fair value of forward contracts at each reporting date:

As at 31st March, 2017	Rs.(50,000)
As at 30th June, 2017	Rs.(30,000)
As at 30th September, 2017	Rs.24,000
Spot rate of USD on 31st December, 2017	Rs.62 per USD

Solution :

1) Assessment of the arrangement using the definition of derivative included under Ind AS 109.

Derivative is a financial instrument or other contract within the scope of this Standard with all three of the following **characteristics**:

- (a) its value changes in response to the change in foreign exchange rate (emphasis laid)
- (b) it requires no initial net investment or an initial net investment is smaller than would be required for other types of contracts with similar response to changes in market factors.
- (c) it is settled at a future date.

Upon evaluation of contract in question, on the basis of the definition of derivative, it is noted that the contract meets the definition of a derivative as follows:

- (a) the value of the contract to purchase USD at a fixed price changes in response to changes in foreign exchange rate.
- (b) the initial amount paid to enter into the contract is zero. A contract which would give the holder a similar response to foreign exchange rate changes would have required an investment of USD 40,000 on inception.
- (c) the contract is settled in future

The derivative is a forward exchange contract.

As per Ind AS 109, derivatives are measured at fair value upon initial recognition and are subsequently measured at fair value through profit and loss.

2) Accounting in each Quarter

(i)	1.1.2017	No Entry	Fair Value is Nil	
(ii)	31.3.2017	Loss (P & L)	50,000	
		To FC (FL)		50,000
(iii)	30.6.2017	FC (FL)	20,000	

		To gain (P & L)	20,000
(iv)	30.9.2017	FC (FL)	30,000
		FC (FA)	24,000
		To gain (P & L)	54,000
(v)	31.12.2017	Bank (USD) (40,000 × 62)	24,80,000
		Loss (P & L)	1,44,000
		To FC(FA)	24,000
		To Bank (40,000 × 65)	26,00,000

Question 4 : Nov 2018 – PAPER

On 1st April 2017, A Ltd. lent Rs.2 crores to a supplier in order to assist them with their expansion plans. The arrangement of the loan cost the company Rs. 10 lakhs. The company has agreed not to charge interest on this loan to help the supplier's short-term cash flow but expected the supplier to repay Rs.2.40 crores on 31st March 2019. As calculated by the finance team of the company, the effective annual rate of interest on this loan is 6.9% On 28th February 2018, the company received the information that poor economic climate has caused the supplier significant problems and in order to help them, the company agreed to reduce the amount repayable by them on 31st March 2019 to Rs.2.20 crores. Suggest the accounting entries as per applicable Ind AS.

Solution :

The loan to the supplier would be regarded as a financial asset. The relevant accounting standard Ind AS 109 provides that financial assets are normally measured at fair value.

If the financial asset in which the only expected future cash inflows are the receipts of principal and interest and the investor intends to collect these inflows rather than dispose of the asset to a third party, then Ind AS 109 allows the asset to be measured at amortised cost using the effective interest method.

If this method is adopted, the costs of issuing the loan are included in its initial carrying value rather than being taken to profit or loss as an immediate expense. This makes the initial carrying value Rs.2,10,00,000.

Under the effective interest method, part of the finance income is recognised in the current period rather than all in the following period when repayment is due. The income recognised in the current period is Rs.14,49,000 (Rs.2,10,00,000 × 6.9%)

In the absence of information regarding the financial difficulties of the supplier the financial asset at 31st March, 2018 would have been measured at Rs.2,24,49,000 (Rs.2,10,00,000 + 14,49,000). The information regarding financial difficulty of the supplier is objective evidence that the financial asset suffered impairment at 31st March 2018.

The asset is re-measured at the present value of the revised estimated future cash inflows, using the original effective interest rate. Under the revised estimates the closing carrying amount of the asset would be Rs.2,05,79,981 (Rs.2,20,00,000 / 1.069). The reduction in carrying value of

Rs.18,69,019 (Rs.2,24,49,000 – 2,05,79,981) would be charged to profit or loss in the current period as an impairment of a financial asset.

Therefore, the net charge to profit or loss in respect of the current period would be Rs.4,20,019 (18,69,019 – 14,49,000).

Question 5 : Nov 2018 – PAPER

NAV Limited granted a loan of Rs.120 lakh to OLD Limited for 5 years @ 10% p.a. which is Treasury bond yield of equivalent maturity. But the incremental borrowing rate of OLD Limited is 12%. In this case, the loan is granted to OLD Limited at below market rate of interest. Ind AS 109 requires that a financial asset or financial liability is to be measured at fair value at the initial recognition. Should the transaction price be treated as fair value? If not, find out the fair value. What is the accounting treatment of the difference between the transaction price and the fair value on initial recognition in the book of NAV Ltd.?

Present value factors at 12%:

Year	1	2	3	4	5
PVF	0.892	0.797	0.712	0.636	0.567

Solution :

Since the loan is granted to OLD Ltd at 10% i.e below market rate of 12%. It will be considered as loan given at off market terms. Hence the Fair value of the transaction will be lower from its transaction price & not the transaction price.

Calculation of fair value

Year	Future cash flow (in lakh)	Discounting factor @ 12%	Present value (in lakh)
1	12	0.892	10.704
2	12	0.797	9.564
3	12	0.712	8.544
4	12	0.636	7.632
5	120+12=132	0.567	<u>74.844</u>
			<u>111.288</u>

The fair value of the transaction be Rs.111.288 lakh.

Since fair value is based on level 1 input or valuation technique that uses only data from observable markets, difference between fair value and transaction price will be recognized in Profit and Loss as fair value loss i.e Rs.120 lakh– Rs.111.288 lakh= Rs.8.712 lakh.

Question 6 : Nov 2018 – PAPER

Veer Limited issues convertible bonds of Rs.75,00,000 on 1st April, 2018. The bonds have a life of five years and a face value of Rs.20 each, and they offer interest payable at the end of each financial year at a rate of 4.5 per cent annum. The bonds are issued at their face value and each bond can be converted into one ordinary share in Veer Ltd at any time in the next five years. Companies of a similar risk profile have recently issued debt at 6 per cent per annum with similar terms but without the option for conversion.

You are required to:

- (i) Provide the appropriate accounting entries for initial recognition as per the relevant Ind AS in the books of the company.
- (ii) Calculate the stream of interest expenses across the five years of the life of the bonds.
- (iii) Provide the accounting entries if the holders of the bonds elect to convert the bonds to ordinary shares at the end of the fourth year.

Solution :

Present value of bonds at the market rate of debt

Present value of principal to be received in 5 years discounted at 6% (75,00,000 x 0.747)	=	56,02,500
Present value of interest stream discounted at 6% for 5 years (3,37,500 x 4.212)	=	14,21,550
Total present value	=	70,24,050
Equity component	=	4,75,950
Total face value of convertible bonds	=	75,00,000

(i) **Journal Entries**

	Dr. (Rs.)	Cr. (Rs.)
1st April, 2018		
Cash	75,00,000	
To Convertible bonds (liability)		70,24,050
To Convertible bonds (equity component)		4,75,950
(Being entry to record the convertible bonds and the recognition of the liability and equity components)		
31st March, 2019		
Interest expense	4,21,443	
To Cash		3,37,500
To Convertible bonds (liability)		83,943
(Being entry to record the interest expense)		

- (ii) The stream of interest expense is summarised below, where interest for a given year is calculated by multiplying the present value of the liability at the beginning of the period by the market rate of interest, this is being 6 per cent.

Date	Payment	Interest expense at 6% (e of previous year x 6%)	Increase in bond liability (c-b)	Total bond liability (e of previous year +d)
(a)	(b)	(c)	(d)	(e)
1st April, 2018				70,24,050
31st March, 2019	3,37,500	4,21,443	83,943	71,07,993
31st March, 2020	3,37,500	4,26,480	88,980	71,96,973
31st March, 2021	3,37,500	4,31,818	94,318	72,91,291

31st March, 2022	3,37,500	4,37,477	99,977	73,91,268
31st March, 2023	3,37,500	4,46,232*	1,08,732	75,00,000

* Difference is due to rounding off.

- (iii) If the holders of the bond elect to convert the bonds to ordinary shares at the end of the fourth year (after receiving their interest payments), the entries in the fourth year would be:

		Dr.(Rs.)	Cr.(Rs.)
31st March, 2022			
Interest expense A/c	Dr.	4,37,477	
To Cash A/c			3,37,500
To Convertible bonds (liability) A/c			99,977
(Being entry to record interest expense for the period)			
31st March, 2022			
Convertible bonds (liability) A/c	Dr.	73,91,268	
Convertible bonds (equity component) A/c	Dr.	4,75,950	
To Ordinary share capital A/c			78,67,218
(Being entry to record the conversion of bonds into ordinary shares of Veer Limited).			

Question 7 : Nov 2018 – PAPER

Growth Limited on 1st April, 2015 issued 50,000, 7% convertible debentures of face value of Rs.100 per debenture at par. The debentures are redeemable at a premium of 10% on 31st March, 2020 or these may be converted into ordinary shares at the option of the holder. The interest rate for equivalent debentures without conversion rights would have been 10%. The date of transition to Ind AS is 1st April, 2017.

Suggest how Growth Limited should account for this compound financial instrument on the date of transition. Also discuss Ind AS on 'Financial Instrument' presentation in the above context.

The present value of Rs.1 receivable at the end of each year based on discount rates of 7% and 10% can be taken as:

End of Year	1	2	3	4	5
7%	0.94	0.87	0.82	0.76	0.71
10%	0.91	0.83	0.75	0.68	0.62

Solution :

Since the liability is outstanding on the date of Ind AS transition, Growth Ltd. is required to split the convertible debentures into debt and equity portion on the date of transition. Accordingly, first the liability component will be measured discounting the contractually determined stream of future cash flows (interest and principal) to present value by using the discount rate of 10% p.a. (being the market interest rate for similar debentures with no conversion option).

Calculation of Equity & Liability component on initial recognition

	Rs.
Present Interest payments for 5 years on debentures by applying annuity factor [(50,000 × 7% × 100) × 3.79]	13,26,500
PV of principal repayment (including premium) (50,000 × 110 × 0.62)	<u>34,10,000</u>
Total liability component	47,36,500
Total equity component (Balancing figure)	<u>2,63,500</u>
Total proceeds from issue of Debentures	<u>50,00,000</u>

Thus, on the date of transition, the amount of Rs.50,00,000 being the amount of debentures will split as under:

Debt	Rs.47,36,500
Equity	Rs.2,63,500

Question 8 : May 2019 – RTP

KK Ltd. has granted an interest free loan of Rs.10,00,000 to its wholly owned Indian Subsidiary YK Ltd. There is no transaction cost attached to the said loan. The Company has not finalised any terms and conditions including the applicable interest rates on such loans. The Board of Directors of the Company are evaluating various options and has requested your firm to provide your views under Ind AS in following situations:

- (i) The Loan given by KK Ltd. to its wholly owned subsidiary YK Ltd. is interest free and such loan is repayable on demand.
- (ii) The said Loan is interest free and will be repayable after 3 years from the date of granting such loan. The current market rate of interest for similar loan is 10%. Considering the same, the fair value of the loan at initial recognition is Rs.8,10,150.
- (iii) The said loan is interest free and will be repaid as and when the YK Ltd. has funds to repay the Loan amount.

Based on the same, KK Ltd. has requested you to suggest the accounting treatment of the above loan in the stand-alone financial statements of KK Ltd. and YK Ltd. and also in the consolidated financial statements of the group. Consider interest for only one year for the above loan. Further the Company is also planning to grant interest free loan from YK Ltd. to KK Ltd. in the subsequent period. What will be the accounting treatment of the same under applicable Ind AS?

Solution :

Scenario (i)

Since the loan is repayable on demand, it has fair value equal to cash consideration given. KK Ltd. and YK Ltd. should recognize financial asset and liability, respectively, at the amount of loan given (assuming that loan is repayable within a year). Upon, repayment, both the entities should reverse the entries that were made at the origination.

Journal entries in the books of KK Ltd.

At origination			
Loan to YK Ltd. A/c	Dr.	Rs.10,00,000	
To Bank A/c			Rs.10,00,000
On repayment			

Bank A/c	Dr.	Rs.10,00,000	
To Loan to YK Ltd. A/c			Rs.10,00,000

Journal entries in the books of YK Ltd.

At origination			
Bank A/c	Dr.	Rs.10,00,000	
To Loan from KK Ltd.			Rs.10,00,000
On repayment			
Loan from KK Ltd. A/c	Dr.	Rs.10,00,000	
To Bank A/c			Rs.10,00,000

In the consolidated financial statements, there will be no entry in this regard since loan receivable and loan payable will get set off.

Scenario (ii)

Applying the guidance in Ind AS 109, a ‘financial asset’ shall be recorded at its fair value upon initial recognition. Fair value is normally the transaction price. However, sometimes certain type of instruments may be exchanged at off market terms (ie, different from market terms for a similar instrument if exchanged between market participants).

If a long-term loan or receivable that carries no interest while similar instruments if exchanged between market participants carry interest, then fair value for such loan receivable will be lower from its transaction price owing to the loss of interest that the holder bears. In such cases where part of the consideration given or received is for something other than the financial instrument, an entity shall measure the fair value of the financial instrument. The difference in fair value and transaction cost will treated as investment in Subsidiary YK Ltd.

Both KK Ltd. and YK Ltd. should recognise financial asset and liability, respectively, at fair value on initial recognition, i.e., the present value of Rs.10,00,000 payable at the end of 3 years using discounting factor of 10%. Since the question mentions fair value of the loan at initial recognition as Rs.8,10,150, the same has been considered. The difference between the loan amount and its fair value is treated as an equity contribution to the subsidiary. This represents a further investment by the parent in the subsidiary.

Journal entries in the books of KK Ltd. (for one year)

At origination			
Loan to YK Ltd. A/c	Dr.	Rs.8,10,150	
Investment in YK Ltd. A/c	Dr.	Rs.1,89,850	
To Bank A/c			Rs.10,00,000
During period to repayment – to recognise interest			

Year 1 – Charging of Interest

At origination			
Loan to YK Ltd. A/c	Dr.	Rs.81,015	
To Interest income A/c			Rs.81,015

Transferring of interest to Profit and Loss

Interest income A/c	Dr.	Rs.81,015	
To Profit and Loss A/c			Rs.81,015
On repayment			
Bank A/c	Dr.	Rs.10,00,000	
To Loan to YK Ltd. A/c			Rs.10,00,000

Note- Interest needs to be recognised in statement of profit and loss. The same cannot be adjusted against capital contribution recognised at origination.

Journal entries in the books of YK Ltd. (for one year)

At origination			
Bank A/c	Dr.	Rs.10,00,000	
To Loan from KK Ltd. A/c			Rs.8,10,150
To Equity Contribution in KK Ltd. A/c			Rs.1,89,850
During period to repayment – to recognise interest			
Year 1			
Interest expense A/c	Dr.	Rs.81,015	
To Loan from KK Ltd. A/c			Rs.81,015
On repayment			
Loan from KK Ltd. A/c	Dr.	Rs.10,00,000	
To Bank A/c			Rs.10,00,000

In the consolidated financial statements, there will be no entry in this regard since loan and interest income/expense will get set off.

Scenario (iii)

Generally, a loan which is repayable when funds are available, cannot be stated as loan repayable on demand. Rather the entity needs to estimate the repayment date and determine its measurement accordingly by applying the concept prescribed in Scenario (ii).

In the consolidated financial statements, there will be no entry in this regard since loan and interest income/expense will get set off.

In case the subsidiary YK Ltd. is planning to grant interest free loan to KK Ltd., then the difference between the fair value of the loan on initial recognition and its nominal value should be treated as dividend distribution by YK Ltd. and dividend income by the parent KK Ltd.

Question 9 : Nov 2019 – RTP

An entity purchases a debt instrument with a fair value of Rs.1,000 on 15th March, 20X1 and measures the debt instrument at fair value through other comprehensive income. The instrument has an interest rate of 5% over the contractual term of 10 years, and has a 5% effective interest rate. At initial recognition, the entity determines that the asset is not a purchased or original credit-impaired asset.

On 31st March 20X1 (the reporting date), the fair value of the debt instrument has decreased to Rs.950 as a result of changes in market interest rates. The entity determines that there has not

been a significant increase in credit risk since initial recognition and that ECL should be measured at an amount equal to 12 month ECL, which amounts to Rs.30.

On 1st April 20X1, the entity decides to sell the debt instrument for Rs.950, which is its fair value at that date.

Pass journal entries for recognition, impairment and sale of debt instruments as per Ind AS 109. Entries relating to interest income are not to be provided.

Solution :

On initial recognition

		Debit (Rs.)	Credit (Rs.)
Financial asset-FVOCI	Dr.	1,000	
To Cash			1,000

On Impairment of debt instrument

		Debit (Rs.)	Credit (Rs.)
Impairment expense (P & L)	Dr.	30	
Other comprehensive income	Dr.	20	
To Financial asset-FVOCI			50

The cumulative loss in other comprehensive income at the reporting date was Rs.20. That amount consists of the total fair value change of Rs.50 (that is, Rs.1,000 – Rs.950) offset by the change in the accumulated impairment amount representing 12-month ECL, that was recognized (Rs.30).

On Sale of debt instrument

		Debit (Rs.)	Credit (Rs.)
Cash		950	
To Financial asset – FVOCI			950
Loss on sale (P & L)		20	
To Other compressive income			20

Question 10 : Nov 2019 – PAPER

Vedika Ltd. issued 80,000 8% convertible debentures @ Rs.100 each on 1st April, 2015. The debentures are due for redemption on 31st March, 2019 at a premium of 20%, convertible into equity shares to the extent of 50% and balance to be settled in cash to the debenture holders. The interest rate on equivalent debenture without conversion right was 12%. The conversion to equity qualifies as fixed for fixed.

You are required to separate the debt and equity component at the time of use and show the accounting entries in Vedika Ltd.’s books at initial recognition only. The following present values of Rupee 1 at 8% and 12% are provided for a period of 5 years.

Interest Rate	Year 1	Year 2	Year 3	Year 4	Year 5
8%	0.923	0.853	0.789	0.731	0.677
12%	0.887	0.788	0.701	0.625	0.557

Solution :

In the books of Vedika Ltd.

Convertible debentures issued by Vedika are compound financial instrument. As per Ind AS 109, entity should separate debt from equity and account accordingly.

Debt – FL

Year	CF		PV @ 12%
31/3/16	6,40,000	Int. @ 8%	5,67,680
31/3/17	6,40,000	Int. @ 8%	5,04,320
31/3/18	6,40,000	Int. @ 8%	4,48,640
31/3/19	6,40,000	Int. @ 8%	4,00,000
	40,00,000	50% Principal	25,00,000
	8,00,000	POR 20%	5,00,000
			49,20,640

$$\begin{aligned} \text{Equity} &= \text{TL} - \text{FL} \\ &= 80,00,000 - 49,20,640 = 30,79,360 \end{aligned}$$

Bank A/c	Dr.	80,00,000	
To Debt (FL)			49,20,640
To Equity			30,79,360

Question 11 : Nov 2019 – PAPER

Make necessary journal entries for accounting of the security deposit made by Admire Ltd., whose details are described below. Assume market interest rate for a deposit for similar period to be 12% per annum.

Particulars	Details
Date of Security Deposit (Starting Date)	1-Apr-2014
Date of Security Deposit (Finishing Date)	31-Mar-2019
Description	Lease
Total Lease Period	5 years
Discount rate	12.00%
Security deposit (A)	20,00,000
Present value factor at the 5 th year	0.567427

Solution :

1) As per IND AS 109, security deposit is an interest free deposit redeemable at end of lease term for Rs.20,00,000. Hence business model is to collect contractual cash flow and shall be accounted for at amortised cost.

2) Deposit should initially be recorded at fair value i.e. $\frac{20,00,000}{(1.12)^5} = 11,34,854$

Security deposit (FA) 11,34,854

Prepaid lease Exp. (P/L)	8,65,146	
To Bank		20,00,000

3) Deposit should be subsequently carried over at amortised cost

Year	OP	Interest (12%)	Closing
1	11,34,854	1,36,183	12,71,037
2	12,71,037	1,52,524	14,23,561
3	14,23,561	1,70,827	15,94,388
4	15,94,388	1,91,327	17,85,715
5	17,85,715	2,14,685	20,00,000

Question 12 : May 2020 – RTP

XYZ issued RS.4,80,000 4% redeemable preference shares on 1st April 20X5 at par. Interest is paid annually in arrears, the first payment of interest amounting RS.19,200 was made on 31st March 20X6 and it is debited directly to retained earnings by accountant. The preference shares are redeemable for a cash amount of Rs.7,20,000 on 31st March 20X8. The effective rate of interest on the redeemable preference shares is 18% per annum. The proceeds of the issue have been recorded within equity by accountant as this reflects the legal nature of the shares. Board of directors intends to issue new equity shares over the next two years to build up cash resources to redeem the preference shares.

Mukesh, Accounts manager of XYZ has been told to review the accounting of aforesaid issue. CFO has asked from Mukesh the closing balance of preference shares at the year end. If you were Mukesh, then how much balance you would have shown to CFO on analysis of the stated issue. Prepare necessary adjusting journal entry in the books of account, if required.

Solution :

The preference shares provide the holder with the right to receive a predetermined amount of annual dividend out of profits of the company, together with a fixed amount on redemption.

Whilst the legal form is equity, the shares are in substance debt. The fixed level of dividend is interest and the redemption amount is equivalent to the repayment of a loan.

Under Ind AS 32 'Financial Instruments: Presentation' these instruments should be classified as financial liabilities because there is a contractual obligation to deliver cash. The preference shares should be accounted for at amortised cost using the effective interest rate of 18%.

Year	1 April, 20X5 Rs.	Interest @18% Rs.	Paid at 4% Rs.	31 March, 20X6 Rs.
20X5 - 20X6	4,80,000	86,400	(19,200)	5,47,200

Accordingly, the closing balance of Preference shares at year end i.e. 31st March, 20X6 would be Rs.5,47,200.

Accountant has inadvertently debited interest of Rs.19,200 in the profit and loss. However, the interest of Rs.86,400 should have been debited to profit and loss as finance charge.

Similarly, amount of Rs.5,47,200 should be included in borrowings (non-current liabilities) and consequently, Equity should be reduced by Rs.480,000 proceeds of issue and Rs.67,200 (86,400 – 19,200) i.e. total by 5,47,200.

Necessary adjusting journal entry to rectify the books of accounts will be:

		Rs.	Rs.
Preference share capital (equity) (Balance sheet)	Dr.	4,80,000	
Finance costs (Profit and loss)	Dr.	86,400	
To Equity – Retained earnings (Balance sheet)			19,200
To Preference shares (Long-term Borrowings) (Balance sheet)			5,47,200

Question 13 : Nov 2020 – Paper

On 1 April 2020, Star Limited has advanced a housing loan of Rs.15 lakhs to one of its employee at an interest rate of 6% per annum which is repayable in 5 equal annual installments along with interest at each year end. Employee is not required to give any specific performance against this benefit. The market rate of similar loan for housing finance by banks is 10% per annum.

The accountant of the company has recognized the staff loan in the balance sheet equivalent to the amount of housing loan disbursed i.e. Rs.15 lakhs. The interest income for the year is recognized at the contracted rate in the Statement of Profit and Loss by the company i.e. Rs.90,000 (6% of Rs.15 lakhs).

Analyze whether the above accounting treatment made by the accountant is in compliance with the relevant Ind AS. If not, advise the correct treatment of housing loan, interest and other expenses in the financial statements of Star Limited for the year 2020-2021 along with workings and applicable Ind AS.

You are required to explain how the housing loan should be reflected in the Ind AS compliant Balance Sheet of Star Limited on 31 March 2021.

Solution :

The accounting treatment made by the accountant is not in compliance with Ind AS 109 'Financial Instruments'. As per Ind AS 109, at initial recognition, an entity shall measure a financial asset or financial liability at its fair value. The fair value of a financial instrument at initial recognition is normally the transaction price i.e. the fair value of the consideration given or received.

After initial recognition, an entity shall measure a financial asset either at amortised cost or at fair value through profit and loss or fair value through other comprehensive income.

Here, the loan given to employee is not at market rate. Hence, the fair value of the loan will not be equal to its initial loan proceeds. As per Ind AS 109, a financial instrument is initially measured and recorded in the books at its fair value. Further, interest income to be recognised in the Statement of Profit and Loss will be the finance income recognised at effective rate of interest i.e. @ 10% and not the rate of interest charged by the company i.e. @ 6%.

The correct accounting treatment as per Ind AS 109 will be as under:

For measuring the fair value or present value of the loan at initial recognition, market rate of interest of similar loan is considered (level 1 observable input) ie @ 10%, to discount the cash outflows.

The fair value of the loan shall be as follows:

Date	Outstanding loan	Principal	Interest income @ 6%	Total inflow	Discount factor @ 10%	PV
31-Mar-21	15,00,000	3,00,000	90,000	3,90,000	0.909	3,54,510
31-Mar-22	12,00,000	3,00,000	72,000	3,72,000	0.826	3,07,272
31-Mar-23	9,00,000	3,00,000	54,000	3,54,000	0.751	2,65,854
31-Mar-24	6,00,000	3,00,000	36,000	3,36,000	0.683	2,29,488
31-Mar-25	3,00,000	3,00,000	18,000	3,18,000	0.621	<u>1,97,478</u>
Fair value of the loan						<u>13,54,602</u>

As per Ind AS 19, employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees or for termination of employment. Difference of loan proceeds and present value of the loan (fair value) will be treated as prepaid employee cost irrespective of the fact that employee is not required to give any specific performance against this benefit. This is because employee is required to be in service of the company to continue availing the benefits of concessional rate of interest on housing loan. Practically, once the employee leaves the organisation, they have to repay the outstanding loan because the company provides the loan at concessional rate of interest only to its employees.

Hence, it is an employee benefit given by the company to its employees. This deemed employee cost of Rs. 1,45,398 (15,00,000 – 13,54,602) will be deferred and amortised over the period of loan on straight line basis.

Calculation of amortised cost of loan to employees

Financial year ending on 31 March	Amortised cost (opening balance)	Interest to be recognised @ 10%	Repayment (including interest)	Amortised cost (closing balance)
2021	13,54,602	1,35,460	3,90,000	11,00,062
2022	11,00,062	1,10,006	3,72,000	8,38,068
2023	8,38,068	83,807	3,54,000	5,67,875
2024	5,67,875	56,788	3,36,000	2,88,663
2025	2,88,663	29,337*	3,18,000	-

* 2,88,663 x 10% = Rs. 28,866. Difference of Rs. 471 (29,337 – 28,866) is due to approximation in computation.

Journal Entries to be recorded at every period end:

1. On 1 April 2020

Particulars		Dr. Amount (Rs.)	Cr. Amount (Rs.)
Loan to employee A/c	Dr.	13,54,602	
Prepaid employee cost A/c	Dr.	1,45,398	
To Bank A/c			15,00,000
(Being loan asset recorded at initial fair value)			

2. On 31 March 2021

Particulars	Dr. Amount (Rs.)	Cr. Amount (Rs.)
Bank A/c Dr. To Finance income A/c (profit and loss) @10% To Loan to employee A/c (Being first instalment of repayment of loan accounted for using the amortised cost and effective interest rate @ 10%)	3,90,000	1,35,460 2,54,540
Employee benefit cost (profit and loss) A/c Dr. To Prepaid employee cost A/c (1,45,398/5) (Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)	29,080	29,080

The Following housing loan balances should appear in the financial statements:

Extracts of Balance sheet of Star Ltd. as at 31 March 2021

Non-current asset	
Financial asset	
Loan to employee (11,00,062 – 3,72,000 + 1,10,006)	8,38,068
Other non-current asset	
Prepaid employee cost	87,238
Current asset	
Financial asset	
Loan to employee (3,72,000-1,10,006)	2,61,994
Other current asset	
Prepaid employee cost	29,080

Deferred tax on temporary differences arising on the above-mentioned account balances (appearing in the balance sheet) should be recognised. However, in the absence of any tax rate in the question no deferred tax has been recognised.

Question 14 : Nov 2020 – Paper

On 1 April 2019, 8% convertible loan with a nominal value of Rs. 12,00,000 was issued at par by Cargo Ltd. It is redeemable on 31 March 2023 also at par. Alternatively, it may be converted into equity shares on the basis of 100 new shares for each Rs. 200 worth of loan.

An equivalent loan without the conversion option would have carried interest at 10%. Interest of Rs. 96,000 has already been paid and included as a finance cost.

Present Value (PV) rates are as follows:

Year End	@ 8%	@ 10%
1	0.93	0.91
2	0.86	0.83
3	0.79	0.75
4	0.73	0.68

How will the Company present the above loan notes in the financial statements for the year ended 31 March 2020?

Solution :

There are both 'equity' and 'debt' features in the instrument. An obligation to pay cash i.e. interest at 8% per annum and a redemption amount will be treated as 'financial liability' while option to convert the loan into equity shares is the equity element in the instrument. Therefore, convertible loan is a compound financial instrument.

Calculation of debt and equity component and amount to be recognised in the books:

S. No	Year	Interest amount	Discounting factor	Amount
		@ 8%	@ 10%	
Year 1	2020	96,000	0.91	87,360
Year 2	2021	96,000	0.83	79,680
Year 3	2022	96,000	0.75	72,000
Year 4	2023	12,96,000*	0.68	<u>8,81,280</u>
Amount to be recognised as a liability				11,20,320
Initial proceeds				<u>(12,00,000)</u>
Amount to be recognised as equity				79,680

* In year 4, the loan note will be redeemed; therefore, the cash outflow would be Rs. 12,96,000 (Rs. 12,00,000 + Rs. 96,000).

Presentation in the Financial Statements:

In Statement of Profit and Loss for the year ended on 31 March 2020

Finance cost to be recognised in the Statement of Profit and Loss (11,20,320 x 10%)	Rs. 1,12,032
Less: Already charged to the income statement	<u>(Rs. 96,000)</u>
Additional finance charge required to be recognised in the Statement of Profit and Loss	<u>Rs. 16,032</u>

In Balance Sheet as at 31 March 2020

Equity and Liabilities	
Equity	
Other Equity (8% convertible loan)	79,680
Non-current liability	
Financial liability [8% convertible loan – [(11,20,320 + 1,12,032 – 96,000)]	11,36,352

Question 15 : Jan 2021 – Paper

Lovely Limited has a policy of providing subsidized loans to its employees for the purpose of buying 2 Wheelers and 4 Wheelers vehicle. Simran who is a Sales Executive, took a loan for a Four-wheeler vehicle from the Company. The following were the terms of the loan:

- Principal Amount : Rs.9,00,000
- Interest: 5% p.a. for the First Rs.3,00,000 and 8% p.a. for the remaining amount.
- Loan disbursed date: 1st April 2017
- Loan Tenure: 3 Years
- Pre-Payment : Full or Partial payment at the option of the employee.
- Simran shall remain in service till the term of the loan ends.
- The Principal amount should be recovered in 3 equal installments at the end of each year and will be first applied to 8% interest bearing principal.
- The accrued interest shall be paid on annual basis.

The market rate of a comparable loan available to Simran is 12% per annum.

Following table shows the expected contractual cash flows from the loan given to Simran.

(In Rs.)

Date	Outflows	Inflows			Principal Outstanding
		Principal	Interest Income 8%	Interest Income 5%	
01.04.2017	(9,00,000)				9,00,000
31.03.2018		3,00,000	48,000	15,000	6,00,000
31.03.2019		3,00,000	24,000	15,000	3,00,000
31.03.2020		3,00,000	-	15,000	-

Simran pre-pays Rs.1,00,000 on 31st March, 2019.

Following table shows the actual cash flows from the loan, considering the prepayment on 31st March 2019.

(In Rs.)

Date	Outflows	Inflows			Principal Outstanding
		Principal	Interest Income 8%	Interest Income 5%	
01.04.2017	(9,00,000)				9,00,000
31.03.2018		3,00,000	48,000	15,000	6,00,000
31.03.2019		4,00,000	24,000	15,000	2,00,000
31.03.2020		2,00,000	-	10,000	-

You are required to pass journal entries in the books of Lovely Limited considering the requirements of Ind AS 109.

Solution :

As per requirement of Ind AS 109, a financial instrument is initially measured and recorded at its fair value. Therefore, considering the market rate of interest of similar loan available to Simran is 12%, the fair value of the contractual cash flows shall be as follows:

Amount in Rs.

Date	Inflows			Total inflow	Discount factor @ 12%	PV
	Principal	Interest income 8%	Interest income 5%			
31.03.2018	3,00,000	48,000	15,000	3,63,000	0.893	3,24,159
31.03.2019	3,00,000	24,000	15,000	3,39,000	0.797	2,70,183
31.03.2020	3,00,000	-	15,000	3,15,000	0.712	<u>2,24,280</u>
Total (fair value)						<u>8,18,622</u>

Benefit to Simran, to be considered as part of employee cost for Lovely Ltd. Rs.81,378 (9,00,000 – 8,18,622).

The deemed employee cost is to be amortised over the period of loan i.e. the minimum period that Simran must remain in service.

The amortization schedule of the Rs.8,18,622 loan is shown in the following table:

Amount in Rs.

Date	Opening outstanding Loan	Total cash inflows (principal repayment + interest)	Interest @ 12%	Closing outstanding Loan
01.04.2017	8,18,622			8,18,622
31.03.2018	8,18,622	3,63,000	98,235	5,53,857
31.03.2019	5,53,857	3,39,000	66,463	2,81,320
31.03.2020	2,81,320	3,15,000	33,680*	Nil

* Difference is due to approximation of discounting factor and interest amount.

Journal Entries to be recorded at every period end:

a. 1 April 2017 –

Particulars	Dr. (Rs.)	Cr. (Rs.)
Loan to employee A/c	Dr. 8,18,622	
Pre-paid employee cost A/c	Dr. 81,378	
To Bank A/c		9,00,000
(Being loan asset recorded at initial fair value)		

b. 31 March 2018 –

Particulars	Dr. (Rs.)	Cr. (Rs.)
Bank A/c	Dr. 3,63,000	
To Interest income A/c		98,235
To Loan to employee A/c		2,64,765

(Being first instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)			
Employee benefit A/c To Pre-paid employee cost A/c (Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost on straight line basis)	Dr. 	27,126 	27,126

- c. On 31 March 2019, due to pre-payment of a part of loan by Simran, the carrying value of the loan shall be re-computed by discounting the future remaining cash flows by the original effective interest rate.

There shall be two sets of accounting entries on 31 March 2019, first the realisation of the contractual cash flow as shown below and then the accounting for the prepayment of Rs.1,00,000 included in (d) below:

31 March 2019 –

Particulars		Dr. (Rs.)	Cr. (Rs.)
Bank A/c To Interest income A/c To Loan to employee A/c (Being second instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)	Dr.	3,39,000	66,463 2,72,537
Employee benefit (profit and loss) A/c To Pre-paid employee cost A/c (Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)	Dr.	27,126	27,126

Computation of new carrying value of loan to employee:

Date	Inflows			Discount factor @12%	PV
	Principal	Interest income 8%	Interest income 5%		
31.03.2020	2,00,000	-	10,000	0.893	1,87,530
Total (revised carrying value)					1,87,530
Less: Current carrying value					<u>2,81,320</u>
Adjustment required					<u>93,790</u>

The difference between the amount of pre-payment and adjustment to loan shall be considered a gain, though will be recorded as an adjustment to pre-paid employee cost, which shall be amortised over the remaining tenure of the loan.

- d. 31 March 2019 prepayment–

Particulars		Dr. (Rs.)	Cr. (Rs.)
Bank A/c	Dr.	1,00,000	
To Pre-paid employee cost A/c			6,210
To Loan to employee A/c			93,790
(Being gain to Lovely Limited recorded as an adjustment to pre-paid employee cost)			

The amortisation schedule of the new carrying amount of loan shall be as follows:

Date	Loan outstanding	Total cash inflows (principal repayment + interest)	Interest @ 12%
31.03.2019	1,87,530		
31.03.2020	-	2,10,000	22,470

Amortisation of employee benefit cost shall be as follows:

Date	Opening Balance	Amortised to P & L	Adjustment	Closing balance
01.04.2017	81,378	27,126		81,378
31.03.2018	81,378	27,126		54,252
31.03.2019	54,252	20,916	6,210	20,916
31.03.2020	20,916			Nil

e. 31 March 2020 –

Particulars		Dr. (Rs.)	Cr. (Rs.)
Bank A/c	Dr.	2,10,000	
To Interest income (profit and loss) @ 12% A/c			22,470
To Loan to employee A/c			1,87,530
(Being last instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)			
Employee benefit (profit and loss) A/c	Dr.	20,916	
To Pre-paid employee cost A/c			20,916
(Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)			

Question 16 : Jan 2021 – Paper

Jewels Ltd. entered into a transaction to purchase 1,000 gms of platinum on 15th January, 2020. The transaction provides for a price payable which is equal to market value of 1,000 gms of platinum on 15th April 2020 and shall be settled by issue of such number of equity shares as is required to settle the aforementioned transaction, at a price of Rs.100 per share on 15th April

2020. Whether this is to be classified as liability or equity as on 31st March 2020 as per Ind AS 109?

You are required to explain with reasons.

Solution :

There is a contract for purchase of 1,000 gms of platinum whose consideration varies in response to changing value of platinum. Analysing this contract as a derivative with all three of the following characteristics:

- (a) Value of contract changes in response to change in market value of platinum;
- (b) There is no initial net investment
- (c) It will be settled at a future date, i.e. 15th April 2020.

Since the above criteria are met, this is a derivative contract.

Now, a derivative contract that is settled in own equity other than exchange of fixed amount of cash for fixed number of shares is classified as 'liability'. In this case, since the contract results in issue of variable number of shares based on transaction price to be determined in future, hence, this shall be classified as 'derivative financial liability' as per Ind AS 109.

Question 17 : May 2021 – RTP

On 1 April 20X1, Sun Limited guarantees a Rs.10,00,000 loan of Subsidiary – Moon Limited, which Bank STDK has provided to Moon Limited for three years at 8%.

Interest payments are made at the end of each year and the principal is repaid at the end of the loan term.

If Sun Limited had not issued a guarantee, Bank STDK would have charged Moon Limited an interest rate of 11%. Sun Limited does not charge Moon Limited for providing the guarantee.

On 31 March 20X2, there is 1% probability that Moon Limited may default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited.

On 31 March 20X3, there is 3% probability that Moon Limited may default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited.

Provide the accounting treatment of financial guarantee as per Ind AS 109 in the books of Sun Ltd., on initial recognition and in subsequent periods till 31 March 20X3.

Solution :

1 April 20X1

A financial guarantee contract is initially recognised at fair value. The fair value of the guarantee will be the present value of the difference between the net contractual cash flows required under the loan, and the net contractual cash flows that would have been required without the guarantee.

Particulars	Year 1 (Rs.)	Year 2 (Rs.)	Year 3 (Rs.)	Total (Rs.)
Cash flows based on interest rate of 11% (A)	1,10,000	1,10,000	1,10,000	3,30,000
Cash flows based on interest rate of 8% (B)	80,000	80,000	80,000	2,40,000

Interest rate differential (A-B)	30,000	30,000	30,000	90,000
Discount factor @ 11%	0.901	0.812	0.731	
Interest rate differential discounted at 11%	27,030	24,360	21,930	<u>73,320</u>
Fair value of financial guarantee contract (at inception)				<u>73,320</u>

Journal Entry

Particulars		Debit (Rs.)	Credit (Rs.)
Investment in subsidiary	Dr.	73,320	
To Financial guarantee (liability)			73,320
(Being financial guarantee initially recorded)			

31 March 20X2

Subsequently at the end of the reporting period, financial guarantee is measured at the higher of:

- the amount of loss allowance; and
- the amount initially recognised less cumulative amortization, where appropriate.

At 31 March 20X2, there is 1% probability that Moon Limited may default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited. The 12-month expected credit losses are therefore Rs.10,000 (Rs.10,00,000 x 1%).

The initial amount recognised less amortisation is Rs.51,385 (Rs.73,320 + Rs.8,065 (interest accrued based on EIR)) – Rs.30,000 (benefit of the guarantee in year 1) Refer table below. The unwound amount is recognised as income in the books of Sun Limited, being the benefit derived by Moon Limited not defaulting on the loan during the period.

Year	Opening balance	EIR @ 11%	Benefits provided	Closing balance
	Rs.		Rs.	Rs.
1	73,320	8,065	(30,000)	51,385
2	51,385	5,652	(30,000)	27,037
3	27,037	2,963*	(30,000)	-

* Difference is due to approximation

The carrying amount of the financial guarantee liability after amortisation is therefore Rs. 51,385, which is higher than the 12-month expected credit losses of Rs. 10,000. The liability is therefore adjusted to Rs. 51,385 (the higher of the two amounts) as follows:

Particulars		Debit (Rs.)	Credit (Rs.)
Financial guarantee (liability)	Dr.	21,935	
To Profit or loss			21,935

(Being financial guarantee subsequently adjusted)		
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31 March 20X3

At 31 March 20X3, there is 3% probability that Moon Limited will default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited. The 12-month expected credit losses are therefore Rs. 30,000 (Rs. 10,00,000 x 3%).

The initial amount recognised less accumulated amortisation is Rs. 27,037, which is lower than the 12-month expected credit losses (Rs. 30,000). The liability is therefore adjusted to Rs. 30,000 (the higher of the two amounts) as follows:

Particulars		Debit (Rs.)	Credit (Rs.)
Financial guarantee (liability)	Dr.	21,385*	
To Profit or loss (Note)			21,385
(Being financial guarantee subsequently adjusted)			

* The carrying amount at the end of 31 March 20X2 = Rs. 51,385 less 12-month expected credit losses of Rs. 30,000.

Question 18 : July 2021 – Paper

Softtech Limited has a policy of providing subsidized loans to its employees for the purpose of buying or construction of residential houses. Mrs.B is Senior Manager in the Company. The Company granted a loan to her on the following terms :

- Principal amount : Rs.25 lakhs
- Interest rate : 4% for the first Rs.10 lakhs and 7% for the next Rs.15 lakhs.
- Loan disbursed on : 1st January, 2019
- Tenure : 5 years
- Pre payment : Full or partial pre-payment at the option of the employee.
- The principal amount of loan shall be recovered in 5 equal instalments and will be first applied to 7% interest bearing principal
- The accrued interest shall be paid on an annual basis.
- Mrs.B must remain in service till the term of the loan ends.
- The market rate of comparable loan available to Mrs.B, is 12% per annum.
- Give your calculations by adopting the present value factor as :

31.12.2019	31.12.2020	31.12.2021	31.12.2022	31.12.2023
0.8929	0.792	0.7118	0.6355	0.5674

Following table shows the contractually expected cash flows from the loan given to Mrs.B.
(Amount in Rs.)

Date	Outflows	Inflows			Principal outstanding
		Principal	Interest income (7%)	Interest income (4%)	

1 st January 2019	(25,00,000)					25,00,000
31 st December, 2019		5,00,000	1,05,000	40,000		20,00,000
31 st December, 2020		5,00,000	70,000	40,000		15,00,000
31 st December, 2021		5,00,000	35,000	40,000		10,00,000
31 st December, 2022		5,00,000	–	40,000		5,00,000
31 st December, 2023		5,00,000	–	20,000		–

Mrs.B pre-pays Rs.5,00,000 on 31st December 2020, reducing the outstanding principal as on date to Rs.10,00,000.

Following table shows the actual cash flows from the loan given to Mrs.B, considering the pre-payment event on 31st December, 2020 :

(Amount in Rs.)

Date	Outflows	Inflows			Principal outstanding
		Principal	Interest income (7%)	Interest income (4%)	
1 st January 2019	(25,00,000)				25,00,000
31 st December, 2019		5,00,000	1,05,000	40,000	20,00,000
31 st December, 2020		10,00,000	70,000	40,000	10,00,000
31 st December, 2021		5,00,000	–	40,000	5,00,000
31 st December, 2022		5,00,000	–	20,000	–
31 st December, 2023		–	–	–	–

Record the journal entries (up to 31st December, 2020) in the books of Softech Limited considering the requirements of Ind AS 109.

Solution :

As per Ind AS 109, a financial instrument is initially measured and recorded at its fair value. Therefore, considering the market rate of interest of similar loan available to Mrs. B is 12%, the fair value of the contractual cash flows shall be as follows:

Date	Inflows			Discount factor @12%	PV
	Principal	Interest income @ 7%	Interest income @ 4%		
31 st December 2019	5,00,000	1,05,000	40000	0.8929	5,75,921

31st December 2020	5,00,000	70000	40000	0.7972	4,86,292
31st December 2021	5,00,000	35000	40000	0.7118	4,09,285
31st December 2022	5,00,000	-	40000	0.6355	3,43,170
31st December 2023	5,00,000	-	20000	0.5674	<u>2,95,048</u>
Total (fair value)					<u>21,09,716</u>

Benefit to Mrs. B, to be considered a part of employee cost for Softech Limited Rs. 3,90,284 (Rs. 25,00,000 – Rs. 21,09,716).

The deemed employee cost is to be amortised over the period of loan i.e. the minimum period that Mrs. B must remain in service.

The amortization schedule of Rs. 21,09,716 loan is shown in the following table:

Date	Opening outstanding loan	Total cash inflows (principal repayment + interest)	Interest @ 12%	Closing outstanding loan
1st January 2019	21,09,716	-	-	21,09,716
31st December 2019	21,09,716	6,45,000	2,53,166	17,17,882
31st December 2020	17,17,882	6,10,000	2,06,146	13,14,028
31st December 2021	13,14,028	5,75,000	1,57,683	8,96,711
31st December 2022	8,96,711	5,40,000	1,07,605	4,64,316
31st December 2023	4,64,316	5,20,000	55,684*	-

* Difference of Rs. 34 (55,718 – 55,684) is due to approximation.

Journal Entries in the books of Softech Limited

a. 1st January 2019

Particulars	Dr. (Rs.)	Cr. (Rs.)
Loan to Mrs. B A/c	Dr. 21,09,716	
Pre-paid employee cost A/c	Dr. 3,90,284	
To Bank A/c		25,00,000
(Being loan asset recorded at initial fair value)		

b. 31st December 2019

Particulars	Dr. (Rs.)	Cr. (Rs.)
Bank A/c	Dr. 6,45,000	
To Interest income (profit and loss) @ 12% A/c		2,53,166
To Loan to Mrs. B A/c		3,91,834
(Being first instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)		
Employee benefit (profit and loss) A/c	Dr. 78,057	

To Pre-paid employee cost A/c (Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)		78,057
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On 31st December 2020, due to pre-payment of a part of loan by Mrs. B, the carrying value of the loan shall be re-computed by discounting the future remaining cash flows by the original effective interest rate.

There shall be two sets of accounting entries on 31st December 2020, first the realisation of the contractual cash flow as shown in (c) below and then the accounting for the pre-payment of Rs. 5,00,000 included in (d) below:

c. 31st December 2020

Particulars		Dr. (Rs.)	Cr. (Rs.)
Bank A/c	Dr.	6,10,000	
To Interest income (profit and loss) @ 12% A/c			2,06,146
To Loan to Mrs. B A/c			4,03,854
(Being second instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)			
Employee benefit (profit and loss) A/c	Dr.	78,057	
To Pre-paid employee cost A/c			78,057
(Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)			

Computation of new carrying value of loan to Mrs. B:

Date	Inflows			Discount factor @ 12%	PV
	Principal	Interest income 7%	Interest income 4%		
31st December 2021	5,00,000	-	40,000	0.8929	4,82,166
31st December 2022	5,00,000	-	20,000	0.7972	<u>4,14,544</u>
Total (revised carrying value)					8,96,710
Less: Current carrying value					<u>(13,14,028)</u>
Adjustment required					<u>4,17,318</u>

The difference between the amount of pre-payment and adjustment to loan shall be considered a gain, though will be recorded as an adjustment to pre-paid employee cost, which shall be amortised over the remaining tenure of the loan.

d. 31st December 2020 prepayment

Particulars		Dr. (Rs.)	Cr. (Rs.)
Bank A/c	Dr.	5,00,000	

To Pre-paid employee cost A/c	82,682
To Loan to Mrs. B A/c	4,17,318
(Being gain to Softech Limited recorded as an adjustment to pre-paid employee cost)	

Amortisation of employee benefit cost shall be as follows:

Date	Opening Balance	Amortised to P&L	Adjustment	Closing Balance
1st January 2019	3,90,284			3,90,284
31st December 2019	3,90,284	78,057		3,12,227
31st December 2020	3,12,227	78,057	82,682	1,51,488

Question 19 : July 2021 – Paper

On 1st October, 2017 Axe Limited issues preference shares to B Limited for a consideration of Rs.18 lakhs. The holder has an option to convert these preference shares to a fixed number of equity instruments of the issuer any time up to period of 4 years. If the holder does not exercise the option, the preference shares are redeemable at the end of 4 years. The preference shares carry a fixed coupon of 5.5% per annum and is payable every year. The prevailing market rate for similar preference shares without the conversion feature is 8% per annum.

Axe Limited has an early redemption option to prepay the instrument at Rs.20 lakhs and on 30th September, 2020, it exercised that option. The interest rate has changed on that date.

At that time, Axe Limited could have issued a 1 year 9that is maturity 30th September, 2021) non-convertible instrument at 6%.

Calculate the value of liability and equity components at the date of initial recognition. Also give amortization schedule.

(Limit discounting factor to 3 decimal places for calculation purpose.)

Solution :

The values of the liability and equity components are calculated as follows:

Present value of principal payable at the end of 4 years (Rs. 18,00,000 discounted at 8% for 4 years i.e. Rs. 18,00,000 x 0.735)	Rs. 13,23,000
Present value of interest payable in arrears for 4 years (Rs. 99,000 (Rs. 18,00,000 x 5.5%) discounted at 8% for each of 4 years (i.e. Rs. 99,000 x 3.312))	Rs. 3,27,888
Total financial liability	Rs. 16,50,888
Consideration amount	(Rs. 18,00,000)
Residual – equity component	Rs. 1,49,112

Therefore, equity component = fair value of compound instrument, say, Rs. 18,00,000 less financial liability component i.e. Rs. 16,50,888 = Rs. 1,49,112.

The amortisation schedule of the instrument is set out below:

Dates	Cash flows	Finance cost at effective interest rate	Liability
1st October 2017	18,00,000	-	16,50,888
30th September 2018	(99,000)	1,32,071	16,83,959
30th September 2019	(99,000)	1,34,717	17,19,676
30th September 2020	(99,000)	1,37,574	17,58,250
30th September 2021	(18,99,000)	1,40,750*	-

***Note:** The difference in amount of finance cost is due to approximation of discounting factor to 3 decimal places

Question 20 : Nov 2021 – RTP

On 1st April, 20X1, PS Limited issued 6,000, 9% convertible debentures with a face value of Rs. 100 each maturing on 31st March, 20X6. The debentures are convertible into equity shares of PS Limited at a conversion price of Rs. 105 per share. Interest is payable annually in cash. At the date of issue, non-convertible debt could have been issued by the company at coupon rate of 13%. On 1st April, 20X4, the convertible debentures have a fair value of Rs. 6,30,000. PS Limited makes a tender offer to debenture-holders to repurchase the debentures for Rs. 6,30,000 which the debenture holders accepted. At the date of repurchase, PS Limited could have issued non-convertible debt with a 2 year term bearing coupon interest @ 10%.

Show accounting entries in the books of PS Limited for recording of equity and liability component:

- At the time of initial recognition
- At the time of repurchase of the convertible debentures

Solution :

(i) At the time of initial recognition

	Rs.
Liability component	
Present value of 5 yearly interest payments of Rs. 54,000, discounted at 13% annuity (54,000 x 3.517)	1,89,918
Present value of Rs. 6,00,000 due at the end of 5 years, discounted at 13%, compounded yearly (6,00,000 x 0.543)	3,25,800
	5,15,718
Equity component	
(Rs. 6,00,000 – Rs. 5,15,718)	84,282
Total proceeds	6,00,000

Note: Since Rs. 105 is the conversion price of debentures into equity shares and not the redemption price, the liability component is calculated @ Rs. 100 each only.

Journal Entry

		Rs.	Rs.
Bank	Dr.	6,00,000	
To 9% Debentures (Liability component)			5,15,718

To 9% Debentures (Equity component) (Being debentures initially recorded at fair value)			84,282
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(ii) **At the time of repurchase of convertible debentures**

The repurchase price is allocated as follows:

	Carrying Value @ 13% Rs.	Fair Value @ 10% Rs.	Difference Rs.
Liability component			
Present value of 2 remaining yearly interest payments of Rs. 54,000, discounted at 13% and 10%, respectively	90,072	93,690	
Present value of Rs. 6,00,000 due in 2 years, discounted at 13% and 10%, compounded yearly, respectively	<u>4,69,800</u>	<u>4,95,600</u>	
Liability component	5,59,872	5,89,290	-29,418
Equity component	84,282*	40,710**	43,572
Total	6,44,154	6,30,000	14,154

*See Note (i)

**6,30,000 – 5,89,290 = 40,710

Journal Entries

		Rs.	Rs.
9% Debentures (Liability component)	Dr.	5,59,872	
Profit and loss A/c (Debt settlement expense)	Dr.	29,418	
To Bank A/c			
(Being the repurchase of the liability component recognised)			
9% Debentures (Equity component)	Dr.	84,282	
To Bank A/c			40,710
To Retained Earnings A/c			43,572
(Being the cash paid for the equity component recognised)			

Question 21 : May 2022 – RTP

On 1st April, 2X01, Entity X issued a 10% convertible debenture with a face value of Rs. 1,000 maturing on 31st March, 2X11. The debenture is convertible into ordinary shares of Entity X at a conversion price of Rs. 50 per share. Interest is payable yearly in cash. On 1st April, 2X02, to induce the holder to convert the convertible debenture promptly, Entity X reduces the conversion price to Rs. 40 if the debenture is converted before 1st June, 2X02 (ie, within 60 days). The market price of Entity X's ordinary shares on the date the terms are amended is Rs. 80 per share. How will the revised terms be accounted?

Solution :

The fair value of the incremental consideration paid by Entity X is calculated as follows:

Number of ordinary shares to be issued to debenture holders under amended terms			
Particulars			
Face value			Rs. 1,000
New conversion price		Rs. 40 per share	
Number of ordinary shares to be issued to debenture holders under amended terms	1,000 / Rs. 40		25 Shares
Number of ordinary shares to be issued to debenture holders under original terms			
Face value			Rs. 1,000
Original conversion price		Rs. 50 per share	
Number of ordinary shares to be issued to debenture holders under original terms	1,000 / Rs. 50		20 Shares
Number of additional shares to be issued to debenture holders under amended terms			5 Shares
Value of additional shares upon conversion (to be recognised as loss in P&L)			
5 shares x Rs. 80 per share			Rs. 400

Question 22 : May 2022 – RTP

ABC Ltd. issues 4% 1,00,000 OCPS at a face value of Rs. 100 per share on 1st April, 20X1 and these are redeemable after 5 years, ie, on 31st March, 20X6. Dividend is non-cumulative. Each preference shares entitles the holders to 10 equity shares and the preference shares are optionally convertible by the holder at any time until maturity.

How will the preference shares be classified at initial recognition assuming that a comparable instrument carries a market interest rate of 7%? Provide journal entries for year 1. Will this classification be changed subsequently in case there is likelihood that OCPS will be encashed at the end of the maturity period?

Solution :

The OCPS is redeemable at the end of the 5th year. Hence, the preference share contains a liability component. Further the dividend payable on the preference shares is non-cumulative. The holder may also be able to convert the preference shares at his option any time until maturity.

Paragraph AG 37 of Ind AS 32, *Financial Instruments: Presentation* states that non-cumulative dividends paid at the discretion of the issuer entity is part of equity element.

Paragraph 29 of Ind AS 32, *Financial Instruments: Presentation*, requires separate recognition of components of a financial instrument that (a) creates a financial liability of the entity; and (b) grants an option to the holder of the instrument to convert it into fixed number of equity instruments of the entity.

From the above paragraphs it is clear that OCPS issued by ABC Ltd. has a financial liability component as well as an equity component, making it a compound financial instrument.

As per paragraph 32, in case of compound financial instruments, the issuer first determines the carrying amount of the financial liability component by measuring the fair value of a similar liability that does not have an associated equity component. The carrying amount of the equity represented by (a) non-cumulative dividend feature and (b) option to convert the preference shares for fixed number of pre-determined ordinary shares is then determined by deducting the fair value of the financial liability component from the fair value of the compound financial instrument as a whole.

Measurement and recognition (Calculations have been done at full scale):

At 7% market rate of interest, the fair value of the financial liability component of the OCPS is Rs. 71,29,862 [100,000 OCPS x Rs. 100 x (1/ (1+7%))⁵]

The fair value of the equity component is (residual value) Rs. 28,70,138 [Rs. 1,00,00,000 - Rs. 71,29,862]

Journal Entries

1st April, 20X1	On Initial recognition			
	Bank	Dr.	1,00,00,000	
	To OCPS (Financial liability)			71,29,862
	To OCPS (Equity)			28,70,138
	(Being OCPS issued and recognised)			
31st March, 20X2	<u>Interest expense – unwinding of discount</u>			
	Interest expense@7% (Refer W.N.)	Dr.	4,99,090	
	To OCPS (Financial liability)			4,99,090
	(Being interest recorded as per EIR)			
	Interest entry will be passed every year till conversion option is not exercised			
	Whenever the option is exercised by the holder to convert to equity shares			
	OCPS (Financial liability)	Dr.	Balance on date of	
	To OCPS (Equity)		exercise of the option	

As per paragraph 30, in case of a convertible financial instrument, the classification of the liability and equity components is not revised as a result of change in the likelihood that a conversion option will be exercised.

In other words, the amount attributable to equity component on initial recognition shall remain in equity and will not be reclassified even if the OCPS are ultimately redeemed in cash by the issuer.

31st March, 20X6	If redeemed in cash on maturity			
	OCPS (financial liability) (Refer W.N.)	Dr.	1,00,00,000	
	To Bank			1,00,00,000
	(Being OCPS redeemed on maturity)			

Working Note:

Calculation of the amortised cost of the financial liability (at full scale):

Year	Opening Balance (Rs.)	Interest @ 7%	Repayment	Closing Balance (Rs.)
1	71,29,862	4,99,090	-	76,28,952
2	76,28,952	5,34,027		81,62,979
3	81,62,979	5,71,409		87,34,388
4	87,34,388	6,11,407		93,45,795
5	93,45,795	6,54,206	10,000,000	-

Question 23 : May 2022 – Paper

X Ltd. issues Rs.1.5 crores convertible bonds on 1st April, 2018. The bonds have a life of 8 years and a face value of Rs.10 each, and offer interest @ 5.5% p.a. payable at the end of the each financial year.

Bonds are issued at their face value and each bond can be converted into one ordinary shares of X Ltd. at any time in the next eight years.

Companies of a similar risk profile have recently issued debt with similar terms, without the options for conversion, at a rate of 7% p.a.

You are required to :

- Provide the journal entries from financial year 2018-19 to financial year 2021-22;
- Calculate the interest expenses across all eight years of the life of the convertible bonds;
- Give the accounting entries in the holders of the bonds elect to convert the bonds to ordinary shares at the end of the fourth year (after receiving interest for the fourth year.)

Solution :

(i)

Journal Entries

	Dr. (Rs.)	Cr. (Rs.)
1st April, 2018		
Bank A/c Dr.	1,50,00,000	
To Convertible bonds A/c (liability) (Refer W.N.)		1,36,56,075
To Convertible bonds A/c (equity) (Refer W.N.)		13,43,925
(Being recognition of convertible bonds at the date of issuance into liability and equity components)		
31st March, 2019		
Interest expense A/c Dr.	9,55,925	
To Bank A/c		8,25,000
To Convertible bonds A/c (liability)		1,30,925
(Being interest expense recorded at market rate of 7% and actual interest paid @ 5.5%)		
31st March, 2020		
Interest expense A/c Dr.	9,65,090	
To Bank A/c		8,25,000
To Convertible bonds A/c (liability)		1,40,090

(Being interest expense recorded at market rate of 7% and actual interest paid @ 5.5%)			
31st March, 2021			
Interest expense A/c	Dr.	9,74,896	
To Bank A/c			8,25,000
To Convertible bonds A/c (liability)			1,49,896
(Being interest expense recorded at market rate of 7% and actual interest paid @ 5.5%)			
31st March, 2022			
Interest expense A/c	Dr.	9,85,389	
To Bank A/c			8,25,000
To Convertible bonds A/c (liability)			1,60,389
(Being interest expense recorded at market rate of 7% and actual interest paid @ 5.5%)			

(ii) **Table showing computation of interest expense at market rate and actual interest outflow @ 5.5%**

Year	Date	Opening bond liability a	Actual interest outflow @ 5.5% b = 1.5 cr x 5.5%	Interest expense @ 7% c = a x 7%	Increase in liability d = c-b	Closing bond liability e = a+d
0	1st April, 2018					1,36,56,075
1	31st March, 2019	1,36,56,075	8,25,000	9,55,925	1,30,925	1,37,87,000
2	31st March, 2020	1,37,87,000	8,25,000	9,65,090	1,40,090	1,39,27,090
3	31st March, 2021	1,39,27,090	8,25,000	9,74,896	1,49,896	1,40,76,986
4	31st March, 2022	1,40,76,986	8,25,000	9,85,389	1,60,389	1,42,37,375
5	31st March, 2023	1,42,37,375	8,25,000	9,96,616	1,71,616	1,44,08,991
6	31st March, 2024	1,44,08,991	8,25,000	10,08,629	1,83,629	1,45,92,620
7	31st March, 2025	1,45,92,620	8,25,000	10,21,483	1,96,483	1,47,89,103
8	31st March, 2026	1,47,89,103	8,25,000	10,35,897*	2,10,897	1,50,00,000

*Difference of Rs. 660 (10,35,897 - 10,35,237) is due to rounding off

(iii) **When holders of the bonds elect to convert the bonds to ordinary shares at the end of the fourth year (after receiving their interest payments), the entries would be:**

	Dr. (Rs.)	Cr. (Rs.)
31st March, 2022		
Convertible bonds A/c (liability)	Dr. 1,42,37,375	
Convertible bonds A/c (equity)	Dr. 13,43,925	
To Ordinary share capital A/c		1,55,81,300
(Being bonds converted into ordinary shares of X Ltd.)		

Working Note:

Computation of equity and liability component of convertible bond at 7% market rate

	Rs.
Present value of principal to be received at the end of eight year discounted at 7% (1,50,00,000 x 0.582)	87,30,000
Annuity of annual interest discounted at 7% for 8 years (1,50,00,000 x 5.5% x 5.971)	49,26,075
Total present value (a)	1,36,56,075
Equity component (balancing figure) (a-b)	13,43,925
Total proceeds received from issuance of convertible bonds (b)	1,50,00,000

Question 24 : May 2022 – Paper

X Ltd. has made a borrowing from RGD Bank for Rs.20,000 at a fixed interest of 12% per annum. Loan processing fees were paid additionally amount to Rs.1,000 and the loan is payable in 4 half-yearly installments of Rs.5,000 each.

Details are as follows :

Particulars	Details
Loan amount	Rs.20,000
Date of loan (Starting Date)	1-Apr-2020
Date of loan (Finishing Date)	31-March-2022
Description of Repayment	Repayment of loan starts from 30-Sept-2020 (To be paid on half yearly basis)
Installment amount	Rs.5,000
Interest rate	12.00% per annum
Interest charge	Interest to be charged and paid quarterly
Upfront fees	Rs.1,000

Compute the interest to be charged to the statement of profit and loss every quarter over the period of loan. The effective interest rate is 16.60% per annum.

Solution :

The loan taken by X Ltd. shall be measured at amortised cost as follows:

Initial measurement = At transaction price less processing fee ie. Rs. 19,000 (20,000 – 1,000)

Subsequent measurement = Interest to be accrued using effective rate of interest as follows:

Quarter	Opening balance (A)	Interest @ 16.60% (B)=[(A) x 16.60%/4]	Cash flows (C) = [Refer column of D of W.N.]	Closing balance (A) + (B) - (C)
1	19,000.00	789.00	600.00	19,189.00
2	19,189.00	796.00	5,600.00	14,385.00
3	14,385.00	597.00	450.00	14,532.00
4	14,532.00	603.00	5,450.00	9,685.00
5	9,685.00	402.00	300.00	9,787.00
6	9,787.00	406.00	5,300.00	4,893.00

7	4,893.00	203.00	150.00	4,946.00
8	4,946.00	204.00*	5,150.00	-

* Difference is due to approximation.

Working Note :

Quarter	Opening balance (A)	Interest @ 12% p.a. (B) = [(A) x 12%/4]	Principal repayment at quarter end (C)	Total Cash flow (D) = (B) + (C)	Closing balance (E) = (A) - (C)
1	20,000.00	600.00	-	600.00	20,000.00
2	20,000.00	600.00	5,000.00	5,600.00	15,000.00
3	15,000.00	450.00	-	450.00	15,000.00
4	15,000.00	450.00	5,000.00	5,450.00	10,000.00
5	10,000.00	300.00	-	300.00	10,000.00
6	10,000.00	300.00	5,000.00	5,300.00	5,000.00
7	5,000.00	150.00	-	150.00	5,000.00
8	5,000.00	150.00	5,000.00	5,150.00	-

Question 25 : Nov 2022 – RTP

On 1st April, 20X1 an entity granted an interest-free loan of Rs. 5,00,000 to an employee for a period of three years. The market rate of interest for similar loans is 5% per year.

On 31st March, 20X3, because of financial difficulties, the employee asked to extend the interest-free loan for further three years. The entity agreed. Under the restructured terms, repayment will take place on 31st March, 20X7. However, the entity only expects to receive a payment of Rs. 2,50,000, given the financial difficulty of the employee.

Explain the accounting treatment on initial recognition of loan and after giving effect of the changes in the terms of the loan as per Ind AS 109. Support your answer with Journal entries and amortised cost calculation, as on the date of initial recognition and on the date of change in terms of loan.

Solution :

As the loan is not at a market interest rate, hence it is not recorded at the transaction price of Rs. 5,00,000. Instead, the entity measures the loan receivable at the present value of the future cash inflows discounted at a market rate of interest available for a similar loan.

The present value of the loan receivable (financial asset) discounted at 5% per year is Rs. 5,00,000 ÷ (1.05)³ = Rs. 4,32,000. Therefore, Rs. 4,32,000 is recorded on initial measurement of the loan receivable. This amount will accrete to Rs. 5,00,000 over the three-year term using the effective interest method.

The difference between Rs. 5,00,000 and Rs. 4,32,000 i.e., Rs. 68,000 is accounted for as prepaid employee cost in accordance with Ind AS 19 'Employee Benefits', which will be deferred and amortised over the period of loan on straight line basis.

The journal entries on initial recognition are:

		Rs.	Rs.
Loan receivable (financial asset)	Dr.	4,32,000	
Prepaid employee cost (asset)	Dr.	68,000	

To Cash / Bank (financial asset) (Being loan granted to the employee recognised)		5,00,000
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The amortised cost calculation at 1st April, 20X1 is as follows :

Period	Carrying amount at 1st April	Interest at 5%	Cash inflow	Carrying amount at 31st March
20X1-20X2	4,32,000	21,600	–	4,53,600
20X2-20X3	4,53,600	22,680	–	4,76,280
20X3-20X4	4,76,280	23,720*	(5,00,000)	–

*Difference of Rs. 94 (Rs. 23,814 – Rs. 23,720) is due to approximation.

On 31st March, 20X3, the carrying amount of the loan receivable is Rs. 4,76,280.

As a result of that modification, on 31st March, 20X3, the present value of estimated cash flows is recalculated to be Rs. 2,05,750 using the asset's original effective interest rate of 5% (Rs. 2,50,000 ÷ (1.05)⁴).

An impairment loss of Rs. 2,70,530 (Rs. 4,76,280 – Rs. 2,05,750) is recognised in profit or loss in the year 20X2-20X3.

The carrying amount of the loan receivable may be reduced directly, as follows :

		Rs.	Rs.
Profit or loss - impairment loss	Dr.	2,70,530	
To Loan receivable (Being impairment loss recognised)			2,70,530

In this case, the loan receivable will be measured at Rs. 2,05,750 at 31st March, 20X3.

The revised amortised cost calculation at 1st April, 20X3 is as follows:

Period	Carrying amount at 1st April	Interest at 5% (the original effective interest rate)	Cash inflow	Carrying amount at 31st March
20X3-20X4	2,05,750	10,288	–	2,16,038
20X4-20X5	2,16,038	10,802	–	2,26,840
20X5-20X6	2,26,840	11,342	–	2,38,182
20X6-20X7	2,38,182	11,818	-2,50,000	–

Question 26 : Nov 2022 – Paper

On 1st April, 2021 "Fortunate Bank" has provided a loan of Rs.25,00,000 to Mohan Limited for 4 years at 10% p.a. and the loan has been guaranteed by Surya Limited, which is a holding company for Mohan Limited Interest payments are made at the end of each year and the principal is repaid at the end of the loan term. If Surya Limited had not issued a guarantee, 'Fortunate Bank' would have changed Mohan Limited as interest rate of 14% p.a. Surya Limited does not charge Mohan Limited for providing the guarantee.

On 31st March 2022, there is 2% probability that Mohan Limited may default on the loan in the next 12 months. If Mohan Limited defaults on the loan, Surya Limited does not expect to recover any amount from Mohan Limited.

On 31st March 2023, there is 4% probability that Mohan Limited may default on the loan in next 12 months. If Mohan Limited defaults on the loan, Surya Limited does not expect to recover any amount from Mohan Limited.

On 31st March 2024, there is 5% probability that Mohan Limited may default on the loan in the next 12 months. If Mohan Limited defaults on the loan, Surya Limited does not expect to recover any amount from Mohan Limited.

You are required to provide accounting treatment of financial guarantee as per Ind AS 109 in the books of Surya Limited on initial recognition and in subsequent period till 31st March, 2024.

Solution :

1st April 2021

A financial guarantee contract is initially recognised at fair value. The fair value of the guarantee will be the present value of the difference between the net contractual cash flows required under the loan, and the net contractual cash flows that would have been required without the guarantee

Particulars	Year 1 (Rs.)	Year 2 (Rs.)	Year 3 (Rs.)	Year 4 (Rs.)	Total (Rs.)
Cash flows based on interest rate of 14% (A)	350000.00	350000.00	350000.00	350000.00	14,00,000
Cash flows based on interest rate of 10% (B)	<u>250000.00</u>	<u>250000.00</u>	<u>250000.00</u>	<u>250000.00</u>	<u>10,00,000</u>
Interest on differential rate (C) = (A-B)	100000.00	100000.00	100000.00	100000.00	4,00,000
Discount factor @ 14%	0.877	0.769	0.675	0.592	
Interest on differential rate discounted @ 14%	87700.00	76900.00	67,500	59,200	2,91,300
Fair value of financial guaranteed contract (at inception)					2,91,300

Alternative manner of presentation for the calculation of fair value of financial guaranteed contract (at inception)

- (i) Interest on loan @ 10% = Rs. 2,50,000
 Present value of cash flow of loan at concessional rate with guarantee @ 14%
 = Rs. 2,50,000 x 2.9138 + Rs. 25,00,000 x 0.5921
 = Rs. 7,28,450 + Rs. 14,80,250 = Rs. 22,08,700
- (ii) Interest on loan at normal rate of 14% = Rs. 3,50,000
 Present Value of Cash flow of loan at 14%
 = Rs. 3,50,000 x 2.9138 + Rs. 25,00,000 x 0.5921
 = Rs. 25,00,080 or Rs. 25,00,000
- Difference (ii) – (i) = Rs. 25,00,000 - Rs. 22,08,700
 Fair value of financial guaranteed contract (at inception) = Rs. 2,91,300

Journal Entry

Particulars		Debit (Rs.)	Credit (Rs.)
Investment in subsidiary	Dr.	291300.00	
To Financial guarantee (liability)			2,91,300
(Being financial guarantee initially recorded)			

31st March 2022

Subsequently at the end of the reporting period, financial guarantee is measured at the higher of:

- the amount of loss allowance; and
- the amount initially recognised less cumulative amortisation, where appropriate.

At 31st March 2022, there is 2% probability that Mohan Limited may default on the loan in the next 12 months. If Mohan Limited defaults on the loan, Surya Limited does not expect to recover any amount from Mohan Limited. The 12-month expected credit losses are therefore Rs. 50,000 (Rs. 25,00,000 x 2%).

The initial amount recognised less amortisation is Rs. 2,32,082 (Refer table below). The unwound amount is recognised as income in the books of Surya Limited, being the benefit derived by Mohan Limited not defaulting on the loan during the period.

Year ended on 31st March	Opening balance (a) Rs.	EIR @ 14% (b) = (a x 14%)	Benefits provided (c) Rs.	Closing balance (d) = (a) + (b) -(c) Rs.
2022	291300.00	40782.00	(1,00,000)	2,32,082
2023	232082.00	32491.00	(1,00,000)	1,64,573
2024	164573.00	23040.00	(1,00,000)	87,613
2025	87613.00	12,387*	(1,00,000)	-

* Difference of Rs. 121 (Rs. 12,387 – Rs. 12,266) is due to approximation.

The carrying amount of the financial guarantee liability after amortisation is therefore Rs. 2,32,082, which is higher than the 12-month expected credit losses of Rs. 50,000. The liability is therefore adjusted to Rs. 2,32,082 (the higher of the two amounts) as follows:

Particulars		Debit (Rs.)	Credit (Rs.)
Financial guarantee (liability)	Dr.	59,218	
To Profit and loss			59,218
(Being financial guarantee subsequently adjusted)			

31st March 2023

At 31st March 2023, there is 4% probability that Mohan Limited will default on the loan in the next 12 months. If Mohan Limited defaults on the loan, Surya Limited does not expect to recover any amount from Mohan Limited. The 12-month expected credit losses are therefore Rs. 1,00,000 (Rs. 25,00,000 x 4%).

The carrying amount of the financial guarantee liability after amortisation is Rs. 1,64,573, which is higher than the 12-month expected credit losses of Rs. 1,00,000. The liability is therefore adjusted to Rs. 1,64,573 (the higher of the two amounts) as follows

Particulars		Debit (Rs.)	Credit (Rs.)
Financial guarantee (liability)	Dr.	67,509	
To Profit and loss			67,509
(Being financial guarantee subsequently adjusted)			

31st March 2024

At 31st March 2024, there is 5% probability that Mohan Limited will default on the loan in the next 12 months. If Mohan Limited defaults on the loan, Surya Limited does not expect to recover any amount from Mohan Limited. The 12-month expected credit losses are therefore Rs. 1,25,000 (Rs. 25,00,000 x 5%).

The initial amount recognised less accumulated amortisation is Rs. 87,613, which is lower than the 12-month expected credit losses (Rs. 1,25,000). The liability is therefore adjusted to Rs. 1,25,000 (the higher of the two amounts) as follows:

Particulars		Debit (Rs.)	Credit (Rs.)
Financial guarantee (liability)	Dr.	39,573*	
To Profit and loss (Refer Note Below)			39,573*
(Being financial guarantee subsequently adjusted)			

* Note: The carrying amount at the end of 31st March 2023 will be Rs. 1,25,000 (i.e. Rs. 1,64,573 less 12-month expected credit losses of Rs. 39,573).

Question 27 : Nov 2022 – Paper

Jackson Limited is engaged in manufacturing and trading activities. It is in the process of preparation of consolidated financial statements of the group for the year ended 31st March 2022. During the year 2021-22, the company made a profit (after tax) of Rs.2,10,00,000 of which Rs.10,00,000 is attributable to Non-Controlling Interest (NCI). The long term finance of the company comprises the following :

- 10 crore equity shares of Rs.1 each at the beginning of the year and the company has further issued 2,50,00,000 shares on 1st October 2021 at full market value.
- 40 lakh irredeemable preference shares of Rs.10 each. These shares were in issue for the whole of the year ended 31st March 2022. The payment of dividend on these preference shares is discretionary.
- Rs.9 crore of 6% convertible debentures issued on 1st April, 2020 and repayable on 31st March, 2025 at par. Interest is payable annually. As an alternative to repayment at par, the holder on maturity can elect to the exchange their convertible debentures for 5 crore ordinary shares in the company. On 1st April, 2021 the prevailing market interest rate for 5 yearly 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 five years is 0.68 and the cumulative present value of Rs.1 payable at the end of years one to five is 3.99.

In the year ended 31st March, 2022 Jackson Limited declared a dividend of Rs.0.10 per share on the irredeemable preference shares.

You are required to :

- (i) Compute the finance cost of convertible debentures and its closing balance as on 31st March, 2022 to be presented in the consolidated financial statements.
- (ii) Compute the basic and diluted earnings per share for the year ended 31st March 2022. Assume that applicable income tax rate is 30% for Jackson Limited and its subsidiaries.

Solution :

(i) Calculation of the liability and equity components on 6% Convertible debentures:

Present value of principal payable at the end of 5th year (Rs. 90,000 thousand x 0.68)
= Rs. 61,200 thousand

Present value of interest payable annually for 5 years (Rs. 90,000 thousand x 6% x 3.99)
= Rs. 21,546 thousand

Total liability component = Rs. 82,746 thousand

Therefore, equity component = Rs. 90,000 thousand – Rs. 82,746 thousand
= Rs. 7,254 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
31.3.2021	82,746	6,620	5,400	83,966
31.3.2022	83,966	6,717	5,400	85,283

Finance cost of convertible debentures for the year ended 31.3.2022 is Rs. 6,717 thousand and closing balance as on 31.3.2022 is Rs. 85,283 thousand.

(ii) (a) Calculation of Basic EPS Rs. in '000

Profit for the year attributable to parent company	20,000
Less: Dividend on preference shares (4,000 thousand x Rs. 0.10)	<u>(400)</u>
Profit attributable to equity shareholders	<u>19,600</u>

Weighted average number of shares = 10,00,00,000 + {2,50,00,000 x (6/12*)}
= 11,25,00,000 shares or 1,12,500 thousand shares

Basic EPS = Rs. 19,600 thousand / 1,12,500 thousand shares
= Rs. 0.174

(b) Calculation of Diluted EPS Rs. in '000

Profit for the year		20,000
Less: Dividend on preference shares (4,000 x 0.10)		<u>(400)</u>
		19,600
Add: Finance cost (as given in the above table)	6,717.00	
Less: Tax @ 30%	<u>(2,015.10)</u>	<u>4,701.90</u>
		<u>24,301.90</u>

Weighted average number of shares = 10,00,00,000 + {2,50,00,000 x (6/12)*} + 5,00,00,000
 = 16,25,00,000 shares or 1,62,500 thousand shares
 Diluted EPS = Rs. 24,301.90 thousand / 1,62,500 thousand shares = Rs. 0.150

Question 28 : Nov 2022 – Paper

ENG Ltd. has developed model to measure the expected credit loss based on the lifetime expected credit loss model. Accordingly, the company has estimated the following provisioning matrix :

	Current	1-30 days past due	31-60 days past due	61-90 days past due	More than 90 days past due
Default Rate	0.3%	1.6%	3.6%	6.6%	10.6%

The Company has a portfolio of trade receivable of Rs.6 crores as on 31st March, 2022 and operates in only one geographical region. The customer base of company consists of large number of small clients and trade receivables are categorized by common risk characteristics that are representative of customer’s abilities to pay all amounts due as per the contractual terms. The trade receivables do not have significant financing component. The above provision matrix is based on its historically observed default rate over the expected life of the trade receivables and is adjusted for forward looking estimate.

The company has asked you to suggest whether the above system of making the provision for the expected credit loss is in accordance with the applicable Ind AS? If yes, then determine the expected credit loss for the Trade Receivables outstanding as on 31st March, 2022 on the following basis :

	Current	1-30 days past due	31-60 days past due	61-90 days past due	More than 90 days past due
% of Trade Receivables	50%	25%	13%	8%	4%

Solution :

To determine the expected credit losses for the portfolio, ENG Ltd. should use a provision matrix. The provision matrix will be based on its historical observed default rates over the expected life of the trade receivables and shall be adjusted for forward-looking estimates. At every reporting date the historical observed default rate shall be updated and changes in the forward-looking estimates shall be analysed. In this case, it is forecast that economic conditions will deteriorate over the next year. Therefore, as per para 5.5.15 of Ind AS 109, the loss allowance for trade receivables shall be measured at an amount equal to lifetime expected credit losses. On that basis, ENG Ltd. estimates the provision matrix.

The trade receivables from the large number of small customers amount to Rs. 6,00,00,000 and are measured using the provision matrix:

	Provision % age	Gross carrying amount	Default rate	Lifetime expected credit loss allowance (Gross carrying amount x

				lifetime expected credit loss rate)
a	b	C = Rs. 6 crore x b Rs.	d	e = c x d Rs.
Current	50%	3,00,00,000	0.3%	Rs. 90,000
1–30 days past due	25%	1,50,00,000	1.6%	Rs. 2,40,000
31–60 days past due	13%	78,00,000	3.6%	Rs. 2,80,800
61–90 days past due	8%	48,00,000	6.6%	Rs. 3,16,800
More than 90 days past due	4%	24,00,000	10.6%	Rs. 2,54,400
		<u>6,00,00,000</u>		<u>Rs. 11,82,000</u>

Question 29 : Nov 2022 – Paper

On 1st April 2021, Honey Limited acquired 40% interest in another entity, Smart Limited. Honey Limited determines that it is able to exercise significant influence over Smart Ltd. Honey Limited has paid total consideration of Rs.95,00,000 for acquiring the interest in Smart Ltd. On the date of acquisition, the book value of Smart Ltd.'s net asset was Rs.1,80,00,000 and their fair value was Rs.2,20,00,000. Honey Ltd. has determined that the difference of Rs.40,00,000 pertains to an item of property, plant and equipment which had remaining useful life of 10 years.

During the year 2021-22, Smart Ltd. made a profit of Rs.16,00,000. Smart Limited paid a dividend of Rs.24,00,000 on 31st March 2022. Smart Limited also holds a long term investment in equity securities. Under Ind AS, investment is classified as at FVTOCI in accordance with Ind AS 109 and Smart Ltd. recognized an increase in value of investment by Rs.4,00,000 in OCI during the year. Ignore deferred tax implications, if any.

You are required to ascertain the closing balance of Honey Limited's investments in Smart Limited as at 31st March 2022 as per the relevant Ind AS. (Use equity method).

Solution :

Calculation of Honey Ltd.'s investment in Smart Ltd. under equity method:

	Rs.	Rs.
Cost of investment		
Share in book value of net assets of Smart Limited (40% x 1,80,00,000)	72,00,000	
Share in fair valuation of net assets of Smart Limited (40% of (2,20,00,000-1,80,00,000))	16,00,000	
Goodwill on Investment in Smart Limited (95,00,000-72,00,000-16,00,000) (Balancing Figure)	<u>7,00,000</u>	95,00,000
Profit during the year		
Share in the profit reported by Smart Ltd. (40% of Rs. 16,00,000)	6,40,000	
Adjustment to reflect effect of fair valuation [40% of (Rs. 40,00,000/10 years)]	<u>(1,60,000)</u>	
Share of profit in Smart Ltd. recognised in income by Honey Ltd.		4,80,000

Long term equity investment	
FVTOCI gain recognised in OCI (40% of Rs. 4,00,000)	1,60,000
Dividend received by Honey Ltd. during the year [40% of Rs. 24,00,000]	<u>(9,60,000)</u>
Closing balance of Honey Ltd.'s investment in Smart Ltd.	<u>91,80,000</u>

Question 30 : May 2023 – RTP

State whether the following items meet the definition of Financial Asset or Financial Liability for an entity:

- (i) A bank advances an entity a five-year loan. The bank also provides the entity with an overdraft facility for a number of years.
- (ii) Entity A owns preference shares in Entity B. The preference shares entitle Entity A to dividends, but not to any voting rights.
- (iii) An entity has a present obligation in respect of income tax due for the prior year.
- (iv) In a lawsuit brought against an entity, a group of people is seeking compensation for damage to their health as a result of land contamination believed to be caused by waste from the entity's production process. It is unclear whether the entity is the source of the contamination since many entities operate in the same area and produce similar waste.

Solution :

- (i) The entity has two financial liabilities namely (a) the obligation to repay the fiveyear loan and (b) the obligation to repay the bank overdraft to the extent that it has borrowed using the overdraft facility. Both the loan and the overdraft result in contractual obligations for the entity to pay cash to the bank for the interest incurred and for the return of the principal.
- (ii) For Entity B: The preference shares may be equity instruments or financial liabilities of Entity B, depending on their terms and conditions. For Entity A: Irrespective of Entity B's treatment, the preference shares are a financial asset because the investment satisfies the definition of a financial asset.
- (iii) An income tax liability is created as a result of statutory requirements imposed by the government. The rights and obligations are not created by a contract. Hence, the liability for income-tax dues is not a financial liability.
- (iv) The fact that a lawsuit may result in the payment of cash does not create a financial liability for the entity because there is no contract between the entity and the affected group. The entity will need to consider providing for the payment as per Ind AS 37 'Provisions, Contingent Liabilities and Contingent Assets'.

Question 31 : May 2023 – RTP

In an arm's length transaction, Entity X buys 10,000 convertible preference shares in Company Z for cash payments of Rs. 40,000, with Rs. 25,000 payable immediately and Rs. 15,000 payable in two years. The market rate of annual interest for a two-year loan to the entity would be 6%.

Explain the accounting treatment for the said transaction.

Solution :

Since payment of Rs. 15,000 is deferred for two years, the fair value of the consideration given for the shares is equal to Rs. 25,000 plus the present value of Rs. 15,000. The present value of Rs. 15,000 deferred payment is Rs. 13,350 (Rs. 15,000 ÷ 1.062).

Entity X will initially measure the shares purchased at Rs. 38,350 (i.e., Rs. 25,000 + Rs. 13,350). Since this transaction took place at an arm's length, this is considered to be fair value for initial recognition in the absence of evidence to the contrary. The difference between the Rs. 40,000 cash paid out and the Rs. 38,350, i.e. Rs. 1,650, will be recognised as interest expense in profit or loss over the two year period of deferred payment.

Question 32 : May 2023 – Paper

Autumn Limited has a policy of providing subsidized loans to its employees for their personal purposes. Mrs. Jama Bai, a senior HR manager in the Company, took a loan of Rs.12.00 lakhs on the following terms:

- Interest rate 4 % per annum
- Loan disbursement date : 1st April 2019
- The principal amount of the loan shall be recovered in 4 equal annual installments commencing from 31st March 2020
- The accumulated interest computed on reducing balance at simple interest is collected in 3 equal annual installments after collection of the principal amount
- Mrs. Jama Bai must remain in service till the principal and interest are paid
- The market rate of a comparable loan to Mrs. Jama Bai is 9% per annum
- The present value of Rs.1 at 9% per annum at the end of respective years is as follows :

Year ending 31 st March	2020	2021	2022	2023	2024	2025	2026
Present Value	0.9174	0.8417	0.7722	0.7084	0.6499	0.5963	0.5470

Under the assumption that no probable future economic benefits except the return of loan has been guaranteed by the employee, you are required to :

- i. Provide the journal entries at the time of initial recognition of loan on 1st April 2019 and as at 31st March 2020; and
- ii. Prepare ledger account of 'Loan to Mrs. Jama Bai' from the inception of the loan till its final payment.

Solution :

(i)

Journal Entry

Date	Particulars	Dr. Rs.	Cr. Rs.
01-04-2019	Loan to Mrs. Jama Bai A/c	Dr. 10,43,638	
	Pre-paid employee cost A/c	Dr. 1,56,362	
	To Bank A/c		12,00,000

	(Being loan to employee recorded at fair value)			
31-03-2020	Loan to Mrs. Jama Bai A/c To Finance Income A/c (Being finance income @ 9% recorded in the books)	Dr.	93,927	93,927
31-03-2020	Bank A/c To Loan to Mrs. Jama Bai A/c (Being installment received at the end of the year)	Dr.	3,00,000	3,00,000

(ii)

In the books of Autumn Ltd.

Loan to Mrs. Jama Bai A/c

Date	Particulars	Amount (Rs.)	Date	Particulars	Amount (Rs.)
1.4.2019	To Bank A/c	10,43,638	31.3.2020	By Bank A/c	3,00,000
31.3.2020	To Finance income (W.N.3)	93,927	31.3.2020	By Balance c/d	8,37,565
		11,37,565			11,37,565
1.4.2020	To Balance b/d	8,37,565	31.3.2021	By Bank A/c	3,00,000
31.3.2021	To Finance income (W.N.3)	75,381	31.3.2021	By Balance c/d	6,12,946
		9,12,946			9,12,946
1.4.2021	To Balance b/d	6,12,946	31.3.2022	By Bank A/c	3,00,000
31.3.2022	To Finance income (W.N.3)	55,165	31.3.2022	By Balance c/d	3,68,111
		6,68,111			6,68,111
1.4.2022	To Balance b/d	3,68,111	31.3.2023	By Bank A/c	3,00,000
31.3.2023	To Finance income (W.N.3)	33,130	31.3.2023	By Balance c/d	1,01,241
		4,01,241			4,01,241
1.4.2023	To Balance b/d	1,01,241	31.3.2024	By Bank A/c	40,000
31.3.2024	To Finance income (W.N.3)	9,112	31.3.2024	By Balance c/d	70,353
		1,10,353			1,10,353
1.4.2024	To Balance b/d	70,353	31.3.2025	By Bank A/c	40,000
31.3.2025	To Finance income (W.N.3)	6,332	31.3.2025	By Balance c/d	36,685
		76,685			76,685
1.4.2025	To Balance b/d	36,685	31.3.2026	By Bank A/c	40,000
31.3.2026	To Finance income (W.N.3)	3,315*			40,000
		40,000			40,000

*Difference of Rs. 13 (Rs. 3,315 – Rs. 3,302) is due to approximation.

Working Notes:

1. Calculation of initial recognition amount of loan to employee

Year	Estimated Cash Flows	PV Factor @9%	Present Value
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	Rs.		Rs.
31-03-2020	3,00,000	0.9174	2,75,220
31-03-2021	3,00,000	0.8417	2,52,510
31-03-2022	3,00,000	0.7722	2,31,660
31-03-2023	3,00,000	0.7084	2,12,520
31-03-2024	40,000 (W.N.2)	0.6499	25,996
31-03-2025	40,000 (W.N.2)	0.5963	23,852
31-03-2026	40,000 (W.N.2)	0.547	21,880
Fair Value of Loan			10,43,638

2. Computation of Interest to be paid

Year	Opening outstanding balance	Cash Flows	Principal outstanding at year end	Interest @ 4% on a	Cumulative Interest
	a	b	c	d	e
		Rs.	Rs.	Rs.	Rs.
31-03-2020	12,00,000	3,00,000	9,00,000	48,000	48,000
31-03-2021	9,00,000	3,00,000	6,00,000	36,000	84,000
31-03-2022	6,00,000	3,00,000	3,00,000	24,000	1,08,000
31-03-2023	3,00,000	3,00,000	Nil	12,000	1,20,000
31-03-2024	1,20,000	40,000 (1,20,000/3)			
31-03-2025		40,000 (1,20,000/3)			
31-03-2026		40,000 (1,20,000/3)			

3. Computation of finance cost as per amortization table

Year	Opening Balance	Interest @ 9%	Repayment	Closing Balance
	(1)	(2)	(3)	(1+2+3)
		Rs.	Rs.	Rs.
01-04-2019				10,43,638
31-03-2020	10,43,638	93,927	3,00,000	8,37,565
31-03-2021	8,37,565	75,381	3,00,000	6,12,946
31-03-2022	6,12,946	55,165	3,00,000	3,68,111
31-03-2023	3,68,111	33,130	3,00,000	1,01,241
31-03-2024	1,01,241	9,112	40,000	70,353
31-03-2025	70,353	6,332	40,000	36,685

31-03-2026	36,685	3,315*	40,000	Nil
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*Difference of Rs.13 (Rs.3,315 – Rs.3,302) is due to approximation.

Question 33 : May 2023 – Paper

Weak Limited, which is a fully owned subsidiary company of Strong Limited approached Strong Limited for an interest free loan for mitigation of its financial difficulties. Strong Limited provide the loan to Weak Limited on the following terms and conditions :

Nature of loan	Interest Free
Amount of Loan	Rs.60,00,000
Date of disbursement of loan	April 1, 2021
Loan period	3 years
Loan repayable by Weak Ltd.	On March 31, 2024
Market rate of interest for similar loan	8% (both for holding and subsidiary) per annum
P.V Factor of Rs.1 at the end of 3 rd year at 8% per annum is	0.7938

Assuming that there are no transaction costs, you are required to pass necessary accounting entries in the books of Weak Limited for all the three years.

Solution :

Accounting in the books of Weak Ltd (Subsidiary)

Date	Particulars	Amount	Amount
1.4.2021	On the date of loan		
	Bank A/c Dr.	60,00,000	
	To Loan from Strong Ltd. (Payable)		47,62,800
	To Equity (Deemed capital contribution from ABC Ltd.)		12,37,200
	(Being the loan taken from Strong Ltd. recognised at fair value)		
31.3.2022	At the end of Year 1		
	Interest expense (Finance cost) Dr.	3,81,024	
	To Loan from Strong Ltd. (Payable)		3,81,024
	(Being interest expense recognised)		
31.3.2023	At the end of Year 2		
	Interest expense (Finance cost) Dr.	4,11,506	
	To Loan from Strong Ltd. (Payable)		4,11,506
	(Being interest expense recognised)		
31.3.2024	At the end of Year 3		
	Interest expense (Finance cost) Dr.	4,44,670*	
	To Loan from Strong Ltd. (Payable)		4,44,670

	(Being interest expense recognised)			
31.3.2024	On repayment of loan			
	Loan from Strong Ltd. (Payable)	Dr.	60,00,000	
	To Bank A/c			60,00,000
	(Being loan repaid by Weak Ltd.)			

*Difference is due to approximation.

Working Notes:

- Present Value of Loan** = Rs. 60,00,000 x 0.7938 = Rs. 47,62,800
- Amortisation table for computation of interest:

Year end	Opening balance (1)	Interest @ 8% (2)	Repayment (3)	Closing balance (1) + (2) - (3)
1	47,62,800.00	3,81,024.00	-	51,43,824.00
2	51,43,824.00	4,11,506.00	-	55,55,330.00
3	55,55,330.00	4,44,670.00*	60,00,000.00	-

*Difference is due to approximation.

Question 34 : Nov 2023 – RTP

On 1st April, 20X1, a bank provides an entity with a four-year loan of Rs. 5,000 on normal market terms, including charging interest at a fixed rate of 8% per year. Interest is payable at the end of each year. The figure of 8% is the market rate for similar four-year fixed-interest loans with interest paid annually in arrears. Transaction cost of Rs. 100 is incurred on originating the loan. Effective interest rate in this case is 8.612%.

In 20X1-20X2, the entity experienced financial difficulties. On 31st March, 20X2, the bank agreed to modify the terms of the loan. Under the new terms, the interest payments in 20X2-20X3 to 20X4-20X5 will be reduced from 8% to 5%. The entity paid the bank a fee of Rs. 50 for paperwork relating to the modification.

Analyse whether the modification of the loan terms constitutes an extinguishment of the original financial liability or not.

Solution :

Since the interest was initially set at the market rate, on 1st April, 20X1 the entity on initial recognition will measure the loan at the transaction price, less transaction costs i.e. at Rs. 4,900. The following is the original amortised cost calculation at 1st April, 20X1:

Time	Carrying amount at 1st April	Effective Interest @ 8.612%	Cash outflow	Carrying amount at 31st March
	(a)	(b=ax8.612%)	(c=5000x8%)	(d = a + b - c)
20X1-20X2	4,900.00	421.99	(400.00)	4,921.99
20X2-20X3	4,921.99	423.88	(400.00)	4,945.87
20X3-20X4	4,945.87	425.94	(400.00)	4,971.81
20X4-20X5	4,971.81	428.19	(5,400.00)	-

At 31st March, 20X2:

1. The present value of the remaining cash flows of the original financial liability is Rs. 4,921.99 discounted at the original effective interest rate of 8.612%.
2. The present value of the cash flows under the new terms discounted using the original effective interest rate is Rs. 4,537.25 (Refer W.N.). Including the Rs. 50 fee, the present value of the total cash flows is Rs. 4,587.25.
3. The difference between Rs. 4,921.99 and Rs. 4,587.25 is Rs. 334.74 which is only 6.8% (Rs. 334.74 ÷ Rs. 4,921.99) of the present value of the remaining cash flows of the original financial liability.

The entity applies its judgement to decide whether the terms of the instruments exchanged are substantially different. Since the difference of the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is less than 10% of the present value of the remaining cash flows of the original financial liability, this modification should not be considered a substantial modification of the terms of the existing loan. Therefore, the modification would not be accounted for as an extinguishment of the original financial liability.

Working Note:

The calculation of the present value of the cash flows under the new terms discounted using the original effective interest rate is as follows:

Time	Cash outflow	Discounting factor @ 8.612%	Present value at 31st March
31st March, 20X3	250.00	0.921	230.25
31st March, 20X4	250.00	0.848	212.00
31st March, 20X5	5,250.00	0.780	<u>4,095.00</u>
Total present value			<u>4,537.25</u>

Question 35 : Nov 2023 – Paper

Ore Exploration Ltd. is engaged in the manufacturing of drilling and mining equipment for over last 25 years. The management of the company is planning to expand the manufacturing activities for which funds are needed. On 1st April, 2019, to meet out the financial requirement Ore Exploration Ltd. issued 50,000, Compulsory Convertible Cumulative Preference Shares (CCCPS) of Rs. 100 each. These preference shares carry a coupon rate of 12% p.a. and is payable every year. The Company has substantial profits for payment of preference dividend. Under the terms of instrument, every two preference shares are convertible into 1 equity share of Rs. 100 each at the end of 4th year. The prevailing annual market interest rate for a similar debt without conversion option is 15% per annum. The transaction cost of completing the issue process of the instrument is 3% of the proceeds. The effective interest rate is 16.60% per annum.

You are required to:

- (i) Compute the liability and equity component;
- (ii) Provide the 'liability' ledger account for various years at amortized cost using the effective interest rate;
- (iii) Pass necessary accounting entries for the whole period.

Note: Use the following present values of Re. 1 at different discounting factors for the purpose of calculation, wherever required.

Year	1	2	3	4
13%	0.8850	0.7831	0.6931	0.6133
15%	0.8696	0.7561	0.6575	0.5718
18%	0.8475	0.7182	0.6086	0.5158

Solution :

This is a compound financial instrument with two components – liability representing present value of future cash outflows (i.e. dividend) and balance represents equity component.

(i) Computation of Liability & Equity Component

Date	Particulars	Cash Flow	Discount Factor @ 15%	Net present Value
1st April, 2019		0	1	0.00
31st March, 2020	Dividend	6,00,000	0.8696	5,21,760
31st March, 2021	Dividend	6,00,000	0.7561	4,53,660
31st March, 2022	Dividend	6,00,000	0.6575	3,94,500
31st March, 2023	Dividend	6,00,000	0.5718	<u>3,43,080</u>
Total Liability Component				17,13,000
Total Proceeds				<u>50,00,000</u>
Total Equity Component (Bal fig)				<u>32,87,000</u>

a. Allocation of transaction costs

Particulars	Amount	Allocation of 3% transaction cost	Net Amount
Liability Component	17,13,000	51,390	16,61,610
Equity Component	<u>32,87,000</u>	<u>98,610</u>	<u>31,88,390</u>
Total Proceeds	<u>50,00,000</u>	<u>1,50,000</u>	<u>48,50,000</u>

b. Accounting for liability at amortised cost:

- Initial accounting = Present value of cash outflows less transaction costs
- Subsequent accounting = At amortised cost, ie, initial fair value adjusted for interest and repayments of the liability.

	Opening Financial Liability A	Interest @ 16.60% B	Cash Flow C	Closing Financial Liability A+B-C
1st April, 2019	16,61,610	-	-	16,61,610
31st March, 2020	16,61,610	2,75,827	6,00,000	13,37,437
31st March, 2021	13,37,437	2,22,015	6,00,000	9,59,452
31st March, 2022	9,59,452	1,59,269	6,00,000	5,18,721
31st March, 2023	5,18,721	81,279*	6,00,000	

* Difference of Rs. 4,829 (i.e. 86,108 – 81,279) is due to approximation.

(ii) **Preference Shares (Liability) Account**

Date	Particulars	Amount	Date	Particulars	Amount
31.3.2020	To Bank	6,00,000.00	1.4.2019	By Bank	16,61,610.00
31.3.2020	To Balance c/d	<u>13,37,437.00</u>	31.3.2020	By Finance Cost	<u>2,75,827.00</u>
		<u>19,37,437.00</u>			<u>19,37,437.00</u>
31.3.2021	To Bank	6,00,000.00	1.4.2020	By Balance b/d	13,37,437.00
31.3.2021	To Balance c/d	<u>9,59,452.00</u>	31.3.2021	By Finance Cost	<u>2,22,015.00</u>
		<u>15,59,452.00</u>			<u>15,59,452.00</u>
31.3.2022	To Bank	6,00,000.00	1.4.2021	By Balance b/d	9,59,452.00
31.3.2022	To Balance c/d	<u>5,18,721.00</u>	31.3.2022	By Finance Cost	<u>1,59,269.00</u>
		<u>11,18,721.00</u>			<u>11,18,721.00</u>
31.3.2022	To Bank	6,00,000.00	1.4.2022	By Balance b/d	5,18,721.00
			31.3.2023	By Finance Cost	<u>81,279.00</u>
		<u>6,00,000.00</u>			<u>6,00,000.00</u>

(iii) **Journal Entries to be recorded for entire term of arrangement**

Date	Particulars	Debit	Credit
1.4.2019	Bank A/c Dr. To Preference Shares (Liability) A/c To Equity Component of Preference shares A/c (Being compulsorily convertible preference shares issued. The same are divided into equity component and liability component as per the calculation)	48,50,000	16,61,610 31,88,390
31.3.2020	Preference Shares (Liability) A/c Dr. To Bank A/c (Being dividend at the coupon rate of 12% paid to the shareholders)	6,00,000	6,00,000
31.3.2020	Finance cost A/c Dr. To Preference Shares (Liability) A/c (Being interest as per EIR recorded)	2,75,827	2,75,827
31.3.2021	Preference Shares (Liability) A/c Dr. To Bank A/c (Being dividend at the coupon rate of 12% paid to the shareholders)	6,00,000	6,00,000
31.3.2021	Finance cost A/c Dr. To Preference Shares (Liability) A/c (Being interest as per EIR recorded)	2,22,015	2,22,015
31.3.2022	Preference Shares (Liability) A/c Dr. To Bank A/c (Being dividend at the coupon rate of 12% paid to the shareholders)	6,00,000	6,00,000
31.3.2022	Finance cost A/c Dr. To Preference Shares (Liability) A/c (Being interest as per EIR recorded)	1,59,269	1,59,269

31.3.2023	Preference Shares (Liability) A/c To Bank A/c (Being dividend at the coupon rate of 12% paid to the shareholders)	Dr.	6,00,000	6,00,000
31.3.2023	Finance cost A/c To Preference Shares (Liability) A/c (Being interest as per EIR recorded)	Dr.	81,279	81,279
31.3.2023	Equity Component of Preference shares A/c To Equity Share Capital A/c To Securities Premium A/c (Being Preference shares converted in equity shares and remaining equity component is recognised as securities premium)	Dr.	31,88,390	25,00,000 6,88,390

Question 36 : Nov 2023 – Paper

Poor Limited borrowed 120 Lakhs from a Scheduled Bank. The terms of loan are as under:

- Rate of Interest @ 10% per annum, payable yearly
- Tenure of Loan 12 Years.
- Principal to be paid at the end of tenure i.e. 12th Year.

Poor Limited defaulted in payment of Interest in year 5, 6, 7 and 8. A loan reschedule agreement took place at the end of 9th year with the Bank. As per the agreement, Poor Limited is required to pay Rs. 220 Lakhs at the end of 10th year. The default continued till the end of 10th year.

You are required to calculate as per relevant Ind AS:

- (i) Book Value of the Loan at the end of the 10th Year.
- (ii) Additional amount to be paid to the Bank on Account of Rescheduling.
(assume interest is compounded in the case of default).

Solution :

(i) Computation of book value of the loan at the end of 10th year

$$= \text{Rs. } 1,20,00,000 \times 1.10 \times 1.10 \times 1.10 \times 1.10 \times 1.10 \times 1.10$$

$$= \text{Rs. } 2,12,58,732 \text{ (i.e. adding interest for 5th to 10th year)}$$

(ii) Computation of additional amount to be paid to bank on rescheduling

$$\text{Rescheduled amount to be paid at the end of the 10th year} = \text{Rs. } 2,20,00,000$$

$$\text{Additional amount to be paid on rescheduling} = \text{Rs. } 2,20,00,000 - \text{Rs. } 2,12,58,732$$

$$= \text{Rs. } 7,41,268$$

Question 37 : May 2024 – Paper

The CFO of GOLD Limited, a manufacturing company, provided you the following information for your valuable opinion.

The Company had issued 8% convertible debentures amounting to Rs. 320 Lakhs on 1st April, 2022 and repayable on 31st March, 2026 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 250 Lakhs ordinary shares in the company. On 1st April, 2022, the prevailing market interest rate

for four-year convertible debentures which had no right of conversion was 10%. Using an annual discount rate of 10%, the present value of Rs. 1 payable in 4th year is 0.683 and the cumulative present value of Rs. 1 payable at the end of years one to four is 3.169. From the above information you are required to calculate the finance cost of convertible debentures and its closing balance as on 31st March, 2024 to be presented in the financial statements.

Solution :

This instrument has two components –

- (1) Mandatory annual interest to be paid by the issuer on convertible debentures of Rs. 3,20,00,000 @ 8% till 4 years, and
- (2) Payment of the principal amount at the end of 4th year.

However, since the holder has the option to convert the debentures into shares on maturity, as per Ind AS 32, the instrument is a compound financial instrument which carries elements of both liability and equity.

Statement showing computation of liability and equity component in the compound financial instrument.

	Rs.
Present value of interest payable during 4 years discounted at 10% (i.e. Rs. 3,20,00,000 x 8% x 3.169)	81,12,640
Present value of principal payable at the end of 4th year discounted at 10% (Rs. 3,20,00,000 x 0.683)	<u>2,18,56,000</u>
Liability component of the compound financial instrument	2,99,68,640
Equity component of the financial instrument (Balancing Figure)	<u>20,31,360</u>
Total proceed	<u>3,20,00,000</u>

Computation of finance cost to be charged to the financial instrument

Date	Opening balance	Finance cost	Interest outflow	Outstanding balance at the end of the year
	a	b = a x 10%	3,20,00,000 x 8%	d = (a+b-c)
	Rs.	Rs.	Rs.	Rs.
31.3.2023	2,99,68,640	29,96,864	25,60,000	3,04,05,504
31.3.2024	3,04,05,504	30,40,550	25,60,000	3,08,86,054
31.3.2025	3,08,86,054	30,88,605	25,60,000	3,14,14,654
31.3.2026	3,14,14,654	31,45,346	25,60,000	3,20,00,000

Rs. 31,45,346 - Rs. 31,41,466 = Rs. 3,880 is due to approximation and rounding off.

According to the above table, finance cost to be charged in the Statement of Profit and Loss = Rs. 30,40,550.

The closing balance of liability component of convertible debentures to be presented in the balance sheet would be Rs. 3,08,86,054 and equity component would be Rs. 20,31,360.

Question 38 : Nov 2024 – Paper

On 1st January 2023, Joe & Co Limited, an Indian listed company which prepares its financial statements on a quarterly basis has entered into a written put option for USD (\$) 40,000 with Box Limited to be settled in future on 31st December 2023 for a rate equal to Rs.78 per USD at the option of Box Limited. Joe & Co Limited did not receive any amount upon entering into the contract.

For the purpose of accounting, use the following information representing marked to market fair value of put option contract at each reporting date.

As at 31st March 2023	– Rs.(50,000)
As at 30th June 2023	– Rs.(30,000)
As at 30th September 2023	– Rs. NIL
Spot rate of USD on 31st December 2023	– Rs.76 per USD.

Evaluate and explain whether the above option meets the definition of derivatives as laid down in Ind AS 109 and record the entries for each quarter ended till the date of actual purchase of USD.

Solution :

(a) Assessment of the arrangement using the definition of derivative included under Ind AS 109

Derivative is a financial instrument or other contract within the scope of this Standard with all three of the following characteristics:

- (a) its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract (sometimes called the 'underlying').
- (b) it requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors.
- (c) it is settled at a future date.

The contract meets the definition of a derivative as follows:

- (a) the value of the contract to purchase USD at a fixed price changes in response to changes in foreign exchange rate.
- (b) the initial amount received to enter into the contract is zero. A contract which would give the holder a similar response to foreign exchange rate changes would have required an investment of USD 40,000 on inception.
- (c) the contract is settled in future

The derivative liability is a written put option contract.

As per Ind AS 109, derivatives are measured at fair value upon initial recognition and are subsequently measured at fair value through profit and loss.

• **Accounting on 1st January, 2023**

As there was no consideration paid and without evidence to the contrary the fair value of the contract on the date of inception is considered to be zero. Accordingly, no accounting entries shall be recorded on the date of entering into the contract.

- **Accounting on 31st March, 2023**

The value of the derivative put option contract shall be recorded as a derivative financial liability in the books of Joe & Co. Ltd. by recording the following journal entry:

Particulars		Dr. (Rs.)	Cr. (Rs.)
Profit and loss A/c	Dr.	50,000	
To Derivative financial liability			50,000
(Being mark to market loss on the put option contract recorded)			

- **Accounting on 30th June, 2023**

The change in value of the derivative put option contract shall be recorded as a derivative financial liability in the books of Joe & Co. Ltd. by recording the following journal entry:

Particulars		Dr. (Rs.)	Cr. (Rs.)
Derivative financial liability A/c	Dr.	20,000	
To Profit and loss A/c			20,000
(Being partial reversal of mark to market loss on the put option contract recorded)			

- **Accounting on 30th September, 2023**

The change in value of the derivative option contract shall be recorded at zero in the books of Joe & Co. Ltd. by recording the following journal entry

Particulars		Dr. (Rs.)	Cr. (Rs.)
Derivative financial liability A/c	Dr.	30,000	
To Profit and loss A/c			30,000
(Being gain on mark to market of put option contract booked to make the value of the derivative liability as zero)			

- **Accounting on 31st December, 2023**

The settlement of the derivative put option contract by actual purchase of USD 40,000 shall be recorded in the books of Joe & Co. Ltd. upon exercise by Box Ltd. by recording the following journal entry:

Particulars		Dr. (Rs.)	Cr. (Rs.)
Bank (USD Account) (@40,000 x Rs. 76)	Dr.	30,40,000	
Profit and loss A/c	Dr.	80,000	
To Bank (@ 40,000 x Rs. 78)			31,20,000
(Being loss on settlement of put option contract booked on actual purchase of USD)			

Question 39 : May 2025 – RTP

On 1st April, 20X1, ABC Ltd. issues a 10- year bond with a par value of Rs. 15,00,000 and an annual fixed coupon rate of 8%, which is consistent with market rates for bonds with similar characteristics. ABC Ltd. uses Secured Overnight Financing Rate (SOFR) as its benchmark interest rate. At the date of inception of the bond, SOFR is 5%. At the end of the first year:

- SOFR has decreased to 4.75%; and
- The fair value of bond is Rs. 15,38,110. This value is consistent with an interest rate of 7.6%.
- The remaining cash flows on bond are Rs. 1,20,000 per year for nine years and Rs. 15,00,000 at the end of ninth year. These cash flows discounted at 7.6% equals Rs. 15,38,110.

ABC Ltd. assumes a flat yield curve, that all changes in interest rates result from a parallel shift in the yield curve, and that the changes in SOFR are the only relevant changes in market conditions. Following discounting factors may be considered

Discount rate @7.75%	Present value of Rs. 1 payable
At the end of year 9	51.1 paise
Cumulatively for the years 1–9	6.312
At the end of year 10	47.4 paise
Cumulatively for the years 1–10	6.786

Required

What is the amount transferred to the OCI at the end of Year 1 when bonds were measured at fair value?

Solution :

The amount of change in fair value of the bond that is not attributable to changes in market conditions giving rise to market risk is estimated as follows:

Step (a)

The bond’s IRR at the start of the period is 8%.

Step (b)

Because the benchmark interest rate (SOFR) is 5%, the instrument - specific component of the IRR is 3%.

Step (c)

The contractual cash flows of the instrument at the end of the period are:

- Interest of Rs. 1,20,000 [Rs. 15,00,000 x 8%] per year for the next 9 years.
- Principal repayment of Rs. 15,00,000 at the end of 9th year.

The present value of these cash flows is calculated using a discount rate of 7.75%. This rate is arrived at as below:

- 4.75% end of period SOFR, plus
- 3% instrument - specific component calculated as at the start of the period

This gives a notional present value of Rs. 15,23,940
 = [(15,00,000 x 0.511) + (1,20,000 x 6.312)].

Step (d)

The fair value of the liability at the end of the period is Rs. 15,38,110. Hence, ABC Ltd. should present Rs. 14,170 [Rs. 15,38,110 – Rs. 15,23,940] in the OCI.

Question 40 : May 2025 – RTP

On 1st April, 2X01, A Ltd. issued a 10% convertible debenture with a face value of Rs. 1,000 maturing on 31st March, 2X11. The debenture is convertible into equity share of A Ltd. at the option of the holder at a conversion price of Rs. 25 per share. Interest is payable half-yearly in cash. At the date of issue, A Ltd. could have issued non-convertible debt with a ten-year term bearing a coupon interest rate of 11%.

On 1st April, 2X06, the convertible debenture has a fair value of Rs. 1,700.

A Ltd. makes a tender offer to the holder of the debenture to repurchase the debenture for Rs. 1,700, which the holder accepts. On the date of repurchase, A Ltd. could have issued non-convertible debt with a five-year term bearing a coupon interest rate of 8%.

Required

How does A Ltd. account for the repurchase?

Solution :

In the financial statements of A Ltd., the carrying amount of the debenture is allocated on issue as follows:

	Rs.
Liability component	
Present value of 20 half-yearly interest payments of Rs. 50, discounted at 11% (Rs. 50 x 11.95)	598
Present value of Rs. 1,000 due in 10 years, discounted at 11%, compounded half-yearly (Rs. 1,000 x 0.342)	<u>342</u>
	940
Equity component	
Difference between Rs. 1,000 total proceeds and Rs. 940 allocated above	<u>60</u>
Total proceeds	1,000

The repurchase price is allocated as follows:

	Carrying Value (Rs.)	Fair Value (Rs.)	Difference (Rs.)
Liability component:			
Present value of 10 remaining half-yearly interest Payments of Rs. 50, discounted at 11% and 8% respectively	377	406	
Present value of Rs. 1,000 due in 5 years, discounted at 11% and 8%, compounded half yearly, respectively	<u>585</u>	<u>676</u>	

	962	1,082	(120)
Equity component	60	618	(558)
Total	1,022	1,700	(678)

A Ltd. recognises the repurchase of the debenture as follows: (Rs.)

Liability component	Dr.	962	
Debt settlement expense (P&L)	Dr.	120	
To Cash			1,082
(To recognize the repurchase of the liability component)			
Equity component	Dr.	60	
Reserves and Surplus	Dr.	558	
To Cash			618
(To recognize the cash paid for the equity component)			

The debt settlement expense represents the difference between the carrying value of the debt component and its fair value.

Question 41 : May 2025 – Paper

On 1st April, 2023, Mera Limited raised a term loan of Rs. 5,00,00,000 from Tera Finance Limited, a Non-Banking Finance Company on the following terms and conditions:

- Rate of Interest: 11% per annum payable annually on accrual basis.
- Repayment: The term loan would be repaid in five annual instalments of Rs. 1,00,00,000 each commencing from 31st March, 2024.

Mera Limited also incurred, upfront, a sum of Rs. 5,90,000 being loan processing charges.

The effective rate of interest on loan was 11.50% per annum.

Due to liquidity constraints, Mera Limited was unable to honour its obligation of repayment of the loan instalment which fell due on 31st March, 2025. Accordingly, it approached the lender on 31st March, 2025. Both the parties agreed to restructure the outstanding term loan on the following terms:

- Rate of Interest: The revised rate of interest on the outstanding loan would be 15% per annum payable annually on accrual basis.
- Repayment: The loan would be repaid in eight annual instalments of Rs. 50,00,000 each commencing from 31st March, 2026.

No further cost is incurred by Mera Limited towards restructuring of the loan.

You are required to record the necessary journal entries in the books of Mera Limited from 1st April, 2023 to 31st March, 2026 after giving effect to the changes in the terms of the loan.

The following present values of Rs. 1 are provided:

Interest Rate	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8
11%	0.901	0.812	0.731	0.659	0.593	0.535	0.482	0.434
11.5%	0.897	0.804	0.721	0.647	0.580	0.520	0.467	0.419
15%	0.870	0.756	0.658	0.572	0.497	0.432	0.376	0.327

Solution :

On the date of initial recognition, the effective interest rate of the loan shall be computed keeping in view the contractual cash flows and upfront processing fee paid. The following table shows the amortisation of loan based on effective interest rate:

Date	Opening Balance	Cash outflows (principal)	Cash outflows (interest and fee)	Interest [EIR @ 11.50%]	Closing Balance (amortised cost)
	(a)	(b)	(c) = [(5,00,00,000 - instalments paid till previous year) x 11%]	(d) = [a x 11.50%]	(e) = (a) – (b) – (c) + (d)
01-Apr-23	-5,00,00,000	5,90,000			4,94,10,000
31-Mar-24	4,94,10,000	1,00,00,000	55,00,000	56,82,150	3,95,92,150
31-Mar-25	3,95,92,150	1,00,00,000	44,00,000	45,53,097	2,97,45,247
31-Mar-26	2,97,45,247	1,00,00,000	33,00,000	34,20,703	1,98,65,950
31-Mar-27	1,98,65,950	1,00,00,000	22,00,000	22,84,584	99,50,534
31-Mar-28	99,50,534	1,00,00,000	11,00,000	11,49,466*	(0)

*Difference of Rs. 5,155 (11,49,466 – 11,44,311) is due to rounding off.

a. 1st April, 2023

Particulars		Rs.	Rs.
Bank A/c	Dr.	4,94,10,000	
To Loan from Tera Finance Limited A/c (Being loan recorded at its fair value less transaction costs on the initial recognition date)			4,94,10,000

31st March, 2024

Particulars		Rs.	Rs.
Loan from Tera Finance Limited A/c	Dr.	98,17,850	
Interest expense (profit and loss)	Dr.	56,82,150	
To Bank A/c (1,00,00,000 + 55,00,000) (Being first instalment of loan and payment of interest accounted for as an adjustment to the amortised cost of loan)			1,55,00,000

31st March, 2025 – Before Mera Limited approached the bank

Particulars		Rs.	Rs.
Interest expense (profit and loss)	Dr.	45,53,097	
To Loan from Tera Finance Limited A/c To Bank A/c (Being loan payment of interest recorded by the Company before it approached the Bank for deferment of principal)			1,53,097 44,00,000

Upon receiving the new terms of the loan, Mera Limited, re-computed the carrying value of the loan by discounting the new cash flows with the original effective interest rate and comparing the same with the current carrying value of the loan. As per requirements of Ind AS 109, any change of more than 10% shall be considered a substantial modification, resulting in fresh accounting for the new loan:

Date	Cash flows (principal)	Interest outflow @15%	Discount factor @ 11.50%	PV of cash flows
	(a)	(b)	(c)	(a + b) x c
31-Mar-25	(4,00,00,000)			
31-Mar-26	50,00,000	60,00,000	0.897	98,67,000
31-Mar-27	50,00,000	52,50,000	0.804	82,41,000
31-Mar-28	50,00,000	45,00,000	0.721	68,49,500
31-Mar-29	50,00,000	37,50,000	0.647	56,61,250
31-Mar-30	50,00,000	30,00,000	0.580	46,40,000
31-Mar-31	50,00,000	22,50,000	0.520	37,70,000
31-Mar-32	50,00,000	15,00,000	0.467	30,35,500
31-Mar-33	50,00,000	7,50,000	0.419	24,09,250
PV of new contractual cash flows discounted at 11.50%				4,44,73,500
Carrying amount of loan (3,95,92,150 +1,53,097)				3,97,45,247
Difference				47,28,253
Percentage of difference to carrying amount				11.90%

Considering a more than 10% change in PV of cash flows compared to the carrying value of the loan, the existing loan shall be considered to have been extinguished and the new loan shall be accounted for as a separate financial liability.

The accounting entries for the same are included below:

b. 31st March, 2025 – Accounting for Extinguishment

Particulars		Rs.	Rs.
Loan from Tera Finance Limited (old) A/c	Dr.	3,97,45,247	
Loss on modification of loan (profit and loss)	Dr.	2,54,753	
To Loan from Tera Finance Limited (new) A/c			4,00,00,000
(Being new loan accounted for at its principal amount by correspondingly derecognising the existing loan)			

31 March, 2026

Particulars		Rs.	Rs.
Loan from Tera Finance Limited A/c	Dr.	50,00,000	
Interest expense (profit and loss)	Dr.	60,00,000	
To Bank A/c			1,10,00,000
(Being first instalment of the principal of new loan and payment of interest accounted)			

Question 42 : Sept 2025 – RTP

Zx issues a fixed-rate loan for Rs. 500,000 and incurs issue costs of Rs. 20,000, resulting in an initial carrying value of Rs. 480,000. The loan carries an interest rate of 8% per annum, and it is repayable at par at the end of year 10. However, under the contract, Zx can call the loan at any time after year 4 by paying a fixed premium of Rs. 30,000. The fair value of the option is Rs. 10,000 at inception. The effective interest rate amounts to 8.30213%.

Required:

- (i) How is the embedded issuer-only call feature accounted for by Zx, the issuer initially?
- (ii) Explain the accounting of the loan when
 - (a) In years 1 and 2, there is no change in interest rate since inception for an instrument of similar maturity and credit rating. The option's fair value (time value) at the end of year 2 is Rs. 6,000.
 - (b) At the end of year 3, interest rates have fallen, and the option's fair value increases to Rs. 9,000.
 - (c) At the end of year 4, interest rates have fallen further. The option's fair value increases to Rs. 20,000, and the entity decides to repay the loan at the end of year 4.

Solution :

It is first necessary to determine whether the call option is closely related to the host debt instrument. Because the fixed premium is required to be paid whenever the call option is exercised after year 4, it is not known if it will be equal to the present value of any interest lost during the remaining term after exercise of the option. Additionally, the call option's exercise price is Rs. 5,30,000 (inclusive of the premium) therefore, it is unlikely to be approximately equal to the debt instrument's amortised cost in year 4, or at any subsequent year. Consequently, the call option shall be separated from the host debt contract and accounted for separately. This assumes that the expected life of the instrument is the full 10-year term. Even if the expected life is assumed to be four years, the 10-year loan with a call option after four years is economically same as a four-year loan with a six-year extension option. Because there is no concurrent adjustment to the interest rate after four years, the term extension option would not be closely related, and it would need to be accounted for separately. Thus, whichever way the loan and option are viewed, the embedded derivative needs to be separated.

Even though the option is out of the money at inception, because the option's exercise price is greater than the debt instrument's carrying value, it has a time value.

Since the value of a callable bond is equal to the value of a straight bond less the value of the option feature, the accounting entries at inception is:

		Dr (Rs.)	Cr. (Rs.)
Embedded option (derivative asset)	Dr.	10,000	
Cash	Dr.	4,80,000	
To Debt instrument (host)			4,90,000

Since the call option will be fair valued and accounted for separately, with fair value movements taken to profit or loss, it has no impact on the entity's estimate of future cash flows; accordingly, the amortisation period will be the debt host's period to original maturity. The amortisation schedule is shown below:

	Opening amortised cost Rs.	Interest expense @ 8.30213% Rs.	Cash payments Rs.	Closing amortised cost Rs.
Year 1	4,90,000	40,680	40,000	4,90,680
Year 2	4,90,680	40,737	40,000	4,91,417
Year 3	4,91,417	40,798	40,000	4,92,216
Year 4	4,92,216	40,864	40,000	4,93,080
Year 5	4,93,080	40,936	40,000	4,94,016
Year 6	4,94,016	41,014	40,000	4,95,030
Year 7	4,95,030	41,098	40,000	4,96,128
Year 8	4,96,128	41,189	40,000	4,97,317
Year 9	4,97,317	41,288	40,000	4,98,605
Year 10	4,98,605	41,395	5,40,000	-

The entity would recognize interest expense in profit or loss and the loan's amortised cost in the balance sheet each year, in accordance with the above amortisation schedule.

In years 1 and 2, there is no change in interest rate since inception for an instrument of similar maturity and credit rating. The option's fair value (time value) at the end of year 2 is Rs. 6,000. The decrease in fair value of Rs. 4,000 since inception will be reported in profit or loss, and the option will be recorded at Rs. 6,000 at the end of year 2.

At the end of year 3, interest rates have fallen, and the option's fair value increases to Rs. 9,000. The increase in value of Rs. 3,000 will be recorded in profit or loss, and the option will be recorded at its fair value of Rs. 9,000 at the end of year 3.

At the end of year 4, interest rates have fallen further. The option's fair value increases to Rs. 20,000, and the entity decides to repay the loan at the end of year 4.

The accounting entries, to reflect the change in the option's fair value and the loan's early repayment at the end of year 4, are as follows:

		Dr (Rs.)	Cr. (Rs.)
Embedded option	Dr.		
To Profit or loss			11,000
(Early repayment of loan)			
Debt instrument (host)	Dr.	4,93,080	
Loss on de- recognition of liability	Dr.	56,920	
To Embedded option (derivative asset)			20,000
To Cash			5,30,000

Question 43 : Sept 2025 – Paper

On 1st April, 2021, Galaxy Limited issued 15,000, 8% Convertible Debentures with a face value of Rs. 100 each maturing on 31st March, 2026. The debentures are convertible into equity shares of

Galaxy Limited at the option of the holder at a conversion price of Rs. 105 per share or are redeemable at face value of Rs. 100 each. Interest is payable annually in cash. At the date of issue, Galaxy Limited could have issued non-convertible debt with a 5 years term bearing a coupon interest rate of 12%. On 1st April, 2024, the convertible debentures have a fair value of Rs. 15,75,000. Galaxy Limited made a tender offer to debenture holders to repurchase the debentures for Rs. 15,75,000, which the holders accepted. At the date of repurchase, Galaxy Limited could have issued non-convertible debt with a 2 years term bearing a coupon interest rate of 9%.

You are required to:

- (i) Provide the appropriate accounting entries for initial recognition as per the relevant Ind AS in the books of Galaxy Limited.
- (ii) Calculate the stream of Interest Expenses across the five years of the term of the Debentures. (Rounding off adjustment, if any, be made in the interest calculation of financial year 2025-2026).
- (iii) Provide the accounting entries at the time of repurchase of the convertible debentures.

The following present values of Rs. 1 at 8%, 9%, and 12% are supplied to you:

Interest Rate	Year 1	Year 2	Year 3	Year 4	Year 5
8%	0.926	0.857	0.794	0.735	0.681
9%	0.917	0.842	0.772	0.708	0.650
12%	0.893	0.797	0.712	0.636	0.567

Solution :

- (i) **At the time of initial recognition**

	Rs.
Liability component	
Present value of 5 yearly interest payments of Rs. 1,20,000, discounted at 12% annuity (1,20,000 x 3.605)	4,32,600
Present value of Rs. 15,00,000 due at the end of 5 years, discounted at 12%, compounded yearly (15,00,000 x 0.567)	8,50,500
	12,83,100
Equity component	
(Rs. 15,00,000 – Rs. 12,83,100)	2,16,900
Total proceeds	15,00,000

Note: Since Rs. 105 is the conversion price of debentures into equity shares and not the redemption price, the liability component is calculated @ Rs. 100 each only.

Journal Entry

		Rs.	Rs.
Bank	Dr.	15,00,000	
To 8% Debentures (Liability component)			12,83,100
To 8% Debentures (Equity component)			2,16,900

(Being debentures initially recorded at fair value)		
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(ii) Calculation of stream of interest expenses during the term of Debentures

	Opening Balance	Finance cost @ 12%	Interest 8%	Closing Balance
1	12,83,100	1,53,972	1,20,000	13,17,072
2	13,17,072	1,58,049	1,20,000	13,55,121
3	13,55,121	1,62,615	1,20,000	13,97,736
4	13,97,736	1,67,728	1,20,000	14,45,464
5	14,45,464	1,74,536*	1,20,000	15,00,000

* Difference of Rs. 1,080 (1,74,536 – 1,73,456) in the finance cost is due to rounding off and approximation to the nearest absolute figure

(iii) At the time of repurchase of convertible debentures

The repurchase price is allocated as follows:

	Carrying Value @ 12%	Fair Value @ 9%	Difference
	Rs.	Rs.	Rs.
Liability component			
Present value of 2 remaining yearly interest payments discounted at 12% and 9%, respectively. [Rs. 1,20,000 x (0.893 + 0.797)]	2,02,800		
[1,20,000 x (0.917 + 0.842)]		2,11,080	
Present value of Rs. 15,00,000 due in 2 years, discounted at 12% and 9%, compounded yearly, respectively (15,00,000 x (0.797))	11,95,500		
(15,00,000 x (0.842))	_____	<u>12,63,000</u>	
Liability component	13,98,300	14,74,080	(75,780)
Equity component	<u>2,16,900</u>	<u>1,00,920</u>	<u>1,15,980</u>
Total	<u>16,15,200</u>	<u>15,75,000</u>	<u>40,200</u>

*See Note (i)

**Rs. 15,75,000 –Rs. 14,74,080 = Rs. 1,00,920

Journal Entries

		Rs.	Rs.
8% Debentures (Liability component)	Dr.	13,98,300	
Profit and loss A/c (Debt settlement expense)	Dr.	75,780	
To Bank A/c			14,74,080
(Being the repurchase of the liability component recognised)			

8% Debentures (Equity component)	2,16,900	
Dr.		
To Bank A/c		1,00,920
To Retained Earnings/Reserves and Surplus A/c		1,15,980
(Being the cash paid for the equity component recognised)		

Note: Alternatively, one may adjust the liability component of debentures taking the closing balance as per amortization table and pass the following journal entry:

		Rs.	Rs.
8% Debentures (Liability component)	Dr.	13,97,736	
Profit and loss A/c (Debt settlement expense)	Dr.	76,344	
To Bank A/c			14,74,080
(Being the repurchase of the liability component recognised)			

Loss on Debt Settlement = Rs. 14,74,080 – Rs. 13,97,736 = Rs. 76,344.

Question 44 : Jan 2026 – RTP

A Ltd. has issued Optionally Convertible Debentures (OCD) amounting to Rs. 300 crores to B Ltd. on following terms:

- o Tenor : 4 years
- o Coupon : Nil
- o IRR : 15% p.a.

During the tenor of OCDs, A Ltd. can call the OCD and redeem it with stated IRR.

The market rate for similar debt without conversion features is 17% p.a.

B Ltd. can also ask for conversion at any time before maturity based on following formula:

No of equity shares = (Investment amount + applicable IRR) / (Face value of equity share; i.e. Rs. 10)

If redemption or conversion doesn't happen before maturity, then OCDs will be redeemed mandatorily at maturity in same manner as for conversion.

Required:

How is this instrument accounted for in the books of A Ltd. in the following two scenarios:

Scenario A – When B Ltd. opts for conversion before maturity at the end of year 1

Scenario B – When B Ltd. doesn't opt for conversion and OCDs are redeemed at maturity.

Solution :

OCD issued by A Ltd. is a compound financial instrument. The host instrument will be classified as liability, since there is contractual obligation to pay cash towards interest (i.e. guaranteed IRR of 15% p.a.) and principal repayment that issuer A Ltd. cannot avoid. The equity conversion option is accounted as equity.

Date	Particulars	Amount (rounded off in crores)
Day 1	Bank Dr.	300

	To Equity (balancing figure representing residual interest)		20	
	To Debentures (future cash flows discounted @17%)		280	
	(Initial recognition of the financial instrument in the nature of a compound instrument comprising of elements of debt and equity)			
Subsequent Accounting				
End of Year 1	Interest on Debentures	Dr.	48	
	To Debentures (classified under “Liability component of compound financial instrument”)			48
	(Interest recognised in P&L @17% i.e. 280 x 17%)			

Scenario A – When B Ltd opts for conversion at end of year 1

Since conversion was allowed under the original terms of instrument, the entity should determine the amortised cost of liability component using the original IRR till the conversion date. It will derecognise the liability component and recognises it as equity.

There is no gain or loss on early conversion.

Date	Particulars		Amount (rounded off in crores)	
End of Year 1	Debentures [280 + 48]	Dr.	328	
	To Equity Share Capital			328
	(Conversion of OCD into equity shares of the Company)			

Scenario B – When B doesn’t opt for conversion and OCDs are redeemed at maturity

Date	Particulars		Amount (rounded off in crores)	
End of Year 1-4	Interest on debentures	Dr.	245	
	(cumulative interest for 4 years)			
	To Debentures			245
	(Interest recognised in P&L @ 17%)			
End of Year 4	Debentures [280 + 245]	Dr.	525	
	To Bank			525
	(Being debentures redeemed)			

Working Note:

Computation of maturity value of OCD as per the formula stated by B Ltd.:

Year	Opening balance (In crores)	Interest @15% IRR (In crores)	Closing balance (In crores)
1	300	45	345
2	345	51.75	396.75
3	396.75	59.5125	456.2625
4	456.2625	<u>68.439</u>	524.7015 or 525
		<u>224.7015 or 225</u>	

Thanks



ANALYSIS OF FINANCIAL STATEMENTS

CHAPTER - 34

Question 1 : May 2022 – RTP

Defense Innovators Limited is a public sector undertaking and is engaged in the construction of warships and submarines. XYZ Private Limited approached Defense Innovators Limited for construction of "specially designed" ships for it, which will be used by XYZ Private Limited for transportation of specific goods. The offer was accepted by the Defense Innovators Limited and both the companies entered into an agreement for the construction and delivery of 3 specially designed ships on 'Fixed Price' basis with variable component in respect to certain items.

Base and depot (B & D) spares for all three ships shall be procured by Defense Innovators Limited and will be paid on the cost of the item with certain percentage.

The contract states that "certain equipment" out of variable cost items, will be supplied by XYZ Private Limited at 'free of cost' for installation on board of ship. It is, therefore, to be noted as under:

- (i) Some equipment are procured by Defense Innovators Limited in the presence of the XYZ Private Limited's representative for technical scrutiny as well as negotiating the prices. The vendors of these equipment are paid by Defense Innovators Limited. The cost of the equipment along with the cost of installation and profit thereon is claimed and reimbursed by XYZ Private Limited to Defense Innovators Limited.
- (ii) There are certain other equipment for which orders are directly placed and also paid by the XYZ Private Limited. These equipment are known as 'Buyer Furnished Equipment (BFE)' and are delivered to the company 'free of cost' for installing in the ship. The labour cost of Installation of these are already included in the price component of the contract. BFEs are returned to the buyer after completion of the ship.

The period required for construction of one ship was approximately four years.

Whether the cost of Buyer Furnished Equipment's (BFE's) supplied by XYZ Private Limited to Defense Innovators Limited for-installing the same in the ships can be considered as 'inventory' by Defense Innovators Limited and then on delivery of ship will be recognised as revenue in its books of account? Elaborate.

Solution :

Before any item can be recognised as an inventory, it should meet the definition of 'asset' as given in the Conceptual Framework for Financial Reporting under Ind AS, issued by the Institute of Chartered Accountants of India as follows:

"An asset is a present economic resource controlled by the entity as a result of past events and economic resource is a right that has the potential to produce economic benefits".

The orders in respect of Buyer Furnished Equipment's (BFEs) are directly placed by the buyer and payment in respect of them is made by the buyer. These are then supplied to the company for installing in the ship and the buyer pays installation charges which are included in the contract price. Thus, the company has neither incurred any cost on BFEs nor any amount is recoverable on account of such equipment except installation charges. Accordingly, such equipment are not 'assets' that may be considered as a part of its contract work-in progress.

In fact, after installation in the ship, BFEs are returned to the buyer after completion of the ship. Thus, these are only held by the company in the capacity of a bailee. Since, it cannot be considered as an 'asset', therefore, it can neither be considered as 'inventory' nor as 'work-in-progress'.

Further, it can also not be considered as a part of sale value or revenue of the company as no consideration would be receivable with respect to the cost of such equipment.

On the basis of the above, it can be concluded that:

- (i) The BFEs cannot be considered as inventories / Work-in-progress for Defense Innovators Limited.
- (ii) The BFE's cost cannot be considered as part of sales value / contract revenue to Defense Innovators Limited.

Thanks



CORPORATE SOCIAL RESPONSIBILITY

CHAPTER - 35

Question 1 : May 2018 – PAPER

What are the provisions of section 135 of the Companies Act, 2013 regarding constitution of a Corporate Social Responsibility (CSR) Committee. Also explain the role of Corporate Social Responsibility (CSR) Committee and Board.

XYZ Limited is a company which has net worth of Rs.250 crore. It manufactures parts for automobiles. The sales of the company are affected due to low demand of the products. The previous year's financial state of company are as below:

(Rs.in crore)

	31st March 2018 (Current Year)	31st March 2017	31st March 2016	31st March 2015
Net Profit	4.25	8.00	3.50	3.25
Turnover	500.00	900.00	400.00	350.00

Examine, whether the company has an obligation to form a CSR committee since the applicability criteria is not satisfied in the current financial year.

Solution :

A. As per section 135 of the Companies Act 2013

Every company having either

- ❖ net worth of Rs.500 crore or more, or
- ❖ turnover of Rs.1,000 crore or more or
- ❖ a net profit of Rs.5 crore or more

during any financial year shall constitute a Corporate Social Responsibility (CSR) Committee of the Board consisting of three or more directors (including at least one independent director).

B. Role of Corporate Social Responsibility (CSR) Committee

The CSR Committee shall—

- (a) formulate and recommend to Board-
 - a. a CSR Policy indicating the activities to be undertaken by the company as specified in Schedule VII;
 - b. the amount of expenditure to be incurred on the above activities and
- (b) monitor the CSR Policy of the company from time to time.

C. Role of Board

Board shall disclose-

- (a) The composition of CSR Committee in its report
- (b) Approve the recommended CSR Policy for the company
- (c) Disclose the contents of such Policy in its report and place it on the company's website
- (d) Ensure that the activities included in CSR Policy of the company are duly executed by the company
- (e) Ensure that the company spends, in every financial year, at least two percent of the average net profits of the company made during the three immediately preceding financial years by giving preference to the local area and areas around it where it operates
- (f) In case the company fails to spend such amount, the Board shall specify the reasons for not spending the amount.

D. In the given scenario

The MCA has clarified that 'any financial year' referred to under sub-section (1) of section 135 of the Act read with Rule 3(2) of Companies CSR Rule, 2014, implies 'any of the three preceding financial years'.

A company which meets the 'net worth', 'turnover' or 'net profits' criteria in any of the preceding three financial years, but which does not meet the criteria in the relevant financial year, is still required to constitute a CSR Committee and comply with provisions of sections 135 of the Companies Act, 2013.

As per the criteria to constitute CSR committee -

- 1) Net worth greater than or equal to Rs.500 Crore: This criterion is not satisfied.
- 2) Sales greater than or equal to Rs.1000 Crore: This criterion is not satisfied.
- 3) Net Profit greater than or equal to Rs.5 Crore: This criterion is satisfied in financial year ended March 31, 2017 when the net profit was Rs.8 crore.

Hence, the XYZ Ltd. is required to form a CSR committee.

Question 2 : Nov 2018 – PAPER

Baby Limited manufactures consumable goods for infants like bath soap, cream, powder, oil etc. As part of its CSR policy, it has decided that for every pack of these goods sold, Rs.0.75 will go towards the "Swachh Bharat Foundation" which will qualify as a CSR spend as per Schedule VII. Consequently, at the year end, the company sold 40,000 such packs and a total of Rs.30,000 was recognized as CSR expenditure. However, this amount was not paid to the Foundation at the end of the financial year. Will the amount of Rs.30,000 qualify to be CSR expenditure?

Solution :

Baby Ltd. has earmarked 75 paise per pack to spend as CSR activities. However, only by earmarking the amount from such sale for CSR expenditure, the company cannot show it as CSR expenditure. To qualify the amount as CSR expenditure, it has to be spent. Hence, Rs.30,000 will not be automatically considered as CSR expenditure till the time it is spent on CSR activities i.e it is deposited to 'Swachh Bharat Foundation'.

Question 3 : May 2019 – RTP

ABC Ltd. is a company which has a net worth of INR 200 crores, it manufactures rubber parts for automobiles. The sales of the company are affected due to low demand of its products.

The previous year’s financial state:

	(Rs.in Crore)			
	March 31, 2019 (Current year)	March 31, 2018	March 31, 2017	March 31, 2016
Net Profit	3.00	8.50	4.00	3.00
Sales (turnover)	850	950	900	800

Does the Company have an obligation to form a CSR committee since the applicability criteria is not satisfied in the current financial year?

Solution :

It has been clarified that ‘any financial year’ referred to under sub-section (1) of section 135 of the Act read with Rule 3(2) of Companies CSR Rule, 2014, implies ‘any of the three preceding financial years’.

A company which meets the net worth, turnover or net profits criteria in any of the preceding three financial years, but which does not meet the criteria in the relevant financial year, will still need to constitute a CSR Committee and comply with provisions of sections 135(2) to (5) read with the CSR Rules.

As per the criteria to constitute CSR committee -

- 1) Net worth greater than or equal to INR 500 Crores: This criterion is not satisfied.
- 2) Sales greater than or equal to INR 1000 Crores: This criterion is not satisfied.
- 3) Net Profit greater than or equal to INR 5 Crores: This criterion is satisfied in financial year ended March 31, 2018.

Hence, the Company will be required to form a CSR committee.

Question 4 : Nov 2020 – RTP

In order to encourage companies and organisations to generously contribute to the Government’s COVID-19 relief fund, taxation laws have been amended to reckon these contributions as deductible for the financial year ending 31st March, 2020 even if the contributions are made after the year end but within three months after year end. Government of India issued the notification on 31st March, 2020 by way of an Ordinance. Such contributions to COVID-19 funds are considered for compliance with annual spends on corporate social responsibility (CSR) for the current accounting year under the Companies Act, 2013. In this scenario, whether the contributions to COVID-19 Relief Funds made subsequent to reporting date of the current accounting period can be provided for as expenses of the current accounting period? Also show its impact on deferred tax, if any.

Solution :

According to Ind AS 37, a provision shall be made if:

- (a) an entity has a present obligation (legal or constructive) as a result of a past event;

- (b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
- (c) a reliable estimate can be made of the amount of the obligation. If these conditions are not met as of reporting date, no provision shall be recognised for that financial year.

Government of India issued the notification on 31st March, 2020 by way of an Ordinance and hence, it is most unlikely for any entity to have a present obligation on 31st March, 2020, for such a commitment. As these conditions are not met as of reporting date of financial year 2019 - 2020, no provision should be recognised in the financial statements for that financial year.

In the fact pattern given above, the accounting implications for the financial year 2019-2020 is as follows:

- Do not recognize expense / liability for the contribution to be made subsequent to the year ended 31st March, 2020 as it does not meet the criteria of a present obligation as at the balance sheet date. However, the expected spend may be explained in the notes to the accounts as the same will also be considered in measurement of deferred tax liability.
- If the entity claims a deduction in the Income Tax return for the financial year 2019 - 2020 for that contribution made subsequent to 31st March, 2020, recognise Deferred Tax Liability as there would be a tax saving in financial year 2019 - 2020 for a spend incurred in subsequent year.

Question 5 : Nov 2020 – Paper

Royal Ltd. is a company which has a net worth of Rs. 200 crore engaged in the manufacturing of rubber products. The sales of the company are badly affected due to pandemic during the Financial year 2019-2020.

Relevant financial details of the following financial years are as follows: (Rs. in crore)

Particulars	31 March 2020 (Current year) estimated	31-Mar-19	31-Mar-18	31-Mar-17
Net Profit	3.00	8.50	4.00	3.00
Sales (turnover)	850	950	900	800

During the pandemic period (till 31 March 2020) various commercial activities were undertaken with considerable concessions/discounts, along the related affected areas. The management intends to highlight the expenditure incurred on such activities as expenditure incurred, on activities undertaken to discharge corporate social responsibility, while publishing its financial statements for the year 2019-2020.

You are requested to advise CFO of Royal Ltd on the below points along with reasons for your advise:

- (i) Whether the Company has an obligation to form a CSR committee since the applicability criteria are not satisfied in the current financial year?
- (ii) The accounting of expenditure during the pandemic period is to be treated as expenditure on CSR in the financial statement according to the view of the accountant of the company.

Solution :

(i) A company which meets the net worth, turnover or net profits criteria in immediate preceding financial year will need to constitute a CSR Committee and comply with provisions of sections 135(2) to (5) read with the CSR Rules.

As per the criteria to constitute CSR committee -

- (1) Net worth should be greater than or equal to ` 500 Crore: This criterion is not satisfied as per the facts given in the question.
- (2) Sales should be greater than or equal to ` 1000 Crore: This criterion is not satisfied as per the facts given in the question.
- (3) Net profit should be greater than or equal to ` 5 Crore: as per the facts given in the question, this criterion is satisfied in financial year ended 31 March 2019 i.e. immediate preceding financial year.

Hence, the Company will be required to form a CSR committee.

(ii) The Companies Act, 2013 mandated the corporate entities that the expenditure incurred for Corporate Social Responsibility (CSR) should not be the expenditure incurred for the activities in the ordinary course of business. If expenditure incurred is for the activities in the ordinary course of business, then it will not be qualified as expenditure incurred on CSR activities.

Further, it is presumed that the commercial activities performed at concessional rates are the activities done in the ordinary course of business of the company other than the activities defined in Schedule VII of the Companies Act, 2013. Therefore, the treatment done by the Management by showing the expenditure incurred on such commercial activities in its financial statements as the expenditure incurred on activities undertaken to discharge CSR, is not correct.

Question 6 : Jan 2021 – Paper

Sun Shine Limited is a company which seems to be covered under the ambit of CSR rules. As part of its CSR contribution an amount of Rs.40,000 p.m. was spent by way of adoption of 2 families of drought hit area.

The average net profits of immediately preceding financial year was Rs.1,80,00,000. Please note that the company commenced its commercial activities only on the first day of the immediately preceding financial year. The Accountant of the company says that CSR provisions are not applicable to his company since it is one year old and in case if it is applicable he wants to carry forward the excess amount spent on account of CSR activities to future years.

You are required to comment with the figures, whether the contention of the Accountant is correct in context of CSR provisions?

Solution :

As per section 135 of the Companies Act 2013, every company having either

- net worth of Rs.500 crore or more, or
- turnover of Rs.1,000 crore or more or
- a net profit of Rs.5 crore or more

during the immediately preceding financial year shall constitute a Corporate Social Responsibility (CSR) Committee.

In the given case, the average net profits of immediate preceding financial year of Sun Shine Limited is Rs.1,80,00,000 (i.e. Rs.1.80 crore). Hence, net profit criteria is not met.

Company is covered under the ambit of CSR rules (assuming that net worth or turnover criteria is met):

Since it is given in the question that the company seems to be covered under the ambit of CSR rules, it is assumed that either the net worth of Sun Shine Limited might have exceeded Rs.500 crore or more, or turnover might have exceeded Rs.1,000 crore or more during immediate preceding financial year. Accordingly, CSR provisions are applicable to Sun Shine Limited irrespective of the fact that the company is in second year of operations.

If the company meets any one of the thresholds in the immediately preceding previous year, then the contention of accountant is incorrect that CSR provisions will not be applicable to the company as it is only one year old.

The accountant wants to carry forward the excess amount spent on account of CSR activities to future years which is Rs.1,20,000 [Rs.40,000 x 12 - (Rs.1,80,00,000 x 2%)]. However, there is no provision to carry forward the excess CSR expenditure spent* in a particular year. Hence, here also the contention of the accountant is incorrect. The excess expenditure made shall be considered as voluntary made by the entity.

*The amendments in section of CSR has been made effective from January, 2021. Hence not applicable for January, 2021 examination.

Question 7 : July 2021 – Paper

Government of India provides loans to MSMEs at a below – market rate of interest to fund the set – up a new manufacturing facility. Sikshma Limited's date of transition to Ind AS is 1st April 2020.

In financial year 2014-15, the Company had receive a loan of Rs.2.0 crores at a below – market rate of interest from the government. Under Indian GAAP, the Company had accounted for the loan as equity and the carrying amount was Rs.2.0 crores at the date of transition. The amount repayable on 31st March 2024 will be Rs.2.50 crores.

The Company has been advised to recognize the difference of Rs.0.50 crores in equity by correspondingly increasing the value of various assets under property, plant and equipment by an equivalent amount on proportionate basis. Further, on 31st March 2024 when the loan has to be repaid, Rs.2.50 crores should be presented as a deduction from property, plant and equipment.

Discuss the above treatment and share your views as per applicable Ind Ass.

Solution :

Requirement as per Ind AS:

A first-time adopter shall classify all government loans received as a financial liability or an equity instrument in accordance with Ind AS 32. A first-time adopter shall apply the requirements in Ind AS 109 and Ind AS 20, prospectively to government loans existing at the date of transition to Ind

AS and shall not recognise the corresponding benefit of the government loan at a below-market rate of interest as a government grant.

Treatment to be done:

Consequently, if a first-time adopter did not, under its previous GAAP, recognise and measure a government loan at a below-market rate of interest on a basis consistent with Ind AS requirements, it shall use its previous GAAP carrying amount of the loan at the date of transition to Ind AS as the carrying amount of the loan in the opening Ind AS Balance Sheet. An entity shall apply Ind AS 109 to the measurement of such loans after the date of transition to Ind AS.

In the instant case, the loan meets the definition of a financial liability in accordance with Ind AS 32. Company therefore reclassifies it from equity to liability. It also uses the previous GAAP carrying amount of the loan at the date of transition as the carrying amount of the loan in the opening Ind AS balance sheet.

It calculates the annual effective interest rate (EIR) starting 1st April 2020 as below:

$$\text{EIR} = \text{Amount} / \text{Principal}(1/t) \text{ i.e. } 2.50/2(1/4) \text{ i.e. } 5.74\% \text{ approx.}$$

At this rate, Rs. 2 crore will accrete to Rs. 2.50 crore as at 31st March 2024.

During the next 4 years, the interest expense charged to statement of profit and loss shall be:

Year ended	Opening amortised cost (Rs.)	Interest expense for the year (Rs.) @ 5.74% p.a. approx.	Closing amortised cost (Rs.)
31st March 2021	2,00,00,000	11,48,000	2,11,48,000
31st March 2022	2,11,48,000	12,13,895	2,23,61,895
31st March 2023	2,23,61,895	12,83,573	2,36,45,468
31st March 2024	2,36,45,468	13,54,532	2,50,00,000

An entity may apply the requirements in Ind AS 109 and Ind AS 20 retrospectively to any government loan originated before the date of transition to Ind AS, provided that the information needed to do so had been obtained at the time of initially accounting for that loan.

The accounting treatment is to be done as per above guidance and the advice which the company has been provided is not in line with the requirements of Ind AS 101.

Question 8 : May 2022 – Paper

PK Ltd. has a net worth of Rs.450 crores. It manufactures bathroom accessories. The sales of the Company are affected due to low demand. Company has provided following information :

Particulars	Amount (Rs in crores) for Year Ended			
	31.03.2022	31.03.2021	31.03.2020	31.03.2019
Net Profit	3.50	7.75	4.25	4.00
Sales (Turnover)	600.00	850.00	700.00	710.00

During the financial year 2021-22, PK Ltd. decided the on sale of certain selected items of bathroom accessories @ Rs.0.50 paisa per unit sold will be contributed to the 'Save Water Foundation' which will qualify as a Corporate Social Responsibility (CSR) expense as per Schedule VII of the Companies Act, 2013.

Consequently, by the year end, the Company recognized Rs.150,000 as CSR expenditure. However, only 50% of the aforesaid amount was paid to the Foundation by the end of the year ending 31st March, 2022. Discuss :

- (i) Whether PK Ltd. has an obligation to form a CSR committee as the applicability criteria is not satisfied in the financial year 2021 – 22? The net worth has always remained below the applicability threshold.
- (ii) Whether Rs.150,000 will qualify as CSR expenditure under section 135 of the Companies Act, 2013 ?

Solution :

- (i) A company which meets the net worth, turnover or net profits criteria in immediately preceding financial year will need to constitute a CSR Committee and comply with provisions of sections 135(2) to (5) read with the CSR Rules.

As per the criteria to constitute CSR committee -

- (1) Net worth greater than or equal to Rs. 500 Crore: This criterion is not satisfied.
- (2) Sales greater than or equal to Rs. 1000 Crore: This criterion is not satisfied.
- (3) Net profit greater than or equal to Rs. 5 crore: The net profit for the immediately preceding financial year ended 31st March, 2021 is Rs. 7.75 crore. Hence, this criterion is satisfied.

Therefore, PK Ltd. will be required to form a CSR committee.

However, sub-section (9) of section 135 of the Companies Act, 2013 provides that if the amount to be spent as CSR expenditure is less than fifty lakh rupees, the requirement of forming a CSR committee will not be applicable and the functions of CSR committee will be discharged by the Board of Directors. In the given case, as the company is required to spend 10.66 lacs being 2% of average net profits Rs. 5.33 crore $[(7.75 + 4.25 + 4)/3]$, the company need not form the CSR committee.

- (ii) The company is obligated to spend a sum of Rs. 1,50,000 by contributing the same to 'Save Water Foundation'; hence, Rs. 1,50,000 shall qualify as CSR expenditure. Since only 50% has been paid to the Foundation, the company will be required to make provision of balance 50% in the books of accounts. It is immaterial whether the company determines the amount of contribution based on sale of product.

Note: The above solution has been provided on integrated reading of the scenario given in the question.

Question 9 : Nov 2023 – Paper

As per the provisions of section 135 of the Companies Act, 2013 read with relevant rules, circulars and notifications related to 'Corporate Social Responsibility' (CSR), discuss the following situations:

- (i) A company is formed under section 8 of the Companies Act, 2013 to undertake charitable activities. The management of the Company is of the opinion that since all the activities of the Company are charitable in the normal course of business, the CSR provisions are not applicable to it. You are required to advise whether the CSR provisions are applicable to

- the Company. The Company fulfils all the criteria listed in section 135 of the Companies Act, 2013.
- (ii) C Limited is covered under the provisions of section 135 of the Companies Act, 2013. The Company fulfils all the criteria listed in section 135 of the Companies Act, 2013. It has a holding company H Limited and a subsidiary company S Limited. Neither H Limited nor S Limited fulfils the criteria listed in section 135 of the Companies Act, 2013. Advise whether H Limited and S Limited are required to comply with the provisions of section 135 of the Companies Act, 2013.
 - (iii) For the financial year 2020-2021, CBC Ltd. was within the purview of CSR provisions as per the Companies Act, 2013 as its net profit for the financial year exceeded Rs. 5 crores. It also satisfied the 'net worth' and 'turnover' criteria. The Company duly discharged its CSR obligations in the financial year 2021-2022. However, due to adverse market conditions during the financial year 2021-2022, the turnover fell below Rs. 1,000 crores and the Company incurred a loss. Its net worth also fell below Rs. 500 crores. The Company is of the opinion that CSR provisions are no longer applicable to it with effect from the financial year 2021-2022. Discuss.
 - (iv) An office building is constructed exclusively for the CSR activities under section 135 of the Companies Act, 2013 of the Company. The entire expenditure is treated as revenue expenditure and charged to statement of profit and loss. Discuss whether the treatment of charging cost of construction of the aforesaid building to statement of profit and loss is correct. Whether any disclosures as per Schedule III of the Companies Act, 2013 have to be made?

Solution :

- (i) Section 135 of the Companies Act applies to every company meeting the specified criteria. As per section 2(20) of the Companies Act, 'company' means a company incorporated under the Companies Act or under any other previous company law. This implies that companies set up for the purposes of CSR / public welfare are also required to comply with the provisions of CSR since they are incorporated under the Companies Act. Further, as per clause 2(d) of the Companies (Corporate Social Responsibility Policy) Rule, 2014, "Corporate Social Responsibility (CSR)" means the activities undertaken by a Company in pursuance of its statutory obligation laid down in section 135 of the Act in accordance with the provisions contained in these rules but shall not include activities undertaken in pursuance of normal course of business of the company except research work. Therefore, though all the activities of the company are charitable in nature, they are activities in the normal course of their business. Hence, those activities do not constitute activities of corporate social responsibility. Based on the above discussions, since the company formed under section 8 of the Companies Act, 2013 is a company under the Companies Act, 2013 and fulfills the criteria prescribed under section 135(1) of the Companies Act, 2013, CSR provisions will be applicable to it.
- (ii) Any company incorporated under the Act, which fulfills the criteria on a standalone basis, irrespective of its status of holding or subsidiary, needs to comply with CSR provisions.

Since neither H Limited nor S Limited fulfils the criteria listed in section 135(1) of the Companies Act, 2013, H Limited and S Limited both are not required to comply with the requirements of Section 135 relating to CSR.

(iii) Section 135(1) of the Companies Act requires that any company fulfilling the net worth / turnover / net profit criterion in the immediately preceding financial year shall constitute a Corporate Responsibility committee and sub-section (5) requires such company to incur 2% of the average profit of the last three years. It is only a computational requirement. Applicability of CSR provisions is based on meeting any of the limits in the 'immediately preceding year'. As the company does not meet the limits in the financial year 2021-2022, the company is not required to fulfill the CSR obligations in the financial year 2022-2023.

(iv) In cases where an expenditure of revenue nature is incurred on any of the activities mentioned in Schedule VII to the Act by the company on its own, the same should be charged as an expense to the statement of profit and loss. In case the expenditure incurred by the company is of such nature which may give rise to an 'asset', a question may arise as to whether such an 'asset' should be recognised by the company in its balance sheet. In this context, it would be relevant to note the definition of the term 'asset' as per the Conceptual Framework for Financial Reporting in accordance with Ind AS issued by ICAI. As per the Conceptual Framework, an 'asset' is a "resource controlled by an enterprise as a result of past events from which future economic benefits are expected to flow to the enterprise". Hence, in cases where the control of the 'asset' is transferred by the company, it should not be recognised as 'asset' in its books and such expenditure would need to be recognized as an expense in the statement of profit and loss as and when incurred.

Rule (7) of the Companies (Corporate Social Responsibility) Rules, 2014 provides for transfer of any capital asset created by the company to (i) a company established under section 8 of the Act, or a Registered Public Trust or Registered Society, having charitable objects and CSR Registration Number under sub-rule (2) of rule 4; or (ii) beneficiaries of the said CSR project, in the form of self-help groups, collectives, entities; or (iii) a public authority. Proviso to rule (7) further provides that if the asset has been created prior to amendment of the Companies (Corporate Social Responsibility Policy) Amendment Rules, 2021, shall within a period of one hundred and eighty days from such commencement shall transfer the same as stated above.

Since, the company has charged the expenses on construction of building to the Statement of Profit and Loss as expenses, it is assumed that the control of the asset has been transferred. Accordingly, the company has to disclose in its financial statements as about it under CSR activities as per General Instructions for Preparation of Statement of Profit and Loss under Schedule III to the Companies Act, 2013.

General Instructions for Preparation of Statement of Profit and Loss under Schedule III to the Companies Act, 2013, requires that in case of companies covered under Section 135, the following shall be disclosed about CSR activities:

- (i) amount required to be spent by the company during the year,
- (ii) amount of expenditure incurred,
- (iii) shortfall at the end of the year, if any
- (iv) total of previous years shortfall, if any

- (v) reason for shortfall, if any
- (vi) nature of CSR activities,
- (vii) details of related party transactions, e.g., contribution to a trust controlled by the company in relation to CSR expenditure as per relevant Accounting Standard,
- (viii) where a provision is made with respect to a liability incurred by entering into a contractual obligation, the movements in the provision during the year shall be shown separately.

Thanks



CONCEPTUAL FRAMEWORK

CHAPTER - 36

Question 1 : May 2022 – Paper

Discuss the following in the context of 'Conceptual Framework for Financial Reporting under Indian Accounting Standards' :

- (i) The cost constraint on useful financial information
- (ii) Executory contracts

Solution :

(i) **The cost constraint on useful financial information;**

Role of Cost: Cost is a pervasive constraint on the information that can be provided by financial reporting. Reporting financial information imposes costs, and it is important that these costs are justified by the benefits of reporting that information.

Basis of Assessment of Cost: Both the providers and users of financial information incur costs in reporting and analysing financial information. In applying the cost constraint, ICAI assesses whether the benefits of reporting particular information are likely to justify the costs incurred to provide and use that information. When applying the cost constraint in formulating a proposed Ind AS, the ICAI seeks information from providers of financial information, users, auditors, academics and others about the expected nature and quantity of the benefits and costs of that Ind AS. In most situations, assessments are based on a combination of quantitative and qualitative information.

Cost Perspective: Due to the inherent subjectivity, assessments of different individuals about the costs and benefits of reporting particular items of financial information will vary. Therefore, ICAI seeks to consider costs and benefits in relation to financial reporting generally, and not just in relation to individual reporting entities.

(ii) **Executory Contracts:**

Definition: An executory contract is a contract, or a portion of a contract, that is equally unperformed — neither party has fulfilled any of its obligations, or both parties have partially fulfilled their obligations to an equal extent.

Outcome of Executory Contract: An executory contract establishes a combined right and obligation to exchange economic resources. The rights and obligations are inter-dependent and cannot be separated. Hence, the combined rights and obligations constitute a single asset or liability.

The entity has an asset if the terms of the exchange are currently favourable; it has a liability if the terms of the exchange are currently unfavourable.

Basis of Disclosure: Whether such an asset or liability is included in the financial statements depends on both the recognition criteria and the measurement basis selected for the asset or liability, including, if applicable, any test for whether the contract is onerous.

Question 2 : Nov 2022 – Paper

Explain the criterion in the Conceptual Framework for Financial Reporting for the recognition of an asset and discuss whether there are inconsistencies with the criterion in Ind AS 38.

Solution :

The Conceptual Framework defines an asset as a present economic resource controlled by the entity as a result of past events. An economic resource is a right that has the potential to produce economic benefits. Assets should be recognized if they meet the Conceptual Framework definition of an asset and such recognition provides users of financial statements with information that is useful i.e. it is relevant as well as results in faithful representation. However, the criteria of a cost-benefit analysis always exists i.e. the benefits of the information must be sufficient to justify the costs of providing such information. The recognition criteria outlined in the Conceptual Framework allows for flexibility in the application in amending or developing the standards.

Para 8 of Ind AS 38 'Intangible Assets', defines an intangible asset as an identifiable non-monetary asset without physical substance. Further, Ind AS 38 defines an asset as a resource:

- (a) controlled by an entity as a result of past events; and
- (b) from which future economic benefits are expected to flow to the entity.

Furthermore, Para 21 of Ind AS 38 states that an intangible asset shall be recognised if, and only if:

- (a) it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity; and
- (b) the cost of the asset can be measured reliably.

This requirement is applicable both in case of an externally acquired intangible asset or an internally generated intangible asset. The probability of expected future economic benefits must be based on reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the useful life of the asset. Further, as per Para 33 of Ind AS 38, the probability recognition criterion is always considered to be satisfied for intangible assets acquired in business combinations. If the recognition criteria are not satisfied, Ind AS 38 requires the expenditure to be expensed as and when it is incurred.

It is notable that the Conceptual Framework does not prescribe a 'probability criterion'. As long as there is a potential to produce economic benefits, even with a low probability, an item can be recognized as an asset according to the Conceptual Framework. However, in terms of intangible assets, it could be argued that recognizing an intangible asset having low probability of generating economic benefits would not be useful to the users of financial statements given that the asset has no physical substance.

The recognition criteria and definition of an asset under Ind AS 38 are different as compared to those outlined in the Conceptual Framework. To put in simple words, the criteria in Ind AS 38 are more specific, but definitely do provide information that is relevant and a faithful representation. When viewed from the prism of relevance and faithful representation, the requirements of Ind AS 38 in terms of recognition appear to be consistent with the Conceptual Framework.

Question 3 : May 2023 – Paper

Discuss with respect to ‘Conceptual Framework for Financial Reporting under Indian Accounting Standards’, ‘faithful representation’, one of the qualitative characteristic of financial information.

Solution :

Faithful representation

To be useful, financial information must faithfully represent the substance of the phenomena that it purports to represent. In many circumstances, the substance of an economic phenomenon and its legal form are the same. If they are not the same, providing information only about the legal form would not faithfully represent the economic phenomenon.

To be a perfectly faithful representation, a depiction would have following three characteristics:

- ◆ **Complete:** A complete depiction includes all information necessary for a user to understand the phenomenon being depicted, including all necessary descriptions and explanations.
- ◆ **Neutral:** A neutral depiction is without bias in the selection or presentation of financial information. Neutrality is supported by the exercise of prudence. Prudence is the exercise of caution when making judgements under conditions of uncertainty. The exercise of prudence means that assets and income are not overstated, and liabilities and expenses are not understated. Equally, the exercise of prudence does not allow for the understatement of assets or income or the overstatement of liabilities or expenses.
- ◆ **Free from error:** Free from error means there are no errors or omissions in the description of the phenomenon, and the process used to produce the reported information has been selected and applied with no errors in the process. In this context, being free from error does not mean perfectly accurate in all respects. For example, an estimate of an unobservable price or value cannot be determined to be accurate or inaccurate. However, a representation of that estimate can be faithful if the amount is described clearly and accurately as being an estimate, the nature and limitations of the estimating process are explained, and no errors have been made in selecting and applying an appropriate process for developing the estimate.

Question 4 : Nov 2024 – Paper

Explain the criteria in the Conceptual Framework for Financial Reporting for the recognition and de-recognition of an asset.

Solution :

Recognition of assets

The Conceptual Framework for Financial Reporting defines an asset as a present economic resource controlled by the entity as a result of past events. An economic resource is a right that has the potential to produce economic benefits. Assets should be recognized if they meet the Conceptual Framework definition of an asset and such recognition provides users of financial statements with information that is useful i.e. with(a)relevant information; and(b)a faithful representation of the asset.

(i) Relevance

Information about assets is relevant to users of financial statements. However, recognition of a particular asset may not always provide relevant information like when:

- (i) it is uncertain whether an asset exists; or
- (ii) an asset exists, but the probability of an inflow or outflow of economic benefits is low

It may be a combination of factors and not any single factor that determines whether recognition provides relevant information.

Whether or not the asset is recognised, explanatory information about the uncertainties associated with it, may need to be provided in the financial statements.

(ii) Faithful representation

Recognition of a particular asset is appropriate if it provides not only relevant information, but also a faithful representation of that asset and of any resulting income, expenses or changes in equity. Whether a faithful representation can be provided may be affected by the level of measurement uncertainty associated with the asset or by other factors.

Faithful representation of a recognised asset involves not only recognition of that item, but also its measurement as well as presentation and disclosure of information about it.

Derecognition of assets

Derecognition is the removal of all or part of a recognised asset from an entity's balance sheet. Derecognition normally occurs when that item no longer meets the definition of an asset i.e. when the entity loses control of all or part of the recognised asset.

In some cases, an entity might appear to transfer an asset but derecognition of that asset is not appropriate. For example, if an entity has apparently transferred an asset but retains exposure to significant positive or negative variations in the amount of economic benefits that may be produced by the asset, this sometimes indicates that the entity might continue to control that asset. If an entity has transferred an asset to another party that holds the asset as an agent for the entity the transferor still controls the asset.

Question 5 : May 2024 – Paper

List out the entities which were covered under Phase I & II under the Companies (Indian Accounting Standards) Rules 2015 as notified by the MCA along with the specific date of coverage with its exclusions, if any.

Solution :

MCA has notified the Companies (Indian Accounting Standards) Rules, 2015. Accordingly, it has notified 39 Ind AS and has laid down mandatory Ind AS transition roadmap for companies and

non- banking finance companies excluding banking companies and insurance companies under following two phases:

Phase I

Following companies were covered under Phase I for accounting periods beginning on or after 1st April 2016, with the comparatives for the periods ending on 31st March 2016:

- (a) companies whose equity or debt securities are listed or are in the process of being listed on any stock exchange in India or outside India and having net worth of rupees five hundred crore or more;
- (b) companies other than those covered by sub-clause (a) above and having net worth of rupees five hundred crore or more;
- (c) holding, subsidiary, joint venture or associate companies of companies covered by sub-clause (a) and sub-clause (b) as mentioned above.

Phase II

Following companies were covered under Phase II for accounting periods beginning on or after 1st April 2017, with the comparatives for the periods ending on 31st March 2017:

- (a) companies whose equity or debt securities are listed or are in the process of being listed on any stock exchange in India or outside India and having net worth of less than rupees five hundred crore;
- (b) companies other than those covered in sub-clause (a) above i.e. unlisted companies having net worth of rupees two hundred and fifty crore or more but less than rupees five hundred crore.
- (c) holding, subsidiary, joint venture or associate companies of companies covered by sub-clause (a) and sub-clause (b) as mentioned above.

Exclusions:

The roadmap shall not be applicable to companies whose securities are listed or are in the process of being listed on SME without initial public offering in accordance with the provisions of SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009.

Ind AS would not be applicable to companies other than listed companies whose net worth is less than Rs. 250 Crores and they will continue to follow AS. However, they can voluntary adopt Ind AS any time.

Question 6 : Sept 2025 – Paper

Define Equity, Income and Expenses as per 'Conceptual Framework' to Ind AS. How the information with respect to income and expenses helps the users in understanding of the financial statements?

Solution :

Definition of Equity

Equity claims are claims on the residual interest in the assets of the entity after deducting all its liabilities. In other words, they are claims against the entity that do not meet the definition of a liability.

Definition of Income

Income is increases in assets, or decreases in liabilities, that result in increases in equity, other than those relating to contributions from holders of equity claims.

Definition of Expenses

Expenses are decreases in assets, or increases in liabilities, that result in decreases in equity, other than those relating to distributions to holders of equity claims. However, contributions from holders of equity claims are not income, and distributions to holders of equity claims are not expenses.

How information with respect to income and expenses helps the users in understanding the financial statements?

Income and expenses are the elements of financial statements that relate to an entity’s financial performance. Users of financial statements need information about both an entity’s financial position and its financial performance. Hence, although income and expenses are defined in terms of changes in assets and liabilities, information about income and expenses is just as important as information about assets and liabilities.

Providing information separately about income and expenses with different characteristics can help users of financial statements to understand the entity’s financial performance.

Thanks



INTEGRATED REPORTING

CHAPTER - 37

Question 1 : May 2022 – Paper

What is Integrated Reporting ? Discuss any 5 salient features of Integrated Reporting Framework.

Solution :

Definition: Integrated reporting is a concept that has been created to better articulate the broader range of measures that contribute to long-term value and the role organizations play in society. Integrated Reporting is enhancing the way organizations think, plan and report the story of their business. Central to this is the proposition that value is increasingly shaped by factors additional to financial performance, such as reliance on the environment, social reputation, human capital skills and others.

The five salient features of Integrated Reporting Framework are as follows:

- 1. Principle Based Approach:** This Framework identifies information to be included in an integrated report for use in assessing an organization's ability to create value. It does not set benchmarks for such things as the quality of an organization's strategy or the level of its performance.
- 2. Targets the Private Sector or Profit-making Companies:** This Framework is written primarily in the context of private sector, for-profit companies of any size but it can also be applied, adapted as necessary, by public sector and not-for-profit organizations.
- 3. Identifiable Communication:** An integrated report may be prepared in response to existing compliance requirements and may be either a standalone report or be included as a distinguishable, prominent and accessible part of another report or communication. An integrated report is intended to be more than a summary of information in other communications (e.g., financial statements, a sustainability report, analyst calls, or on a website); rather, it makes explicit the connectivity of information to communicate how value is created over time.
- 4. Financial and Non-financial Items:** The primary purpose of an integrated report is to explain to providers of financial capital how an organization creates value over time. It, therefore, contains relevant information, both financial and other.
- 5. Value Creation:** Value created by an organization over time manifests itself in increases, decreases or transformations of the capitals caused by the organization's business activities and outputs. That value has two interrelated aspects – value created for:
 - The organization itself, which enables financial returns to the providers of financial capital
 - Others (i.e., stakeholders and society at large)

Question 2 : Nov 2022 – Paper

State the categories of capital as defined in the Integrated Reporting Framework. Can an integrated reporting be done in compliance to the requirements of the local laws to prepared a management commentary or other reports?

Solution :

The Integrated Reporting Framework has categorised the capital into 6 main forms. However, at the same time, it stresses upon that not necessary the same categorisation of capital be followed by the entities in their integrated reporting.

1. **Financial Capital:** The pool of funds available to an organization for use in the production of goods or the provision of services obtained through financing, such as debt, equity or grants; or generated through operations or investments.
2. **Manufactured Capital:** Manufactured physical objects (as distinct from natural physical objects) that are available to an organization for use in the production of goods or the provision of services, including buildings, equipment and infrastructure (such as roads, ports, bridges, and waste and water treatment plants).
3. **Intellectual Capital:** Organizational, knowledge-based intangibles, including intellectual property, such as patents, copyrights, software, rights and licences and organizational capital such as tacit knowledge, systems, procedures and protocols.
4. **Human Capital:** People's competencies, capabilities and experience, and their motivations to innovate, including their loyalties and motivations for improving processes, goods and services, including their ability to lead, manage and collaborate.
5. **Social and Relationship Capital:** The institutions and the relationships within and between communities, groups of stakeholders and other networks, and the ability to share information to enhance individual and collective well-being.
6. **Natural Capital:** All renewable and non-renewable environmental resources and processes that provide goods or services that support the past, current, or future prosperity of an organization.

An integrated report may be prepared in response to existing compliance requirements. For example, an organization may be required by local law to prepare a management commentary or other report that provides context for its financial statements. If that report is also prepared in accordance with this Framework, it can be considered an integrated report. If the report is required to include specified information beyond that required by this Framework, the report can still be considered an integrated report if that other information does not obscure the concise information required by this Framework.

Question 3 : May 2023 – Paper

Discuss the Organizational Structure / Issuing Authority of Integrated Reporting.

Solution :

Integrated Reporting is a concept first introduced in South Africa. Later on, this concept travelled to many countries like German, France, Spain, Brazil and UK and integrated reporting was made along with their financial statements in one or the other manner. In 2010, the International Integrated Reporting Council (IIRC) was set up which aims to create the globally accepted integrated reporting framework.

The International Integrated Reporting Council (IIRC) is a global coalition of:

- Regulators
- Investors
- Companies
- Standard setters
- The accounting profession and NGOs

Together, this coalition shares the view that communication about value creation should be the next step in the evolution of corporate reporting. With this purpose they issued the International Integrated Reporting (IR) Framework.

Thanks



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