PAPER – 1 : FINANCIAL REPORTING

*Question No.**1** is compulsory. Candidates are required to answer any **four** questions from the remaining **five** questions.*

Wherever necessary, suitable assumptions may be made and disclosed by way of a note.

Working notes should form part of the answers.

Question 1

(a) *Given below are the balance sheets of a group of companies comprising LX Limited, MX Limited and NX Limited as on 31st March 2021:* **₹ in lakh**

Particulars	LX Limited	MX Limited	NX Limited
Assets			
Non-current Assets			
Property, Plant and Equipment	1,500	1,600	1,400
Investment			
17.0 lakh share in MX Limited	2,620	-	-
9.6 lakh shares in NX Limited	-	1,350	-
Current Assets			
Inventories	1,230	730	1,180
Financial Assets			
Trade Receivables	1,415	270	620
Bills Receivables	650	60	-
Cash in hand and at Bank	1,085	90	150
	8,500	**4,100**	**3,350**
Equity and Liabilities			
Shareholders' Equity			
Share Capital (₹ 100 per share)	3,400	2,000	1,600
Other Equity			
Reserves	1,150	810	580
Retained earnings	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 balances stood in the books of MX Limited and NX Limited as on 1st April 2020:

	MX Limited **₹ in lakh**	*NX Limited* **₹ in lakh**
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 fair value applying Ind AS 103. The fair value is to be determined at quoted market price. The given market price of MX Limited is ₹ 120 per share and NX Limited is ₹ 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. ***(16 Marks)***

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

With respect to the following transactions, which took place during the financial year 2020-2021, give your opinion based on relevant Ind AS:

- *The Company has received a contract of ₹ 10 crore on 31st March 2021. The terms of the contract require the Company to make a security deposit of 20% of the contract value with the customer. The Company made a security deposit of ₹ 2 crore on 31st March 2021. This contract will be completed in about 14 months. 70% of the deposit will be refunded immediately and the balance 30% of the deposit will be refunded after 3 months from the completion of the contract. The Company wants to present the security deposit of ₹ 2 crore as non-current. Is the management's decision correct?*
- *The Company has some trade receivables that are due after 14 months from the date of the balance sheet; the management of the Company expects to receive the amount within the period of the operating cycle. Despite the fact that these are receivables in 14 months, the management would like to present these as current. Is the management's decision correct?*
- *In the normal course of business, the Company has given 2 contracts and received a total security deposit of ₹ 4 crore. ₹ 3 crore is received from X Limited and ₹ 1 crore is received from Y Limited on 31st March 2021. These are repayable on completion*

of the contract. However, if the contract is cancelled within the contract term of 18 months, then the deposit becomes payable immediately. The Company is positive about the contract with X Limited but is in doubt about the contract received from Y Limited. The Company wants to present the amount of ₹ 3 crore as non-current and ₹ 1 crore as current in the balance sheet. Is the management's decision correct?

- *The Company is planning to replace a machinery. It has given an advance of ₹ 1 crore for purchase of new machinery which will be delivered in 6 months from the date of the balance sheet. It has sold the old machinery for ₹ 0.5 crore, the payment of which is due in 10 months from the date of the balance sheet. The Company wants to present both these amounts as current since they will be settled within twelve months from the end of the reporting period. Is the management's decision correct?*

(4 Marks)

Answer

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

Particulars	*Note No.*	*₹ 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	655.00
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 ***(₹ in lakh)***

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

Working Notes:

1. **Analysis of Reserves and Surplus** *(₹ in lakh)*

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

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

Acquisition by LX Ltd. in MX Ltd. = 85%

Acquisition by MX Ltd. in NX Ltd. = 60%

Acquisition by Group in NX Ltd. (85% x 60%) = 51%

Non-controlling Interest = 49%

3. **Calculation of Goodwill / Capital Reserve on the acquisition**

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

Capital Reserve	260.00	252.50
Total Capital Reserve (260 + 252.50)	512.50	

4. Calculation of Non-controlling Interest

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

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

5. Calculation of Consolidated Other Equity

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

(b) Operating cycle of Charm Limited = 15 months

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

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

(ii) Yes, the Company's decision of presenting the trade receivables as Current Assets is correct despite the fact that these are receivables in 14 months' time since the operating cycle of the company is 15 months and any event arising due to trade will be considered as current if its settlement is within the tenure of operating cycle. Additionally, the Company also need to disclose amounts that are receivable within a period of 12 months and after 12 months from the reporting date. (Refer Para 60 and 61 of Ind AS 1)

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

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

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

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

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

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

Question 2

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

Particulars	*Property 1*	*Property 2*	*Property 3*
Purchase Price	*₹ 7,50,000*	*₹ 10,50,000*	*₹ 12,00,000*
Estimated life	*10 years*	*15 years*	*15 years*
Fair value as on 31st March, 2021	*₹ 8,00,000*	*₹ 9,50,000*	*₹ 13,00,000*

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

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

Analyze whether the accounting policies adopted by the Company in relation to the given properties are in accordance with Ind AS. If not, advise the correct treatment and present an extract of the Balance Sheet for the year ended 31st March 2021. ***(8 Marks)***

(b) GTM Limited has provided the following 4 independent scenarios. You are advised to respond to the queries mentioned at the end of each scenario. Support your answer with the relevant extracts of the applicable Ind AS.

Scenario 1

GTM Limited enters into a contract with a customer to sell product G, T and M in exchange for ₹ 1,90,000. GTM Limited will satisfy the performance obligations for each of the product at different points in time. GTM Limited regularly sells product G separately and therefore the stand-alone selling price is directly observable. The stand-alone selling prices of product T and M are not directly observable.

Because the stand-alone selling prices for Product T and M are not directly observable, the Company has to estimate them. To estimate the stand-alone selling prices, the Company uses the adjusted market assessment approach for product T and the expected cost plus a margin approach for product M. In making these estimates, the Company maximizes the use of observable inputs.

The entity estimated the stand -alone selling prices as follows:

Product	Stand-alone selling price (₹)
Product G	90,000
Product T	44,000
Product M	66,000
Total	2,00,000

Determine the transaction price allocated to each Product.

Scenario 2

GTM Limited regularly sells Products G, T and M individually. The standalone selling prices are as under:

Product	***Stand-alone selling price (₹)***
Product G	*90,000*
Product T	*44,000*
Product M	*66,000*
Total	*2,00,000*

In addition, the Company regularly sells Products T and M together for ₹ 1,00,000.

The Company enters into a contract with another customer to sell Products G, T and M in exchange for ₹ 1,90,000. GTM Limited will satisfy the performance obligations for each of the products at different points in time; or Product T and M at same point in time.

Determine the allocation of transaction price to Product T and M.

Scenario 3

GTM Limited enters into a contract with a customer to sell products G, T and M as described in scenario 2. The contract also includes a promise to transfer product 'Hope'. Total consideration in the contract is ₹ 2,40,000. The stand-alone selling price for product 'Hope' is highly variable because the company sells Product 'Hope' to different customers for a broad range of amounts (₹ 40,000 to ₹ 65,000).

Determine the selling price of Products G, T, M and Hope using the residual approach.

Scenario 4

The same facts as in scenario 3 applies to scenario 4 except that the transaction price is ₹ 2,25,000 instead of ₹ 2,40,000.

Discuss how the transaction price should be allocated. ***(12 Marks)***

Answer

(a) Preamble:

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

Guidance given in relevant Ind AS:

1. Property '1' and '2'

Definition and applicability:

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

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

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

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

Accounting Principles:

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

If an asset's carrying amount is decreased as a result of revaluation, the decrease shall be recognised in profit and loss statement.

2. Property '3'

Definition and applicability:

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

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

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

Accounting Principles:

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

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

a. Property, Plant and Equipment

b. Investment Property.

Analysis:

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

a. Presented all three properties in balance sheet as 'property, plant and equipment';

b. Not charged depreciation to Property '1' and '3';

c. Upward revaluation is recognised in the statement of profit and loss as profit; and

d. Applied revaluation model to Property '3' being classified as Investment Property.

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

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

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

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

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

Assets		**₹**
Non-Current Assets		
Property, Plant and Equipment		
Property '1'	8,00,000	
Property '2'	9,50,000	17,50,000

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

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

Working Notes:

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

(b) Scenario 1

The customer receives a discount for purchasing the bundle of goods because the sum of the stand-alone selling prices (₹ 2,00,000) exceeds the promised consideration (₹ 1,90,000). The entity considers that there is no observable evidence about the performance obligation to which the entire discount belongs. The discount is allocated proportionately across Products G, T and M. The discount, and therefore the transaction price, is allocated as follows:

Product	Allocated transaction price	
	₹	
Product G	85,500	(₹ 90,000 ÷ ₹ 2,00,000 × ₹ 1,90,000)
Product T	41,800	(₹ 44,000 ÷ ₹ 2,00,000 × ₹ 1,90,000)
Product M	62,700	(₹ 66,000 ÷ ₹ 2,00,000 × ₹ 1,90,000)
Total	1,90,000	

Scenario 2

The contract includes a discount of ₹ 10,000 on the overall transaction, which would be allocated proportionately to all three performance obligations when allocating the transaction price using the relative stand-alone selling price method.

However, because the entity regularly sells Products T and M together for ₹ 1,00,000 and Product G for ₹ 90,000, it has evidence that the entire discount of ₹ 10,000 should be allocated to the promises to transfer Products T and M in accordance with paragraph 82 of Ind AS 115.

If the entity transfers control of Products T and M at the same point in time, then the entity could, as a practical matter, account for the transfer of those products as a single performance obligation. That is, the entity could allocate ₹ 90,000 of the transaction prices to the single performance obligation of G and recognise revenue of ₹ 1,00,000 when Products T and M simultaneously transfer to the customer.

If the contract requires the entity to transfer control of Products T and M at different points in time, then the allocated amount of ₹ 1,00,000 is individually allocated to the promises to transfer Product T (stand-alone selling price of ₹ 44,000) and Product M (stand-alone selling price of ₹ 66,000) as follows:

Product	**Allocated transaction price**	
	₹	
Product T	40,000	(₹ 44,000 ÷ ₹ 1,10,000 total stand-alone selling price × ₹ 1,00,000)
Product M	60,000	(₹ 66,000 ÷ ₹ 1,10,000 total stand-alone selling price × ₹ 1,00,000)
Total	1,00,000	

Scenario 3

Before estimating the stand-alone selling price of Product Hope using the residual approach, the entity determines whether any discount should be allocated to the other performance obligations in the contract.

As in Scenario 2, because the entity regularly sells Products T and M together for ₹ 1,00,000 and Product G for ₹ 90,000, it has observable evidence that ₹ 1,90,000 should be allocated to those three products and ₹ 10,000 discount should be allocated to the promises to transfer Products T and M in accordance with paragraph 82 of Ind AS 115.

Using the residual approach, the entity estimates the stand-alone selling price of Product Hope to be ₹ 50,000 as follows:

Product	Stand-alone selling price	Method
	₹	
Product G	90,000	Directly observable
Products T and M	1,00,000	Directly observable with discount
Product Hope	50,000	Residual approach
Total	2,40,000	

The entity observes that the resulting ₹ 50,000 allocated to Product Hope is within the range of its observable selling prices (₹ 40,000 to ₹ 65,000).

Scenario 4

The same facts as in Scenario 3 apply to Scenario 4 except the transaction price is ₹ 2,25,000 instead of ₹ 2,40,000. Consequently, the application of the residual approach would result in a stand-alone selling price of ₹ 35,000 for Product Hope (₹ 2,25,000 transaction price less ₹ 1,90,000 allocated to Products G, T and M).

The entity concludes that ₹ 35,000 would not faithfully depict the amount of consideration to which the entity expects to be entitled in exchange for satisfying its performance obligation to transfer Product Hope, because ₹ 35,000 does not approximate the stand-alone selling price of Product Hope, which ranges from ₹ 40,000 to ₹ 65,000.

Consequently, the entity reviews its observable data, including sales and margin reports, to estimate the stand-alone selling price of Product Hope using another suitable method. The entity allocates the transaction price of ₹ 2,25,000 to Products G, T, M and Hope using the relative stand-alone selling prices of those products in accordance with paragraphs 73–80 of Ind AS 115.

Question 3

(a) *Sewa Dairy Limited prepares financial statements on 31st March each year. On 1st April 2020 the Company carried out the following transactions:*

- *Purchased a land for ₹ 60 lakh.*
- *Purchased 200 dairy cows (Average age at 1st April 2020 - 2 years) for ₹ 20 lakh. Received a non-refundable grant of ₹ 10 lakh towards the acquisition of the cows.*

During the year ending 31st March 2021, the Company on its dairy cows incurred ₹ 8.50 lakh to maintain their condition (food and protection) and ₹ 4.60 lakh as breeding fee to a local farmer.

On 1st October 2020,120 calves were born. There were no other changes in the number of animals during the year ended 31st March 2021. Sewa Dairy Limited had 3,200 litres of unsold milk in inventory as on 31st March 2021. The milk was sold on 1st and 2nd April· 2021 at market prices.

The information regarding fair values is as follows:

Items	*Fair values less cost to sell*		*(All values in ₹)*
	1st April 2020	*1st October 2020*	*31st March 2021*
Land	*60 Lakhs*	*70 Lakhs*	*80 Lakhs*
New born calves (per calf)	*2,000*	*2,300*	*2,500*
6 months old calves (per calf)	*2.,200*	*2;500*	*2,800*
2 years old cow (per cow)	*10,000*	*10,250*	*10,500*
3 years old cow (per cow)	*10,500*	*10,800*	*11,000*
Milk per litre	*25*	*27*	*30*

Prepare extracts from the Balance Sheet (assuming land under cost method) and Statement of Profit and Loss that would be reflected in the financial statements of Sewa Dairy Limited for the year ended 31st March 2021. Discuss the relevant Ind AS in support of your workings. ***(9 Marks)***

(b) A Limited purchased an asset of ₹ 200 lakh on 1st April 2017. It has useful life of 4 years with no residual value. Recoverable amount of the asset is as follows:

As on	*Recoverable amount*
31st March 2018	*₹ 120 lakh*
31st March 2019	*₹ 80 lakh*
31st March 2020	*₹ 56 lakh*

Calculate the amount of impairment loss or its reversal, if any,

- *On 31st March 2018;*
- *On 31st March 2019;*
- *On 31st March 2020.*

Depreciation is provided on SLM basis under the cost method. ***(6 Marks)***

(c) SB Limited is engaged in the business of producing extracts from the natural plants for pharmaceuticals and Ayurvedic companies. It has a wholly owned subsidiary, UB Limited which is engaged in the business of pharmaceuticals. UB Limited purchases the pharmaceuticals extracts from its parent company. The demand of UB Limited is very high and hence to cater its shortfall, UB Limited also purchases the pharmaceutical extracts from other companies. Purchases are made at the competitive prices.

SB Limited sold pharmaceutical extracts to UB Limited for Euro 10 lakhs on 1st February, 2021. The cost of these extracts was ₹ 770 lakh in the books of SB Limited at the time of sale. At the year-end, i.e. 31st March 2021, all these pharmaceutical extracts were lying as closing stock and payable with UB Limited.

Euro is the functional currency of UB Limited while Indian-Rupee is the functional currency of SB Limited.

Following additional information is available:

Exchange rate on 1st February 2021 — 1 Euro = ₹ 85

Exchange rate on 31st March 2021 — 1 Euro = ₹ 88

Provide the accounting treatment of the above in the books of SB Limited and UB Limited.

Also show its impact on consolidated financial statements. Support your answer by journal entries, wherever necessary. Assume NRV to be higher than the cost. ***(5 Marks)***

Answer

(a) Extract from the Statement of Profit and Loss of Sewa Diary Limited for the period ended on 31st March, 2021

		WN	Amount
Income			
Change in fair value of purchased dairy cow		WN 2	2,00,000
Government Grant		WN 3	10,00,000
Change in the fair value of newly born calves		WN 4	3,36,000
Fair Value of Milk		WN 5	96,000
Total Income	**(A)**		16,32,000
Expenses			
Maintenance Costs		WN 2	8,50,000
Breeding Fee		WN 2	4,60,000
Total Expense	**(B)**		(13,10,000)
Net Income	**(A-B)**		3,22,000

Extracts from Balance Sheet of Sewa Diary Limited As at 31st March, 2021

			₹
Property, Plant and Equipment:			
Land	WN 1		60,00,000

Biological assets other than bearer plants:			
Dairy Cow	WN 2	22,00,000	
Calves	WN 4	3,36,000	25,36,000
Inventory:			
Milk	WN 5		96,000

Working Notes:

1. **Land:** The purchase of the land is not covered by Ind AS 41. The relevant standard which would apply to this transaction is Ind AS 16. Under this standard, the land would initially be recorded at cost and depreciated over its useful economic life, which is usually considered to be infinite. Hence, no depreciation would be appropriate. Under Cost Model, no recognition would be made for post-acquisition changes in the value of land.

2. **Dairy Cows:** Under the 'fair value model' laid down in Ind AS 41 the mature cows would be recognised in the Balance Sheet at 31st March, 2021 at the fair value of 200 x ₹ 11,000 = ₹ 22,00,000.

   Increase in price change 200 x (10,500 - 10,000) = 1,00,000

   Increase in physical change 200 x (11,000 – 10,500) = 1,00,000

   The total difference between the fair value of matured herd and its initial cost (₹ 22,00,000 – ₹ 20,00,000 = a gain of ₹ 2,00,000) would be recognised in the profit and loss along with the maintenance cost and breeding fee of ₹ 8,50,000 and ₹ 4,60,000 respectively.

3. **Grant:** Grant relating to agricultural activity is not subject to the normal requirement of Ind AS 20. Under Ind AS 41 such grants are credited to income as soon as they are unconditionally receivable rather than being recognised over the useful economic life of the herd. Therefore, ₹ 10,00,000 would be credited to income of the company.

4. **Calves:** They are a biological asset and the fair value model is applied. The breeding fee is charged to income and an asset of 120 x ₹ 2,800 = ₹ 3,36,000 recognised in the Balance sheet and credited to Profit and loss.

5. **Milk:** This is agricultural produce and initially recognised on the same basis as biological assets. Thus, the milk would be valued at 3,200 x ₹ 30 = ₹ 96,000. This is regarded as 'cost' for the future application of Ind AS 2 to the unsold milk.

(b) As on 31st March, 2018

Carrying amount of the asset (opening balance)	₹ 200 lakh
Depreciation (₹ 200 lakh / 4 years)	(₹ 50 lakh)
Carrying amount of the asset (closing balance)	₹ 150 lakh
Recoverable amount (given)	₹ 120 lakh
Difference	₹ 30 lakh

Therefore, an impairment loss of ₹ 30 lakh should be recognised as on 31st March, 2018. Depreciation for subsequent years should be charged on the carrying amount of the asset (after providing for impairment loss), i.e., ₹ 120 lakh.

As on 31st March, 2019

Carrying amount of the asset (opening balance)	₹ 120 lakh
Depreciation (₹ 120 lakh / 3 years)	(₹ 40 lakh)
Carrying amount of the asset (closing balance)	₹ 80 lakh
Recoverable amount (Given)	₹ 80 lakh
Difference	NIL

Therefore, no impairment loss should be recognised as on 31st March, 2019.

As on 31st March, 2020

Carrying amount of the asset (opening balance)	₹ 80 lakh
Depreciation (₹ 80 lakh / 2 years)	(₹ 40 lakh)
Carrying amount of the asset (closing balance)	₹ 40 lakh
Recoverable amount (given)	₹ 56 lakh
Difference	(₹ 16 lakh)

Since, the recoverable amount of the asset exceeds the carrying amount of the asset by ₹ 16 lakh, impairment loss recognised earlier should be reversed. However, reversal of an impairment loss should not exceed the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognised for the asset in prior years.

Carrying amount as on 31st March, 2020 had no impairment loss being recognised would have been ₹ 50 lakh [ie. ₹ 200 lakh – (200 lakh / 4 x 3)]. Therefore, the reversal of an impairment loss of ₹ 10 lakh (₹ 50 lakh - ₹ 40 lakh) should be done as on 31st March, 2020.

(c) Accounting treatment in the books of SB Ltd (Functional Currency INR)

SB Ltd will recognize sales of ₹ 850 lakh (10 lacs Euro x ₹ 85)

Profit on sale of inventory = 850 lakh – 770 lakh = ₹ 80 lakh.

On balance sheet date receivable from UB Ltd. will be translated at closing rate i.e. 1 Euro = ₹ 88. Therefore, unrealised forex gain will be recorded in standalone profit and loss of ₹ 30 lakh [i.e. (₹ 88 - ₹ 85) x 10 lakh Euro].

Journal Entries

Date		(₹ in lakh)	(₹ in lakh)
1.2.2021	UB Ltd. A/c Dr.	850	
	To Sales		850
	(Being revenue recorded on initial recognition)		
31.3.2021	UB Ltd. A/c Dr.	30	
	To Foreign exchange difference (unrealised)		30
	(Being foreign exchange difference recorded at year end)		

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

Date		in Euros	in Euros
1.2.2021	Purchase account Dr.	10 lakh	
	To SB limited		10 lakh
	(Being purchased recorded at the date of transaction)		

UB Ltd will recognize inventory on 1st February, 2021 of Euro 10 lakh which will also be its closing stock at year end

Accounting treatment in the consolidated financial statements

Receivable and payable in respect of abovementioned sale / purchase between SB Ltd and UB Ltd will get eliminated

The closing stock of UB Ltd will be recorded at lower of cost or NRV.

Since the question ask to assume that NRV is higher than cost, inventory will be measured at cost only. Therefore, no write off is required.

The amount of closing stock of ₹ 850 lakh include two components–

- Cost of inventory for ₹ 770 lakh ; and
- Profit element of ₹ 80 lakh; and

At the time of consolidation, the second element amounting to ₹ 80 lakh will be eliminated from the closing stock.

Journal Entry

	(₹ in lakh)	(₹ in lakh)
Consolidated P&L A/c Dr.	80	
To Inventory		80
(Being profit element of intragroup transaction eliminated)		

Question 4

(a) *Softech Limited has a policy of providing subsidized loans to its employees for the purpose of buying or construction of residential houses. Mrs. B is a Senior Manager in the Company. The Company granted a loan to her on the following terms:*

- *Principal amount : ₹ 25 lakh*
- *Interest rate: 4% for the first ₹ 10 lakh and 7% for the next ₹ 15 lakh*
- *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 installments 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 a 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	*0.7972*	*0.7118*	*0.6355*	*0.5674*

Following table shows the contractually expected cash flows from the loan given to Mrs. B. *(Amount in ₹)*

Date	*Outflows*	*Inflows*			*Principal outstanding*
		Principal	*Interest income (7%)*	*Interest income (4%)*	
1st January 2019	*(25,00,000)*				*25,00,000*
31st December 2019		*5,00,000*	*1,05,000*	*40,000*	*20,00,000*

31st December 2020		5,00,000	70,000	40,000	15,00,000
31st December 2021		5,00,000	35,000	40,000	10,00,000
31st December 2022		5,00,000	-	40,000	5,00,000
31st December 2023		5,00,000	-	20,000	-

Mrs. B pre-pays ₹ 5,00,000 on 31st December 2020, reducing the outstanding principal as on date to ₹ 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 ₹)

Date	Outflows	Inflows			Principal outstanding
		Principal	Interest income (7%)	Interest income (4%)	
1st January 2019	(25,00,000)				25,00,000
31st December 2019		5,00,000	1,05,000	40,000	20,00,000
31st December 2020		10,00,000	70,000	40,000	10,00,000
31st December 2021		5,00,000	-	40,000	5,00,000
31st December 2022		5,00,000	-	20,000	-
31st December 2023		-	-	-	-

Record the journal entries (up to 31st December, 2020) in the books of Softech Limited considering the requirements of Ind AS 109. ***(14 Marks)***

(b) Government of India provides loans to MSMEs at a below-market rate of interest to fund the set-up of a new manufacturing facility. Sukshma Limited's date of transition to Ind AS is 1st April 2020.

In financial year 2014-2015, the Company had received a loan of ₹ 2.0 crore 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 ₹ 2.0 crore at the date of transition. The amount repayable on 31st March 2024 will be ₹ 2.50 crore.

The Company has been advised to recognize the difference of ₹ 0.50 crores in equity by correspondingly increasing the value of various assets under property, plant & equipment by an equivalent amount on proportionate basis. Further, on 31st March 2024 when the loan has to be repaid, ₹ 2.50 crore should be presented as a deduction from property, plant & equipment.

Discuss the above treatment and share your views as per applicable Ind AS. ***(6 Marks)***

OR

Nice Limited is a company incorporated on 1st April 2019. The Company has a net worth of ₹ 350 crore. The business of the company was affected due to low demand of its products. The following financial data is available as on 31st March 2021:

₹ in crore

	31st March 2020 Audited	*31st March 2020 Provisional*
Net Profit	*7.10*	*4.80*
Turnover	*550.00*	*1,050.00*

During the financial year 2020-2021:

- *The Company has spent ₹ 55,000 per month for developing vocational skills of local youth;*
- *The Company has also provided its products at a considerable discount for the benefit of the under-privileged, the cost of which to the Company is ₹ 3,50,000.*

The Company wants to carry forward its entire expenditure to next year as it is of the opinion that it does not have to spend anything on CSR activities during the current year.

Comment on the Company's applicability under Corporate Social Responsibility as per section 135 of the Companies Act, 2013 for the financial year 2020-2021. Does it have any obligation to transfer any amount to any fund? ***(6 Marks)***

Answer

(a) 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:

	Inflows				
Date	Principal	Interest income @ 7%	Interest income @ 4%	Discount factor @12%	PV
31st December 2019	5,00,000	1,05,000	40,000	0.8929	5,75,921
31st December 2020	5,00,000	70,000	40,000	0.7972	4,86,292
31st December 2021	5,00,000	35,000	40,000	0.7118	4,09,285
31st December 2022	5,00,000	-	40,000	0.6355	3,43,170
31st December 2023	5,00,000	-	20,000	0.5674	2,95,048
Total (fair value)					21,09,716

Benefit to Mrs. B, to be considered a part of employee cost for Softech Limited ₹ 3,90,284 (₹ 25,00,000 – ₹ 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 ₹ 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 ₹ 34 (55,718 – 55,684) is due to approximation.

Journal Entries in the books of Softech Limited

a. 1st January 2019

Particulars		Dr. (₹)	Cr. (₹)
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. (₹)	Cr. (₹)
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		78,057
(Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)		

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 ₹ 5,00,000 included in (d) below:

c. 31st December 2020

Particulars	Dr. (₹)	Cr. (₹)
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:

	Inflows				
Date	Principal	Interest income 7%	Interest income 4%	Discount factor @ 12%	PV
31st December 2021	5,00,000	-	40,000	0.8929	4,82,166
31st December 2022	5,00,000	-	20,000	0.7972	4,14,544
Total (revised carrying value)					8,96,710
Less: Current carrying value					(13,14,028)
Adjustment required					4,17,318

The difference between the amount of pre-payment and adjustment to loan shall be considered a gain, though will be recorded as an adjustment to pre-paid employee cost, which shall be amortised over the remaining tenure of the loan.

d. 31st December 2020 prepayment

Particulars		Dr. (₹)	Cr. (₹)
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

(b) **EITHER**

Requirement as per Ind AS:

A first-time adopter shall classify all government loans received as a financial liability or an equity instrument in accordance with Ind AS 32. A first-time adopter shall apply the requirements in Ind AS 109 and Ind AS 20, prospectively to government loans existing at the date of transition to Ind AS and shall not recognise the corresponding benefit of the government loan at a below-market rate of interest as a government grant.

Treatment to be done:

Consequently, if a first-time adopter did not, under its previous GAAP, recognise and measure a government loan at a below-market rate of interest on a basis consistent with Ind AS requirements, it shall use its previous GAAP carrying amount of the loan at the date of transition to Ind AS as the carrying amount of the loan in the opening Ind AS Balance Sheet. An entity shall apply Ind AS 109 to the measurement of such loans after the date of transition to Ind AS.

In the instant case, the loan meets the definition of a financial liability in accordance with Ind AS 32. Company therefore reclassifies it from equity to liability. It also uses the previous GAAP carrying amount of the loan at the date of transition as the carrying amount of the loan in the opening Ind AS balance sheet.

It calculates the annual effective interest rate (EIR) starting 1st April 2020 as below:

EIR = Amount / Principal$^{(1/t)}$ i.e. 2.50/2$^{(1/4)}$ i.e. 5.74%. approx.

At this rate, ₹ 2 crore will accrete to ₹ 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 (₹)	Interest expense for the year (₹) @ 5.74% p.a. approx.	Closing amortised cost (₹)
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.

(b) **OR**

Applicability of CSR:

A company which meets the net worth, turnover or net profits criteria in immediately preceding financial year will need to comply with provisions of sections 135(2) to (5) read with the CSR Rules.

According to the Act, the Board of every company shall 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 or where the company has not completed the period of three financial years since its incorporation, during such immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy.

Analysis of given case:

As per the criteria

(1) Net worth greater than or equal to ₹ 500 crore: This criterion is not satisfied.

(2) Sales greater than or equal to ₹ 1,000 crore: This criterion is not satisfied.

(3) Net profit greater than or equal to ₹ 5 crore: This criterion is satisfied in financial year ended 31st March 2020 ie immediate preceding financial year.

Hence, the Board has to spend on CSR Activities.

Quantification and mode of utilisation: As per the facts given in the question amount spent on CSR Activities during the year 2020-2021 pertains to the average net profits of the immediately preceding financial year i.e. 2019-2020. Accordingly, the company is under the obligation to transfer/expense 2% of ₹ 7.10 crore i.e. 0.142 crore = ₹ 14,20,000 in the year 2020-2021.

Nice Limited has spent ₹ 6,60,000 during the financial year 2020-2021 for developing vocational skills of local youth which is a permissible activity of Corporate Social Responsibility under Schedule VII to the Companies Act, 2013. However, expenditure of ₹ 3,50,000 spent on commercial activities at concessional rate does not qualify as expenditure on CSR activity. Hence, the amount spent of ₹ 6,60,000 by Nice Limited for financial year 2020-2021 is less than the required expenditure of ₹ 14,20,000 to be spent as per the provisions of CSR Rules.

Decision:

Since the company fails to spend such amount, the Board has to report the reasons for not spending the amount as per section 135(5). Further, because the company does not have any on-going project, the unspent amount of ₹ 7,60,000 (₹ 14,20,000 – ₹ 6,60,000) will be transferred to a Fund specified in Schedule VII to the Companies Act, 2013 within a period of 6 months of the expiry of the financial year 2020-2021.

Question 5

(a) At 31st March, 2019 the issued share capital of SB Limited consisted of 20,00,000 ordinary shares of ₹ 1 each. On 1st July 2019, the Company issued ₹ 25,00,000 of 8% convertible loan stock for cash at par. Each ₹ 100 nominal of the loan stock may be converted, at any time during the years ended 2024 to 2027, into the number of ordinary shares set out below:

- *31st March, 2024: 135 Ordinary Shares*
- *31st March, 2025: 130 Ordinary Shares*
- *31st March, 2026: 125 Ordinary Shares*
- *31st March, 2027: 120 Ordinary Shares*

If the loan stock is not converted by 2027, they would be redeemed at par.

It is assumed that the written equity conversion option is accounted for as a derivative liability and marked to market through profit or loss. The change in the options fair value reported on 31st March 2020 and 31st March 2021 amounted to losses of ₹ 5,000 and ₹ 5,300 respectively. Further, it is assumed that there are no tax consequences arising from these losses.

The profit before interest, fair value movements and taxation for the year ended 31st March, 2020 and 2021 amounted to ₹ 16,50,000 and ₹ 17,90,000 respectively and relate wholly to continuing operations. The rate of tax for both the periods is 33% (including cess and surcharge if any).

Calculate Basic and Diluted EPS for 31st March 2020 & 31st March 2021. ***(8 Marks)***

(b) *U Limited is operating in paint industry. Its business segments comprise paints (wall paints, lead paints, zinc paints, aluminium paints etc.), and others (consisting of primer, varnish, thinner and related products). Certain information for financial year 2020-2021 is given below:* ***₹ in lakh***

Segments	External Revenue (Inc. GST)	GST	Other operating income	Result	Assets	Liabilities
Paints	10,000	250	2000	500	2500	1500
Other	3,500	150	750	200	1500	500

Additional Information:

(i) *Unallocated income (Net of expenses) is ₹ 1,50,00,000.*

(ii) *Interest and bank charges is ₹ 1,00,00,000.*

(iii) *Income tax expenses is ₹ 1,00,00,000 (Current tax ₹ 97,50,000 and deferred tax ₹ 2,50,000)*

(iv) *Unallocated investments are ₹ 5,00,00,000 and other assets are ₹ 5,00,00,000.*

(v) *Unallocated liabilities, reserve and surplus and share capital are ₹ 10,00,00,000, ₹ 15,00,00,000 and ₹ 5,00,00,000 respectively.*

(vi) *Depreciation amounts for paints and others are ₹ 50,00,000 and ₹ 15,00,000 respectively.*

(vii) *Capital expenditure for paints and others are ₹ 2,50,00,000 and ₹ 1,00,00,000 respectively.*

(viii) *Revenue from outside India is ₹ 31,00,00,000 and segment assets outside India is ₹ 5,00,00,000.*

Based on the above information, how U Limited would disclose information about reportable segment revenue, profit or loss, assets and liabilities and others for financial year 2020-2021. Ignore corresponding figures for the previous year. ***(8 Marks)***

(c) *Ted entered into a lease contract with lessor to lease 2,000 sqm of retail space for 5 years. The rentals are payable monthly in advance. The lease commenced on 1st April 2019. In the year 2020, as a direct consequence of Covid 19 pandemic, Ted has negotiated with the lessor which may results in the following situations:*

- *Lessor agrees a rent concession under which the monthly rent will be reduced by 30% per month for the 12 months commencing 1st October 2020.*
- *Ted is granted a rent concession by the lessor whereby the lease payments for the period October 2020 to December 2020 are deferred. Three months are added to the end of the lease term at same monthly rent.*
- *Lessor offers to reduce monthly rent by 50% for the months October 2020 to March 2021 on the condition that its space is reduced from 2,000 sq m to 1,500 sq m.*

Analyze the given situations in the light of Ind AS 116 and comment on whether rent concession/deferral is eligible for practical expedient? ***(4 Marks)***

Answer

(a)

	2021	2020
Trading results	₹	₹
A. Profit before interest, fair value movements and tax	17,90,000	16,50,000
B. Interest on 8% convertible loan stock (2020: 9/12 × ₹ 2,00,000)	(2,00,000)	(1,50,000)
C. Change in fair value of embedded option	(5,300)	(5,000)
Profit before tax	15,84,700	14,95,000
Taxation @ 33% on (A-B)	(5,24,700)	(4,95,000)
Profit after tax	10,60,000	10,00,000
Calculation of basic EPS		
Number of equity shares outstanding	20,00,000	20,00,000
Earnings	10,60,000	10,00,000
Basic EPS	53 paise	50 paise

Calculation of diluted EPS

Test whether convertibles are dilutive:

The saving in after-tax earnings, resulting from the conversion of ₹ 100 nominal of loan stock, amounts to (₹ 100 × 8% × 67%) + (₹ 5,300 / 25,000) = ₹ 5.36 + ₹ 0.21 = ₹ 5.57.

There will then be 135 extra shares in issue.

Therefore, the incremental EPS is 4 paise (ie. ₹ 5.57 / 135). As this incremental EPS is less than the basic EPS at the continuing level, it will have the effect of reducing the basic EPS of 53 paise. Hence the convertibles are dilutive.

	2021	2020
Adjusted earnings	₹	₹
Profit for basic EPS	10,60,000	10,00,000
Add: Interest and other charges on earnings saved as a result of the conversion	(2,00,000 + 5,300) 2,05,300	(1,50,000 + 5,000) 1,55,000
Less: Tax relief on interest portion	(66,000)	(49,500)
Adjusted earnings for equity	11,99,300	11,05,500

Adjusted number of shares

From the conversion terms, it is clear that the maximum number of shares issuable on conversion of ₹ 25,00,000 loan stock after the end of the financial year would be at the rate of 135 shares per ₹ 100 nominal (that is, 33,75,000 shares).

	2021	2020
Number of equity shares for basic EPS	20,00,000	20,00,000
Maximum conversion at date of issue (33,75,000 × 9/12)	-	25,31,250
Maximum conversion after balance sheet date	33,75,000	–
Adjusted shares	53,75,000	45,31,250
Adjusted earnings for equity	11,99,300	11,05,500
Diluted EPS (approx.)	22 paise	24 paise

(b) Segment information

(A) Information about operating segment

(1) the company's operating segments comprise:

Paints: consisting of wall paints, lead paints, zinc paints, aluminum paints etc.

Others: consisting of primer, varnish, thinner and related products.

(2) Segment revenues, results and other information:

(₹ in lakh)

	Revenue	Paints	Others	Total
1.	External Revenue (gross)	10,000	3,500	13,500
	GST	(250)	(150)	(400)
	Total Revenue (net)	9,750	3,350	13,100
	Other operating Income	2,000	750	2,750
	Total Revenue	11,750	4,100	15,850

2.	Results			
	Segment results	500	200	700
	Unallocated income (net of unallocated expenses)			150
	Profit from operation before interest, taxation and exceptional items			850
	Interest and bank charges			(100)
	Profit before exceptional items			750
	Exceptional items			Nil
	Profit before taxation			750
	Income Taxes			
	-Current taxes			(97.5)
	-Deferred taxes			(2.5)
	Profit after taxation			650
3.	Other Information			
(a)	Assets			
	Segment Assets	2,500	1,500	4,000
	Investments			500
	Unallocated assets			500
	Total Assets			5,000
(b)	Liabilities/Shareholder's funds			
	Segment liabilities	1,500	500	2,000
	Unallocated liabilities			1,000
	Share capital			500
	Reserves and surplus			1,500
	Total liabilities / shareholder's funds			5,000
(c)	Others			
	Capital Expenditure	(250)	(100)	
	Depreciation	(50)	(15)	

Geographical Information				(₹ in lakh)
		India	Outside India	Total
	Revenue	12,750	3,100	15,850
	Segment assets	4,500	500	5,000
	Capital expenditure (250 + 100)	350		350

(c) Applicability of practical expedient:

The practical expedient applies only to rent concessions occurring as a direct consequence of the covid-19 pandemic.

As a practical expedient, a lessee may elect not to assess a rent concession as a lease modification only if **all** of the following conditions are met:

(a) the change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change;

(b) any reduction in lease payments affects only payments originally due on or before the 30th June, 2021; and

(c) there is no substantive change to other terms and conditions of the contract

Analysis:

Based on above guidance, answer to the given situations with the lessor would be as follows:

- Lessor agrees a rent concession under which the monthly rent will be reduced by 30% per month for the 12 months commencing 1st October 2020:

  The rent deferral does not satisfy the criteria to apply the practical expedient because out of the listed eligibility criteria given in Ind AS 116, rent concession reduces lease payments starting from October, 2020 and reduction will continue till September, 2021 which is beyond 30th June 2021. Therefore, Ted is not permitted to apply the practical expedient.

- Ted is granted a rent concession by the lessor whereby the lease payments for the period October 2020 to December 2020 are deferred. Three months are added to the end of the lease term at same monthly rent:

  (a) condition is met since revised consideration in the lease is substantially the same as the original

  (b) condition is met since the rent concession only reduces lease payments originally due in 2020 – i.e. before 30th June 2021.

(c) condition is met since the lessee assesses that three-month extension at the end of the lease term is with substantially the same lease payments. Hence, it would not constitute a substantive change.

Since, the rent concession is a direct consequence of COVID-19 and all three conditions are met, rent concession is eligible for application of practical expedient in this case.

- Lessor offers to reduce monthly rent by 50% for the months October 2020 to March 2021 on the condition that its space is reduced from 2,000 sqm to 1,500 sqm:

  The rent concession does not satisfy the criteria to apply the practical expedient because out of the listed eligibility criteria given in Ind AS 116, there is a substantive change to the terms and conditions of the lease as there is a change in the scope of lease by reducing the space from 2,000 sqm to 1,500 sqm. Therefore, Ted is not permitted to apply the practical expedient.

Question 6

(a) Heavy Limited has a plant with normal capacity to produce 90,000 units of a product per annum and expected fixed production overhead for the year is ₹ 18,00,000. There are no quarterly / seasonal variations.

Hence, normal expected production of each quarter is uniform. The actual production of the year is 87,000 units. The production details of each quarter are as under:

Quarter I:	*20,000 units*
Quarter II:	*24,000 units*
Quarter III:	*23,500 units*
Quarter IV:	*19,500 units*

Calculate the allocation of fixed production overhead for all the four quarters. Will the quarterly results affect annual result?

Give your answer as per Ind AS 34 read with Ind AS 2. ***(5 Marks)***

(b) On 1st October, 2017 Axe Limited issues preference shares to B Limited for a consideration of ₹ 18 lakh. The holder has an option to convert these preference shares to a fixed number of equity instruments of the issuer any time up to a 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 ₹ 20 lakh 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 (that 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). ***(5 Marks)***

(c) *Voya Limited issued 1,000 share options to each of its 200 employees for an exercise price of ₹ 10. The employees are required to stay in employment for next 3 years. The fair value of the option is estimated at ₹ 18.*

90% of the employees are expected to vest the option.

The Company faced severe crisis during the 2nd year and it was decided to cancel the scheme with immediate effect. The market price of the share at the date of cancellation was ₹ 15.

The following information is available:

- Fair value of the option at the date of cancellation is ₹ 12.
- The company paid compensation to the employees at the rate of ₹ 13.50. There were only 190 employees in the employment at that time.

You are required to show how cancellation will be recorded in the books of the Company as per relevant Ind AS. ***(5 Marks)***

(d) *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 ₹ 1,750 lakh. The fair value of AG Limited's net assets was ₹ 750 lakh, but this fair value does not include:

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

UG Limited has requested you to suggest the accounting treatment of the above transaction under applicable Ind AS. ***(5 Marks)***

Answer

(a) Since it is considered that there is no quarterly / seasonal variation, then normal expected production for each quarter is 22,500 units (90,000 units / 4 quarters) and fixed production overheads for the quarter are ₹ 4,50,000 (₹ 18,00,000 / 4 quarters).

Fixed production overhead to be allocated per unit of production in every quarter will be ₹ 20 per unit.

(Fixed overheads / Normal production i.e. ₹ 4,50,000 / 22,500 units

Particulars	Quarters			
	I	II	III	IV
Actual fixed production overheads on year to date basis (₹)	4,50,000	9,00,000	13,50,000	18,00,000
Actual production (Units)	20,000	24,000	23,500	19,500
Actual production year to date basis (Units)	20,000	44,000	67,500	87,000
Fixed overheads to be absorbed on year to date basis (₹)	4,00,000	8,80,000	13,50,000	17,40,000
Under recovery year to date (₹)	**50,000**	**20,000**	**NIL**	**60,000**

Quarter I:

Unallocated fixed production overheads ₹ 50,000 (i.e. ₹ 4,50,000 – ₹ 4,00,000) to be charged as expense as per Ind AS 2 and consequently as per Ind AS 34.

Quarter II:

Since production increased in second quarter by 1,500 units (24,000 – 22,500) i.e. more than the normal expected production, hence ₹ 30,000 (1,500 units x ₹ 20 per unit) will be reversed by way of a credit to the statement of profit and loss of the 2nd quarter and debit to cost of production / inventory cost.

Quarter III:

Earlier, ₹ 50,000 was not allocated to production / inventory cost in the 1st quarter. Out of it, ₹ 30,000 was reversed in the 2nd quarter. To allocate entire ₹ 13,50,000 till third quarter to the production, as per Ind AS 34, remaining ₹ 20,000 (₹ 50,000 – ₹ 30,000) will be reversed by way of a credit to the statement of profit and loss of the 3rd quarter and debit to the cost of production / inventory cost.

Quarter IV:

Unallocated fixed production overheads ₹ 60,000 {i.e. ₹ 4,50,000 – (₹ 20 x 19,500)} in the 4th quarter will be expensed off as per the principles of Ind AS 2 and Ind AS 34 by way of a charge to the statement of profit and loss.

For the year:

The cumulative result of all the quarters would also result in unallocated overheads of ₹ 60,000, thus, meeting the requirements of Ind AS 34 that the quarterly results should not affect the measurement of the annual result.

(b) The values of the liability and equity components are calculated as follows:

Present value of principal payable at the end of 4 years (₹ 18,00,000 discounted at 8% for 4 years i.e. ₹ 18,00,000 x 0.735)	₹ 13,23,000
Present value of interest payable in arrears for 4 years (₹ 99,000 (₹ 18,00,000 x 5.5%) discounted at 8% for each of 4 years (i.e. ₹ 99,000 x 3.312))	₹ 3,27,888
Total financial liability	₹ 16,50,888
Consideration amount	(₹ 18,00,000)
Residual – equity component	₹ 1,49,112

Therefore, equity component = fair value of compound instrument, say, ₹ 18,00,000 less financial liability component i.e. ₹ 16,50,888 = ₹ 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.

(c) (A) Calculation of employee compensation expense

	Year 1	Year 2	
Expected employees to remain in the employment during the vesting period	180	190	
Fair value of option	18	18	
Number of options	1,000	1,000	
Total	32,40,000	34,20,000	

Expense weightage	1/3	2/3	Balance 2/3rd in full, as it is cancelled
Expense for the year	10,80,000	23,40,000	Remaining amount since cancelled

(B) Cancellation compensation to be charged in the year 2

Cancellation compensation		
Number of employees (A)	190	
Amount agreed to pay (B)	13.50	
Number of options/ employee (C)	1,000	
Compensation amount (A x B x C)		25,65,000
Less: Amount to be deducted from Equity		
Number of employees (D)	190	
Fair value of option (at the date of cancellation) (E)	12	
Number of options / employee (F)	1,000	
Amount to be deducted from Equity (D x E x F)		(22,80,000)
Balance transferred to Profit and Loss		2,85,000

(d) Recognition Principle as per Ind AS:

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

Accounting Treatment:

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

(i) **Patent owned by AG Limited:** The patent owned will be recognised at fair value by UG Limited even though it was not recognised by AG Limited in its financial statements. The patent will be amortised over the remaining useful life of the asset i.e. 10 years. Since the company is awaiting the outcome of the trials, the value of the patent cannot be estimated at ₹ 750 lakh and the extra ₹ 250 lakh should only be disclosed as a Contingent Asset and not recognised.

(ii) **Patent internally developed by AG Limited:** As per para 18 of Ind AS 103 'Business Combinations', the acquirer shall measure the identifiable assets acquired and the liabilities assumed at their acquisition date fair values. Since the patent developed has been approved for clinical use, it is an identifiable asset, hence the same will be measured at fair value i.e. ₹ 1,000 lakh on the acquisition date.

Hence the revised working would be as follows:

	₹
Fair value of net assets of AG Limited	750 lakh
Add: Patent (500 lakh + 1,000 lakh)	1,500 lakh
	2,250 lakh
Purchase consideration	(1,750 lakh)
Gain on bargain purchase	500 lakh