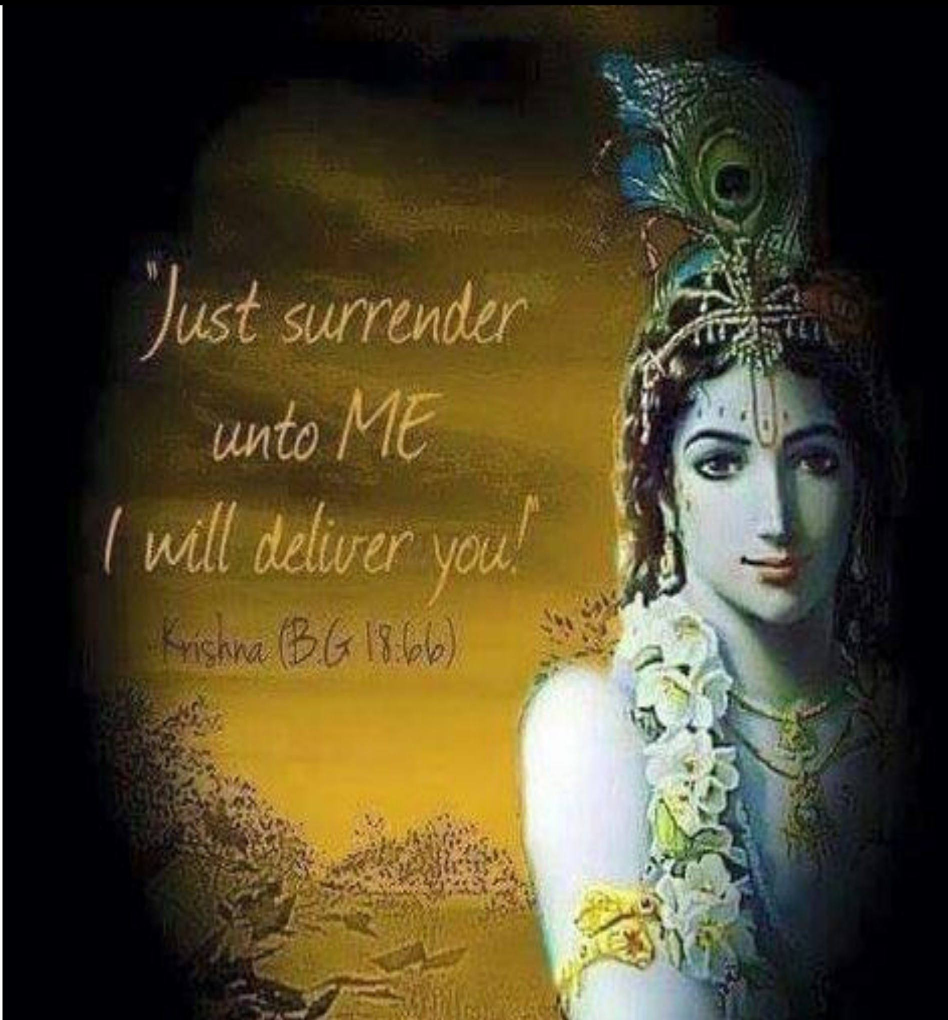
AIR1CA CAREER INSTITUTE

CA FINAL

FINANCIAL REPORTING



CONCEPT NOTES

(Relevant for **MAY & NOV 2024** examination)

These Concept Notes are prepared by **CA AJAY AGARWAL (AIR 1)**. All concepts of CA Final FR are covered in **253 pages**. Refer these Notes alongwith the Question Bank and Lectures/ Revision Videos.

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Best Wishes… Radhe Radhe!!

Financial Reporting

Edition: 2024

These Concept Notes are Black & White.

Coloured Concept Notes for CA Final FR are separately available in Hard Copy mode only.

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FINANCIAL REPORTING

Introduction to Indian Accounting Standards [Ind AS]

Generally Accepted Accounting Principles [GAAP]

India
↓
AS (1 to 32)
issued by ASB of ICAI

Internationally
↓
IFRS [IAS 1 to 41, IFRS 1 to 16]
issued by IASB
↓
To make our financial statements as per International Level
↓
We have the Option to

- Adopt IFRS as it is

OR

- **Converge IFRS**
  ↓
  Ind AS
  - Carve Out ↓ Change in Accounting Treatment as given in IFRS
  - Carve In ↓ Additional Guidance which is not given in IFRS

List of Ind AS

As on date, 39 Ind AS are notified ; out of which 35 Ind AS are in syllabus

IND AS	Description
Ind AS 1	Presentation of Financial Statements
Ind AS 2	Inventories
Ind AS 7	Statement of Cash Flows
Ind AS 8	Accounting Policies, Changes in Accounting Estimates and Errors
Ind AS 10	Events after the Reporting Period
Ind AS 12	Income Taxes
Ind AS 16	Property, Plant and Equipment
Ind AS 19	Employee Benefits
Ind AS 20	Accounting for Government Grants and Disclosure of Government Assistance
Ind AS 21	The Effects of Changes in Foreign Exchange Rates
Ind AS 23	Borrowing Costs
Ind AS 24	Related Party Disclosures
Ind AS 33	Earnings per Share
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Ind AS 36	Impairment of Assets
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Ind AS 38	Intangible Assets
Ind AS 40	Investment Property
Ind AS 41	Agriculture
Ind AS 101	First-time Adoption of Indian Accounting Standard
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Ind AS 105	Non-current Assets Held for Sale and Discontinued Operations
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Ind AS 27, 28, 110, 111, 112	Consolidated and Separate Financial Statements of Group Entities
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Ind AS 116	Leases
Not in Syllabus	
Ind AS 29	Financial Reporting in Hyperinflationary Economies
Ind AS 104	Insurance Contracts
Ind AS 106	Exploration for and Evaluation of Mineral Resources
Ind AS 114	Regulatory Deferral Accounts

Applicability of Ind AS

(1) On Indian Companies

Phase I
[From 1st April 2016]

- All Companies [Listed & Unlisted] having Net Worth ≥ ₹ 500 Crore as on 31.3.14 or 31.3.15 or 31.3.16
- Parent, Subsidiary, Associate & Joint Venture of above (except foreign Company & NBFC)

Phase II
[From 1st April 2017]

- All Listed Companies
- All Unlisted Companies having Net Worth ≥ ₹ 250 Crore as on 31.3.14 or 31.3.15 or 31.3.16 or 31.3.17
- Parent, Subsidiary, Associate & Joint Venture of above (except foreign Company & NBFC)

If a Company meets the criteria specified in Phase II in any year after 31.3.17, then it shall apply Ind AS from the immediate next year (after meeting the criteria)

(2) On Non Banking Financial Companies [NBFCs]

Phase I
[From 1st April 2018]

- All Companies [Listed & Unlisted] having Net Worth ≥ ₹ 500 Crore as on 31.3.16 or 31.3.17 or 31.3.18
- Parent, Subsidiary, Associate & Joint Venture of above (except foreign Company)

Phase II
[From 1st April 2019]

- All Listed Companies
- All Unlisted Companies having Net Worth ≥ ₹ 250 Crore as on 31.3.16 or 31.3.17 or 31.3.18 or 31.3.19
- Parent, Subsidiary, Associate & Joint Venture of above (except foreign Company)

If a Company meets the criteria specified in Phase II in any year after 31.3.19, then it shall apply Ind AS from the immediate next year (after meeting the criteria)

Note :-

(i) Calculation of Net Worth :

Equity Share Capital	xx
(+) Securities Premium	xx
(+) General Reserve	xx
(±) P&L Balance [Surplus or Deficit]	xx / (xx)
(-) Miscellaneous Expenditure not written off	(xx)
	xx

(ii) Indian Companies can apply Ind AS on Voluntary Basis also. [NBFCs are not allowed to apply Ind AS on Voluntary Basis]

(iii) Once Entity starts following Ind AS, it shall be required to follow Ind AS forever.

(iv) Companies Listed on SME Exchange are not required to apply Ind AS.

(v) At present, Ind AS are not applicable to Banking & Insurance Companies.

Ind AS Financial Statements

Ind AS 1 prescribes Ind AS Financial Statements [Format is given under Division II of Schedule III of Companies Act 2013]

- Balance Sheet
- Statement of Profit & Loss
- Statement of Changes in Equity
- Statement of Cash flows [Ind AS 7]
- Notes to Accounts

Introduction to Conceptual Framework

- It is not a Standard & does not override any Standard.
- It provides assistance to
  - Standard Setter [ICAI] ⇓ in formulation of New Ind AS
  - Preparer of financial Statements ⇓ To develop accounting policy when No Ind AS is available for a particular transaction

Objective of General Purpose financial Reporting

- Objective of General Purpose financial Reports is to provide financial information about the entity for assisting users in decision making
- Financial Statements are not intended to reflect the value of an entity.
- Hence, it does not mean that Ind AS are not reflecting usefulness of financial Statements as they do not reflect the financial value of the entity.

Qualitative Characteristics of Useful Financial Information

- If financial Information is to be useful, it must have
  - Fundamental Qualitative Characteristics
    - Relevant Information
    - Faithful Representation ⇓ It must be
      - → Complete
      - → Neutral
      - → Free from Error
  - Enhancing Qualitative Characteristics
    - Comparability
    - Verifiability
    - Timeliness
    - Understandability

- Cost Constraint on Useful financial Information :-

  (i) Role of Cost : Reporting of financial Information imposes cost which must be justified by benefits of reporting that information.

  (ii) Basis of Assessment of Cost : Assess whether benefits of reporting information can justify the costs incurred on the basis of quantitative & qualitative information.

(iii) Cost Perspective : Costs & Benefits of reporting financial information should be considered in relation to financial reporting generally, not in relation to individual entities.

Elements of Financial Statements

- There are 5 Elements of Financial Statements as follows :

Assets	Liabilities	Equity	Income	Expenses
It means Present Economic Resource [A Right that has potential to produce economic benefits, even if probability of producing economic benefits is Low] controlled by the entity	It means Present obligation to transfer economic resources	It means Residual Interest in Net Assets of the entity	It means Increase in Assets or Decrease in Liabilities which results in Increase in Equity	It means Decrease in Assets or Increase in Liabilities which results in Decrease in Equity

- Recognition Criteria :

These Elements are recognised in Financial Statements only if
→ meet the above definition , &
→ Recognition provides useful information to users of financial statements [i.e. Relevant Information & Faithful Representation]

- Derecognition of Assets or Liabilities [i.e. Removal from Balance Sheet] :

→ Asset should be derecognised when control on that Asset is Lost.
[If entity has transferred an asset but retains exposure to its economic benefits, then it indicates that control on that asset is not lost.]

→ Liability should be derecognised when Present Obligation no longer exists.

Measurement Basis for Recognising Elements in Financial Statements

- Measurement Bases :
  - Historical Cost
  - Current Value
    - Fair Value [Exit Price]
    - Value in Use
    - Current Cost [Entry Price]

- Hence, Ind AS does not implement a Fair Value Model only. It is based on 'Mixed Measurement Approach' because using a common basis for all elements may not provide relevant information to users.

Other Points

(1) Conceptual Framework states that users need information which allow them to assess future cash flows of the entity.
So, According to Conceptual framework, if entity has made a decision to sell the subsidiary, then it should be classified as Discontinued Operation even if criteria as per Ind AS 105 has not been met.

(2) In case of differences between Conceptual Framework & Ind AS, Ind AS would prevail.

(3) Executory Contracts :-

- A contract which is equally unperformed, i.e.

Neither Party has performed its obligations — OR — Both Parties have partially performed the obligations to equal extent

- It establishes a Combined Right & Obligation to exchange economic resources.

Concept of Capital Maintenance

- It is used to calculate whether entity has maintained the Capital in business to repeat the whole process endlessly.

- Approaches to Capital Maintenance :-

(i) Financial Capital Maintenance at Historical Cost :

Closing Capital [Opening Capital ± Profit / (Loss) during the year − Capital Withdrawal during the year]	xxx
(-) Capital to be maintained [Same as Opening Capital]	(xxx)
Extra Capital / (Less Capital)	xxx / (xxx)

(ii) Financial Capital Maintenance at Current Purchasing Power :

Closing Capital $\left[\text{Opening Capital} \pm \text{Profit / (Loss) during the year} - \text{Capital Withdrawal during the year}\right]$	xxx
(-) Capital to be maintained $\left[\text{Opening Capital} \times \dfrac{\text{Price Index at Year End}}{\text{Price Index at Year Beginning}}\right]$	(xxx)
Extra Capital / (Less Capital)	xxx / (xxx)

(ii) Physical Capital Maintenance :

Closing Capital $\left[\text{Opening Capital} \pm \text{Profit / (Loss) during the year} - \text{Capital Withdrawal during the year}\right]$	xxx
(-) Capital to be maintained $\left[\text{Opening Capital} \times \dfrac{\text{Price of Product at Year End}}{\text{Price of Product at Year Beginning}}\right]$	(xxx)
Extra Capital / (Less Capital)	xxx / (xxx)

Complete Set of Financial Statements

- Balance Sheet
- Statement of Profit & Loss
- Statement of Changes in Equity
- Statement of Cash flows
- Notes to Accounts

- For Current Year
- Comparative for Previous Year

Note :-

(i) Format for Preparation of Ind AS complied financial Statements is prescribed by Division II of Schedule III to the Companies Act 2013.

If there is any conflict in accounting treatment or disclosure in any Ind AS and Schedule III, then Companies are required to comply with Ind AS.

(ii) Entity can present Comparative financial Statements for More than 1 Previous Year.

(iii) Entity shall also present a 3rd Balance Sheet at the beginning of previous year if it

- Applies Accounting Policy Retrospectively which has an effect on the items in Balance Sheet at the beginning of Previous Year

OR

- Makes Retrospective Restatement which has an effect on the items in Balance Sheet at the beginning of Previous Year

OR

- Reclassifies an Item in Balance Sheet

(iv) Entity shall clearly write the currency in which financial Statements are presented.

Features of Financial Statements

- **Presentation of True & Fair View :-**

Entity shall comply with all Ind AS and make an Explicit & Unreserved Statement of such compliance in Notes to Accounts. However, Auditor of Entity may qualify the audit report because of disagreement with the application of Ind AS by the Entity.

- **Going Concern :-**

→ Financial Statements should be prepared on a Going Concern Basis.

→ If Management has significant doubt on the Entity's ability to continue as a Going Concern & financial Statements are not prepared on Going Concern basis, then the fact should be disclosed in Notes to Accounts.

- **Frequency of Reporting :-**

Entity shall prepare Financial Statements at least Annually.

- Offsetting :-
  Entity shall not offset Assets or Liabilities, Income or Expense unless required by Ind AS.
- Accrual Basis of Accounting
- Materiality
- Consistency
- Comparative Information

Classification of Assets & Liabilities as Current and Non Current

(1) Assets :-

Entity shall classify an Asset as Current if

- It expects to realise the Asset in its Normal Operating Cycle

OR

- It expects to realise the Asset within 12 months from Balance Sheet Date

OR

- It holds the Asset for Trading Purpose [Eg: Inventory, DFA, etc.]

OR

- Asset is Cash & Cash Equivalent

* All Other Assets are classified as Non Current.

(2) Liabilities :-

Entity shall classify a Liability as Current if

- It expects to settle the Liability in its Normal Operating Cycle

OR

- Liability is due for settlement within 12 Months from Balance Sheet Date

OR

- It holds the Liability for Trading Purpose [Eg: DFL]

OR

- It cannot defer settlement of Liability for atleast 12 Months from Balance Sheet Date [Eg: Liability which becomes immediately payable if contract is cancelled]

* All Other Liabilities are classified as Non Current.

Note :-

(i) Operating Cycle :

→ It means the time between acquisition of assets for processing & their realisation in cash.

→ Operating Cycle =
Raw Material Holding Period
(+) WIP Holding Period
(+) Finished Goods Holding Period
(+) Debtors Collection Period

(ii) Advance given for PPE Purchase [Capital Advance] should be treated as Non Current Asset.

(iii) Current Portion of Non Current Financial Asset or Financial Liability should be classified as Current Asset | Liability

(iv) If Loan Payable within 12 Months from Balance Sheet Date [i.e. Current Liability] is Refinanced / Rolled Over for atleast 12 Months from Balance Sheet Date via

- Existing Lender
  - Before Balance Sheet Date ⇓ Non Current Liability
  - After Balance Sheet Date ⇓ Current Liability
- New Lender ⇓ Current Liability

* If Entity has not refinanced the loan but has potential to refinance it, then Loan will be classified as Current Liability only.

(v) If there is a Breach in Material Provision / Covenant | Condition of a Loan Payable after 12 Months from Balance Sheet Date [i.e. Non Current Liability], then the Loan becomes payable on demand.
Hence, it will be classified as a Current Liability.
⇓
But If Entity before Date of approval of Financial Statements takes Grace Period of atleast 12 Months to rectify the breach [i.e. Waiver from Lender to not demand payment immediately as a consequence of breach], then this Loan will continue to be classified as a Non Current Liability.

* If Entity approaches the Lender for extension of compliance date in antincipation of Breach [i.e. Actual Breach has not taken place], then the Loan will remain as a Non Current Liability only.

Meaning of Inventories

Inventories are Assets

- Held for Sale in Ordinary Course of Business [Finished Goods]
- In Production Process for such sale [WIP]
- Materials & Supplies used in Production Process [Raw Material]

Measurement of Inventories

- Finished Goods or WIP
  - ⇓ Lower of Cost or Net Realisable Value (NRV)
- Raw Material
  - If Finished Goods are expected to be sold at ≥ Cost
    - ⇓ Raw Material is measured at Cost
  - If Finished Goods are expected to be sold at < Cost
    - ⇓ Raw Material is measured at Lower of Cost or Replacement Cost

Note:-

(i) Inventory can be measured at

→ Item by Item Basis ✓

OR

→ Group Basis

Example:

Garments Showroom

Shirts	Cost	NRV	Valuation [Item by Item]	Valuation [Group]
1	200	150	150	
2	300	400	300	
3	500	550	500	
	1,000	1,100		1,000
Jeans				
1	600	800	600	
2	850	700	700	
3	750	900	750	
	2,200	2,400		2,200
			3,000	3,200

(ii) Inventory is measured at each Balance Sheet Date.

Example:

Year Ending	Cost	NRV	Valuation
31.3.20X1	100	80	80
31.3.20X2	100	90	90
31.3.20X3	100	110	100

Cost of Inventories

(1) **If Inventory is Purchased or Produced:-**

- It includes any cost necessary to bring Inventory to Present location & condition.
- For Calculation of Cost of Closing Stock, We have to Calculate Cost of Total Purchase | Production during the period firstly as follows:

In Case of Purchased Goods

Purchase Price	xx
(-) Trade Discount / Rebate	xx
(+) Import Duty & Taxes like GST [Only if Non Refundable]	xx
(+) Transport / Freight Charges	xx
(+) Other Handling Cost	xx
(+) Insurance on Purchase	xx
(+) Brokerage to Indenting Agents [Example: Buying Commission]	xx
Cost of Purchases	xx

In Case of Produced Goods

Direct Material Cost	xx
(+) Direct Labour Cost	xx
(+) Production / Manufacturing Overheads:	
Variable Overheads [Example: Designing Cost]	xx
Fixed Overheads [Example: Depreciation of Factory Building & Plant, Factory Rent, Energy Cost, etc.]	xx
Cost of Production	xx

$$\therefore \text{Cost per unit} = \frac{\text{Cost of Purchases / Production}}{\text{Actual Units Purchased / Produced}}$$

Now, This Cost of Purchases | Production will be bifurcated as follows:

Cost of Closing Stock

Units in Closing Stock × Cost Per Unit

Cost of Goods Sold out of this Purchase / Production [Balancing figure]

Cost of Purchases | Production − Cost of Closing Stock

OR

Units Sold × Cost per unit

* Total Cost of Goods Sold [COGS] / Cost of Sales

$\Rightarrow$ Cost of Opening Stock + Cost of Purchases / Production − Cost of Closing Stock

Note :-

(i) In Silent Situation, Assume All Taxes are Non Refundable.

(ii) Following Items are not included in Cost of Purchases / Production :

→ Abnormal Loss

→ Storage Cost unless necessary for Production

→ Administrative Overheads [Example : Salary of Accounting Department]

→ Selling Overheads / Costs [Example : Sales Commission, Warranty Costs, etc.]

→ Cash Discount / Early Settlement Discount

→ Interest Cost / Loan Raising Fees on Loan taken to purchase or produce the inventories (unless allowed by Ind AS 23)

(iii) Allocation of Fixed Overheads :

↓ Fixed Overheads allocated to Cost of Production during the period [Absorbed Fixed Overheads]

⇓

Actual Units Produced × Fixed Overheads Recovery Rate Per Unit

↓ Remaining Fixed Overheads are expensed to P&L during the period [Unabsorbed Fixed Overheads]

⇓

Balancing figure

⇓

Total Fixed Overheads − Absorbed Fixed Overheads

Here,

$$\text{Fixed Overheads Recovery Rate Per Unit} = \frac{\text{Total Fixed Overheads}}{\text{Higher of Normal Units or Actual Units Produced}}$$

* If Actual Units Produced during the period are not given in question, then it can be calculated as follows :

Units in Closing Stock of Finished Goods + Units Sold of Finished Goods − Units in Opening Stock of Finished Goods

Example :

Total Fixed Overheads = ₹ 12,000 , Normal Production = 500 Units

Allocate Fixed Overheads if

(i) Actual Production = 400 units

(ii) Actual Production = 600 units

Solution :

(i) $\text{Fixed Overhead Recovery Rate per unit} = \frac{₹\ 12{,}000}{500 \text{ units}} = ₹\ 24$ per unit

∴ Allocation of Total fixed Overheads of ₹ 12,000 are as follows:

Cost of Production ⇒ 400 units × ₹ 24 = ₹ 9,600

P&L [B/f] ⇒ ₹ 12,000 − ₹ 9,600 = ₹ 2,400

(iii) Fixed Overhead Recovery Rate per unit = $\frac{₹\ 12,000}{600 \text{ units}}$ = ₹ 20 per unit

∴ Allocation of Total fixed Overheads of ₹ 12,000 are as follows:

Cost of Production ⇒ 600 units × ₹ 20 = ₹ 12,000

P&L [B/f] ⇒ ₹ 12,000 − ₹ 12,000 = Nil

(iv) Profit Earned on Sale of Inventory during the period [Gross Profit]
⇒ Sales Value − Total COGS

(2) <u>If Inventory is Acquired on Deferred Settlement Terms [i.e. Payment beyond Normal Credit Terms]</u> :-

Extra Amount paid over the Normal Purchase Price [Cash Price] is recognised as Interest Expense [Finance Cost] over the credit period in P&L and not included in Inventory Cost.

<u>Note</u>:

If Normal Purchase Price is not given in question, then it is calculated by discounting the future payments [i.e. P.V. of Cash Outflow]

(3) <u>If More than 1 Product are produced jointly [Allocation of Costs to Joint Products]</u>:-

Calculate Joint Cost of Production & then Allocate such Joint Cost between each Joint Product in ratio of Sales Value of Total Units Produced
[i.e. Total Units Produced × Sales Price per unit]

<u>Note</u>: Calculation of Joint Cost:

Total Common Cost of Production	xxx
(−) NRV of By-Product	(xxx)
(−) Amount Realised from Sale of Scrap	(xxx)
Joint Cost	xxx

Cost Measurement Techniques or Formula

- Interchangeable Inventories
  - Historical Cost Methods
  - Non Historical Cost Methods
- Inventories not Interchangeable
  - Specific Identification Method

FIFO [First In First Out]	Weighted Average Cost	Retail Method OR Adjusted Selling Price Method	Standard Cost Method	[generally used in Jewellery & Tailor-made Industries]
Units Purchased/ Produced first are sold first	$\dfrac{\text{Cost of Opening Stock} + \text{Cost of Purchases/ Production during the period}}{\text{Units in Opening Stock} + \text{Units Purchased/ Produced during the period}}$	Retail Price of Closing Stock − Gross Margin % **OR** Retail Price of Closing Stock × Cost % of Retail Price	Fix Standard Cost per unit is used	Cost is specifically calculated

Note:- Entity shall use Same Cost formula for All Inventories having same nature & use.

Net Realisable Value [NRV]

Estimated Selling Price	xxx
(-) Estimated Completion Costs [Example : Processing & Packing Charges]	(xxx)
(-) Estimated Selling Costs / Expenses [Example : Sales Commission]	(xxx)
NRV	xxx

Note:- NRV is calculated on the basis of expected date for sale of such inventory.

Meaning of Statement of Cash Flows

- It is a Statement which provides details about how the cash is generated & applied by the Entity during the period.
- Cash Flows are classified into 3 Categories as follows:-

Cash Flows from Operating Activities	Cash Flows from Investing Activities	Cash Flows from Financing Activities
⇓	⇓	⇓
These are the cash flows from Principal Revenue generating activities [i.e. Activities which are not Investing or financing Activities]	These are the Cash flows from purchase & sale of Long Term Assets like PPE, Intangible Assets, Investment, etc.	These are the cash flows from Issue & Redemption of Equity & Borrowings

Preparation of Statement of Cash Flows

Statement of Cash Flows can be prepared by following 2 Methods :-

(1) Direct Method:

Statement of Cash Flows for the year ended ....

Particulars	Amount
(A) Cash Flows from Operating Activities	
Cash Received from Debtors	xxx
Cash Paid to Creditors	(xxx)
Cash Paid for Operating Expenses [Eg: Wages / Salary / Payroll, Administration & Selling Expenses, Overheads, Insurance, etc.]	(xxx)
	xxx
Income Tax Paid in Cash relating to Operating Activities [Eg: Tax on Business Profit]	(xxx)
	xxx
Exceptional Items [Eg: Fire Insurance Claim Received]	xxx / (xxx)
Net Cash flows from Operating Activities [A]	xxx
(B) Cash Flows from Investing Activities	
Cash Received from Sale of PPE / Intangible Assets / Investment Property etc.	xxx
Cash Paid for Purchase of PPE / Intangible Assets / Investment Property etc.	(xxx)
Cash Received from Sale of Investment	xxx
Cash Paid for Purchase of Investment	(xxx)
Interest Received in Cash	xxx
Dividend Received in Cash	xxx
	xxx

Income Tax Paid in Cash relating to Investing Activities [Eg: Capital Gain Tax]	(xxx)
Net Cash flows from Investing Activities [B]	xxx
(C) <u>Cash flows from Financing Activities</u>	
Cash Received from Issue of Share Capital / Debentures / Loan	xxx
Cash Paid for Redemption of Share Capital / Debentures / Loan	(xxx)
Interest Paid in Cash	(xxx)
Dividend Paid in Cash	(xxx)
	xxx
Income Tax Paid in Cash relating to Financing Activities [Eg: DDT]	(xxx)
Net Cash flows from Financing Activities [C]	xxx
Net Cash flows from All the Activities [A + B + C]	xxx
(+) Opening Balance of Cash & Cash Equivalents	xxx
Closing Balance of Cash & Cash Equivalents	xxx

(2) <u>Indirect Method</u>: ☑

Statement of Cash flows for the year ended ....

Particulars	Amount
(A) <u>Cash flows from Operating Activities</u>	
Profit After Tax as per P&L	xxx
(+) Tax Amount charged to P&L	(xxx)
Profit Before Tax as per P&L	xxx
(+) Non Cash Expenses [Eg: Depreciation & Amortisation, Impairment Loss, etc.]	xxx
(±) Non Operating Items [i.e. Items of Investing or financing Activities]:	
Loss on Sale of PPE / Intangible Asset / Investment Property etc.	xxx
Interest Expense	xxx
Profit on Sale of PPE / Intangible Asset / Investment Property etc.	(xxx)
Interest Income	(xxx)
(±) Exchange Loss / (Gain) on Items of Investing or financing Activities	xxx / (xxx)
(±) Exchange Loss / (Gain) on Bank Balance held in foreign Currency	xxx / (xxx)
	xxx
(–) Increase in Operating Assets [Eg: Inventory, Trade Receivables, Prepaid Insurance, DTA, etc.]	(xxx)
(+) Decrease in Operating Assets	xxx
(+) Increase in Operating Liabilities [Eg: Trade Payables, Expense Payables, DTL, etc.]	xxx
(–) Decrease in Operating Liabilities	(xxx)
	xxx
Income Tax Paid in Cash relating to Operating Activities [Eg: Tax on Business Profit]	(xxx)
	xxx

Exceptional Items [Eg: fire Insurance Claim Received]	xxx / (xxx)
Net Cash flows from Operating Activities [A]	xxx
(B) <u>Cash Flows from Investing Activities</u>	
Cash Received from Sale of PPE | Intangible Assets | Investment Property etc.	xxx
Cash Paid for Purchase of PPE | Intangible Assets | Investment Property etc.	(xxx)
Cash Received from Sale of Investment	xxx
Cash Paid for Purchase of Investment	(xxx)
Interest Received in Cash	xxx
Dividend Received in Cash	xxx
	xxx
Income Tax Paid in Cash relating to Investing Activities [Eg: Capital Gain Tax]	(xxx)
Net Cash flows from Investing Activities [B]	xxx
(C) <u>Cash Flows from Financing Activities</u>	
Cash Received from Issue of Share Capital / Debentures | Loan	xxx
Cash Paid for Redemption of Share Capital / Debentures | Loan	(xxx)
Interest Paid in Cash	(xxx)
Dividend Paid in Cash	(xxx)
	xxx
Income Tax Paid in Cash relating to Financing Activities [Eg: DDT]	(xxx)
Net Cash flows from Financing Activities [C]	xxx
Net Cash flows from All the Activities [A + B + C]	xxx
(+) Opening Balance of Cash & Cash Equivalents	xxx
Closing Balance of Cash & Cash Equivalents	xxx

<u>Note</u>:-

(i) Amount of All Items in Statement of Cash flows are directly given in question ; Otherwise it can be calculated by preparing respective Ledger Accounts.

<u>Examples</u>:

Debtors A/c [For Calculation of Cash Received from Debtors]			
To Balance b/d [Opening Balance]	xx	By Bank [Balancing figure]	xx
To Sales	xx	By Balance c/d [Closing Balance]	xx
	xx		xx

Creditors A/c [For Calculation of Cash Paid to Creditors]			
To Bank [Balancing figure]	xx	By Balance b/d [Opening Balance]	xx
To Balance c/d [Closing Balance]	xx	By Purchases*	xx
	xx		xx

* Purchases = COGS (Cost of Sales) − Opening Stock + Closing Stock

(ii) Non Cash Transactions are excluded from Statement of Cash flows.
Example: A Car is purchased in exchange of other PPE

(iii) Cash flows should not be presented on Net basis. These should be presented on Gross basis only [i.e. Cash Receipts & Payments will be shown separately].

(iv) Cash & Cash Equivalents ⇒
Cash Balance + Bank Balance + Investment with Maturity of 3 Months or Less from Acquisition Date − Bank Overdraft

(v) Preparation of Consolidated Statement of Cash flows using Consolidated Balance Sheet & Consolidated Statement of Profit or Loss :

Apply same concept for Preparation of Statement of Cash flows as discussed above with following extra adjustments :

→ In Cash flows from Operating Activities [Indirect Method]
⇓
(+) Share in Loss of Associate Company OR (−) Share in Profit of Associate Company

→ In Cash flows from Investing Activities
⇓
(−) Cash Paid to acquire Subsidiary Company [Cash Consideration Paid − Cash Balance of Subsidiary Company]

(−) Cash Paid for Investment in Associate Company

→ If Subsidiary Company is acquired during the year, then Add Assets & Liabilities acquired from Subsidiary Company to Opening Balance of Assets & Liabilities in Consolidated Balance Sheet for calculation of Cash flows.

(vi) Foreign Currency Cash flows :

→ Cash flows in Foreign Currency are converted in Functional Currency using Exchange Rate at the date of Transaction.

→ Exchange Gain / (Loss) arising on Bank Balance held in foreign Currency should be added / (deducted) from Opening Balance of Cash & Cash Equivalents to reconcile the Closing Balance of Cash & Cash Equivalents in Statement of Cash Flows with Balance Sheet.

(vii) If Entity is Financial Institution (Bank), then following Cash flows will be part of Operating Activities:

- Loan given to Customer
- Loan Repaid by Customer
- Deposits Accepted or Repaid
- Interest or Dividend Received
- Interest Paid

* Dividend paid will be part of financing Activities for financial Institution also.

Accounting Policies

Meaning of Accounting Policies

These are Specific Principles, Bases, Conventions, Rules & Practices applied in Preparation of Financial Statements.

Examples :

(i) Methods for determination of Cost of Inventories ⇒ FIFO, Weighted Average, etc.

(ii) Measurement Basis for PPE & Intangible Assets ⇒ Cost Model or Revaluation Model

Selection & Application of Accounting Policies

- If Specific Ind AS is available for a particular transaction, then Entity shall apply Accounting Policy as determined by that Ind AS.

  ⇓

  Otherwise Entity shall refer following sources in descending order :-

  (i) Any Other Ind AS on similar transaction.

  (ii) Framework of Ind AS

  (iii) Pronouncement of International Accounting Standards Board [IASB]

  (iv) Pronouncement of Other Standard Setting Bodies [Example: US GAAP, etc.]

  (v) Accepted Industry Practices

- Entity shall Select & Apply its Accounting Policy consistently for similar transactions. [Consistency of Accounting Policies]

Changes in Accounting Policies

- Entity shall change an Accounting Policy only if :

  → Required by Ind AS, or

  → Results in providing more relevant & reliable information [i.e. Voluntary Change of Accounting Policy]

- Followings are not considered as Change in Accounting Policy :-

  (i) Application of Accounting Policy for transactions that differ in substance from Previous.

  Example: Reclassification of PPE (Revaluation Model) to Investment Property (Cost Model).

  (ii) Application of New Accounting Policy for transactions that did not occur previously.

  Example : Measuring Newly Purchased PPE at Cost Model.

- Applying Change in Accounting Policy :-

→ Entity shall account for Change in Accounting Policy retrospectively, i.e. Apply such Accounting Policy on the transaction from the very 1st day in Past as follows:

Adjusting the Comparative Amounts of Previous Year

Or

Adjusting the Opening Balances of Previous Year for effects of change in accounting policy relating to all prior periods [if any]

→ If Retrospective Application is Impracticable, i.e. Entity cannot apply Accounting Policy retrospectively after making every reasonable effort to do so; then Entity should apply Accounting Policy prospectively.

- Disclosures in Financial Statements regarding Change in Accounting Policy :-
  - Nature of Change in Accounting Policy
  - Effect (Amount of Adjustment for each affected item in Financial Statements) on Current Year & Previous Year due to Change in Accounting Policy
  - If Retrospective Application is Impracticable, Disclose Reasons of it

Accounting Estimates

Meaning of Accounting Estimates

Many Items in Financial Statements cannot be measured but only can be estimated. Estimation involves judgement on the basis of latest available information.

Examples: Provision for Bad Debts, Warranty Obligations, Depreciation Method, Useful Life, Residual Value, etc.

Changes in Accounting Estimates

- Entity shall revise an Accounting Estimate if circumstances change as a result of new information or more experience.
- Entity shall account for Change in Accounting Estimate prospectively, i.e. Apply change from the date of Change in Estimate.
- Disclosures in Financial Statements regarding Change in Accounting Estimate :-
  - Nature of Change in Accounting Estimate
  - Effect (Amount of Adjustment for each affected item in Financial Statements) on Current Year & Future Years due to Change in Accounting Estimate
  - If it is not possible to estimate effect on future years, then this fact must be disclosed

Other Points

- Change in Accounting Estimate cannot be treated as a Correction of Prior Period Error.
- If it is difficult to distinguish between a change in accounting policy & change in accounting estimate, then treat it as change in accounting estimate.

Errors

Meaning of Prior Period Errors

These are omissions & misstatements in financial statements of Previous Years.

Examples:

Error of Commission, Error of Omission, Error of Principle, Fraud, Classification Error, etc.

Treatment of Prior Period Errors

- Entity shall correct the Prior Period Errors Retrospectively, i.e. Correct such Errors from the very 1st day in Past as follows:

Restating the Comparative Amounts of Previous Year

&

Restating the Opening Balances of Previous Year for correction relating to All Prior Periods [if Any]

- If Retrospective Restatement is Impracticable, i.e. Entity cannot restate prior period errors retrospectively after making every reasonable effort to do so; then Entity should restate prior period errors prospectively.

Disclosures in Financial Statements for Prior Period Errors

- Nature of Prior Period Error
- Effect (Amount of Adjustment for each affected item in financial Statements) on Previous Years due to Prior Period Error
- If Retrospective Restatement is Impracticable, Disclose Reasons of it

Meaning of Events after the Reporting Period

These are Favourable & Unfavourable Events occurring after the end of Reporting Period [i.e. Balance Sheet Date] but before approval of Financial Statements by Board of Directors [BOD]

Example:

End of Reporting Period [Balance Sheet Date]	Date of Approval of FS by BOD	FS made available to Shareholders	Date of AGM
31st March	20th June	1st July	10th September

Events after the Reporting Period as per Ind AS 10 (31st March to 20th June)

Types of Events after the Reporting Period & their Accounting Treatment

Events after the Reporting Period are classified into 2 Categories as follows :-

Adjusting Events

Events which provide evidence of conditions existing on Balance Sheet Date

Examples:

(i) Debtor suffering heavy losses before Balance Sheet Date has become bankrupt after Balance Sheet Date

(ii) Discount provided after Balance Sheet Date on goods sold before Balance Sheet Date

(iii) Determination of Cost after Balance Sheet Date for Assets Purchased before Balance Sheet Date

(iv) Settlement after Balance Sheet Date of a Court Case started before Balance Sheet Date

(v) Excise Demand Notice received after Balance Sheet Date for goods manufactured before Balance Sheet Date

⇓

Adjust the respective amount in Financial Statements

Non Adjusting Events

Events which are indicative of conditions arising after Balance Sheet Date

Example:

(i) Loss by fire after Balance Sheet Date

(ii) Change in Fair Value of Investments after Balance Sheet Date

(iii) Negotiation to acquire land started before Balance Sheet Date but transaction completed after Balance Sheet Date

⇓

Do not adjust the amount in Financial Statements.

But if Non Adjusting Event is Material, then Disclose in Financial Statements:

→ Nature of the Event &

→ Estimate of its Financial Effect

OR

Statement that such Estimate cannot be made.

Special Cases

(1) If NRV of Inventory changes after Balance Sheet Date but before approval of Financial Statements due to

- Change in Selling Price
  ⇓
  Adjusting Event
- Damage in Inventory occurred after Balance Sheet Date by Fire, Water Leakage etc.
  ⇓
  Non Adjusting Event

(2) Dividends :-

- If Entity declares dividend after Balance Sheet Date But before approval of Financial Statements, then such dividend is not recognised as a Liability at Balance Sheet Date because no obligation exists at that time. [Non Adjusting Event]
- Such Dividends are disclosed in the Notes in Financial Statements.

(3) Going Concern :-

If Entity intends to liquidate the business [i.e. Not Continuing Operations] after Balance Sheet Date But before approval of financial Statements, then the Entity should not prepare its Financial Statements on a Going Concern Basis. [Adjusting Event]

Example:

Major Fire incurred after Balance Sheet Date but before approval of financial Statements, damaging the operations of business on a large scale due to which continuity of business is in doubt.

⇓

Hence, Entity should not prepare its Financial Statements on a Going Concern Basis

Tax Expense

- It means Tax Expense recognised in Books as per Ind AS
  ⇒ Current Tax Expense ± Deferred Tax Expense
- Current Tax Expense :- It is the Amount of Tax Payable on Profit calculated as per Income Tax Act
- Deferred Tax Expense :- It is Temporary Saving in Tax or Payment of Additional Tax due to Temporary Differences between Carrying Amount and Tax Base of Assets & Liabilities

Example :-

A Ltd. purchased a PPE costing ₹ 5,000. Depreciation is charged @ 20%. p.a. on SLM Basis in Books. Depreciation is charged @ 25% p.a. on SLM Basis in Income Tax.
Profit Before Depreciation & Tax p.a. for Years 1 to 5 = ₹ 10,000 [As per Books & Income Tax]
Tax Rate is 30%

Solution :-

Depreciation p.a. as per Books = 5000 x 20% = ₹ 1,000
Depreciation p.a. as per Income Tax = 5000 x 25% = ₹ 1,250

Calculation of Tax Payment as per Books :-

	Year 1	Year 2	Year 3	Year 4	Year 5
PBDT	10,000	10,000	10,000	10,000	10,000
(-) Depreciation	1,000	1,000	1,000	1,000	1,000
	9,000	9,000	9,000	9,000	9,000
Tax @ 30%	2,700	2,700	2,700	2,700	2,700

⇓ 13,500

Calculation of Tax Payment as per Income Tax Act :-

	Year 1	Year 2	Year 3	Year 4	Year 5
PBDT	10,000	10,000	10,000	10,000	10,000
(-) Depreciation	1,250	1,250	1,250	1,250	–
	8,750	8,750	8,750	8,750	10,000
Tax @ 30%	2,625	2,625	2,625	2,625	3,000

⇓ 13,500

Here, In Year 1 to 4, Actual Tax to be paid is ₹ 2,625 p.a. [Current Tax Expense] But As per Books, it should be ₹ 2,700 p.a.
Hence, ₹ 75 [2,700 – 2,625] should be recognised in Each Year as Future Tax Liability [Deferred Tax] to meet the Matching Concept & At End of Year 5, Total Deferred Tax of ₹ 300 [75 x 4] will be Reversed.

Current Tax

Journal Entries :-

(1.) To Recognise Current Tax Expense

Current Tax Expense [P&L | OCI]

To Provision for Tax [Current Tax Liability]

Note :- Current Tax Expense is recognised in P&L or OCI accordingly to the Item on which it is created

(2.) To Recognise Advance Tax Paid

Advance Tax [Current Tax Asset]

To Bank

Deferred Tax

(1.) As per Ind AS, Balance Sheet Approach is used to Calculate Deferred Tax as follows :-

- It is calculated on Temporary Differences between Carrying Amount and Tax Base of Assets & Liabilities
- Carrying Amount means Balance of Relevant Asset or Liability in Books as per Ind AS
- Tax Base means Amount of Relevant Asset or Liability that would appear in Income Tax Balance Sheet (if Prepared as per Income Tax Act)
- Temporary Difference :- Difference between Carrying Amount & Tax Base

Taxable Temporary Difference

⇓

If it leads to Additional Payment of Tax in future

⇓

Deferred Tax Liability (DTL) is created on Taxable Temporary Difference (TTD)

- If Carrying Amount of Asset > Tax Base of Asset
- If Carrying Amount of Liability < Tax Base of Liability

Deductible Temporary Difference

⇓

If it leads to Saving of Tax in future

⇓

Deferred Tax Asset (DTA) is created on Deductible Temporary Difference (DTD)

- If Carrying Amount of Asset < Tax Base of Asset
- If Carrying Amount of Liability > Tax Base of Liability

- Some Important Examples :-

(i) A Ltd. purchased a PPE costing ₹ 5,000. Depreciation is charged @ 20%. p.a. on SLM Basis in Books. Depreciation is charged @ 25% p.a. on SLM Basis in Income Tax. Tax Rate is 30%

Year 1 : PPE [Asset]

Carrying Amount ⇒ 5000 − 1000 = 4,000

Tax Base ⇒ 5,000 − 1,250 = 3,750

Taxable Temporary Difference ₹ 250 → DTL will be created on this @ 30% Tax Rate

∴ DTL = 250 × 30% = ₹ 75

(ii) A Ltd. has Interest Income Receivable of ₹ 1,000. In Income Tax, Interest Income is taxable on Cash Basis. Tax Rate is 30%

Year 1 : Interest Income Receivable [Asset]

Carrying Amount ⇒ 1,000

Tax Base ⇒ 0 [Since Interest Income will be recognised in Income Tax on Date of Actual Receipt Only]

TTD 1,000

∴ DTL = 1,000 × 30% = ₹ 300

(iii) A Ltd. has made Investment in Equity Shares for ₹ 1,000. It is shown At FVTPL. At Year End, Fair Value of Investment in Equity Shares is ₹ 800

Year 1 : Investment in Equity Shares [Asset]

Carrying Amount ⇒ 800

Tax Base ⇒ 1,000 [Since Fair Value Gain / Loss is Not Recorded in Income Tax]

DTD 200 → DTA will be created on this @ 30% Tax Rate

∴ DTA = 200 × 30% = ₹ 60

(iv) A ltd. has made a Provision for Division Closure Cost of ₹ 1,000. In Income Tax, Closure Cost is allowed only when it is Actually Paid. Tax Rate is 30%

Year 1 : Provision for Closure Cost [Liability]

Carrying Amount ⇒ 1,000

Tax Base ⇒ 0 [Since Closure Cost is Allowed Only on Actual Payment Date in Income Tax]

DTD 1,000

∴ DTA = 1,000 × 30% = ₹ 300

(v) A Ltd. has received an Income of ₹ 500 in Advance. In Income Tax, Income Received is taxable on Cash Basis. Tax Rate is 30%

Year 1 : Income Received in Advance [Liability]

Carrying Amount ⇒ 500

Tax Base ⇒ 0 [Since Income Received in Advance is Taxed on Receipt Date itself]

DTD 500

∴ DTA = 500 × 30% = ₹ 150

(vi) A Ltd. has taken a Loan of ₹ 1,000. Transaction Cost is ₹ 200. In Income Tax, Transaction Cost is allowed for Deduction on Payment Date itself. Tax Rate is 30%

Year 1: Loan Taken [Liability]

Carrying Amount ⇒ 1,000 − 200 = 800

Tax Base ⇒ 1000 [Since Transaction Cost etc. Adjustment are Not done in Loan A/c in Income Tax. It is allowed as Deduction on Payment Date itself]

TTD 200

∴ DTL = 200 × 30% = ₹ 60

(2) Calculation of DTA | DTL :-

- Closing Balance of DTA | DTL that would appear in Balance Sheet
  ⇒ Temporary Difference × Tax Rate
- Amount of DTA | DTL to be recorded in P&L / OCI in Current Year
  ⇒ Closing Balance of DTA / DTL as Calculated above − Opening Balance of DTA | DTL

Note :-

(i.) Deferred Tax Expense is recognised in P&L or OCI accordingly to the Item on which it is created.

(ii.) DTA | DTL recognised in a Year are Reversed in future.

(iii.) Tax Rate to be Used for Calculation of DTA / DTL
⇒ Future Tax Rate Specific to the Transaction, i.e. Substantively Enacted Tax Rate [Tax Rate Announced by Government Before Balance Sheet Date for upcoming Year]

(3) Journal Entries for DTA | DTL :-

→ To Recognise DTA
Deferred Tax Asset (DTA)
To Deferred Tax Expense [P&L / OCI]

→ To Reverse DTA
Deferred Tax Expense [P&L / OCI]
To Deferred Tax Asset (DTA)

→ To Recognise DTL
Deferred Tax Expense [P&L / OCI]
To Deferred Tax Liability (DTL)

→ To Reverse DTL
Deferred Tax Liability (DTL)
To Deferred Tax Expense [P&L / OCI]

(4) Steps to Solve the Practical Questions :-

Step 1 : Calculate Carrying Amount of Asset or Liability as per Books

Step 2 : Calculate Tax Base of Asset or Liability as per Income Tax Act

Step 3 : Calculate Temporary Difference (i.e. TTD or DTD)

Step 4 : Calculate DTA | DTL on Temporary Difference
→ Closing Balance of DTA | DTL and
→ Amount of DTA / DTL to be recorded in P&L / OCI

Step 5 : Pass Journal Entries (if Required in Question)

Deferred Tax in Some Special Cases

(1.) Investment in Subsidiary, Associate or Joint Venture [Asset] :-

Carrying Amount = Investment Amount [Cost] ± Share in Profit / Loss of Subsidiary / Associate / Joint Venture

Tax Base = Investment Amount [Cost]

Note :- In Case of Investment in Subsidiary, No DTA / DTL is recognised on Temporary Difference as Parent Entity will be able to Control the Timing of its Reversal

(2.) Asset taken on Lease [RoU Asset & Lease Liability] :-

Carrying Amount = Net of RoU Asset & Lease Liability Balance in Books, i.e.

Closing Balance of RoU Asset on Balance Sheet Date − Closing Balance of Lease Liability on Balance Sheet Date

Tax Base = Nil [Since Lease Rent is Allowed for Deduction on Payment Basis in Income Tax]

(3.) Share Based Payment Transaction :-

Carrying Amount = Nil

Tax Base = Employee Benefit Expense to be recognised till date based on Intrinsic Value of Option

Note :- SBP Transaction is considered as an Asset. Hence, Always DTA will be recognised on SBP Transaction.

(4.) Asset / Liability relating to Any Expense Not Deductible / Not Allowed in Income Tax or Any Income Not Taxable in Income Tax [Eg. Charitable Donations to Unregistered Trusts, Penalties, Income Tax Demand, etc.] :-

No DTA / DTL is Recognised [Assume Tax Base equals to Carrying Amount]

(5.) Carryforward Losses as per Income Tax Act is Deductible Temporary Difference [DTD] on which DTA is created.

(6.) MAT Credit as per Income Tax Act is recognised as a Deferred Tax Asset [DTA]

(7.) Assets & Liabilities Acquired in Business Combination :-

For Net Assets Taken Over in Business Combination

If Fair Value [Treated as Carrying Amount as per Books]	If Fair Value [Treated as Carrying Amount as per Books]
>	<
Tax Base	Tax Base
⇓	⇓

DTL is Created | DTA is Created

Note :-

(i) DTA | DTL will be recognised through Goodwill / Capital Reserve on Assets & Liabilities taken over in Business Combination

(ii) DTA | DTL will not be created on Goodwill arised in Business Combination Since it will make a Circular Reference

(iii) In this Case, Tax Rate for Calculating DTA | DTL will be Rate Applicable to Acquiree Entity

(iv) If Tax Base is Not Specifically given in Question, Existing Carrying Amount of Assets & Liabilities in Books of Acquiree will be considered as Tax Base

Other Points

(1) Conditions for Recognising DTA :-

- Entity should recognise DTA only if it is probable that there would be sufficient Taxable Profits in future

- If Entity Anticipates Losses in future (i.e. No Profits in Future), then DTA is recognised on following Amount :

1st Priority

⇓

LOWER OF

Deductible Temporary Difference (DTD) Amount

OR

Profits that can be generated by Implementing Tax Planning Strategy

—

Cost of Implementing such Strategy

2nd Priority

⇓

LOWER OF

Reversal Amount of DTD in Future Years

OR

Reversal Amount of Any TTD in Future Years

(2) Tax Reconciliation Disclosures in Financial Statements :-

(i) Tax Reconciliation in Absolute Numbers [i.e. Reconciliation between Tax Expense & Tax on PBT as per Books] :

Particulars	₹
PBT as per Books	xxx
Tax @ Applicable Tax Rate [PBT as per Books x Tax Rate]	xxx
(+) Tax on Items Not Deductible / Not Allowed in Income Tax [i.e. Items on which DTA | DTL is Not Created]	xxx
Tax Expense [Current Tax Expense & Deferred Tax Expense]	xxx

(ii) Tax Rate Reconciliation [i.e. Reconciliation between Average Effective Tax Rate & Applicable Tax Rate] :

Particulars	%
Applicable Tax Rate	✓
(+) [Tax on Items Not Deductible / Not Allowed in Income Tax ÷ PBT as per Books] x 100	✓
Average Effective Tax Rate [Tax Expense ÷ PBT As per Books]	✓

(3) <u>Offsetting of Current Tax Asset & Current Tax Liability</u> :-

OR

<u>Offsetting of Deferred Tax Asset & Deferred Tax Liability</u> :-

⇓

Only if Entity has Legal Enforceable Right to Set off the Respective Tax Asset & Liability (i.e. Both Tax Asset & Tax Liability are Levied by Same Tax Authority)

Meaning of PPE

PPE are Tangible Items

- Held for
  - Use in Production or Supply of Goods or Services
  - OR Rental to Others [Other than Land & Building]
  - OR Administrative Purposes
- and Expected to be Used for More than 1 Period

Note :-

(i) Treatment of Land & Building [i.e. Property] :-

- Property Held for
  - Use in Production or Supply of Goods or Services
  - OR Administrative Purposes

  ⇓ Treat it as Owner Occupied Property (PPE)

  ⇓ Apply Ind AS 16

- Property Held for
  - Rental to Others [operating Lease]
  - OR Capital Appreciation
  - OR Undetermined Use

  ⇓ Treat it as Investment Property

  ⇓ Apply Ind AS 40

Examples :-

(i) Business is of giving Building on Rent ⇒ Building is PPE

(ii) Business is of selling Mobile Phone & We are giving L&B on Rent ⇒ L&B is IP

(iii) Any Asset Other than L&B given on Rent ⇒ PPE

(iv) Factory Building, Office Building, Company Quarters (Building for Staff Accomodation) ⇒ PPE

(v) L&B held for Sale in Ordinary Course of Business ⇒ Inventory (ii.) Treatment of Spare Parts (Eg. Bearings, Screws etc.) and Stand-by Equipments (Eg. Fire Extinguishers) :-

- If it meets definition of PPE → Apply Ind AS 16
- Otherwise → Treat it As Inventory [Apply Ind AS 2]

Recognition Criteria

PPE is recognised in Books Only if

Probable FEB **and** Cost can be measured reliably

Initial Recognition of PPE

(1.) If PPE is Purchased or Self Constructed :-

- PPE is recognised at Cost
- Cost includes Any directly attributable cost necessary to bring PPE to location & condition intended by Management
- Calculation of Cost of PPE :-

Purchase Price	xxx
(-) Trade Discount / Rebate	(xxx)
(+) Import Duty & Purchase Taxes like Entry Tax, GST etc. [Only if Non-Refundable]	xxx
(+) Property Transfer Tax (Only if Non-Refundable)	xxx
(+) Stamp Duty Cost	xxx
(+) Legal Fee / Cost	xxx
(+) One Time Joining fee of Building Association [In Case of Property Only]	xxx
(+) Initial Delivery / Transport Cost	xxx
(+) Other Handling Cost	xxx
(+) Installation & Assembling Cost	xxx
(+) Professional fee / Consultant fee / Advisor fee / Architect fee	xxx
(+) Site Preparation Cost [Eg. Cost of Preparation & Levelling of Land]	xxx
(+) Building Plan Approval / Permission Cost	xxx
(+) Direct Material, Labour or Overhead Cost on Construction	xxx

(+) Employment Cost of Construction Workers	xxx
(+) Testing Cost	xxx
(+) P.V. of Estimated dismantling, decommissioning, restoration or demolition Cost	xxx
(+) Any Other direct attributable Cost	xxx
	xxx

Note :-

(i.) In Silent Situation, Assume All taxes are Non-Refundable

(ii.) Following Items are not included in Cost of PPE :-

→ Cost of Staff Training
→ Cost of Relocation of Staff / Employees
→ Cost of Opening or Inaugration Ceremony
→ Advertisement Cost
→ Purchase of Maintenance Contract of PPE
→ Day to Day Repair & Maintenance Cost
→ Administrative, General, Selling & Allocated Overheads
→ Cost of Abnormal Amount of Wasted Material, Labour or Other Resources [Eg. Due to Faulty design, Spoiled Material, Industrial Strike, etc.]
→ Operating Losses
→ Cash Discount / Early Settlement Discount
→ Interest Cost on Loan taken to buy or Construct the PPE (unless allowed by Ind AS 23)

(iii.) Income from Incidental Activities done by Entity during Construction of PPE but are not necessary for its construction

⇓

Such Income will be recognised in P&L and not included in PPE Cost

Eg:- Income from Car Parking on Factory Premises during Construction

• Accounting of PPE (Journal Entry) :-

(i.) At beginning

For PPE Purchase / Construction

	Dr	Cr
PPE	xxx	
To Bank / Payables		xxx
To Provision for Decommissioning Liability (if any)		At Present Value

(ii.) At Each Year End

For Unwinding of Discount on Provision for Decommissioning Liability

Interest Expense / Finance Cost [Op. Bal. of Prov. for D.L. × Discounting Rate]	xxx	
To Provision for Decommissioning Liability		xxx

For Transferring Interest Expense to P&L

P&L	xxx	
To Interest Expense / Finance Cost		xxx

For Depreciation on PPE

Depreciation	xxx	
To PPE		xxx

$\boxed{\text{OR}}$

Depreciation	xxx	
To Provision for Depreciation / Accumulated Depreciation		xxx

For Transferring Depreciation to P&L

P&L	xxx	
To Depreciation		xxx

Example:-

A Ltd. purchased a Machine of ₹ 50,000, Useful Life = 3 yrs., Dep. = SLM Basis, Decommissioning Cost will be ₹ 10,000 after 3 yrs., Discounting Rate = 10%. Pass necessary J.E. of 1st Year.

Solution:-

1st Year Begining	PPE (50,000 + 7,510)	57,510	
	To Bank		50,000
	To Prov. for D.L. (10,000 × 0.751)		7,510
1st Year End	Int. Exp. (7,510 × 10%)	751	
	To Prov for D.L.		751

Dep. (57,510 ÷ 3)	19,170	
To PPE		19,170
P&L	19,921	
To Int Exp		751
To Dep.		19,170

Working Note:- Table showing Interest Exp. on Provision for D.L.

Year	Opening Balance	Interest @ Discounting Rate	Actual Payment	Closing Balance
(A)	(B)	(C)	(D)	(E) = (B)+(C)-(D)
1	7,510	751	–	8,261
2	8,261	826	–	9,087
3	9087	913	–	10,000

(2.) If PPE is Acquired on Deferred Settlement Terms [i.e. Payment Beyond Normal Credit Terms]

⇓

Extra Amount paid over the Normal Purchase Price (Cash Price) is recognised as Interest Expense (Finance Cost) over the credit period in P&L and not included in PPE Cost

Note:- If Normal Purchase Price is not given in question, then It is calculated by discounting the future payments [i.e. PV of Cash Outflow]

Example:-

A Ltd. purchased a Machine for which Payment will be made in 3 Equal Annual Installments of ₹ 5000 starting from 1st Year End. Disc. Rate is 10%. Pass J.E. for the 1st Year

Solution:-

Calculate Normal Purchase Price (Cash Price):-

Year	Payment	PVF @ Disc. Rate	P.V.
1	5,000	0.909	4,545
2	5,000	0.826	4,130
3	5,000	0.751	3,755
			12,430

Calculation of Interest Expense:-

Year	Op. Bal.	Interest @ Disc. Rate	Actual Payment	Cl. Bal.
1	12,430	1,243	5,000	8,673
2	8,673	867	5,000	4,540
3	4,540	460	5,000	–

Journal Entry :-

		Dr.	Cr.
1st Year Beginning	PPE	12,430	
	To Payables		12,430
1st Year End	Interest Expense [P&L]	1,243	
	To Payables		1,243
	Payables	5,000	
	To Bank		5,000
	$\boxed{\text{OR}}$		
	Int. Exp.	1243	
	Payables	3757	
	To Bank		5000

(3.) If PPE is Acquired in Exchange of Assets :-

If Exchange Transaction has Commercial Substance $\boxed{\checkmark}$

⇓

Recognise PPE Acquired at following in Priority :-

→ Fair Value of Asset Given Up

→ Fair Value of Asset Received

→ Carrying Amount of Asset Given Up

If Exchange Transaction Lacks Commercial Substance

⇓

Recognise PPE Acquired At Carrying Amount of Asset Given Up

Note :-

(i.) If Some Cash is also paid alongwith the Asset to Acquire the PPE, then Add Amount of Cash Paid in the above amount

(ii.) If Some Cash is also received alongwith the PPE in Exchange, then Deduct Amount of Cash Received from the above amount

(iii.) Commercial Substance means which Affects Cash flows of the Entity.

Eg. of Commercial Substance :- If We Acquire PPE producing 10000 units by giving PPE producing 8000 units

Eg. of Lack of Commercial Substance :- If We exchange our warehouse with Other Entity's Warehouse in Same Area

(iv.) Accounting of PPE Acquired in Exchange of Assets (Journal Entry)

PPE [Acquired]	At Above Amount	
Cash [Received if Any]	xxx	
Loss on Exchange of Asset [B/f]	xxx	
To Cash [Paid if Any]		xxx
To Asset [Given]		Carrying Amt.
To Profit on Exchange of Asset [B/f]		xxx

(v.) Calculation of Profit / Loss on Exchange of Asset :-

Value at which PPE Acquired is Recognised	xxx
Add / (Less) : Cash Received / (Paid)	xxx / (xxx)
Less : Carrying Amount of Asset Given Up	(xxx)
	xxx

Depreciation of PPE

(i.) Methods for Charging Depreciation

- Straight Line Method (SLM) ✓
  - $\text{Depreciation} = \dfrac{\text{Cost} - \text{Residual Value}}{\text{Useful Life}}$
- Diminishing / Reducing Balance Method (WDV)
  - Depreciation = Opening Carrying Amount × Depreciation Rate
- Units of Production Method
  - Depreciation is charged in Ratio of Estimated Production Units

Note :-

(i.) Depreciation on PPE begins when it is Available for Use [i.e. Ready to Use Condition]

(ii.) Depreciation on PPE ceases when PPE is
- Derecognised (i.e. Sold)
- OR
- Classified as Held for Sale [Ind AS 105]

(iii) Depreciation on PPE consisting of Land & Building Both [Eg. Office Building, Factory Building]

- On Land Cost
  ⇓
  No Depreciation will be charged as its Useful Life is Unlimited

- On Building Cost
  ⇓
  Depreciation will be charged as its Useful Life is Limited

(iv.) If there is a Change in Depreciation Method, Useful Life, Residual Value

⇓

It is a Change in Accounting Estimate

⇓

Prospective Effect will be given [i.e. Effect will be given in Remaining future Period]

* Also, In Case of Change in Depreciation Method, Useful Life, Residual Value; We Will use Carrying Amount instead of Cost in SLM Depreciation formula for calculating Depreciation for remaining future period

(2.) **Accounting for Depreciation on PPE (Journal Entry)** :- At each year End

- Depreciation
  To PPE

  OR

  Depreciation
  To Provision for Depreciation / Accumulated Depreciation

- P&L
  To Depreciation

Component Accounting

- Part of a PPE which has significant Cost should be depreciated separately [Eg:- Engine in a Car or Aircraft, Turbine in a Machine, Interior Walls of a Building, Roof of a Building, Major Inspection & Overhauling, etc.]

Note:- If Part having Significant Cost has Same Useful Life as of PPE, then No need to depreciate it separately

Example:- Car Costing ₹ 20 Lakh (incl. Engine of ₹ 5 Lakh), Useful Life of Car is 30 Yrs but of Engine is 5 Yrs.

Solution:-

Depreciation on Car Engine Part $\Rightarrow \frac{5,00,000}{5} = ₹\ 1,00,000$ p.a.

Depreciation on Other Parts of Car $\Rightarrow \frac{15,00,000}{30} = ₹\ 50,000$ p.a.

Carrying Amount of Car at 1st Year End

$\Rightarrow$ Engine + Other Parts

$\Rightarrow [5,00,000 - 1,00,000] + [15,00,000 - 50,000] \Rightarrow ₹\ 18,50,000$

- If Part having Significant Cost is Replaced, then
  - → Cost of New Part is Added to Carrying Amount of PPE, and
  - → Carrying Amount of Old Part is derecognised from Carrying Amount of PPE

i.e. New Carrying Amount of PPE = Carrying Amount of PPE on Part Replacement Date + Cost of New Part − Carrying Amount of Old Part on Part Replacement Date

<u>Note</u>:- If Carrying Amount of Old Part on Replacement Date is not given in Question, then Calculate it in following Steps :-

Step 1 : Take Cost of New Part

Step 2 : PV it to the date of installation of Old Part $\Rightarrow$ It is treated as the Cost of Old Part

Step 3 : Deduct Depreciation on above amount upto Part Replacement Date $\Rightarrow$ It is treated as the Carrying Amount of Old Part on Part Replacement Date

[Assuming Useful Life of such part same as of PPE]

<u>Example</u>:-

Car Purchased at ₹ 10 Lakh, Useful Life is 10 Yrs.
Engine is Replaced in Car after 3 Yrs, Cost of New Engine is ₹ 2 Lakh
Discounting Rate is 10%

<u>Solution</u>:-

Carrying Amount of Car on Replacement Date $\Rightarrow$ 10 Lakh $- \left[\frac{10 \text{ Lakh}}{10} \times 3\right]$

$\Rightarrow$ 7 Lakh ₹

Carrying Amt. of Old Engine on Replacement Date $\Rightarrow$

Cost of Old Engine ⇒ 2 Lakh ₹ × 0.751 ⇒ ₹ 1,50,200

Carrying Amt. of Old Engine ⇒ 1,50,200 − $\left[\frac{1,50,200}{10} \times 3\right]$ ⇒ ₹ 1,05,140

∴ New Carrying Amt. of Car after 3 yrs. [After Engine Replacement] ⇒ 7 Lakh + 2 Lakh − 1,05,140

⇒ ₹ 7,94,860

Subsequent Recognition of PPE (At Each Balance Sheet Date)

- PPE will be shown at either Cost Model or Revaluation Model
- Chosen Accounting Policy (i.e. Cost Model or Revaluation Model) will apply to Entire Class of PPE

  Note:- Class of PPE means Group of Assets having Similar Nature & Use.

  Eg:- Land & Building, Machinery, Furniture, etc.

(1.) Cost Model :-

Carrying Amount = Cost − Accumulated Depreciation − Accumulated Impairment Loss

(2.) Revaluation Model :-

(i.) Carrying Amount = Fair Value At Date of Revaluation

(ii.) Depreciation will be charged on this Revalued Amount in future

(iii.) Accounting in case of Revaluation of PPE :-

(A.) If Depreciation on PPE is charged directly [i.e. Depreciation To PPE]

⇓

then It means PPE is shown in Books at Net Carrying Amount Only

OR

Journal Entry if there is Revaluation Gain [FV > NCA]

⇓

PPE

To Revaluation Gain [FV − NCA]

Journal Entry if there is Revaluation Loss [FV < NCA]

⇓

Revaluation Loss [NCA − FV]

To PPE

(B.) If Provision for Depreciation (i.e. Accumulated Depreciation) is made instead of Charging Depreciation to PPE ✓

⇓

then It means PPE is shown in Books at Gross Amount

&

Provision for Depreciation (i.e. Acc. Dep.) is shown as Liability

⇓

So, Gross Carrying Amount − Accumulated Depreciation = Net Carrying Amount

⇓

Methods for Accounting for Revaluation of PPE

Method I:
Accumulated Depreciation Elimination Approach

⇓

Accumulated Depreciation is Eliminated, & then Net Carrying Amount shall be increased / decreased

⇓

→ Journal Entry for Eliminating Accumulated Depreciation

Accumulated Depreciation
    To PPE

→ Journal Entry if there is Reval. Gain [FV > NCA]

PPE
    To Reval. Gain [FV-NCA]

OR

→ Journal Entry if there is Reval. Loss [NCA > FV]

Reval. Loss [NCA − FV]
    To PPE

Method II: Restatement Approach

⇓

Proportionately Adjust (Increase/Decrease) Gross Carrying Amount & Accumulated Dep.

⇓

→ Calculate Revaluation Gain / Loss % = $\frac{F.V. - NCA}{NCA} \times 100$

→ Journal Entry if there is Revaluation Gain [FV > NCA]

PPE [GCA × Reval Gain %]
    To Acc. Dep. [Acc. Dep. × Reval Gain %]
    To Reval. Gain [FV − NCA]

OR

→ Journal Entry if there is Revaluation Loss [FV < NCA]

Acc. Dep. [Acc. Dep. × Reval. Loss %]
Reval. Loss [NCA − FV]
    To PPE [GCA × Reval Loss %]

(iv.) Treatment of Revaluation Gain or Loss :-

First Time Revaluation

- (+) ⇓ Credit to Revaluation Surplus [OCI]
- (−) ⇓ Debit to P&L

Subsequent Revaluation

- (+) Previously
  - (+) ⇓ Credit to Revaluation Surplus [OCI]
  - (−) ⇓
    - Credit P&L upto Previous Debit in it &
    - For Balance (+), Credit Revaluation Surplus [OCI]
- (−) Previously
  - (+) ⇓
    - Debit Revaluation Surplus upto Any Balance Existing in it &
    - For Balance (−), Debit to P&L
  - (−) ⇓ Debit to P&L

(v.) Treatment of Revaluation Surplus [OCI] Balance :-

- When PPE is derecognised or classified as Held for Sale
  ⇓
  Whole Revaluation Surplus Balance is transferred to Retained Earnings
  [It is Mandatory]

- Some of the Revaluation Surplus may also be transferred to Retained Earnings during the Asset is used by the Entity
  [It is Optional]
  ⇓
  It is Amount of Excess Depreciation due to Revaluation Gain
  =

Depreciation on Revalued Amount	xxx
Less:- Depreciation on Original Cost	(xxx)
	xxx

* In Silent situation, It is Assumed that Company is not opting for this Policy

Note:- Transfer to Retained Earnings is not made through P&L [i.e. Revaluation Surplus (OCI) is Item that will not be reclassified to P&L]

Other Points

- Gain or Loss on Sale of PPE is recorded in P&L
- Compensation Receivable from Insurance Company due to damage in PPE is accounted for separately as Other Income in P&L

Change in Estimated Dismantling, Decommissioning, Restoration or Demolition Cost

Step 1 :- Check Whether Provision for Decommissioning Liability has been increased or decreased due to change in Estimated Decommissioning Cost :-

Calculate P.V. of Revised Estimated Decommissioning Cost on date of change	xxx
Less:- Carrying Amount of Provision for Decommissioning Liability on date of change	(xxx)
Increase / (Decrease) in Liability	xxx

Step 2 :- Accounting for Change in Decommissioning Liability

- If Asset is Measured At Cost Model
  ⇓
  Adjust increase/decrease in Liability from Cost of Asset

- If Asset is Measured At Revaluation Model
  ⇓
  Same Treatment as of Revaluation Gain or Loss
  - If Increase in Liability [i.e. Loss]
  - If Decrease in Liability [i.e. Gain]

- If Increase in Liability
  - ⇓ Added to Cost of PPE
  - ⇓ PPE
    To Prov. for D.L.
- If Decrease in Liability
  - ⇓ Deducted from Cost of PPE
  - ⇓ Prov. for D.L.
    To PPE

⇓

- Debit Revaluation Surplus upto any Balance existing in it

&

- For remaining increase in liability, Debit to P&L

⇓

Reval. Surplus (if any existing)
P&L
    To Prov. for D.L.

⇓

- Credit P&L upto Previous Debit in it

&

- For remaining decrease in liability, Credit to Revaluation Surplus [OCI]

⇓

Prov. for D.L.
    To P&L (if any prev. debit)
    To Reval. Surplus (OCI)

Introduction to Ind AS 19

- Employee benefits means any type of consideration given by Entity to its Employees for Services rendered by them. [Eg. Salary]
- Employee benefits are of following types :-

Short Term Employee Benefits	Post Employment Benefits	Other Long Term Employee Benefits	Termination Benefits
That will be paid within 12 Months from Balance Sheet Date	That will be paid after employment i.e. on Retirement	That will be paid after 12 Months from Balance Sheet Date	That will be paid on Termination of Employment
Example:- Salary, Wages, etc.	Example:- PF, Gratuity, Pension, etc.	Example :- Jubilee Benefits	Example :- Retrenchment Compensation

Note:- SBP to Employees is Employee Benefit for which Accounting is covered under a Separate Ind AS [Ind AS 102]

- Accounting of Employee Benefits is completely based on Accrual concept [i.e. Record the Employee Benefit Expense in the period in which employee renders the Service]

Accounting for Short Term Employee Benefits

(1) Salary / Wages :-

(i) When Salary is accrued & paid :-

Salary A/c [P&L – Employee Benefits Expense]
  To Bank A/c

(ii) When Salary is accrued but not paid :-

Salary A/c [P&L – Employee Benefits Expense]
  To Salary Outstanding A/c [Liability]

(iii) When Salary is paid in Advance :-

Prepaid Salary A/c [Asset]
  To Bank A/c

(2) Bonus :-

- It is recognised on the date when the condition to receive bonus is met by the employees
- Journal Entries :-

(i) When condition to receive bonus is met by the employees [Bonus accrued]

Bonus A/c [P&L – Employee Benefits Expense]
  To Provision for Bonus A/c [Liability]

(ii) When Bonus is paid after accrual

Provision for Bonus A/c
  To Bank A/c

- Calculation of Bonus payable to Employees :-

⇒ Amount of Bonus per employee × No. of employees who met the condition

Note :- Sometimes Entity announces Bonus in form of Profit Sharing Plan, i.e. Share in Profit is given to employees as Bonus on meeting the condition.

⇓

In this Case, Bonus [Share in Profit] payable to employees is calculated as follows:

⇒ Profit earned by Entity during the year × Share in Profit Expected Payout %

(3) Leave Compensation [Paid Leaves | Paid Vacation | Compensating Absences] :-

- Paid Leaves are leaves given to the employees for which their Salary will not be deducted. [These leaves are provided to employees in addition to Sundays & Public Holidays]
- Entity may provide various types of Paid Leaves to its Employees like Casual Leaves, Privilege Leaves, Sick Leaves etc.
- Leave Compensation is recognised as follows :-

If Unused or Unutilized Leaves can be carried forward to Next Year [Accumulating Paid Leaves]

If Employee is entitled to take Cash for carry forwarded unused leaves in Next Year [Vesting]

⇓

It is recognised on the date when leaves are earned by the employees i.e. the Year in which Unused leaves arises

⇓

Journal Entries:

(i) When leaves are earned by the employees [Leaves Accrued]

Leave Compensation A/c [P&L - EBE]
  To Provision for Leave Compensation A/c [Liability]

(ii) When Cash is paid to employees in Next Year against carry forwarded leaves

Provision for Leave Compensation A/c
  To Bank A/c

⇓

Calculation of Leave Compensation payable to employee

If Employee is entitled to take excess leaves for carry forwarded unused leaves in Next Year [Non-Vesting]

⇓

It is recognised on the date when leaves are earned by the employees i.e. the Year in which Unused leaves arises

⇓

Journal Entries:

(i) When leaves are earned by the employees [Leaves Accrued]

Leave Compensation A/c [P&L - EBE]
  To Provision for Leave Compensation A/c [Liability]

(ii) When employees take carry forwarded leaves in Next Year or it lapses in Next Year

Provision for Leave Compensation A/c
[Instead of Current Year Salary A/c for this Amount]
  To Bank A/c

⇓

If Unused or Unutilized leaves cannot be carried forward to Next Year [Non-Accumulating Paid Leaves]

⇓

No Accounting Treatment

$\Rightarrow$ Total No. of Employees × Total No. of Unused leaves × Salary Per Day

Calculation of Leave Compensation payable to employee

$\Rightarrow$ No. of employees expected to utilize the unused leaves in Next Year × No. of unused leaves expected to be utilized by each employee in Next Year × Salary Per Day

Note:- Salary Per Day = $\dfrac{\text{Annual Salary}}{\text{No. of Working Days in the Year}}$

* No. of Working Days in the Year means days on which office of company remains open (i.e. All days except Sundays & Public Holidays)

Example 1:-

Mr. A is an employee in ABC Ltd. following are the details related to his Salary :-

Annual Salary = ₹ 30,00,000
No. of Working Days during the Year = 300 days
Paid Leaves Allowed = 20 days

In Year 1, Mr. A has taken 5 days Paid Leaves only & remaining leaves has been carried forward to next year.
In Year 2 (Next Year), Mr. A has taken all Paid Leaves of 35 days [20 + 15].
Pass Journal Entry for Year 1 & 2.

Solution:-

Salary per day $\Rightarrow \dfrac{₹\ 30,00,000}{300 \text{ days}}$ = ₹ 10,000 per day

No. of days to be worked by Mr. A to get full Salary in each year $\Rightarrow$ 300 − 20 = 280 days

Year 1:

No. of days for which Mr. A has done work $\Rightarrow$ 300 − 5 = 295 days
Unused Leaves $\Rightarrow$ 20 − 5 = 15 days
∴ Leave Compensation Amount $\Rightarrow$ 1 employee × 15 days × ₹ 10,000 = ₹ 1,50,000

Journal Entry :

(i)	Salary A/c [P/L - EBE]	30,00,000	
	To Bank A/c		30,00,000
(ii)	Leave Compensation A/c [P/L - EBE]	1,50,000	
	To Provision for Leave Compensation A/c		1,50,000

Year 2 :

No. of days for which Mr. A has done work $\Rightarrow$ 300 − [20 + 15] = 265 days
Unused Leaves $\Rightarrow$ 0
∴ No Leave Compensation

Journal Entry :

(i)	Salary A/c [P/L - EBE] (30,00,000 − 1,50,000)	28,50,000	
	Provision for Leave Compensation A/c	1,50,000	
	To Bank A/c		30,00,000

Example 2 :-

Mr. A is an employee in ABC Ltd. following are the details related to his Salary :-

Annual Salary = ₹ 30,00,000
No. of Working Days during the Year = 300 days
Paid Leaves Allowed = 20 days

In Year 1, Mr. A has taken 5 days Paid Leaves only & remaining leaves are settled by way of Payment in next year.
In Year 2 (Next Year), Mr. A has taken all Paid Leaves of 20 days.
Pass Journal Entry for Year 1 & 2.

Solution:-

Salary per day ⇒ $\frac{₹\ 30,00,000}{300 \text{ days}}$ = ₹ 10,000 per day

No. of days to be worked by Mr. A to get full Salary in each year ⇒ 300 − 20 = 280 days

Year 1:

No. of days for which Mr. A has done work ⇒ 300 − 5 = 295 days
Unused Leaves ⇒ 20 − 5 = 15 days
∴ Leave Compensation Amount ⇒ 1 employee × 15 days × ₹ 10,000 = ₹ 1,50,000

Journal Entry:

(i)	Salary A/c [P/L - EBE]	30,00,000	
	To Bank A/c		30,00,000
(ii)	Leave Compensation A/c [P/L - EBE]	1,50,000	
	To Provision for Leave Compensation A/c		1,50,000

Year 2:

No. of days for which Mr. A has done work ⇒ 300 − 20 = 280 days
Unused Leaves ⇒ 0
∴ No Leave Compensation

Journal Entry:

(i)	Salary A/c [P/L - EBE]	30,00,000	
	To Bank A/c		30,00,000
(ii)	Provision for Leave Compensation A/c	1,50,000	
	To Bank A/c		1,50,000

Accounting for Post Employment Benefits

(1) Defined Contribution Plan:-

- These are Post Employment Benefits under which Entity pays fixed contributions into a fund on behalf of the employee & will have no further obligation to pay any amount to employee post employment in any case.
  Example: PF Contribution by a Company to EPFO for its Employees
- Journal Entries:-
  (i) When it is accrued
  Defined Contribution Expense A/c [P&L − EBE]
  To Defined Contribution Payable A/c [Liability]
  [Salary × Contribution %]
  (ii) When it is paid
  Defined Contribution Payable A/c [Liability]
  To Bank A/c

Note:- If it is to be paid after 12 Months from Balance Sheet Date, then it should be recognised at Present Value & Interest Cost is charged over the period to unwind the discount.

Journal Entry at End of each period to unwind the discount :

Interest Cost A/c [P&L - EBE]
    To Defined Contribution Payable A/c [Liability]

[Opening Balance of Defined Contribution Payable × Discounting Rate]

(2) Defined Benefit Plan :-

- These are Post Employment Benefits under which Entity has obligation to pay agreed benefits directly to employees post employment in any case.
  Example : Gratuity
- It is recognised over the period of service by employee for which benefit will be paid after his employment.
- Steps to be followed for Accounting of Defined Benefit Plan :-

Step 1: Defined Benefit Obligation [DBO] :

(i) Total Benefits to be paid to employee post employment
    ⇒ Benefit % × Expected Final Salary p.a. × No. of Years of Service

(ii) Benefits attributed to each year of service

$$\Rightarrow \frac{\text{Total Benefits to be paid to employee post employment}}{\text{No. of Years of Service}}$$

(iii) Current Service Cost
→ Recognise Current Service Cost [Defined Benefit Expense] each year at P.V. of Benefit attributed to that Year.
→ Journal Entry at Each Year End

Current Service Cost A/c [P&L - EBE]
    To Defined Benefit Obligation A/c [Liability]

(iv) Interest Cost
→ Charge Interest Cost at Each year end on Opening Balance of Defined Benefit Obligation to unwind the discount because Current Service Cost [Defined Benefit Expense] is recognised each year at Present Value.
→ Journal Entry at Each Year End

Interest Cost A/c [P&L - EBE]
    To Defined Benefit Obligation A/c [Liability]

[Opening Balance of Defined Benefit Obligation × Discounting Rate]

(v) Actuarial Gain or Loss
→ Recognise Actuarial Gain or Loss (if any) at each year end on Defined Benefit Obligation as calculated by the Actuary due to Change in financial or demographic assumptions or Experience Variance like Estimates of Expected Final Salary, No. of Years of Service, Discounting Rate, etc.
→ Journal Entry at Each Year End

If Actuarial Loss [Increase in DBO]
⇓
Actuarial Loss A/c [OCI (NR)]
    To DBO A/c [Liability]

If Actuarial Gain [Decrease in DBO]
⇓
DBO A/c [Liability]
    To Actuarial Gain A/c [OCI (NR)]

(vi) Past Service Cost

→ Recognise Past Service Cost (if any) on DBO due to change in Defined Benefit Plan announced by the Entity i.e. Changing Benefit % in the Plan

→ Journal Entry on change in Defined Benefit Plan

If Change in Plan results in Additional Benefits to Employees [Increase in Benefit % in Plan]	If Change in Plan results in Reduction of Benefits to Employees [Decrease in Benefit % in Plan]
⇓	⇓
Past Service Cost A/c [P&L - EBE] To DBO A/c [Liability]	DBO A/c [Liability] To Past Service Cost A/c [P&L - EBE]

(vii) Payment of Benefits to Employees

→ Recognise Payment of Benefits to Employees from DBO on the date of Payment to Employees post employment

→ Journal Entry on the date of Payment

DBO A/c [Liability]
To Bank A/c

(viii) Curtailment and Settlement

→ If Entity curtails the benefits of employees under a Defined Benefit Plan and settles it before the maturity, then Recognise the Curtailment transaction with Settlement Gain or Loss on that date

→ Journal Entry on the date of Curtailment & Settlement

DBO A/c [Liability]	Reduction in DBO due to Curtailment
Loss on Settlement A/c [P&L - EBE]	Balancing figure
To Bank A/c	Payment for Settlement of Curtailment in Benefits
To Gain on Settlement A/c [P&L - EBE]	Balancing figure

(ix) Calculation of Closing Balance of Defined Benefit Obligation [Liability] at each year end

→ By Preparing Ledger A/c after considering above Journal Entries

Defined Benefit Obligation A/c [Liability]

To Actuarial Gain A/c	xxx	By Balance b/d [Opening Balance]	xxx
To Past Service Cost A/c [Reduction in Benefits]	xxx	By Current Service Cost A/c	xxx
To Bank A/c [Payment of Benefits]	xxx	By Interest Cost A/c	xxx
To Bank A/c [Payment for Settlement]	xxx	By Actuarial Loss A/c	xxx
To Gain on Settlement A/c	xxx	By Past Service Cost A/c [Additional Benefits]	xxx
To Balance c/d [Closing Balance] (B/F)	xxx	By Loss on Settlement A/c	xxx
	xxx		xxx

→ By Preparing Statement as follows

Particulars	Amount
Opening Balance of DBO	xxx
(+) Current Service Cost	xxx
(+) Interest Cost	xxx
(±) Actuarial Loss / (Actuarial Gain)	xxx / (xxx)

(±) Past Service Cost	xxx | (xxx)
(−) Payment of Benefits to Employees post employment	(xxx)
(−) Reduction in DBO due to Curtailment	(xxx)
Closing Balance of DBO	xxx

Step 2: Plan Assets :

→ It is planned investment (savings) for meeting the Defined Benefit Obligation.

→ It is recognised at Fair Value at each year end.

(i) Contribution in the Plan Assets

→ Recognise contribution made (Amount Invested) in the Plan Asset on the date of investment.

→ Journal Entry for Contribution in Plan Assets

Plan Assets A/c [Asset]
    To Bank A/c

(ii) Expected Return on Plan Assets

→ Recognise Expected Interest Income on Opening Balance of Plan Assets at each year end using same rate at which Interest Cost is charged on DBO.

[If Contributions are made in between of a year, then Recognise Expected Interest Income on such contributions also for that period]

→ Journal Entry at each year end

Plan Assets A/c [Asset]
    To Expected Return on Plan Assets A/c [P&L- EBE]

[Balance of Plan Assets × Interest Rate]

(iii) Actuarial Gain or Loss on Plan Assets

→ Recognise Actuarial Gain or Loss on Plan Assets at each year end as Plan Asset is measured at Fair Value.

→ Journal Entry at Each Year End

If Actuarial Gain
[Increase in Fair Value of Plan Asset]
⇓
Plan Assets A/c [Asset]
    To Actuarial Gain [OCI (NR)]

If Actuarial Loss
[Decrease in Fair Value of Plan Asset]
⇓
Actuarial Loss [OCI (NR)]
    To Plan Assets A/c [Asset]

(iv) Withdrawal of Amount from Plan Assets for Payment of Benefits to Employees

→ Recognise withdrawal of amount from Plan Assets for payment of benefits to employees on date of payment to employees post employment.

→ Journal Entry on date of withdrawal

Bank A/c
    To Plan Assets A/c [Asset]

(v) Withdrawal of Amount from Plan Assets for Payment of Settlement Amount for Curtailment in Benefits

→ Recognise withdrawal of amount from Plan Assets for payment of settlement amount for curtailment in benefits on date of payment.

→ Journal Entry on date of withdrawal

Bank A/c

To Plan Assets A/c [Asset]

(vi) Calculation of Closing Balance of Plan Assets [Asset] at each year end

→ By Preparing Ledger A/c after considering above Journal Entries

Plan Assets A/c [Asset]			
To Balance b/d [Opening Balance]	xxx	By Bank A/c [Withdrawal]	xxx
To Bank A/c [Contribution]	xxx	By Actuarial Loss A/c	xxx
To Expected Return on Plan Assets A/c	xxx	By Balance c/d [Closing Balance] (B/f)	xxx
To Actuarial Gain A/c	xxx		
	xxx		xxx

→ By Preparing Statement as follows

Particulars	Amount
Opening Balance of Plan Asset	xxx
(+) Expected Return on Plan Asset	xxx
(+) Contribution in the Plan Asset	xxx
(−) Withdrawal for Payment of Benefits to Employees post employment	(xxx)
(−) Withdrawal for Payment of Settlement Amount on Curtailment	(xxx)
(±) Actuarial Gain / (Actuarial Loss)	xxx / (xxx)
Closing Balance of Plan Asset	xxx

(vii) Calculation of Actual Return on Plan Assets

⇒ Expected Return on Plan Assets ± Actuarial Gain / (Actuarial Loss) on Plan Assets

Step 3: Net Defined Liability / (Asset) :

→ In Balance Sheet, Defined Benefit Obligation and Plan Asset are shown at Net amount as follows:

Closing Balance of DBO	xxx
(−) Closing Balance of Plan Asset	(xxx)
Net Defined Liability / (Asset)	xxx / (xxx)

→ If it is Net Defined Asset, then it will be shown at Lower of

OR

Above calculated Net Defined Asset Amount — Asset Ceiling

⇓

If Asset Ceiling Amount is Lower, then Difference Amount will be recognised as Loss on Plan Asset due to Asset Ceiling [OCI (NR)] as follows:

Loss on Plan Asset due to Asset Ceiling A/c [OCI (NR)]

To Plan Asset A/c [Asset]

Step 4: Net Interest Cost / (Income) :

→ In P&L, Interest Cost charged on DBO and Expected Interest Income on Plan Asset are shown at Net Amount as follows:

Interest Cost charged on DBO	xxx
(−) Expected Interest Income on Plan Asset	(xxx)
Net Interest Cost / (Income)	xxx / (xxx)

Step 5: Total Employee Benefit Expense in P&L related to Defined Benefit Plan:

→ In P&L, Total Employee Benefit Expense related to Defined Benefit Plan will be as follows:

Current Service Cost	xxx
(±) Net Interest Cost | (Income)	xxx | (xxx)
(±) Past Service Cost	xxx | (xxx)
(±) Loss on Settlement | (Gain on Settlement)	xxx | (xxx)
	xxx | (xxx)

Step 6: Net Remeasurement Gain | (Loss) in OCI related to Defined Benefit Plan:

→ In OCI, Actuarial Gain | (Loss) on DBO & Plan Asset and Loss on Plan Asset due to Asset Ceiling are shown at Net Amount as follows:

Actuarial Gain | (Loss) on DBO	xxx | (xxx)
(±) Actuarial Gain | (Loss) on Plan Asset	xxx | (xxx)
(–) Loss on Plan Asset due to Asset Ceiling	(xxx)
Net Remeasurement Gain | (Loss)	xxx | (xxx)

Accounting for Other Long Term Employee Benefits

Same Accounting as of Defined Benefit Plan

Accounting for Termination Benefits

- It is recognised on the date when the Entity announces the Termination Plan [Retrenchment Compensation Accrued]
- Journal Entries :-

Amount paid exclusively for Termination of Employment

↓

(i) When it is accrued

Retrenchment Compensation A/c [P&L – EBE]

To Retrenchment Compensation Payable A/c [Liability]

(ii) When it is paid

Retrenchment Compensation Payable A/c

To Bank A/c

Part of Amount is paid to Employees for receiving services from them in future

↓

Accounted as Normal Salary

Meaning & Recognition of Government Grants

- Government Grant means assistance by Government in form of transfer of resources to Entity.
- Entity shall recognise Government Grant in Books only when there is Reasonable Assurance that
  → Entity will comply with conditions of Grant (if any)
  and
  → Grant will be received

Accounting of Government Grants Related to Asset

It means grant given by Government to Entity for Purchase | Construction of Long Term Asset (PPE) [Example : Establishment / Setup of a Plant ; Purchase | Development of Equipment, Machinery or Land, etc.]

(1) Accounting of Monetary Government Grant Related to Asset [i.e. When Government Grant is receivable in Cash] :-

Entity has 2 Options for Accounting of this type of Government Grant

Option 1
⇓
Deduct the Amount of Grant received from Cost of Asset

J. E.

Grant Receivable A/c | Bank A/c
To Asset A/c

Option 2

- If Grant is received for a Depreciable Asset
  ⇓
  Recognise the Grant as Deferred Income in Balance Sheet & Transfer it to P&L in Ratio of Depreciation over the Useful Life of Asset

  J. E.

  Grant Receivable A/c | Bank A/c
  To Deferred Grant A/c

- If Grant is received for a Non Depreciable Asset [Eg : Land]
  - Grant is Conditional [i.e. Some Obligation on Entity]
    ⇓
    Recognise the Grant as Deferred Income in Balance Sheet & Transfer it to P & L in Ratio of obligation over the period of condition

    J. E.

    Grant Receivable A/c | Bank A/c
    To Deferred Grant A/c
  - Grant is Unconditional
    ⇓
    Recognise Grant immediately in P&L as Income

    J. E.

    Grant Receivable A/c | Bank A/c
    To Grant Income [P&L]

(2) Accounting of Non Monetary Government Grant Related to Asset [i.e. When Government Grant is receivable in Kind] :-

Entity has 2 Options for Accounting of this type of Government Grant

Option 1
⇓
Recognise the Asset received at Nominal Value

Option 2

- If Asset received in grant is a Depreciable Asset
  ⇓
- If Asset received in grant is a Non Depreciable Asset [Eg : Land]

* Nominal Value means:

→ Nominal Amount that Entity has paid to Government to acquire the Asset

→ If Asset is received for free from Government, then Nominal Value means ₹ 1

J.E.

Asset A/c [Nominal Value]
To Bank A/c

· Recognise the Asset at Fair Value

· Recognise the Grant at Fair Value as Deferred Income in Balance Sheet & Transfer it to P&L in Ratio of Depreciation over the Useful Life of Asset

J.E.

Asset A/c [Fair Value]
To Deferred Grant A/c

Grant is Conditional [i.e. Some Obligation on Entity]

↓

· Recognise the Asset at Fair Value

· Recognise the Grant at Fair Value as Deferred Income in Balance Sheet & Transfer it to P&L in Ratio of Obligation over the period of Condition

J.E.

Asset A/c [Fair Value]
To Deferred Grant A/c

Grant is Unconditional

↓

· Recognise the Asset at Fair Value

· Recognise the Grant at Fair Value immediately in P&L as Income

J.E.

Asset A/c [Fair Value]
To Grant Income [P&L]

Accounting of Government Grants Related to Income

· It means grant given by Government to Entity for incurring expenses or for relief in case of losses in business [Example: For Immediate Startup of Business / Relief Measure; Subsidy for Staff Training Expense, for Research & Development, for incurring expense to protect environment; Subsidy to sell goods at Lower Price, etc.]

· Entity shall do Accounting for this type of Government Grant as follows :-

If Grant is receivable for expenses already incurred or for immediate startup / relief [i.e. Unconditional]

↓

Recognise the Grant immediately in P&L as Income

J.E.

Grant Receivable A/c | Bank A/c
To Grant Income [P&L]

If Grant is receivable for future expenses [i.e. Conditional]

↓

Recognise the Grant as Deferred Income in Balance Sheet & Transfer it to P&L in Ratio of related future expenses over the period in which those expenses are to be incurred

J.E.

Grant Receivable A/c | Bank A/c
To Deferred Grant A/c

Presentation of Government Grants

(1) Balance Sheet :-

Deferred Grant is shown in Liability as Current or Non Current

(2) Statement of Profit or Loss :-

Option 1 ⇒ Grant Income is shown separately in 'Other Income'.

Option 2 ⇒ Grant Income is deducted from the related Expense.

(3) Statement of Cash Flows :-

Grant received is shown under Financing Activities.

Accounting of Repayment (Refund) of Government Grants

Entity has to do Accounting of Repayment of Government Grants according to the following cases :-

If Grant was recognised directly in P&L as Income

⇓

Repayment of Grant will be debited to P&L

J.E.

P&L [Refund Amount]
To Grant Payable A/c | Bank A/c

If Grant was recognised as Deferred Income

⇓

Repayment of Grant will be debited to Deferred Grant & any remaining amount of refund will be debited to P&L

J.E.

Deferred Grant A/c [Carrying Amount]
P&L [Balancing figure]
To Grant Payable A/c | Bank A/c [Refund Amount]

If Grant was recognised by way of deduction from Cost of Asset

⇓

Repayment of Grant will be debited to that Asset A/c

J.E.

Asset A/c [Refund Amount]
To Grant Payable A/c | Bank A/c

Note:- Depreciation that would have been recognised on this Asset (if there were no Grant) shall be recognised immediately in P&L

Accounting of Loan Received from Government at Less than Market Interest Rate

- Apply Financial Liability (Loan Taken) Accounting as per Ind AS 109.
- At Initial Recognition, Difference between Loan Amount Received & Fair Value of Loan (Financial Liability) will be treated as Government Grant.

⇓

This difference amount of Government Grant will be accounted as per Ind AS 20 [i.e. according to the nature of Grant (Purpose of Loan) as discussed in above topics]

Journal Entry at Initial Recognition of Loan

	Dr	Cr
Bank A/c	Amount Received	
To Loan A/c		Fair Value
To Deferred Grant A/c | P&L		Balancing figure

Introduction to Ind AS 21

- This Ind AS prescribes :

(i) Accounting for Foreign Currency Transactions.

(ii) Translation of Financial Statements of Foreign Operation into Presentation Currency of Parent Entity & Intra Group Transactions between Parent Entity & its Foreign Operation

(iii) Translation of Financial Statements of Entity into Presentation Currency.

- Types of Currency :-

Functional Currency

⇓

It is the Currency in which Books of the Entity are maintained

⇓

It is determined as the Currency of Primary Economic Environment of the Entity using following Indicators :

Primary Indicators

⇓

→ Currency which influences the Sales Price of its Goods or Services

→ Currency which influences the Cost of providing Goods or Services

Secondary Indicators

⇓

→ Currency in which funds are raised

→ Currency in which receipts from operations are retained

Foreign Currency

⇓

Any Currency other than Functional Currency of the Entity

⇓

Transactions in Foreign Currency need to be Converted in Functional Currency

Presentation Currency

⇓

It is the Currency in which Financial Statements of the Entity are presented

[It can be Functional Currency or Foreign Currency]

Accounting for Foreign Currency Transactions

- Foreign Currency Transaction means any transaction that will be settled in Foreign Currency which includes :

→ Purchase or Sale of Goods, PPE, etc. in Foreign Currency

→ Borrowing or Investing Amounts in Foreign Currency

- Initial Recognition of Foreign Currency Transaction :-

It is initially recorded by converting into Functional Currency at the Exchange Rate on Transaction Date.

Example 1 :-

On 1st January, A ltd. [Indian Company] purchased a PPE from USA for \$ 1,000 on credit. A ltd.'s Functional Currency is ₹. Exchange Rate on date of transaction is 1 \$ = ₹ 80

Pass Journal Entry to recognise this transactional initially.

Solution :-

Journal Entry on 1st January

PPE A/c Dr.	₹ 80,000	
To Creditors A/c [$ 1,000 × ₹ 80]		₹ 80,000

- **Subsequent Recognition of Foreign Currency Transaction (At Each Balance Sheet Date) :-**

If Asset or Liability initially recognised in Foreign Currency Transaction is

Monetary Item

[Assets & Liabilities which will be settled in fixed amount of Cash
Eg:- T/R, T/P, Loan given, Loan taken, Investment in Redeemable Bonds, etc.]

⇓

It will be Remeasured at the Exchange Rate on Balance Sheet Date [i.e. Closing Rate at Year End]

⇓

Difference Amount will be recorded as Exchange Gain/Loss (Translation Gain/Loss) in P&L

Non Monetary Item

[Other than Monetary Items
Eg:- PPE, Intangible Assets, Inventory, Income received in advance, Prepaid expense, etc.]

- If it is shown at Historical Cost [Cost Model]

  ⇓

  It will not be Remeasured

- If it is shown at Fair Value [Revaluation Model]

  ⇓

  It will be Remeasured at the Exchange Rate on Fair Value Determination Date

  ⇓

  Difference Amount will be recorded as Exchange Gain/Loss (Translation Gain/Loss) in

  - P&L [If Fair Value Gain/Loss on such item is recorded in P&L]
  - OCI [If Fair Value Gain/Loss on such item is recorded in OCI]

Example 2 :-

In Continuation to Example 1 ; Suppose Exchange Rate on 31st March (Year End) is 1$ = ₹82
A ltd. follows Cost Model on PPE.
Pass Journal Entry on 31st March as per Ind AS 21.

Solution :-

Items initially recognised in Foreign Currency Transaction are :

(i) PPE ⇒ Non Monetary Item shown at Cost Model ⇒ Not Remeasured

(ii) Creditors ⇒ Monetary Item Remeasured at 1$ = ₹ 82 ⇒ $ 1,000 × ₹ 82 = ₹ 82,000

∴ Increase in Creditors = ₹ 82,000 − ₹ 80,000 = ₹ 2,000

Journal Entry on 31st March :

Exchange Loss A/c (P&L)	₹ 2,000	
To Creditors A/c [$ 1,000 (₹ 82 − ₹ 80)]		₹ 2,000

Note : Application of Ind AS 21 in Some Special Cases :-

(i) On Items of Amortisation Table in case of Loan or Investment in Foreign Currency (Monetary Item) as follows:

	Year	Opening Balance	Interest @ Discounting Rate	Actual Payment	Exchange Gain/Loss	Closing Balance
Foreign Currency	✓	xx	xx	xx		xx
Convert it in Functional Currency	✓	At Exchange Rate on Opening Date	At Average Exchange Rate for the Year	At Exchange Rate on Payment Date	Balancing figure	At Exchange Rate on Balance Sheet Date [i.e. Closing Rate at Year End]

(ii) Inventory purchased in Foreign Currency (Non Monetary Item) is measured at Year End as follows:

Cost [Foreign Currency]
⇓
It is converted in Functional Currency at the Exchange Rate on Transaction Date (i.e. Purchase Date)

NRV [Foreign Currency]
⇓
It is converted in functional Currency at the Exchange Rate on NRV Determination Date (i.e. Closing Rate on Year End)

This Inventory will be measured at Lower of Cost or NRV in functional Currency

(iii) Asset subject to Impairment Loss purchased in Foreign Currency (Non Monetary Item) is measured at Year End as follows:

Carrying Amount [Foreign Currency]
⇓
It is converted in Functional Currency at the Exchange Rate on Transaction Date (i.e. Purchase Date)

Recoverable Amount [Foreign Currency]
⇓
It is converted in functional Currency at the Exchange Rate on Recoverable Amount Determination Date (i.e. Closing Rate on Year End)

This Asset will be measured at Lower of Carrying Amount or Recoverable Amount in functional Currency.
[If Carrying Amount > Recoverable Amount, then Difference will be Impairment Loss as per Ind AS 36]

Foreign Operation

(1) Meaning of Foreign Operation & its Functional Currency :-

- Foreign Operation means Subsidiary, Associate, Joint Venture or Branch of the Entity in any other country.
- Functional Currency of Foreign Operation will be same as of Parent Entity if all the following conditions are fulfilled:

Activities of Foreign Operation are carried out as an extension of Parent Entity	Transactions of foreign Operation with Parent Entity are in High Proportion of its activities	Cash flows of foreign Operation are readily available for Remittance to Parent Entity	Cash flows of foreign Operation are not sufficient for settlement of its debt

* If any of the above condition is not fulfilled, Foreign Operation has to determine its functional Currency by applying Primary & Secondary Indicators

(2) Translation of financial Statements of Foreign Operation into Presentation Currency of Parent Entity [For Consolidation Purpose] :-

- Since Foreign Operation prepares its Financial Statements in its Functional Currency. Hence, Foreign Operation is required to translate its Financial Statements into Currency in which Parent Entity is preparing its financial Statements so that Consolidation can be done.

- Financial Statements of Foreign Operation are translated as follows :

Assets & Liabilities	Inventory & Asset subject to Impairment Loss	Share Capital	Other Equity & Opening Retained Earnings	Profit / Retained Earnings during the Year [Items of Income and Expenses]
⇓ Converted at the Exchange Rate on Balance Sheet Date [i.e. Closing Rate on Year End]	⇓ Converted using special cases (ii) & (iii) as discussed in above Topic	⇓ Converted at the Exchange Rate on Actual Transaction Date (i.e. Share Capital Issue Date) [Converted Amount can be directly given in Question]	⇓ Converted at the Exchange Rate on Actual Transaction Date [Converted Amount can be directly given in Question]	⇓ Converted at the Average Exchange Rate for the Year

⇓

Difference Amount will be recognised as Foreign Currency Translation Reserve (FCTR) in OCI

Note :-

(i) While preparing CFS
→ Share of Parent Entity in FCTR (OCI) will be shown in Consolidated Other Equity.
→ Share of NCI in FCTR (OCI) will be added to NCI.

(ii) Treatment of FCTR (OCI) Balance on disposal (sale) of that Foreign Operation

Full Disposal of Foreign Operation [i.e. Loss of Control in Foreign Operation]	Partial Disposal of Foreign Operation [i.e. No Loss of Control in Foreign Operation]
⇓ Share of Parent Entity in FCTR (OCI) Balance will be reclassified to P&L	⇓ Proportionate Share of Parent Entity (upto % Stake sold in Foreign Operation) in FCTR (OCI) Balance will be transferred to NCI

(iii) Goodwill arising on acquisition of Foreign Operation is calculated in Functional Currency of Foreign Operation & then Translated at the Exchange Rate on Balance Sheet Date [i.e. Closing Rate at Year End]

(3) Intra Group Transactions [Transaction between Parent Entity & its Foreign Operation] :-

- Intra Group Transactions can be :
  → Sale | Purchase of Goods between Parent Entity & its Foreign Operation, or
  → Loan transaction between Parent Entity & its Foreign Operation

- In Case of Intra Group Transaction between Parent Entity & its Subsidiary (Foreign Operation), then such Intra Group Transaction will be eliminated in CFS as per Ind AS 110.
  ⇓
  But Exchange Gain | Loss arising on such transaction will not be eliminated in CFS because Group has real exposure to foreign Currency.

- Exchange Gain | Loss arising on items in Intra Group Transactions will be recorded in CFS through same head [P&L | OCI] as in SFS
  ⇓
  But In Case of Intra Group Loan Transaction for which settlement is not planned in forseeable future
  ↓
  Exchange Gain Loss arising on such transaction will be recorded

In SFS	In CFS
⇓	⇓
P&L (Since it is a Monetary Item)	OCI & will be reclassified to P&L on disposal of such foreign Operation

- If there is any Unrealised Profit on Intra Group Transaction, it will be eliminated in CFS as per Ind AS 110 by converting Profit (Foreign Currency) at the Exchange Rate on Intra Group Transaction Date.

Translation of Financial Statements of Entity into Presentation Currency

Books of Accounts of an Entity are maintained in Functional Currency But Entity is required to submit its financial Statements in Another Currency [i.e. Presentation Currency].
⇓
In this Case, Entity is required to translate its financial Statements into such Presentation Currency
⇓
Apply Same Procedure as in case of Translation of Financial Statements of Foreign Operation into Presentation Currency of Parent Entity

Change in Functional Currency

If due to facts & circumstances, Functional Currency of Entity changes ; All Items of Financial Statements of Entity are converted to New Functional Currency at the Exchange Rate on Functional Currency Change Date [No Exchange Gain | Loss will arise]

Meaning & Treatment of Borrowing Costs

(1) **Meaning of Borrowing Costs :-**

It means costs incurred for borrowing the funds including
→ Interest Costs
→ Exchange Difference on foreign Currency Borrowing upto some extent

(2) **Treatment of Borrowing Costs :-**

If Borrowing is taken for Acquisition or Construction of a Qualifying Asset
⇓
Capitalise it to the Cost of that Asset

Otherwise
⇓
Recognise as an Expense in P&L

Note : Qualifying Asset :-

→ It means any Asset [Example : Inventory, PPE, Intangible Assets, Investment Property, etc.] which takes substantial period of time to get ready for its intended use or sale [i.e. Installation or Construction of Asset is taking substantial period of time]

→ 'Substantial Period of Time' is not defined under the Ind AS. It will be as per the judgement of the Entity. In silent question, we will assume that Asset is taking substantial period of time to get ready.

Period of Capitalisation of Borrowing Costs

Commencement Date of Capitalisation of Borrowing Costs
⇓
Capitalisation of Borrowing Costs should start from Later of following dates :
(i) Loan Taken
(ii) Development Activities on the Asset has been Started
(iii) Expense is incurred on the Asset

Cessation Date of Capitalisation of Borrowing Costs
⇓
- Capitalisation of Borrowing Costs should stop on the date when the Asset gets ready for its intended use or sale.
- If Entity is completing construction of Asset in Parts & each part can be used individually, then Entity should stop capitalisation of Borrowing Costs on completed part on the date when that part gets ready for its intended use or sale.
[Example : Building Construction Project in Phases]

Note :- If Entity pause development work on the Asset for unnecessary reason, then Capitalisation of Borrowing Costs on that Asset will be suspended for such period.

Capitalisation of Borrowing Costs

- Entity can have 2 types of Borrowings as follows :-

Specific Borrowings ⇓ Amount Borrowed specifically for Acquisition or Construction of a Qualifying Asset

General Borrowings ⇓ All Other Borrowings of Entity which can be used for any purpose

- It is assumed that :
  → Specific Borrowings are firstly used to incur expense on qualifying asset, and then
  → General Borrowings are used to incur remaining expense on qualifying asset

- Calculation of Borrowing Cost to be Capitalised on Qualifying Asset during the year as follows :-

Step 1 : Specific Borrowing Cost :

Actual Interest Cost incurred on Specific Borrowings irrespective of expense incurred on qualifying asset on different dates — xxx

$$\left[\text{Specific Borrowing Amount} \times \text{Interest Rate on Specific Borrowing} \times \frac{\text{Months}}{12} \right]$$

Here, Months will be taken
- FROM ⇒ Later of
  - Commencement Date of Capitalisation
  - Year Beginning
- TO ⇒ Earlier of
  - Cessation Date of Capitalisation
  - Year End

(–) Investment Income on Temporary Investment of these Specific Borrowings [if any] — (xxx)

Specific Borrowing Cost to be Capitalised — xxx

Step 2 : General Borrowing Cost :

(i) Calculate Capitalisation Rate [Weighted Average Borrowing Rate]

$$\Rightarrow \frac{\text{Total Actual Interest on All General Borrowings}}{\text{Total Amount of General Borrowings weighted average on time basis}} \times 100$$

(ii) Calculate Eligible General Borrowing Cost

$$\Rightarrow \text{Expense incurred on Qualifying Asset on each date (after utilising Specific Borrowing)} \times \text{Capitalisation Rate} \times \frac{\text{Months}}{12}$$

Here, Months will be taken
- FROM ⇒ Later of
  - Commencement Date of Capitalisation
  - Respective Expense Incurred Date
  - Year Beginning
- TO ⇒ Earlier of
  - Cessation Date of Capitalisation
  - Year End

* Expense incurred should be considered on Actual Outflow basis [Not Accrual]
* Borrowing Costs already capitalised on Qualifying Asset till Previous Year should also be considered as Expense incurred on Qualifying Asset for calculation of Eligible General Borrowing Cost for the Current Year

(iii) Calculate General Borrowing Cost to be Capitalised

Eligible General Borrowing Cost as calculated above
OR
Total Actual Interest on All General Borrowings

} Lower

Step 3 : Total Borrowing Cost to be Capitalised on Qualifying Asset during the year :
⇒ Step 1 + Step 2

Note :-

(i) If Specific Borrowings are taken for More than 1 Asset, then Allocate Specific Borrowing Cost to All Asset as follows :

$$\Rightarrow \text{Total Specific Borrowing Cost} \times \frac{\text{Expense incurred on 1 Asset}}{\text{Total Expense incurred on All Assets}}$$

(ii) If Borrowing taken is in nature of Bonds issued at Discount, then EIR as per Ind AS 109 will be considered for calculation of borrowing Costs.

Example :-

A ltd. started construction of a building on 1st April for which it obtained a Specific Loan of ₹ 2 Lakh at 9% p.a.

A ltd. has also taken other loans as follows :

₹ 8,00,000 @ 10% p.a.

₹ 12,00,000 @ 13% p.a.

Expense incurred on construction of Building :

Date	Amount in ₹
1st April	1,50,000
1st August	1,40,000
1st October	3,00,000

Construction completed on 31st December. Calculate Borrowing Cost to be capitalised.

Solution :-

Step 1 : Specific Borrowing Cost ⇒ $₹ 2 \text{ Lakh} \times 9\% \times \frac{9}{12} = ₹ 13,500$

Step 2 : General Borrowing Cost :

(i) WABR $\Rightarrow \frac{\left(8,00,000 \times 10\% \times \frac{12}{12}\right) + \left(12,00,000 \times 13\% \times \frac{12}{12}\right)}{\left(8,00,000 \times \frac{12}{12}\right) + \left(12,00,000 \times \frac{12}{12}\right)} \times 100 \Rightarrow \frac{2,36,000}{20,00,000} \times 100 \Rightarrow 11.80\%$

(ii) Eligible General Borrowing Cost on expense incurred

1st April ⇒ 1,50,000 − 1,50,000 (Specific) = 0

1^{st} August ⇒ 1,40,000 − 50,000 (Specific) = 90,000 × 11.80% × $\frac{5}{12}$ = ₹ 4,425
1^{st} October ⇒ 3,00,000 × 11.80% × $\frac{3}{12}$ = ₹ 8,850
₹ 13,275

(iii) General Borrowing Cost to be Capitalised

Eligible General Borrowing Cost = ₹ 13,275
OR
Total Actual Interest on All General Borrowings = ₹ 2,36,000

→ Lower, i.e. ₹ 13,275

Step 3: Total Borrowing Cost to be capitalised ⇒ ₹ 13,500 + ₹ 13,275 ⇒ ₹ 26,775

Capitalisation of Borrowing Costs by Group Companies

(1) In SFS of each Group Company :-

- Apply Same Principles as discussed above in this Ind AS.
- Capitalise Borrowing Costs into Qualifying Asset in SFS of Company if it has taken Borrowing & has incurred Expense on Qualifying Asset.

(2) In CFS of the Group :-

- Capitalise Borrowing Costs into Qualifying Asset in CFS by considering all the borrowings taken by each company in the group & all expense incurred on qualifying assets by each Company in the group.

- If Inter Company Profit is charged on Construction of Qualifying Asset within the Group, then such profit will be eliminated in CFS while considering Expense incurred on Qualifying Assets.

Exchange Difference on Foreign Currency Borrowing to be treated as Borrowing Cost

- Exchange Loss arising on Foreign Currency Borrowing upto Saving in Interest Cost is treated as Borrowing Cost as per Ind AS 23 & Remaining Exchange Loss will be recognised in P&L as per Ind AS 21.

- Steps to be followed to solve the question :-

Step 1: Calculate Actual Interest Cost on Foreign Currency Borrowing

⇒ Foreign Currency Borrowing Amount × Foreign Currency Borrowing Interest Rate × Exchange Rate at Year End

Step 2: Calculate Saving in Interest Cost

⇒ Interest Cost on Functional Currency Borrowing − Interest Cost on Foreign Currency Borrowing [Step 1]

* Interest Cost on Functional Currency Borrowing ⇒ Foreign Currency Borrowing Amount × Exchange Rate on date of Borrowing × Functional Currency Borrowing Interest Rate

Step 3: Calculate Exchange Difference on Foreign Currency Borrowing

⇒ Foreign Currency Borrowing Amount × [Exchange Rate at Year End − Exchange Rate at Beginning]

If Positive
⇓
Exchange Loss
⇓
→ Lower of Exchange Loss & Saving in Interest Cost [as per Step 2] will be treated as Borrowing Cost as per Ind AS 23

→ Remaining Exchange Loss (if any) will be recognised in P&L as per Ind AS 21 [Balancing figure]

If Negative
⇓
Exchange Gain
⇓
Recognised in P&L as per Ind AS 21

[No Treatment as per Ind AS 23 of Exchange Gain initially arising on such Loan]

Step 4: Total Borrowing Cost on Foreign Currency Borrowing

⇒ Actual Interest Cost on Foreign Currency Borrowing [Step 1] + Exchange Loss arising on Foreign Currency Borrowing upto Saving in Interest Cost [Step 3]

Note:- If Exchange Loss on Foreign Currency Borrowing is treated as Borrowing Cost in a Year & Exchange Gain arises on that Foreign Currency Borrowing in Subsequent Year, then such Exchange Gain (upto the amount of previously recorded Exchange Loss as Borrowing Cost on remaining outstanding Loan) will be deducted from the Borrowing Cost.

Example:-

A ltd. [Indian Company] has taken a loan of \$ 1,000 on 1st April for constructing a Qualifying Asset at 4% p.a. Equivalent Amount of Loan could have been taken in Functional Currency at 12% p.a. Exchange Rate on 1st April was 1\$ = ₹ 40 and on Year end (31st March) was 1\$ = ₹ 41

(a) Calculate Total Borrowing Cost to be capitalised during the year.

(b) If Exchange Rate at 2nd Year End becomes 1\$ = ₹ 39.50, Calculate amount to be adjusted in Borrowing Cost.

Solution:-

(a) Step 1: Actual Interest Cost on Foreign Currency [\$] Borrowing

⇒ 1,000 \$ × 4% × ₹ 41 ⇒ ₹ 1,640

Step 2: Saving in Interest Cost:

⇒ ₹ 4,800 − ₹ 1,640 ⇒ ₹ 3,160

*Interest on Functional Currency [₹] Borrowing ⇒ 1,000 \$ × ₹ 40 × 12% ⇒ ₹ 4,800

Step 3: Exchange Loss ⇒ \$ 1,000 × (₹ 41 − ₹ 40) ⇒ ₹ 1,000

Exchange Loss as Borrowing Cost ⇒ Lower of ₹ 1,000 & ₹ 3,160 i.e. ₹ 1,000

Step 4: Total Borrowing Cost to be capitalised during the year ⇒ ₹ 1,640 + ₹ 1,000 ⇒ ₹ 2,640 (b.) Exchange Gain at 2^{nd} Year End ⇒ \$ 1,000 (₹ 39.50 − ₹ 41) ⇒ ₹ 1,500

So, Exchange Gain upto previous Exchange Loss recognised as Borrowing Cost i.e. ₹ 1,000 will be deducted from Borrowing Cost as per Ind AS 23 & Remaining Exchange Gain of ₹ 500 will be recognised in P&L as per Ind AS 21.

The Objective of this Ind AS is to identify & disclose the transactions with Related Parties in Financial Statements.

Related Party

(i) Related Party of an Entity can be < A Person OR Another Entity

• A Person will be considered as Related Party of an Entity if that person :-

- Has Control | Joint Control over the Entity
- OR Has Significant Influence over the Entity
- OR Is KMP [Director] of the Entity

Note :-

Close Member of Above Person's family will also be considered as Related Party of Entity. It includes :

→ Children, Spouse / Domestic Partner, Brother, Sister, Father & Mother of that Person.

→ Children of that Person's Spouse | Domestic Partner.

→ Dependents of that Person or his Spouse | Domestic Partner

• Another Entity will be considered as Related Party of an Entity :-

(i) Parent & its All Subsidiaries (including fellow Subsidiaries) are Related to each other.

Example :

$$\begin{tikzcd} & S_1 & \\ P \arrow[ur] \arrow[dr] & & \\ & S_2 \arrow[r] & S_3 \end{tikzcd}$$

(ii) Associate Company of Parent or its Subsidiary or Fellow Subsidiary are related to the Parent & its All Subsidiaries (including Fellow Subsidiaries)

Example :

$P < S_1,\ S_2 \rightarrow S_3,\ A_1$

$P < S_1 \rightarrow A_1,\ S_2 \rightarrow S_3$

$P < S_1,\ S_2 \rightarrow S_3 \rightarrow A_1$

Note :-

→ Subsidiary of Above Associate Company is also related to the Parent & its All Subsidiaries (including fellow Subsidiaries).

Example :

$P < S_1,\ S_2 \rightarrow S_3,\ A_1 \rightarrow S_4$

$P < S_1 \rightarrow A_1 \rightarrow S_4,\ S_2 \rightarrow S_3$

$P < S_1,\ S_2 \rightarrow S_3 \rightarrow A_1 \rightarrow S_4$

→ Associate of Above Associate Company is not related to the Parent & its All Subsidiaries (including fellow Subsidiaries).

Example :

$P \longrightarrow A_1 \longrightarrow A_2$

$\underbrace{P \qquad A_2}_{\text{Not a Related Party}}$

→ Associate Company of a Group is not related to any other Associate Company in that Group.

Example:

P → A_1, P → A_2 — Not a Related Party

(iii) If a Person (including Close Member of his Family) or an Entity has

Control | Joint Control over 1 Entity **and** Control | Joint Control or Significant Influence or KMP of Another Entity

Note:- Subsidiary of above companies are also related to each other.

Example:

Mr. A $\xrightarrow{\text{control}}$ P Ltd., Mr. A $\xrightarrow{\text{KMP}}$ Q Ltd. — Related Party

Mr. A $\xrightarrow{\text{Sig. Influence}}$ P Ltd., Mr. A $\xrightarrow{\text{KMP}}$ Q Ltd. — Not a Related Party

(2) Followings are not considered as Related Parties :-

- Co-ventureres of a Single Joint Venture.

  Example:

  Not a Related Party — P Ltd., Q Ltd. → Running a "Joint Venture"

- Major Customers, Suppliers, Agents, Distributors, Financers, Trade Unions, etc. only because of their dealings with the entity.

Related Party Disclosures

- Disclosure requirements are classified into 2 Categories as follows :-

Category 1 Disclosures

⇓

Related Party Relationships will be disclosed even if there are no transactions between them

⇓

Relationship between Parent & Subsidiaries

⇓

Disclose the Name of its Parent & Ultimate Controlling Entity [if Any]

Category 2 Disclosures

⇓

Related Party Relationships will be disclosed only if there are transactions between them

[Even if transactions are at arm's length basis or insignificant]

⇓

All Other Relationships

⇓

Disclose the following

Nature of Related Party Relationship	Amount of Transactions in Relationship Period	Amount of Outstanding Balance on Balance Sheet Date	Expense recognised in P&L from Related Party Transaction [if Any]	Commitments with Related Party [if Any]

- Entity is exempt from disclosure requirements [Transaction, Outstanding Balance & Commitments] if Related Party is
  - → Government, or
  - → Another Entity over which Government has Control | Joint Control or Significant Influence

  However, Entity has to disclose the following even in this case :-
  - → Name of the Government & Nature of its Relationship with the Entity
  - → Nature & Amount of Significant Transactions between them

Introduction to Ind AS 33

- Earnings Per Share (EPS) is a measure of performance of the company.
- This Ind AS requires the entity to calculate & present the EPS on the face of Statement of Profit & Loss for Current Year & Previous Year.
- EPS is of 2 types : Basic EPS & Diluted EPS

Basic EPS

Calculation of Basic EPS

$$BEPS = \frac{\text{Profit | Loss attributable to Ordinary Equity Shareholders}}{\text{Weighted Average No. of Ordinary Equity Shares}}$$

Note :-

(i) EPS can be negative also.

(ii) Ordinary Equity Share means Original Equity Shares only [i.e. It does not consider classified Equity Instruments as per Ind AS 109.

Profit | Loss attributable to Ordinary Equity Shareholders

It is calculated as follows :-

Earnings Before Interest & Tax [EBIT]	xxx
(-) Interest Expense on Loan | Debentures | Bonds etc.	(xxx)
Profit Before Tax [PBT]	xxx
(-) Tax	(xxx)
Profit After Tax | Profit for the Year | Net Profit [PAT]	xxx
(-) Preference Dividend	(xxx)
Profit | (Loss) attributable to Ordinary Equity Shareholders	xxx / (xxx)

Note :-

(i) Other Comprehensive Income (OCI) part is not considered for calculation of EPS.

(ii) General Assumption for Ind AS 33 Questions

⇓

Ignore Ind AS 109 [Unless Market Interest Rate on such financial Instrument is given in question]

Loan | Debenture | Bonds [Treated as Liability]

⇓

Preference Shares [Treated as Equity]

⇓

Interest = Face Value × Coupon Interest Rate

Dividend = Face Value × Coupon Dividend Rate

Weighted Average No. of Ordinary Equity Shares [WANES]

(1) It means No. of Ordinary Equity Shares are adjusted by Time Factor [i.e. No. of days for which shares are outstanding as a proportion of Total No. of Days in a Year]

(2) It is calculated as follows :-

No. of Equity Shares Outstanding at the beginning of Year	✓
(+) No. of Equity Shares issued during the year × $\frac{\text{No. of days / months}}{365 / 12}$	✓
(−) No. of Equity Shares Buy Back during the Year (Treasury Shares) × $\frac{\text{No. of days / months}}{365 / 12}$	(✓)
	✓

(3) Calculation of Weighted Average No. of Ordinary Equity Shares in following Special Cases :-

- **Partly Paid up Shares** :

  If Shares are partly paid up, then Multiply No. of Shares by $\left[\frac{\text{Partly Paid up Value}}{\text{Issue Price}}\right]$ in WANES Calculation

- **Bonus Issue** :

  In Case of Bonus Issue, Shares are issued to existing shareholders without consideration by capitalisation of reserves.

  ⇓

  Therefore

  - Multiply No. of Shares Outstanding before date of bonus issue by Bonus Adjustment factor [BAF] in WANES calculation
  - Previous Year EPS is also Restated by Multiplying No. of Shares by BAF in WANES calculation for Previous Year

  Note :- Bonus Adjustment factor [BAF] = 1 + Bonus Ratio

  Example : If Bonus Ratio is 1:4 ; So BAF $= 1 + \frac{1}{4} = \frac{4+1}{4} = \frac{5}{4}$

- **Rights Issue** :

  In Case of Rights Issue, Shares are issued to existing shareholders at a Price below the Current Market Price of Share.

  ⇓

  Therefore Rights Issue has some Bonus element which needs to be adjusted

  - Multiply No. of Shares Outstanding before date of rights issue by Rights Adjustment factor [RAF] in WANES calculation as follows

    ⇓
  - Previous Year EPS is also Restated by Multiplying No. of Shares by RAF in WANES calculation for Previous Year

$$\left[\text{No. of Equity Shares outstanding before date of Rights Issue} \times RAF \times \frac{\text{No. of months till date of Rights Issue}}{12}\right]$$

$$+$$

$$\left[\text{Total No. of Equity Shares after Rights Issue} \times \frac{\text{No. of months after date of Rights Issue}}{12}\right]$$

Note:- Rights Adjustment Factor [RAF] is calculated as follows:

Step 1: Calculate Theoretical Ex Rights Value Per Share

$$\Rightarrow \frac{\left[\text{Existing MPS} \times \text{No. of Existing Shares}\right] + \left[\text{Right Issue Price} \times \text{No. of Right Shares}\right]}{\text{No. of Existing Shares} + \text{No. of Right Shares}}$$

Step 2: Calculate RAF

$$\Rightarrow \frac{\text{MPS}}{\text{Theoretical Ex Rights Value Per Share}}$$

Example:

F.Y. : 1^{st} Jan. 20X1 to 31^{st} Dec. 20X1

A ltd. has 1,000 Equity Shares outstanding on 1^{st} Jan. 20X1.

On 31. Mar. 20X1, Right Issue is made for 1 New share against each 5 outstanding shares.

MPS before Right Issue is ₹ 10; Rights Issue Exercise Price is ₹ 7.

Profit attributable to Equity Shareholders for 20X1 & Previous Year [20X0] is ₹ 1,10,000 & ₹ 1,00,000 respectively.

Calculate Basic EPS for 20X0 and 20X1.

Solution:

Calculation of RAF ⇒

Step 1: Theoretical Ex Rights Value Per Share $= \frac{10 \times 1{,}000 + 7 \times 200}{1{,}000 + 200} = ₹\ 9.50$

* No. of Right Shares $= 1{,}000 \times \frac{1}{5} = 200$ shares

Step 2: RAF $= \frac{10}{9.50}$

BEPS for Current Year [20X1] $= \frac{1{,}10{,}000}{\left[1{,}000 \times \frac{10}{9.5} \times \frac{3}{12}\right] + \left[1{,}200 \times \frac{9}{12}\right]} = ₹\ 94.57$

BEPS for Previous Year [20X0] (Original) $= \frac{1{,}00{,}000}{1{,}000} = ₹\ 100$

BEPS for Previous Year [20X0] (Restated) $= \frac{1{,}00{,}000}{1{,}000 \times \frac{10}{9.5}} = ₹\ 95$

Calculation of Basic EPS in case of Participating Preference Shares

- Participating Preference Shares are those Preference Shares which also participate in Undistributed Earnings [i.e. Right in Earnings remaining after distribution of dividend on Equity Shares].

- Steps to be followed to Calculate Basic EPS in this case :-

Step 1: Calculate Undistributed Earnings

PAT	xxx
(–) Dividend distributed on Preference Shares	(xxx)
(–) Dividend distributed on Equity Shares	(xxx)
	xxx

Step 2: Now, Allocate Undistributed Earnings to Equity Shares & Participating Preference Shares [By Assuming Allocation per Equity Share as 'x' & accordingly Allocation per Participating Preference Share is decided as per the information given in question]

⇓

Then, Make & Solve the Equation :

$$\text{Undistributed Earnings} = \left[\text{No. of Equity Shares} \times \text{Allocation of Undistributed Earnings per Equity Share}\right] + \left[\text{No. of Participating Preference Shares} \times \text{Allocation of Undistributed Earnings Per Participating Preference Share}\right]$$

Step 4: Basic EPS

⇒ Dividend distributed per Equity Share + Allocated Undistributed Earnings Per Equity Share (as calculated in Step 2)

Diluted EPS

- Diluted EPS means Reduction in Basic EPS calculated on the assumption that Potential Equity Shares are issued.

- Potential Equity Shares [PES] include Convertible Preference Shares, Convertible Bonds | Debentures, Options | Warrants, Contingent Shares.

Calculation of Diluted EPS

$$\text{DEPS} = \frac{\text{Profit | Loss used in BEPS} + \text{Adjustment in Earnings due to PES}}{\text{WANES used in BEPS} + \text{Adjustment in Shares due to PES}}$$

If it is Less than BEPS
⇓
It is dilutive & Hence, Reported as DEPS

If it is More than BEPS
⇓
It is Anti Dilutive & Hence, Not Reported as DEPS
⇓
Consider DEPS as same as BEPS

Note:- Sometimes question asks to Calculate Incremental EPS for PES

$$\text{Incremental EPS} = \frac{\text{Adjustment in Earnings due to PES}}{\text{Adjustment in Shares due to PES}}$$

Adjustment due to Potential Equity Shares in Calculation of Diluted EPS

Potential Equity Share [PES]	Adjustment in Earnings [Numerator]	Adjustment in Shares [Denominator]	Apply Time Factor in Numerator & Denominator: FROM Later of	Apply Time Factor in Numerator & Denominator: TO Earlier of
(1) Convertible Instruments • Convertible Preference Shares • Convertible Debentures / Bonds	 + Preference Dividend + Interest (1−Tax)	 + No. of Equity Shares on Conversion + No. of Equity Shares on Conversion	Year Beginning OR Convertible Instrument Issue Date	Year End OR Conversion Date
(2) Options | Warrants	–	No. of Equity Shares Under Options × $\left[\frac{\text{Market Price} - \text{Exercise Price}}{\text{Market Price}}\right]$	Year Beginning OR Grant Date	Year End OR Exercise Date
(3) Contingent Shares [It means shares to be issued in Business Combination subject to fulfillment of any Condition in future. Eg:- Opening Retail Stores, Profit Targets, etc.]	–	No. of Equity Shares Promised	Year Beginning OR Contingent Share Agreement Date	Year End OR Share Issue Date

Note :- (for Convertible Instruments)

(i) While calculating adjustment in earnings, Also consider all other impacts due to PES like Increase in Management Bonus along with its Tax impact, Fair Value Gain | Loss, etc.

(ii) If there are Multiple Conversion Ratios [i.e. Multiple Possible Scenarios for No. of Equity Shares on conversion], then Consider the Conversion Ratio involving Maximum No. of Equity Shares on Conversion.

Calculation of Diluted EPS in case of Multiple Potential Equity Shares

Steps to be followed to solve the question if more than 1 type of PES are given in question :-

Step 1: Calculate Incremental EPS for each type of PES

Step 2: Rank each PES in ascending order of Incremental EPS
[i.e. Most Dilutive PES (Lowest Incremental EPS) are Ranked First]

Step 3: Calculate Diluted EPS by considering each PES one by one in order of Ranking on a cumulative basis.
[i.e. firstly, Calculate DEPS by considering Rank 1 PES and then calculate DEPS by considering Rank 1 & Rank 2 PES and so on.]

Step 4: Diluted EPS will be Lowest of All the EPS calculated in Step 3.

Other Topics

Presentation of EPS

- Entity shall present BEPS & DEPS on the face of Statement of Profit & Loss.
- Further, Entity needs to disclose EPS from
  → Continuing Operations
  → Discontinued Operations
  → Total Operations
- If DEPS calculated for Continuing Operations is

Dilutive
⇓
Then, Calculate & Present DEPS for Discontinued Operations and Total Operations irrespective of whether their DEPS is dilutive or anti-dilutive

Anti-Dilutive
⇓
Then, Consider DEPS as same as BEPS for Continuing Operations, Discontinued Operations and Total Operations
⇓
Do not calculate DEPS separately for any of the Operations

Calculation of EPS in Consolidated Financial Statements [CFS]

- EPS calculated for Consolidated Financial Statements is known as Group EPS or Consolidated EPS.
- $$\text{Group's Basic EPS} = \frac{\text{Profit / Loss attributable to Equity Shareholders of Parent Entity}}{\text{Weighted Average No. of Ordinary Equity Shares in Parent Entity}}$$

Here,
→ Profit / Loss attributable to Equity Shareholders of Parent Entity = Parent's own Profit / Loss attributable to its Equity Shareholders + [No. of Equity Shares of Subsidiary held by Parent × BEPS of Subsidiary]

- Group's Diluted EPS = $\dfrac{\text{Profit | Loss attributable to Equity Shareholders of Parent Entity adjusted due to effect of PES}}{\text{Weighted Average No. of Ordinary Equity Shares in Parent Entity adjusted due to effect of PES}}$

Here,

→ Profit | Loss attributable to Equity Shareholders of Parent Entity adjusted due to effect of PES = Parent's own Profit | Loss attributable to its Equity Shareholders + [No. of Equity Shares (including) Diluted Shares of Subsidiary held by Parent × DEPS of Subsidiary] + Parent's own adjustment in Earnings due to its PES [if any]

→ Weighted Average No. of Ordinary Equity Shares in Parent Entity adjusted due to effect of PES = Weighted Average No. of Ordinary Equity Shares in Parent Entity + Parent's own adjustment in Shares due to its PES [If Any]

Financial Reporting

Annual Financial Reporting

↓

Preparation of Financial Statements for 1 Financial Year

Eg:- 1.4.20x1 to 31.3.20x2 [12 Months]

Interim Financial Reporting

↓

Preparation of Financial Statements for less than 1 Financial Year

Eg:- 1.4.20x1 to 30.6.20x1 [3 Months]

Preparation of Interim Financial Report

- Company can prepare Interim Financial Statements for the Interim Period as follows:-

As a Complete Set of Financial Statements

↓

Detailed Financial Statements as per Ind AS 1 & Schedule III

OR

As a Condensed Set of Financial Statements

↓

Condensed Financial Statements having Headings & Sub-headings with Selected Notes

- Interim Financial Statements are required to be presented for following periods [for Comparatives Purpose]:-

Example:- If Interim Reporting Period is 1.7.20x1 to 30.9.20x1 [3 Months]

Balance Sheet

- As at the end of Current Interim Period [B/s as on 30.9.20x1]
- Comparative Balance Sheet as at the end of Previous Financial Year [B/s as on 31.3.20x1]

Statement of Profit & Loss

- For Current Interim Period [1.7.20x1 to 30.9.20x1]
- Comparative P&L for Current Year to Date [1.4.20x1 to 30.9.20x1]
- Comparative P&L for Comparable Interim Period of Previous Financial Year [1.7.20x0 to 30.9.20x0]
- Comparative P&L for Comparable Year to Date of Previous Financial Year [1.4.20x0 to 30.9.20x0]

Statement of Changes in Equity / **Statement of Cash Flows**

- For Current Year to Date [1.4.20x1 to 30.9.20x1]
- Comparative Statement for Comparable Year to Date of Previous Financial Year [1.4.20x0 to 30.9.20x0]

Recognition of Items in Interim Financial Statements

All items, i.e. Assets, Liabilities, Income & Expenses are recognised in Interim Financial Statements using Same Principles of Accounting as for Annual Financial Statements as follows:-

(1) Any Income earned or Expense incurred in the Interim Reporting Period:-

- It should be recognised completely in the Interim Period in which they are earned or incurred.
- Expenses should not be deferred to the upcoming Interim Periods on the basis that Sales will be more in upcoming Interim Periods.

Example :- Bad Debts, Sales Promotion Expense, Depreciation, Employee Benefits Expense, Finance Costs, Administrative Expenses, Exceptional Loss, etc. incurring in a Interim Period should be recognised in that Interim Period only

⇓

These will not be deferred to the upcoming Interim Periods in any case

(2) <u>Income Tax Expense for the Interim Reporting Period</u> :-

It is recognised in each Interim Reporting Period using Weighted Average Tax Rate (WATR) as follows :

Step 1 : Calculate Estimated Annual Income

Step 2 : Calculate Estimated Annual Tax

⇒ [Estimated Annual Income − Carried Forward Loss as per Income Tax Act (if any)] × Applicable Tax Rate

Step 3 : Weighted Average Tax Rate [WATR] = $\dfrac{\text{Estimated Annual Tax [Step 2]}}{\text{Estimated Annual Income [Step 1]}} \times 100$

Step 4 : Income Tax Expense for each Interim Period

⇒ Profit / (Loss) of each Interim Period × WATR

<u>Notes</u> :-

(i) If Estimated Annual Tax is 'Zero' because Estimated Annual Income is 'Zero', then WATR will not be calculated. Tax Rate as given in the question will be used for calculating Income Tax Expense for each Interim Period.

(ii) If Different Tax Rates are applicable for 2 different Financial Years

and

Some Interim Period falls in 1 Financial Year & Some Interim Period falls in another Financial Year

⇓

Then, WATR will not be calculated. Applicable Tax Rate for each Interim Period [with respect to financial Year] will be used for calculating Income Tax Expense for each Interim Period.

(iii) If Income under different heads are given in question [Example : Normal Income & Capital Gains] which are Taxable at different Tax Rates, then 2 different Tax Rates will be used for calculating Income Tax Expense for each Interim Period as follows :

→ For Normal Income ⇒ WATR

→ For Capital Gains ⇒ Applicable Tax Rate on Capital Gains

(3) <u>Allocation of Fixed Overheads to Production Units in each Interim Reporting Period</u> :-

- Fixed Overhead per unit is calculated on the basis of Normal Production Units or Actual Production Units, whichever is Higher as per Ind AS 2
  [Production Units are considered on Year to Date Basis]

- Total Fixed Overhead [Year to Date] is allocated as follows:

Fixed Overhead Allocated to Actual Production Units (Year to Date)
[Absorbed Fixed Overhead]
⇓
Actual Production Units [Year to Date]
×
Fixed Overhead per unit

Remaining Fixed Overhead expensed to P&L
[Unabsorbed Fixed Overhead]
⇓
Balancing Figure
⇓
Total Fixed Overhead [Year to Date]
−
Absorbed Fixed Overhead [Year to Date]

Introduction to Ind AS 36

- Impairment of Assets means decline in value of assets due to changes in technological or legal environment or physical damage of asset.

- This Ind AS is applicable to following Assets :
  - PPE [As per Ind AS 16]
  - Intangible Assets [As per Ind AS 38]
  - Investment Property [As per Ind AS 40]
  - Goodwill Acquired in Business Combination [As per Ind AS 103]

Recognition & Measurement of Impairment Loss [IL] on an Individual Asset

Steps to be followed for Calculation & Recognition of Impairment Loss on Individual Asset :

Step 1 : Identify whether the Asset is Impaired [Impairment Testing]

Asset is impaired if its Carrying Amount > Recoverable Amount

Step 2 : Calculate Impairment Loss

Impairment Loss = Carrying Amount - Recoverable Amount

Step 3 : Recognition of Impairment Loss

- Impairment Loss is generally recognised in P&L

  ↓

  However, If there is any balance in Revaluation Surplus [OCI] relating to Impaired Asset, then Impairment Loss is firstly recognised in Revaluation Surplus [OCI] upto any balance existing in it.

- Journal Entry :

(i) Impairment Loss A/c	xxx	
To Asset A/c		xxx
(ii) Revaluation Surplus [OCI] A/c	upto Balance in this A/c	
P&L A/c	Balancing figure	
To Impairment Loss A/c		xxx

Step 4 : Revised Carrying Amount [RCA]

RCA = Carrying Amount after Impairment Loss is charged

= Carrying Amount before Impairment Loss - Impairment Loss

* Depreciation will be charged on this RCA in future

Note :-

(i) When Impairment Testing needs to be done :

Intangible Assets which are not amortised
[Example : Goodwill acquired in Business Combination]
⇓
Impairment Testing should be done Annually

Impairment Testing should be done if there are any indications that asset is Impaired
[Example : Changes in technological or legal environment or physical damage of asset]

(ii) Recoverable Amount :

→ Recoverable Amount of an asset is Higher of < Fair Value Less Cost to Sell [FVLCTS] / Value in Use

(a) Fair Value Less Cost to Sell [FVLCTS] or Fair Value Less Cost to disposal

Fair Value as per Ind AS 113 (Market Value)	xxx
(-) Cost to sell / disposal (Transaction Cost i.e. Selling Expenses like Dismantling cost, Packaging Cost, Legal fees, etc.)	(xxx)
FVLCTS	xxx

(b) Value in Use

▸ Value in Use is the Present Value of future cash flows expected to be derived from Asset

Expected future Cash flows

To be Included
⇓
- Cash Inflow & Outflow from Continuing Use of Asset
- Net Cash Inflow from disposal of Asset at the end of its useful life [Residual Value]

To be Ignored
⇓
- Interest & Tax Expense
- Cash flow expected from future improvements not yet committed

[Example : future expectation to Invest in new technology which will reduce the cost of manufacturing]

Discount Rate to be used
⇓
It should be Pre Tax Cost of Capital

▸ If Cash flows are in foreign currency, then Present Value of Cash flows is calculated by discounting the foreign currency cash flows using foreign currency discounting rate
⇓
And then Convert such Present Value in Functional Currency using Spot Exchange Rate on the date of Value in Use Calculation

→ If FVLCTS of an asset is not available, then Value in Use is considered as Recoverable Amount

→ If Value in Use of an asset is not available, then Recoverable Amount of such asset cannot be determined [i.e. Impairment of such asset will be done in CGU]

Example 1:

A ltd. purchased a PPE for ₹ 1,00,000 on 1st April 20X1. Its useful life is 10 years. On 31st March 20X3, A ltd. estimates the FVLCTS & Value in Use of PPE as ₹ 65,000 & ₹ 72,000 respectively.

Calculate the Impairment Loss, Revised Carrying Amount & Subsequent Depreciation p.a. thereon.

Solution:

Step 1: Impairment Testing

Carrying Amount as on 31st March 20X3:

Carrying Amount on 1st April 20X1	1,00,000
(-) Depreciation for 2 years $\left[\frac{100000}{10} \times 2\right]$	(20,000)
	80,000

Recoverable Amount on 31st March 20X3 is Higher of ₹ 65,000 & ₹ 72,000, i.e. ₹ 72,000

Since Carrying Amount > Recoverable Amount ; Impairment Loss is there.

Step 2: Impairment Loss = 80,000 - 72,000 = ₹ 8,000

Step 3: Journal Entry

Impairment Loss A/c (P&L)	8,000	
To PPE A/c		8,000

Step 4: Revised Carrying Amount = 80,000 - 8,000 = ₹ 72,000

Subsequent Depreciation p.a. from 3rd Year onwards = $\frac{₹\ 72,000}{8 \text{ years}}$ = ₹ 9,000 p.a.

Reversal of Impairment Loss on Individual Asset

- Impairment Loss recognised on an asset in earlier years can be reversed if on date of reversal its Carrying Amount < Recoverable Amount

- Steps to be followed for Reversal of Impairment Loss on Individual Asset:

Step 1: Calculate Carrying Amount of Asset on date of reversal of Impairment Loss

Step 2: Calculate Carrying Amount at which asset should be shown after reversal of IL

⇓

Lower of

Recoverable Amount of Asset on date of Reversal of IL

Carrying Amount of Asset on date of Reversal of IL if this Asset were never Impaired

Step 3: Calculate Amount of Reversal of Impairment Loss

⇒ Step 2 - Step 1

Step 4 : Recognition of Reversal of Impairment Loss

→ Reversal of Impairment Loss is generally recognised in P & L

⇓

However, If Impairment Loss is recognised in Revaluation Surplus [OCI] in earlier years, then Reversal of Impairment Loss is firstly recognised in Revaluation Surplus [OCI] upto Impairment Loss recognised in Revaluation Surplus [OCI] in earlier years.

→ Journal Entry

(i) Asset A/c	xxx		
To Impairment Loss Reversal A/c		xxx	
(ii) Impairment Loss Reversal A/c	xxx		
To Revaluation Surplus [OCI] A/c			upto IL recognised in earlier years
To P&L A/c			Balancing figure

Step 5 : Revised Carrying Amount [RCA]

RCA = Carrying Amount after Reversal of IL

= Carrying Amount before Reversal of IL + Reversal of IL

* Depreciation will be charged on this RCA in future

Note : If Recoverable Amount of asset becomes higher than Carrying Amount only due to unwinding of discount on future cash flows (i.e. Value in Use), then Impairment Loss cannot be reversed.

Example 2 :

In Continuation to Example 1 ; On 31st March 20x6, Recoverable Amount of PPE is estimated to be ₹ 51,000.

Calculate Reversal of IL, Revised Carrying Amount & Subsequent Depreciation p.a. thereon.

Solution :

Step 1 : Carrying Amount on 31st March 20x6

Carrying amount on 31st March 20x3 after charging IL	72,000
(-) Depreciation for 3 Years $\left[\frac{72,000}{8} \times 3\right]$	(27,000)
	45,000

Step 2 : Carrying Amount at which PPE should be shown on 31st March 20x6

Recoverable Amount = ₹ 51,000

Carrying Amount on 31.3.20x6 if PPE were never impaired

Carrying Amount on 1.4.20x1	1,00,000
(-) Depreciation for 5 Years $\left[\frac{1,00,000}{10} \times 5\right]$	(50,000)
	₹ 50,000

Lower, i.e. ₹ 50,000

Step 3 : Reversal of IL = 50,000 – 45,000 = ₹ 5,000

Step 4 : Journal Entry

PPE A/c	5,000	
To IL Reversal A/c (P&L)		5,000

Step 5 : Revised Carrying Amount on 31.3.20x6 = 45,000 + 5,000 ⇒ ₹ 50,000

Subsequent Depreciation p.a. from 6^{th} Year onwards $= \frac{₹ 50,000}{5 \text{ years}} = ₹ 10,000$ p.a.

Recognition & Measurement of Impairment Loss [IL] on Cash Generating Unit [CGU]

(1) **Cash Generating Unit [CGU] :-**

- Sometimes Recoverable Amount of Individual Asset cannot be determined because that asset cannot generate independent cash flows from which Value in Use is calculated.

⇓

So, Impairment of such asset will be done in CGU

- CGU is the smallest group of assets which are capable of generating independent cash flows.

Example 3 :

A ltd. (Juice Company) prepares juice concentration by using Machine 1 & Pack it in the bottles for sale by using Machine 2.

Here, Machine 1 & 2 cannot generate independent cash flows for the business.

Hence, they should be clubbed together as a CGU for Impairment Testing because they can generate independent cash flows together.

- Goodwill acquired in Business Combination & Corporate Assets [Eg: Office Building] cannot be tested for impairment individually because they cannot generate independent cash flows.

Since Goodwill & Corporate Assets contribute Other Assets in generating cash flows

⇓

So, Impairment of Goodwill & Corporate Assets will be done in CGU only

Note : Allocation of Goodwill & Corporate Assets to multiple CGUs for Impairment Testing :-

→ Goodwill & Corporate Assets are allocated to multiple CGUs on the basis/ratio given in question.

→ If question ask to allocate on "Pro rata basis", then Allocate these to multiple CGUs in [Carrying Amount of Other Assets in CGU × Useful life of CGU] Ratio of each CGU.

→ There may be some Unallocable Goodwill or Corporate Asset which will be tested for impairment in a different manner.

(2) Steps to be followed for Calculation & Recognition of Impairment Loss on CGU :

Step 1 : Identify whether the CGU is Impaired [Impairment Testing]

CGU is impaired if its Carrying Amount > Recoverable Amount

- Calculation of Carrying Amount of CGU ⇒

Carrying Amount of PPE in CGU	xxx
Carrying Amount of Intangible Asset in CGU	xxx
Carrying Amount of Current Asset [Eg : Inventory] in CGU	xxx
Carrying Amount of Goodwill allocated to CGU	xxx
Carrying Amount of Corporate Asset allocated to CGU	xxx
	xxx

Step 2 : Calculate Impairment Loss

Impairment Loss = Carrying Amount of CGU - Recoverable Amount of CGU

⇓

This Impairment Loss will be borne by Assets in CGU as following :

- Firstly, By Goodwill [Upto Carrying Amount of Goodwill]
- Then, By that Asset which can be tested for Impairment individually also [Upto the Amount of Impairment Loss calculated as per topic 'Recognition & Measurement of Impairment Loss on Individual Asset']
- At Last, Remaining Impairment Loss of CGU will be borne by all other assets in CGU (including Corporate Assets) in ratio of their Carrying Amounts

Note :- No Impairment Loss of CGU will be borne by Current Asset [Eg: Inventory] in CGU since this asset is out of scope of Ind AS 36

Step 3 : Calculate Impairment Loss for Unallocable Goodwill or Unallocable Corporate Asset [if Any]

It is calculated by Impairment Testing for the Entity as a whole as follows :

Particulars	CGU_1	CGU_2	CGU_3	Unallocable Goodwill or Corporate Asset	Total
Carrying Amount	xx	xx	xx	xx	xx
(-) IL on each CGU as calculated in Step 2	(xx)	(xx)	(xx)	–	(xx)
RCA of each CGU after Impairment	xx	xx	xx	xx	$\boxed{xx}$ → A
Recoverable Amount of Entity as a whole					$\boxed{xx}$ → B

Now, If A > B, then this Impairment Loss will be borne by Unallocable Goodwill or Unallocable Corporate Asset only ; because CGUs are already impaired in Step 2.

Step 4 : Recognition of Impairment Loss

- Impairment Loss is generally recognised in P&L

⇓

However, If there is any balance in Revaluation Surplus [OCI] relating to Impaired Asset, then Impairment Loss is firstly recognised in Revaluation Surplus [OCI] upto any balance existing in it.

- Journal Entry :

(i) Impairment Loss A/c	xxx	
To Asset A/c		xxx
(ii) Revaluation Surplus [OCI] A/c	upto Balance in this A/c	
P&L A/c	Balancing figure	
To Impairment Loss A/c		xxx

Step 5 : Revised Carrying Amount [RCA] of each Asset in CGU

RCA = Carrying Amount after Impairment Loss is charged

= Carrying Amount before Impairment Loss − Impairment Loss

* Depreciation will be charged on this RCA in future

Example 4 :

On 31st March 20X1, A ltd. has a CGU having following Assets with their Carrying Amounts as below :-

Machine A = ₹ 5,25,000
Machine B = ₹ 2,50,000
Machine C = ₹ 1,00,000
Inventory = ₹ 2,00,000
Goodwill = ₹ 1,50,000

Recoverable Amount of CGU is ₹ 10,00,000.
Machine A can be tested for Impairment individually also, its Recoverable Amount is ₹ 5,00,000.
Calculate Impairment Loss & Revised Carrying Amount of each asset after impairment.

Solution :

Step 1 : Impairment Testing

Carrying Amount of CGU ⇒ 5,25,000 + 2,50,000 + 1,00,000 + 2,00,000 + 1,50,000
⇒ ₹ 12,25,000

Recoverable Amount of CGU ⇒ ₹ 10,00,000

Since Carrying Amount > Recoverable Amount ; Impairment Loss is there.

Step 2 : Impairment Loss in CGU = 12,25,000 − 10,00,000
= ₹ 2,25,000
⇓
This Impairment Loss will be borne by following assets :

(i) Goodwill = ₹ 1,50,000

(ii) Machine A = upto Individual Impairment Loss on it
i.e. 5,25,000 − 5,00,000 ⇒ ₹ 25,000

(iii) Machine B & Machine C = Remaining IL [i.e. 2,25,000 − 1,50,000 − 25,000 = ₹ 50,000]

in ratio of Carrying Amounts of Machine B & C [i.e. 2,50,000 : 1,00,000 or 5 : 2]

⇓

Machine B = 50,000 × $\frac{5}{7}$ = ₹ 35,714

Machine C = 50,000 × $\frac{2}{7}$ = ₹ 14,286

(iv) No Impairment Loss will be borne by Inventory (out of scope of Ind AS 36)

Step 3 : Not Applicable

Step 4 : Not Asked to Pass Journal Entry in question

Step 5 : Revised Carrying Amount of each asset in CGU after Impairment

	Goodwill	Machine A	Machine B	Machine C	Inventory	Total of CGU
Carrying Amt.	1,50,000	5,25,000	2,50,000	1,00,000	2,00,000	12,25,000
(−) IL	(1,50,000)	(25,000)	(35,714)	(14,286)	-	(2,25,000)
RCA	-	5,00,000	2,14,286	85,714	2,00,000	10,00,000

Note : If Goodwill acquired in Business Combination is Partial Goodwill [i.e. NCI is measured as per PSNA method], then Unrecognised Goodwill attributable to NCI is also considered for calculating Impairment Loss only.

Unrecognised Goodwill attributable to NCI = $\frac{\text{Partial Goodwill}}{\text{Parent's Share}}$ × NCI Share

Example 5 :

A ltd. acquires 80% shares of B ltd. Goodwill arising on acquisition is ₹ 800 (NCI is measured at PSNA). Carrying Amount of Net Assets (excluding Goodwill) is ₹ 2,700. Calculate IL allocable to Parent & NCI and the Revised Carrying Amount if :

(a) Recoverable Amount of CGU is ₹ 2,000

(b) Recoverable Amount of CGU is ₹ 2,800

Solution :

(a) If Recoverable Amount of CGU is ₹ 2,000 :

	Goodwill	Net Assets	Total of CGU
Carrying Amount	800	2,700	3,500
(+) Unrecognised Goodwill for NCI $\left[\frac{800}{80\%} \times 20\%\right]$	200	-	200
	1,000	2,700	3,700
Recoverable Amount of CGU			2,000
Total Impairment Loss			1,700
Impairment Loss Allocation	(1,000)	(700)	
Revised Carrying Amount	-	2,000	2,000

Impairment Loss allocable to:	Parent	NCI
On Goodwill	800 [1,000 x 80%]	–
On Other Assets	560 [700 x 80%]	140 [700 x 20%]
	1,360	140

(b) If Recoverable Amount of CGU is ₹ 2,800:

	Goodwill	Net Assets	Total of CGU
Carrying Amount	800	2,700	3,500
(+) Unrecognised Goodwill for NCI $\left[\frac{800}{80\%} \times 20\%\right]$	200	–	200
	1,000	2,700	3,700
Recoverable Amount of CGU			2,800
Total Impairment Loss			900
Impairment Loss Allocation	(900)		
	100	2,700	2,800

Since only Goodwill attributable to Parent has been recorded in books ⇒

Revised Carrying Amount in Books	80 [100 x 80%]	2,700	2,780

Impairment Loss allocable to:	Parent	NCI
On Goodwill	720 [900 x 80%]	–
On Other Assets	–	–
	720	–

Reversal of Impairment Loss on CGU

- Impairment Loss recognised on an CGU in earlier years can be reversed if on date of reversal its Carrying Amount < Recoverable Amount

- Steps to be followed for Reversal of Impairment Loss on CGU:

Step 1: Calculate Carrying Amount of each asset in CGU on date of reversal of IL

Step 2: Calculate Amount of Reversal of Impairment Loss

Maximum Possible Amount of Reversal of Impairment Loss = Recoverable Amount of CGU on date of Reversal − Carrying Amount of CGU on date of Reversal

⇓

This Reversal of Impairment Loss will be done in Assets in CGU as follows:

→ firstly, To that Asset for which Recoverable Amount is also available individually [Upto the Amount of Reversal of Impairment Loss calculated as per Topic 'Reversal of Impairment Loss on Individual Asset'.]

→ Then, Remaining Maximum Possible Amount of Reversal of Impairment Loss will be done in all other assets which were impaired earlier in CGU (excluding Goodwill) in Ratio of their Carrying Amounts on date of reversal

[But Revised Carrying Amount of these Assets after above Reversal should not exceed their Carrying Amount on date of reversal if these Assets were never impaired.]

Note: No Reversal of Impairment Loss will be done in Goodwill.

Step 3 : Recognition of Reversal of Impairment Loss

→ Reversal of Impairment Loss is generally recognised in P & L

⇓

However, If Impairment Loss is recognised in Revaluation Surplus [OCI] in earlier years, then Reversal of Impairment Loss is firstly recognised in Revaluation Surplus [OCI] upto Impairment Loss recognised in Revaluation Surplus [OCI] in earlier years.

→ Journal Entry

(i) Asset A/c	xxx		
To Impairment Loss Reversal A/c		xxx	
(ii) Impairment Loss Reversal A/c	xxx		
To Revaluation Surplus [OCI] A/c			upto IL recognised in earlier years
To P&L A/c			Balancing figure

Step 4 : Revised Carrying Amount [RCA] of each Asset in CGU

RCA = Carrying Amount after Reversal of IL

= Carrying Amount before Reversal of IL + Reversal of IL

* Depreciation will be charged on this RCA in future

Example 6 :

In Continuation to Example 4 ;

Remaining Useful Life of each Machine on 31st March 20X1 was 10 years.

On 31st March 20X2, Recoverable Amount of CGU becomes ₹ 11,00,000 and Recoverable Amount of Machine A becomes ₹ 4,80,000.

Calculate Reversal of Impairment Loss & the Revised Carrying Amount after Reversal.

Solution:

Step 1: Carrying Amount of each asset in CGU on date of reversal

	Goodwill	Machine A	Machine B	Machine C	Inventory	Total of CGU
CA after IL on 31.3.X1	-	500,000	2,14,286	85,714	2,00,000	10,00,000
(-) Dep. for 1 Year	-	(50,000)	(21,429)	(8,571)	-	(80,000)
	-	4,50,000	1,92,857	77,143	2,00,000	9,20,000

Step 2 : Maximum Possible Reversal of IL = 11,00,000 − 9,20,000

= ₹ 1,80,000

⇓

This Reversal of IL will be done in Assets in CGU as follows:

(i) Machine A = upto Individual Reversal of Impairment Loss on it i.e. It can be shown at Lower of

Recoverable Amount = ₹ 4,80,000

Carrying Amount if it was never impaired = 5,25,000 (cost) - 52,500 (Dep. for 1 Year) = ₹ 4,72,500

∴ Reversal of IL = 4,72,500 - 4,50,000 = ₹ 22,500

(ii) Machine B & Machine C = Remaining Reversal of IL [i.e. 180000 - 22,500 = ₹ 1,57,500] in ratio of Carrying Amounts of Machine B & C [i.e. 192,857 : 77,143 or 5 : 2]

⇓

Machine B = 1,57,500 × $\frac{5}{7}$ = ₹ 1,12,500

Machine C = 1,57,500 × $\frac{2}{7}$ = ₹ 45,000

[Carrying Amount of Machine B & C if never impaired
Machine B = 2,50,000 (Cost) - 25,000 (Dep. for 1 Year) = ₹ 2,25,000
Machine C = 1,00,000 (cost) - 10,000 (Dep. for 1 Year) = ₹ 90,000]

∴ Reversal to be done in

Machine B = 2,25,000 - 1,92,857 = ₹ 32,143

Machine C = 90,000 - 77,143 = ₹ 12,857

(iii) No Reversal of Impairment Loss will be done in Goodwill.

Step 3: Not Asked to Pass Journal Entry in question

Step 4: Revised Carrying Amount of each asset in CGU after Reversal

	Goodwill	Machine A	Machine B	Machine C	Inventory	Total of CGU
Carrying Amount	–	4,50,000	1,92,857	77,143	2,00,000	9,20,000
(+) Reversal of IL	–	22,500	32,143	12,857	–	67,500
RCA after Reversal	–	4,72,500	2,25,000	90,000	–	9,87,500

Liability

Liability is a

Present Obligation arising from Past Events **and** Settlement of Obligation will result in outflow of resources

⇓

It can be

Legal Obligation that derives from a Contract or Legislation

OR

Constructive Obligation that derives from Past Practice or Commitment of the Entity

Provisions

(1) Meaning of Provision :-

Provision is a Liability of Uncertain Amount or Timing, i.e.

Present Obligation arising from Past Events **and** Outflow of Resources is Probable [50% or More] **and** Amount can be estimated reliably

(2) Recognition of Provision :-

- Provision shall be recognised as a Liability in Financial Statements.
- Amount of Provision :

→ It should be measured as follows [Best Estimate of Expenditure to be incurred]:

If there are many possible outcomes, then calculate Expected Value by using the Probability of each outcome

If there is only 1 Possible outcome, then consider such amount directly

→ If Expenditure is to be incurred after 1 Year, then Provision should be recognised at Present Value by discounting the expenditure using Pre Tax Discounting Rate

and

Charge Interest Expense (Finance Cost) on such Provision to unwind the discount over the period in P&L at discounting rate.

→ If there is Risk that Actual Outflow would be more than the Expected Present Value of Outflow, then Risk Adjustment is done by adding it to the Expected Present Value of Outflow as follows

Expected Present Value of Outflow	xxx
(+) Risk Adjustment @ Risk Factor %	xxx
Provision Amount	xxx

→ Journal Entries

(i) P&L A/c
    To Provision A/c

(ii) Interest Expense A/c (Finance Cost)
    To Provision A/c

[Opening Balance of Provision × Discounting Rate]

- Provision should be Reviewed at each Balance Sheet Date & adjusted to reflect the current best estimate. If it is no longer required, then it should be reversed.

Note:- If Entity can avoid any expenditure by its future actions, then No Provision is recognised for such expenditure.

Example: Future Operating Costs like Overhauling or Inspection of Ships, Future Operating Losses, etc.

(3) Special Points:-

- Onerous Contract:

→ It is a Contract in which unavoidable costs of meeting the obligation exceeds economic benefits to be received under it.

→ Provision is recognised on Onerous Contract at Lower of

OR

Loss on fulfilling the Onerous Contract | Penalty for Non Performance of the Contract [i.e. Exiting from the Contract]

- Restructuring:

→ It is a plan to change the scope of business or manner of conducting business.

Example: Discontinuing a Line of business or Closure of Operations in an Area.

→ Provision for Restructuring Costs is recognised when Constructive Obligation to Restructure arises, i.e.

AND

Entity has a detailed Formal Plan | Entity has raised a valid expectation for restructuring by announcing the Plan

→ Amount of Provision for Restructuring Costs include only direct expenditures arising from Restructuring i.e. Staff Termination | Redundancy Costs, Compensation to Customer, Lease Termination Cost, etc.

[Relocation | Retraining Cost for employees remained in Company & Impairment on Assets are not considered in Provision Amount for Restructuring]

- Reimbursements:

→ If Expenditure required to settle a obligation is expected to be reimbursed by other party & it is virtually certain [More than 95% Chance] that reimbursement will be received

- Reimbursement shall be recognised as a Separate Asset in Balance Sheet
- Provision Expense & Reimbursement Income can be presented by Netting off in P&L
- Reimbursement shall not exceed Provision Amount

→ If Reimbursement is not virtually certain, then Disclose in Notes to Financial Statements.

Contingent Liabilities

(1) Meaning of Contingent Liability :-

Possible Obligation arising from Past Events that will be confirmed only on occurrence or non occurrence of uncertain future events

OR

Present Obligation arising from Past Events and

- Outflow of Resources is Not Probable [Less than 50%]

OR

- Amount cannot be estimated reliably

(2) Recognition of Contingent Liability :-

- Contingent Liability shall not be recognised But It should be disclosed in Notes in Financial Statements.
- However, If Possibility of Outflow is Remote [Less than 5%], then Disclosure is also not required.

Contingent Assets

(1) Meaning of Contingent Assets :-

Possible Asset arising from Past Events that will be confirmed only on occurrence or non occurrence of uncertain future events.

(2) Recognition of Contingent Assets :-

- If Inflow of Resources is Virtually Certain [More than 95%]
  ⇓
  It is no more a Contingent Asset. It becomes an Asset. So, Recognise the Asset.
- If Inflow of Resources is Probable But Not Virtually Certain [50% or More]
  ⇓
  Contingent Asset shall not be recognised But It should be disclosed in Notes in Financial Statements
- If Inflow of Resources is Not Probable [Less than 50%]
  ⇓
  Contingent Asset shall neither be recognised nor disclosed

Meaning of Intangible Assets

- Intangible Asset is an Asset which has
  - → No Physical Substance → i.e. Not Tangible
  - → Existence of FEB & Entity has Control over those FEB
    - * Control over FEB means
      - Power to Obtain those benefits
      - and
      - Ability to restrict others to Access those Benefits
  - → Identifiable → i.e. Separable & Transferable Individually OR Arises from a Contract

- **Some Examples of Intangible Assets are :-**

  Trade Mark, Patent, Copyright, Franchises, Non-Compete fee, License, Computer Software, Technical Know-How, Customer Lists, etc.

- **Following are Not Considered as Intangible Assets :-**
  - → Market Share since it is Not Identifiable
  - → Marketing & Advertisement Campaign [i.e. Promotional Activity] since FEB are Not Certain
  - → Staff Training Programme Since Entity has No Control over the Staff as they can Resign Anytime
  - → Cash Paid to obtain Skilled Staff Since Entity has No Control over the Staff as they can Resign Anytime

    [But if there is Some Restriction like Recruited Person have to Work for atleast Sometime, then It will be Intangible Asset]

Recognition Criteria

Intangible Asset is recognised in Books Only if

- Probable FEB
- and
- Cost can be measured reliably

Initial Recognition of Intangible Asset

(1) **If Intangible Asset is Purchased OR Internally Generated :-**

- Intangible Asset is recognised At Cost

- Cost includes Any directly Attributable Cost necessary to bring Intangible Asset to condition intended by Management

- Calculation of Cost of Intangible Asset :-

Purchase Price	xxx
(–) Trade Discount / Rebate	(xxx)
(+) Import Duty & Purchase Taxes like Entry Tax, GST etc. [Only if Non-Refundable]	xxx
(+) Legal Fee / Cost	xxx
(+) Professional fee / Consultant fee / Advisor fee	xxx
(+) Customisation Cost [Generally for Software]	xxx
(+) Testing Cost	xxx
(+) Employment Costs [Eg. Salary paid for Software Coding, etc.]	xxx
(+) Any other Development Phase Expense [In Case of Internally Generated Intangible Asset]	xxx
(+) Any Other Directly Attributable Cost	xxx
	xxx

Notes :-

(i) In Silent Situation, Assume All Taxes are Non-Refundable

(ii) Following Items are Not Included in Cost of Intangible Asset :-

→ Cost of Staff Training
→ Cost of Conducting Conference for introduction / launch of Intangible Asset
→ Cost of Advertisement or Promotion
→ Preliminary Expenses [Startup Cost]
→ Administrative, General, Selling & Allocated Overheads
→ Operating Losses
→ Purchase of Maintenance Contract of Intangible Asset
→ Subsequent Cost on Intangible Asset [Eg. Annual fee / Royalty as a percentage of Sales on Franchisee]
→ Cash Discount / Early Settlement Discount
→ Interest on Loan taken to purchase or internally generate the Intangible Asset (unless allowed by Ind AS 23)
→ Research Phase Expense [In Case of Internally Generated Intangible Asset]

(iii) Specific Points to remember in case of Internally Generated Intangible Asset

→ Intangible Asset is Internally Generated in 2 Phases

Research Phase

⇓

Planned Investigation to gain New Knowledge

⇓

Expense made during Research Phase is Not recognised as Intangible Asset

Development Phase

⇓

Application of Research Findings to develop the Intangible Asset

⇓

Development Phase Starts After Establishment of Technical feasibility & Regulatory Approval

[i.e. It is the Date on which Recognition Criteria of Internally Generated Intangible Asset is Met]

⇓

Expense made during Development Phase is recognised as Intangible Asset

→ Internally Generated Brands, Mastheads, Publishing Titles, Customer Lists, Goodwill are not recognised as Intangible Asset Since their Cost cannot be measured reliably

→ If Research Project (Expense on Research Phase) is Acquired in a Business Combination, then It is recognised as Intangible Asset At Fair Value

- Accounting of Intangible Asset (Journal Entry) :-

(i) At Beginning

→ For Intangible Asset Purchase | Internally Generated

Intangible Asset
    To Bank | Payables

(ii) At Each Year End

→ For Amortisation on Intangible Asset

Amortisation
    To Intangible Asset

OR

Amortisation
    To Provision for Amortisation / Accumulated Amortisation

→ For Transferring Amortisation to P&L

P&L
    To Amortisation

(2.) If Intangible Asset is Acquired on Deferred Settlement Terms

⇓

Same As in Ind AS 16

(3.) If Intangible Asset is Acquired in Exchange of Assets

⇓

Same As in Ind AS 16

(4.) If Goodwill is Acquired in a Business Combination

⇓

Apply Ind AS 103

Amortisation of Intangible Asset

(1.) Methods for Charging Amortisation

- Straight Line Method (SLM)

  ⇓

  $$\text{Amortisation} = \frac{\text{Cost} - \text{Residual Value}}{\text{Useful Life}}$$

- Diminishing | Reducing Balance Method (WDV)

  ⇓

  Amortisation = Opening Carrying Amount × Amortisation Rate

- Units of Production Method

  ⇓

  Amortisation is charged in Ratio of Estimated Production Units

  [If Estimated Production Units are Revised in future, then Amortisation is charged in Revised Ratio of Estimated Production Units from the Year in which Estimate has been Revised]

Note :-

(i.) Amortisation on Intangible Asset begins when it is Available for Use [i.e. Ready to Use]

(ii.) Amortisation on Intangible Asset ceases when it is
- Derecognised (i.e. Sold)
- OR
- Classified as Held for Sale [Ind AS 105]

(iii.) If there is a Change in Amortisation Method, Useful Life, Residual Value

⇓

It is a Change in Accounting Estimate

⇓

Prospective Effect will be given [i.e. Effect will be given in Remaining future Period]

* Also, In Case of Change in Amortisation Method, Useful Life, Residual Value; We Will use Carrying Amount instead of Cost in SLM Amortisation formula for calculating Amortisation for remaining future period

(iv.) Estimated Useful Life is considered [Legal Life of Intangible Asset is Not Relevant]

(2.) Accounting for Amortisation on Intangible Asset (Journal Entry) :- At Each Year End

- Amortisation
    To Intangible Asset

$\boxed{\text{OR}}$

Amortisation
    To Provision for Amortisation / Accumulated Amortisation

- P & L
    To Amortisation

$\boxed{\text{Subsequent Recognition of Intangible Asset (At Each Balance Sheet Date)}}$

⇓

Same As in Ind AS 16

$\boxed{\text{Other Points}}$

- Gain or Loss on Sale of Intangible Asset is recorded in P&L

Meaning of Investment Property

Land and Building [i.e. Property] Held for

- Rental to Others [Operating Lease]
- OR
- Capital Appreciation
- OR
- Undetermined Use

Recognition Criteria

Investment Property is recognised in Books Only if

- Probable FEB
- and
- Cost can be measured reliably

Initial Recognition of Investment Property

⇓

Same As in Ind AS 16

Depreciation of Investment Property

⇓

Same As in Ind AS 16

Component Accounting

⇓

Same As in Ind AS 16

Subsequent Recognition of Investment Property (At Each Balance Sheet Date)

- Investment Property will be shown At Cost Model Only
- Carrying Amount = Cost − Accumulated Depreciation − Accumulated Impairment Loss

Other Points

⇓

Same As in Ind AS 16

Property Held For More than 1 Purpose

- If some portion of Property is held for business (i.e. Owner Occupied) & some portion of Property is held for Rental (ie. Investment), then

If Entity is Able to Split them [i.e. If there is Separate legal title of each portion & they can be sold separately]

- Owner Occupied Property Portion ⇓ Apply Ind AS 16
- Investment Property Portion ⇓ Apply Ind AS 40

Otherwise

- If Owner Occupied Property Portion is Significant ⇓ Treat Complete Property as Owner Occupied Property ⇓ Apply Ind AS 16
- If Owner Occupied Property Portion is Insignificant ⇓ Treat Complete Property as Investment Property ⇓ Apply Ind AS 40

Note:- Significancy is related to Management's Judgement

Property given on Lease / Rental to Subsidiary Co. by its Parent Co. or Vice-Versa

It will be classified in Books as follows :-

- In Lessor's Separate Financial Statements ⇓ Investment Property [Ind AS 40]
- In Consolidated Financial Statements ⇓ Owner Occupied Property [Ind AS 16]

Transfer of Property To or From Investment Property in case of Change in Use

- Transfer should be done At Carrying Amount
- Examples of Transfer :-

(i) Commencement of Owner Occupation from Investment Property

[Ind AS 40 → Ind AS 16]

(ii) End of Owner Occupation to Investment Property

[Ind AS 16 → Ind AS 40]

(iii) Commencement of development to Sale in Ordinary Course from Investment Property

[Ind AS 40 → Ind AS 2]

(iv) Inception of Operating Lease on Building Held for Sale

[Ind AS 2 → Ind AS 40]

- It is Not Change in Accounting Policy or Prior Period Error. It is only due to Change in Use of Property
- Change in Use of Property should be Actual. [Mere Management's Intention of Change in Use of Property are Not Considered]

Disclosure regarding Investment Property in Notes to Financial Statements

(1) Fair Value Disclosure :-

- Entity is required to disclose Fair Value of Investment Property in Notes
- If Entity is not able to determine the Fair Value of Investment Property, then
  - If Investment Property is Under Construction ⇓ Determine the Fair Value when it is reliably measurable or Construction is completed (whichever is Earlier)
  - Otherwise ⇓ Disclose the Fact & Reasons thereof
- Also, Disclosure of Valuation Techniques & Key Inputs Used in Valuation is given as follows :-

Valuation Technique	Key Inputs Used in Valuation	Range of Inputs Used
(Name)	(Name)	(Unit)

(2) Measurement Disclosure of Carrying Amount :-

Gross Carrying Amount			Accumulated Depreciation			Net Carrying Amount
Opening Balance	Addition/ (Deletion)	Closing Balance	Opening Balance	During the Year	Closing Balance	Closing Balance
(A)	(B)	(C) = (A) + (B)	(D)	(E)	(F) = (D) + (E)	(G) = (C) − (F)
✓	✓	✓	✓	✓	✓	✓

(3.) Disclosure relating to Amount recognised in P&L for Investment Property :-

Particulars	Amount
Rental Income from Investment Properties	xxx
Less:- Direct Operating Expenses incurred to generate Rental Income	(xxx)
Profit Before Depreciation from Investment Properties	xxx
Less :- Depreciation during the year on Investment Properties	(xxx)
Profit from Investment Properties	xxx

Introduction to Ind AS 41

- This Ind AS prescribes accounting of following items for an entity engaged in Agriculture Activity :-

Biological Assets [Except Bearer Plants]
⇓
It means
- Living Plants
  Example: Cotton Plants, Wheat Crop, etc.
- Living Animals (Livestock)
  Example: Sheeps, Goats, Cattle, etc.

Agriculture Produce
⇓
It means harvested product from Biological Assets (i.e. Output of Biological Assets)

Example: Milk from Cows, Carcass from Goats, Wool from Sheeps, Cotton from Cotton Plants, etc.

Government Grants on Biological Assets

- This Ind AS does not apply to following items even if entity is engaged in Agriculture Activity :-

Bearer Plants
⇓
It means Living Plants which are used in production of Agriculture Produce for more than 12 Months
Example: Fruit Trees (Mango Tree), Rubber Trees, etc.
⇓
Ind AS 16 (PPE) will apply

PPE
Example: Land, Tractor, etc.
⇓
Ind AS 16 (PPE) will apply

Intangible Assets
Example: License for doing Agriculture Activity
⇓
Ind AS 38 (Intangible Assets) will apply

Accounting for Biological Assets

- Initial Recognition :-

Biological Asset is initially recognised at its Fair Value Less Costs to sell [FVLCTS] as follows:

Biological Asset A/c	FVLCTS	
Loss on Initial Recognition A/c [P&L]	Balancing figure	
To Bank A/c		Total Payment to Buy Biological Asset
To Gain on Initial Recognition A/c [P&L]		Balancing figure

Note:-

(i) Fair Value Less Costs to Sell :

Sales Price of Biological Asset	xxx
(-) Transportation Cost to transport the Asset to Auction Place borne by Seller	(xxx)
Fair Value of Biological Asset [As per Ind AS 113]	xxx
(-) Costs to Sell [Transaction Cost like Auctioneer's fee borne by Seller]	(xxx)
Fair Value Less Costs to Sell [FVLCTS]	xxx

(ii) Total Payment to Buy Biological Asset :

Purchase Price of Biological Asset	xxx
(+) Transportation Cost to transport the Asset to Entity's Farm borne by Buyer	xxx
(+) Transaction Cost like Auctioneer's fee borne by Buyer	xxx
	xxx

(iii) If FVLCTS cannot be measured reliably, then Entity can initially recognise Biological Asset at its Cost.

- **Subsequent Recognition [At Each Balance Sheet Date]:-**

Biological Asset is remeasured at their new FVLCTS on each Balance Sheet date.

⇓

Change in FVLCTS of Biological Asset from previous recognition will be recognised as Gain or Loss on Remeasurement of Biological Asset in P&L as follows:

If there is increase in FVLCTS

⇓

Biological Asset A/c
 To Gain on Remeasurement A/c [P&L]

If there is decrease in FVLCTS

⇓

Loss on Remeasurement A/c [P&L]
 To Biological Asset A/c

Note:- FVLCTS of a Biological Asset changes due to Price Change & Physical Change in the Biological Asset.

- **Recognition of New Born Calves [Animals के बच्चे होने पर]:-**

New Born Calves are recognised as an Income in P&L at their FVLCTS on Birth Date as follows:

Biological Asset A/c [New Born Calves]
 To Gain of New Born Calves (Physical Change) A/c [P&L]

Note:- New Born Calves will also be subsequently remeasured at their new FVLCTS on each Balance Sheet date.

- **Derecognition of Biological Asset:-**

(a) On Sale of Animal:

Bank A/c	Net Amount Received on Sale
Loss on Sale of Biological Asset A/c [P&L]	Balancing figure
To Biological Asset A/c	Proportionate Carrying Amount
To Gain on Sale of Biological Asset A/c [P&L]	Balancing figure

(b) On Death of Animal:

Loss on Death of Biological Asset A/c [P&L]	[Proportionate Carrying Amount of Biological Asset died]
To Biological Asset A/c	

(c) On Conversion of Biological Asset into Agriculture Produce [Slaughtering of Animal to get Carcass]:

Agriculture Produce A/c [Inventory]	FVLCTS of Agriculture Produce
Loss on Initial Recognition of Agriculture Produce A/c [P&L]	Balancing figure
To Biological Asset A/c	Proportionate Carrying Amount
To Bank A/c [Conversion Cost like Slaughtering Cost]	Cost Paid
To Gain on Initial Recognition of Agriculture Produce A/c [P&L]	Balancing figure

- Recognition of Expenses incurred on Biological Asset :-

→ Expenses are incurred on Biological Assets for their growth & maintenance. Example : Food Cost, Breeding Fee, Fertilisers, Seeds, etc.

→ These are recognised as an Expense in P&L as follows :

Expense incurred on Biological Asset A/c [P&L]	[Expense Amount incurred]
To Bank A/c	

Accounting for Agriculture Produce

- Initial Recognition :-

Agriculture Produce is initially recognised as an Income in P&L at its Fair Value Less Costs to sell [FVLCTS] as follows:

Agriculture Produce A/c [Inventory]	[FVLCTS of Agriculture Produce]
To Gain on Initial Recognition A/c [P&L]	

- Subsequent Recognition [At Each Balance Sheet Date] :-

Agriculture Produce is measured as per Ind AS 2 [Inventories] at each Balance Sheet date.

Government Grants on Biological Asset

If Government Grant on Biological Asset is Unconditional [i.e. Non Refundable]
⇓
Recognise the Grant immediately in P&L as Income

If Government Grant on Biological Asset is Conditional [i.e. Refundable on failure to meet the condition of Grant]

- If Grant is fully Refundable in case of failure to meet the condition of Grant
⇓
Recognise the Grant as Deferred Income in Balance Sheet & transfer it to P&L when all the conditions of Grant are met

- If Grant is Partially Refundable according to Time lapsed in case of failure to meet the condition of Grant
⇓
Recognise the Grant as Deferred Income in Balance Sheet & transfer it to P&L over the period of condition

Introduction to Ind AS 101

This Ind AS prescribes transition requirements when an Entity adopts Ind AS for the first time, i.e. A move from AS (Previous GAAP) to Ind AS.

Example:

A ltd. has to prepare its Financial Statements as per Ind AS from 1.4.20x2

So, its first Ind AS Reporting Period is 1.4.20x2 to 31.3.20x3 → It has to prepare its comparatives for Previous Year also as per Ind AS, i.e. 1.4.20x1 to 31.3.20x2 → Now, Opening Ind AS Balance Sheet is also prepared at beginning of Previous Year, i.e. 1.4.20x1 [Date of Transition to Ind AS]

⇓

All adjustments for Transition are done on this date

Accounting for Transition to Ind AS

(1) Entity shall apply all Ind AS retrospectively in the Opening Ind AS Balance Sheet on date of transition to Ind AS.

i.e. Opening Ind AS Balance Sheet should carry the balances as if Ind AS has always been applied by the Entity in the Past.

⇓

Any difference arising due to above adjustments will be recognised through Retained Earnings [or OCI if Gain | Loss on such item is recorded through OCI].

(2) There are some Mandatory Exceptions to the Retrospective Application of Ind AS :-

- Estimates :

  Use previous estimates made as per AS [Previous GAAP]

- Measurement of financial Assets & financial Liabilities :

  If it is Impracticable [No Proper Information Available] to apply Ind AS 109 retrospectively, then fair Value as on the date of Transition to Ind AS will be the New Carrying Amount of that financial Asset or financial Liability at the Date of Transition to Ind AS.

- Loan Received from Government at Less than Market Interest Rate :

  If it is Impracticable [No Proper Information Available] to apply Ind AS 109 & 20 retrospectively, then Previous GAAP Carrying Amount of Government Loan at the Date of Transition will be used as the Carrying Amount of such Government Loan in the Opening Ind AS Balance Sheet as on Date of Transition to Ind AS also and Entity shall apply Ind AS 109 [Calculate EIR] to measure such Government Loan after Date of Transition.

(3) Also There are Some Optional Exemptions from Retrospective Application of Ind AS :-

- PPE / Intangible Asset / Investment Property / Investment in Subsidiary, Associate or Joint Venture in SFS :

Recognise at Deemed Cost
→ Carrying Amount as per Previous GAAP on Date of Transition

OR

→ Fair Value as on Date of Transition
[Fair Value Option is not available for Investment Property]

OR

Apply Ind AS 16 / 38 / 40 / 27 Retrospectively

- Compound Financial Instruments :

If Liability is not outstanding as per Previous GAAP on Date of Transition
⇓
No need to split Compound Financial Instrument into Liability & Equity Component separately

If Liability is outstanding as per Previous GAAP on Date of Transition
⇓
Apply Ind AS 109 retrospectively to recognise Liability & Equity Component separately on Date of Transition

- Share Based Payment [ESOP] Transaction :

ESOP Vested Before Date of Transition
⇓
Recognise SBP Reserve at
- Carrying Amount as per Previous GAAP on Date of Transition

OR

- Fair Value of Option at Grant Date by Applying Ind AS 102 retrospectively

ESOP Unvested on Date of Transition
⇓
Recognise SBP Reserve at Fair Value of Option at Grant Date by applying Ind AS 102 retrospectively

- Cumulative Translation Difference on Foreign Operation :

Reset the Cumulative Translation Difference A/c Balance to Zero

OR

Apply Ind AS 21 retrospectively

- Business Combination :

No need to apply Ind AS 103 retrospectively on Business Combinations before Date of Transition.

- Investment in Joint Venture in CFS :

It is to be accounted as per Equity Method according to Ind AS 111 but according to Previous GAAP, It is to be accounted as per Proportionate Consolidation Method
⇓
Hence, Transition is done from Proportionate Consolidation Method to Equity Method by Recognising Investment in Joint Venture A/c in CFS on Date of Transition & Derecognising Proportionate Share of Assets & Liabilities of Joint Venture from respective Assets & Liabilities

Recognise Investment in Joint Venture in CFS at Deemed Cost on Date of Transition

Apply Ind AS 111 Retrospectively

=

Carrying Amount of Net Assets of Joint Venture consolidated in CFS as per Previous GAAP on Date of Transition

(+) Proportionate Goodwill of Joint Venture

$$\left[\text{Total Goodwill on Consolidation of Subsidiary \& Joint Venture in CFS} \times \frac{\text{Carrying Amount of Net Assets of Joint Venture consolidated in CFS}}{\text{Carrying Amount of Total Relative Net Assets including Total Goodwill in CFS}}\right]$$

Reconciliation between Total Equity as per AS and Ind AS to be presented in the Opening Ind AS Balance Sheet

Share Capital [Equity + Preference]	xxx
Reserves & Surplus	xxx
Total Equity as per AS	xxx
(-) Preference Share Capital [if classified as financial Liability]	(xxx)
(±) Transition Adjustments in Retained Earnings or OCI	xxx / (xxx)
Total Equity as per Ind AS	xxx

Introduction to Ind AS 102

- SBP is an agreement in which Entity agrees to pay for goods or services received in the form of its own Equity Shares or Cash Amount based on the Price of its own Equity Shares
- We have to understand Accounting for SBP to Employees and SBP to Other Parties
- Types of SBP

Equity Settled → SBP Transaction which will be settled by issuing Equity Shares

Cash Settled → SBP Transaction which will be settled by Paying Cash based on Entity's Share Price

Accounting for SBP to Employees

Some Important Definitions :

(1) Grant Date :- Date on which SBP Plan is communicated to the Employees & approved by the Shareholders of the Company

(2) Vesting Condition :- Condition to be fulfilled by the Employees to receive the SBP
[Eg. Employee need to remain in Service for 3 years to become entitled for SBP]

(3) Vesting Date :- Date on which Employee will be entitled to SBP (i.e. Date on which Vesting Condition is fulfilled)

(4) Vesting Period :- Period from Grant Date to Vesting Date

(5) Exercise Period :- Period during which SBP can be exercised by Employees

(6.) Exercise Price :- Price at which Employees can purchase shares in a Equity Settled SBP
[It can be 'Zero' Also]

(7) Fair Value of SBP to Employees :-

→ Value of Option calculated using Option Pricing Methods Like Binomial Model, Black Scholes Model
→ It will always be given in question
→ In Case of Equity Settled SBP to Employees [ESOP], Fair Value of Options / Shares At Grant Date will be considered
→ In Case of Cash Settled SBP to Employees [SAR], Fair Value of SARs / Shares At Each Balance Sheet Date will be considered

Grant Date — Vesting Period — Vesting Date — Exercise Period — Exercise Date

1/4/22 — 31/3/25 — 31/3/26

22-23
23-24
24-25
] Service Condition of 3 Yrs. (Vesting Condition)

Equity Settled SBP to Employees [ESOP]

- ESOP Expense is to be Booked over the Vesting Period on SLM Basis [Exercise Period is Not Relevant]
- Calculation of Expense to be recognised Each Year [During the Vesting Period] :-

$$\frac{\text{No. of Employees expected to fulfill the condition at each year end} \times \text{No. of Options per Employee} \times \text{Fair Value of Option At Grant Date}}{\text{Total Vesting Period}} \times \text{Vesting Period Completed till Date} \qquad xxx$$

Less :- Expense Already Recognised Upto Previous Years (x x x)

x x x

Note :-

(i.) If Amount calculated above comes to Negative, then it means Amount of Expense to be Reversed in that Year

(ii.) No. of Employees expected to fulfill the condition at each year end

⇒ Total No. of Employees − Employees Actually Left till Date − Employees expected to Leave

(iii) Total Vesting Period is considered as follows

- If there is Service Condition
  - ⇓ Total Vesting Period will be Service Condition Period
- If there is Performance Condition
  - Non-Market Linked [Target relating to Sales, Earnings, Production Cost, etc.]
    - ⇓
    - → Total Vesting Period will be Expected Period of Achieving the Target by Employees
    - → Total Vesting Period will be Revised At Each Year End on Change in Expectations of Target Achievement
    - → If As per Entity's expectation, Target will not be Achieved, then All Expense recognised till Date will be Reversed
  - Market Linked [Achievement of Specific Market Price / Growth in Price of Share]
    - ⇓
    - → Total Vesting Period will be Expected Achievement Period At Grant Date
    - → Change in Expectation of Target Achievement At Each Year End will be Ignored
    - → If Target Market Price is Achieved before Initially Expected Period, then All Remaining Expense will be recognised immediately in Year of Actual Achievement

· Journal Entries :-

→ On ESOP Grant Date : No Entry

→ During Vesting Period [At Each Year End] :

- For Expense to be Booked
  - ⇓
  - Employee Benefit Expense A/c (P&L)
  - To SBP Reserve A/c (Equity)
- For Expense to be Reversed [If Any]
  - ⇓
  - SBP Reserve A/c (Equity)
  - To Employee Benefit Expense A/c (P&L)

→ During Exercise Period [On Exercise of ESOP by Employees]

Bank A/c	Exercise Price
SBP Reserve A/c (Equity)	Carrying Amount

To Equity Share Capital A/c	No. of Shares × Face Value
To Securities Premium A/c	B/F
To Retained Earnings A/c	SBP Reserve Balance for Employees Not Exercising the Options till End of Exercise Period

$\downarrow$ [No. of Employees not Exercising the Options × No. of Options per Employee × Fair Value of Option At Grant Date]

Modification / Repricing of Equity Settled SBP to Employees [ESOP]

Entity modifies the ESOP by changing the Exercise Price

If Entity Decreases the Exercise Price of ESOP

⇓

It is an Increase in Benefit of Employee (i.e. Increase in Fair Value of Option)

⇓

→ Accounting of Original Plan will continue normally as it is

→ Modification will be Treated as a Separate Plan, i.e. Incremental Fair Value of Option will be recognised as an Expense over the remaining Vesting Period on SLM Basis

* Incremental Fair Value of Option ⇒
Fair Value of Modified / Repriced Option on Modification Date
−
Fair Value of Original Option on Modification Date

Example :- Vesting Period = 1.4.2022 to 31.3.26
Modification is done on 30.9.23
∴ Incremental Fair Value of Option due to Modification will be recognised as Expense in Remaining Vesting Period (30.9.23 to 31.3.26), i.e. 2.5 Years

If Entity Increases the Exercise Price of ESOP

⇓

It is a Decrease in Benefit of Employee (i.e. Decrease in Fair Value of Option)

⇓

Ignore this Modification

Cancellation of Equity Settled SBP to Employees [ESOP]

If an Entity cancels the ESOP, then following Steps need to be followed :

Step 1 : Recognise the Entire Remaining ESOP Expense in the Year of Cancellation on the basis of No. of Employees on Date of Cancellation

Step 2 : Calculate Total Compensation Amount Paid to Employees due to Cancellation of ESOP

⇒ No. of Employees on Date of Cancellation × No. of Options Per Employee × Compensation Amount Per Option

Step 3 : Bifurcate the Compensation to be paid from

SBP Reserve

⇓

No. of Employees on Date of Cancellation
×
No. of Options Per Employee

P&L [Loss on Cancellation]

⇓

Total Compensation Amount
−
Compensation Paid from SBP Reserve

×

Fair Value of Option on Date of Cancellation

Step 4 : Pass Final Journal Entry

SBP Reserve (Equity)	Carrying Amount	
P&L	Loss on Cancellation	
To Bank		Total Compensation Paid
To Retained Earnings		B/f

Cash Settled SBP to Employees [SARs]

- Same As Accounting of ESOP But Use Fair Value of SAR At Each Balance Sheet Date for Calculation of Expense to be recognised each year during the Vesting Period, i.e.

$$\frac{\text{No. of Employees expected to fulfill the condition at each year end} \times \text{No. of SARs per Employee} \times \text{Fair Value of SAR At Each B/s Date}}{\text{Total Vesting Period}} \times \text{Vesting Period Completed till Date} \qquad xxx$$

Less :- Expense Already Recognised Upto Previous Years (xxx)

xxx

- Further, In Case of SARs, SBP Liability is also Remeasured At Each Balance Sheet Date in Exercise Period Using No. of Employees expected to exercise SAR
- Journal Entries :-

→ On SAR Grant Date : No Entry

→ During Vesting Period [At Each Year End] :

For Expense to be Booked	For Expense to be Reversed [If Any]
Employee Benefit Expense A/c (P&L)	SBP Liability A/c
To SBP Liability A/c	To Employee Benefit Expense A/c (P&L)

→ During Exercise Period

(a) For Remeasurement of SAR [At Each Balance Sheet Date in Exercise Period]

For Expense to be Booked	For Expense to be Reversed [If Any]
Employee Benefit Expense A/c (P&L)	SBP Liability A/c
To SBP Liability A/c	To Employee Benefit Expense A/c (P&L)

(b) On Exercise of SAR by Employees

SBP Liability A/c

To Bank A/c

Note :-

(i) If Intrinsic Value of SAR is also given in question, then SAR will be exercised by Employees at Intrinsic Value [i.e. Payment of SAR will be done At Intrinsic Value]

* Intrinsic Value means Actual Appreciation in Market Price of Share since Grant Date

(ii) If it is given in question that SAR vests immediately, then Recognise All Expense immediately on Grant Date [Since Grant Date will become as Vesting Date]

Modification of Cash Settled SBP to Employees [SARs]

Entity modifies the SAR by changing the Vesting Period

If Entity Reduces the Vesting Period of SAR

⇓

It is an Increase in Benefit of Employee

⇓

So, Entity shall consider such Reduced Vesting Period as Total Vesting Period for recognising Expense from that Date

If Entity Increases the Vesting Period of SAR

⇓

It is a Decrease in Benefit of Employee

⇓

Ignore this Modification

Cash Settled SBP With Equity Alternative

- It is a SBP transaction in which an Entity provides a choice to Employee to take Entity's Equity Shares on Settlement or Cash based on Entity's Share Price
- It is a Compound Instrument. Hence, Entity shall account it as Complete Cash Settled SBP with an Extra Option of Equity Shares
- Steps to Solve the Practical Questions :-

Step 1 : Calculate Amount of ESOP Component [Equity] :

Total Fair Value of ESOP At Grant Date Assuming All Employees will Exercise Equity Plan	xxx
(-) Total Fair Value of SAR At Grant Date Assuming All Employees will Exercise Cash Plan	(xxx)
ESOP Component	xxx

⇓

Apply Accounting of ESOP

[i.e. Recognise it as an Expense over the Vesting Period]

* Also Accounting for SAR will be done Normally

Step 2 : Pass Journal Entries :

→ On Grant Date : No Entry

→ During Vesting Period [At Each Year End] :

Employee Benefit Expense A/c (P&L)

To SBP Liability A/c

To SBP Reserve A/c (Equity)

→ On Exercise Date

If All Employees Exercise SAR

(i) SBP Liability A/c — Carrying Amt.
    To Bank A/c

(ii) SBP Reserve A/c (Equity) — Carrying Amt.
    To Retained Earnings A/c

If All Employees Exercise ESOP

(i) SBP Liability A/c — Carrying Amt.
    To SBP Reserve A/c (Equity)

(ii) SBP Reserve A/c (Equity) — Carrying Amt.
    To Equity Share Capital A/c — No. of Shares × Face Value
    To Securities Premium A/c — Fair Value of Option At Grant Date − Eq. Sh Capital
    To Retained Earnings A/c — B/F

Group Share Based Payment (SBP) Plan

(i) If Parent Company issues its Own Shares to Employees of Subsidiary Co. For SBP of Subsidiary

Accounting in Books of Parent Company

→ Investment in Subsidiary A/c
    To SBP Reserve A/c (Equity)

→ SBP Reserve A/c (Equity)
    To Equity Share Capital A/c
    To Securities Premium A/c

Accounting in Books of Subsidiary Company

Employee Benefit Expense A/c (P&L)
    To Capital Contribution from Parent A/c (Equity)

(i) If Subsidiary Company issues its Own Shares to Employees of Parent Co. For SBP of Parent

Accounting in Books of Parent Company

Employee Benefit Expense A/c (P&L)
    To Dividend Income A/c (P&L)

Accounting in Books of Subsidiary Company

→ Dividend Distribution A/c
    To SBP Reserve A/c (Equity)

→ SBP Reserve A/c (Equity)
    To Equity Share Capital A/c
    To Securities Premium A/c

Accounting for SBP to Other Parties

- When Entity do Share Based Payment (SBP) for Purchase of PPE, Goods or Services
- In this, Recognise PPE, Goods or Services Acquired At Fair Value of PPE, Goods or Services Received
- Journal Entries :-

Equity Settled

→ PPE / Expense A/c
    To SBP Reserve A/c (Equity)

→ SBP Reserve A/c (Equity)
    To Equity Share Capital A/c
    To Securities Premium A/c

Cash Settled

→ PPE / Expense A/c
    To SBP Liability A/c

→ SBP Liability A/c
    To Bank A/c

<u>Note</u>:- In Case of Service received on a continuous monthly basis, then Recognise Expense proportionately in every month, i.e.

$$\Rightarrow \frac{\text{Total Fair Value of Services Received}}{\text{No. of Months of Service}}$$

(1.) If a Company [Investor] invests in Equity Shares of Another Company [Investee]

- **Less than 20%**
  - ⇓ It is a Normal Investment
  - ⇓ Investor Co. will account it as per Ind AS 109 [SFS Only]
- **20% or More But Less than 50%**
  - ⇓ Investee Co. becomes Our 'Associate'
  - ⇓ Investor Co. has to prepare 2 types of FS, i.e. SFS & CFS
    - In SFS ⇓ Investor Co. will account it as per Ind AS 27
    - In CFS ⇓ Investor Co. will account it as per Ind AS 28
- **More than 50%**
  - ⇓ Investee Co. becomes Our 'Subsidiary' [i.e. We have Control over it]
  - ⇓ It is known as Business Acquisition
  - ⇓ Investor Co. has to prepare 2 types of FS, i.e. SFS & CFS
    - In SFS ⇓ Investor Co. will account it as per Ind AS 27
    - In CFS
      - On Date of Acquisition [Day 1] ⇓ Investor Co. will account it as per Ind AS 103
      - At Each Year End ⇓ Investor Co. will account it as per Ind AS 110
- **Joint Arrangements**
  - Joint Operation ⇓ Investor Co. will account it as per Ind AS 111 [SFS Only]
  - Joint Venture ⇓ Investor Co. has to prepare 2 types of FS i.e. SFS & CFS
    - In SFS ⇓ Ind AS 27
    - In CFS ⇓ Ind AS 28

<u>Note</u> :- In Case of Investment in Subsidiary ; Investor Co. is also known as Parent Co., Holding Co., Acquirer Co.

(2.) Investor Co. & its Subsidiary, Associate, Joint Arrangements are in all together known as 'Group Companies'

(3.) <u>Accounting of Investment in Subsidiary, Associate or Joint Venture in Separate Financial Statements [SFS] by Investor Company [Ind AS 27 : SFS]</u> :-

- Investor Co. can show it
  - At Cost
  - At Fair Value i.e. FVTPL or FVTOCI [As per Ind AS 109]
- Any Dividend Income Received from these Investments is recognised in P&L in SFS

Meaning of Business Combination

Business Combination occurs when a Company acquires "Control" over "Business of Other Company"

→ Business means an integrated set of activities having following 3 Elements:

- **Inputs** ⇓ It means resources/ assets required to generate output
  Eg:- PPE, Intangible Assets, Manpower, etc.
- **Processes** ⇓ It means processes/ techniques used on Inputs to generate Output
  Eg:- Production Process, Management Process, etc.
- **Outputs** ⇓ It means ability to generate Revenue by using Inputs & Processes

→ Control over Business of Other Company can be obtained

- **By Acquiring Net Assets of Other Company**
  [इस Case में B.C. के बाद सामने वाली Company बंद हो जाती है]
  ⇓
  In this Case, Acquirer Co. will account for Business Combination in its SFS Only as per Ind AS 103
  [No need to prepare CFS separately]

- **By Acquiring More than 50% Equity Shares of Other Company**
  i.e. Making Other Company as Our 'Subsidiary'
  [इस Case में B.C. के बाद भी सामने वाली Company as it is चलती रहती है]
  ⇓
  In this Case, Acquirer Co. has to prepare 2 types of FS, i.e. SFS & CFS
  - In SFS ⇓ Acquirer Co. will account it as per Ind AS 27
  - In CFS
    - On Date of Acquisition [Day 1] ⇓ Acquirer Co. will account it as per Ind AS 103
    - At Each Year End ⇓ Acquirer Co. will account it as per Ind AS 110

→ Acquirer Company ⇒ Purchasing Company
→ Acquiree Company ⇒ Selling Company

Accounting for Business Combination [Acquisition Method]

Ind AS 103 provides Accounting for a Business Combination in CFS of Acquirer Co. on the Date of Acquisition using following Steps:

Step 1: Identifying the Acquirer Com any :-

Acquirer is the Company who obtains the control over the business of Acquiree Company i.e. generally the Company who pays the Purchase Consideration (PC) except in case of Reverse Acquisition

Step 2: Determining the Date of Acquisition :-

Date on which Acquirer Company obtains control over the Acquiree Company i.e. Agreed Date of Control

But if any approval is required from the Government, then Date of Approval by Government will be considered as Acquisition Date

Step 3: Determining the Purchase Consideration (PC) :-

- PC means amount paid to Owners of Acquiree Company to obtain control of its business
- PC is calculated on Acquisition Date at fair Value as follows:

Cash Paid	To Owners of Acquiree Company	xxx
(+) Fair Value of Any Assets Transferred		xxx
(+) Fair Value of Equity Shares Issued		xxx
(+) Fair Value of Debentures Issued		xxx
(+) Present Value of Deferred Consideration		xxx
(+) Fair Value of Contingent Consideration		xxx
(+) Fair Value of ESOP relating to Pre Combination Period in case of Replacement Awards		xxx
Total PC		xxx

Notes:-

(i) Treatment of Deferred Consideration :-

- Initially ⇓ At Present Value [Considered as part of PC]
- At Each Year End ⇓ Financial Liability At Amortised Cost Method (ACM)

Example:- A Ltd. acquires B Ltd. by paying PC of ₹ 50 Lakhs in Cash & will also pay ₹ 10 Lakh after 2 years. Discounting Rate is 10%. PVF @ 10% for 2nd Year is 0.8264

Solution:-

Calculation of P.V. of Deferred Consideration:

Year	Cash flow	PVF@ 10%	P.V.
2	10,00,000	0.8264	8,26,400

Calculation of Total PC :

Cash	50,00,000
(+) P.V. of Deferred Consideration	8,26,400
	58,26,400

Amortisation Table for Deferred Consideration :

Year	Opening Balance	Interest @ 10%	Actual Payment	Closing Balance
1	8,26,400	82,640	–	9,09,040
2	9,09,040	90,960	10,00,000	–

Journal Entries :

→ Initially on Date of Acquisition [Business Combination Entry]

Assets	Dr.	✓	
To Liabilities A/c			✓
To Cash A/c [PC]			5000000
To Provision for Deferred Consideration A/c [PC]			8,26,400

→ 1^{st} Year End [Charging Interest Expense (Finance Cost) on Prov. for Def. Cons.]

Interest Expense A/c [P&L]	Dr.	82,640	
To Provision for Deferred Consideration A/c			82,640

→ 2^{nd} Year End [Charging Int. Exp. & Payment of Deferred Consideration]

Interest Expense A/c [P&L]	Dr.	90,960	
To Provision for Deferred Consideration A/c			90,960
Provision for Deferred Consideration A/c	Dr.	1000,000	
To Cash A/c			1000000

(ii) Treatment of Contingent Consideration :-

- Initially
  - ⇓ At Fair Value (given in question) [Considered as part of PC]
- At Each Year End
  - If it is Payable in Cash OR Variable No. of Equity Shares to be issued ⇓ Financial Liability At FVTPL
  - OR
  - If Fixed No. of Equity Shares to be issued ⇓ Equity Instrument

Example :- A Ltd. acquires B Ltd. by paying PC of ₹ 50 Lakhs in Cash & will also pay ₹ 10 Lakh after 2 years if Profit of B Ltd. for the 2nd Year exceed 1 Crore ₹.
Fair Value of Contingent Consideration on Date of Acquisition is ₹ 6,50,000
Fair Value of Contingent Consideration at 1^{st} Year End is ₹ 8,00,000

Solution :-

Journal Entries :

→ Initially on Date of Acquisition [Business Combination Entry]

Assets	Dr.	✓

To Liabilities A/c ✓
To Cash A/c [PC] 5000000
To Provision for Contingent Consideration A/c [PC] 6,50,000

→ 1st Year End

P&L A/c [Fair Value Change] Dr. 1,50,000
To Provision for Contingent Consideration A/c 1,50,000
[8,00,000 − 6,50,000]

→ 2nd Year End

If Target Profit Achieved

Prov. for Cont. Cons. A/c Dr. 8,00,000
P&L A/c (B/f) Dr. 2,00,000
To Cash A/c 10,00,000

If Target Profit Not Achieved

Prov. for Cont. Cons. A/c Dr. 8,00,000
To P&L A/c 8,00,000

(iii) Contingent Consideration Payable to Employee Shareholders of Acquiree Company :-

If it is payable to them for being in Employment of the Company after Acquisition also
[i.e. Amount is paid to receive services from the employee for some years after acquisition]
⇓
It is Not Considered as part of PC
[It is recognised over the period as Employee Benefit Expense (P&L)]

If it is payable to them in capacity of Shareholders of Acquiree Company
⇓
It is Considered as part of PC
[Recorded as PC in Business Combination Entry on Date of Acquisition]

(iv) Acquisition Related Cost [Transaction Cost for Business Combination] i.e. Cost incurred in relation to acquisition of a Company such as Legal fee, Regulator's fee, Stamp Duty, Professional fee, Valuation fee, etc.
⇓
It is recorded as Expense in P&L [Not Considered as part of PC]

(v) ESOP [Equity Settled SBP Awards] of Acquiree Company :-

Replacement Awards
⇓
If Acquirer Company Replaces the SBP Awards of Acquiree Company
↓
It means Acquirer Company will issue its own Equity Shares on maturity of ESOP
↓

Non-Replacement Awards
⇓
If Acquirer Company does not Replace the SBP Awards of Acquiree Company
↓
It means Acquiree Company will issue its own Equity Shares on maturity of ESOP
↓

Portion of Replacement Awards related to

Pre Combination Period

- Considered as part of PC
- Fair Value of ESOP relating to Pre Combination Period

=

Fair Value of Original SBP Awards on Acquisition Date × (Vesting Period expired till Acquisition Date / Higher of Total Original Vesting Period or Total Revised Vesting Period)

- Journal Entry for Example :
  [B.L. Entry on DOA]

  Assets A/c
  To Liabilities A/c
  To Cash A/c [PC]
  To SBP Reserve A/c [PC]

Post Combination Period

- Recognised as Employee Benefit Expense in P&L over the remaining Vesting Period [As per Ind AS 102]
- Fair Value of ESOP relating to Post Combination Period (Balancing figure)

=

Fair Value of Replacement Awards

−

Fair Value of ESOP relating to Pre Combination Period

- Journal Entry for Example :
  [In Remaining Vesting Period]

  Emp. Ben. Exp. A/c (P&L)
  To SBP Reserve A/c

Portion of Non-Replacement Awards related to

Pre Combination Period

- Considered as part of NCI
- Fair Value of ESOP relating to Pre Combination Period is calculated exactly same as in case of Replacement Awards
- Journal Entry for Example :
  [B.L. Entry on DOA]

  Assets A/c
  To Liabilities A/c
  To Cash A/c [PC]
  To NCI A/c [SBP]

Post Combination Period

- Recognised as Employee Benefit Expense in P&L over the remaining Vesting Period [As per Ind AS 102]

  But

  NCI will be Credited instead of SBP Reserve
- Fair Value of ESOP relating to Post Combination Period is calculated exactly same as in case of Replacement Awards
- Journal Entry for Example :
  [In Remaining Vesting Period]

  Emp. Ben. Exp. A/c (P&L)
  To NCI A/c

[इस Case में Acquirer Co. को Pre Combination Period का ESOP का Expense Record करने को नहीं मिला, पर फिर भी Acquirer Co. ने ही ESOP में Share Issue करके देने हैं
⇓
इसलिए Pre Combination Period से Related Fair Value of ESOP को PC का Part consider करेगी Acquirer Company (Assuming Acquirer Co. ने Pre Combination Period के ESOP का पैसा Acquiree Co. को दिया है)
⇓
बाकी Post Combination Period का ESOP Expense Acquirer Co. Ind AS 102 के According Normally Book करता रहेगा]

[इस Case में Acquiree Co. को ही ESOP में Share Issue करने हैं
⇓
इस वजह से Acquiree Co. में हमारा (Acquirer Co.) का Stake कम हो जाएगा और NCI का Stake बढ़ जाएगा]

Example :-

A Ltd. acquired B Ltd. & replaced existing equity settled awards of B Ltd. Original Vesting Period was 6 Years out of which 2 Years has already been completed. A Ltd. has also reduced the Vesting Period to 3 Years from Acquisition Date.

Fair Value of Awards on Acquisition Date :

Original Awards = ₹ 600

Replacement Awards = ₹ 700

Solution :-

Replacement Awards

Pre Combination Period [PC]

⇓

$600 \times \frac{2}{6} \Rightarrow$ ₹ 200

Post Combination Period

[Rec. as Exp. in Remaining Vesting Period]

⇓

700 − 200 = ₹ 500

Here,

Total Original V.P. = 6 Yrs.

Total Revised V.P. = 2 + 3 = 5 Yrs.

Higher is 6 Yrs.

(vi) If there is Any Pre Existing Relationship between Acquirer & Acquiree before Business Combination, then PC paid to Acquiree is considered as inclusive of Settlement Amount for such pre existing relationship

⇓

So Settlement Amount for such Pre Existing Relationship needs to be deducted from PC

⇓

Calculation of Settlement Amount paid to Acquiree Co. for Pre Existing Relationship

If there is Non Contractual Pre Existing Relationship

[Eg:- Law suit filed against Acquirer Co. by Acquiree Co.]

⇓

- Settlement Amount for this Pre Existing Relationship

  =

  Fair Value of Litigation Liability

- This Amount is to be deducted from PC

  &

  Recognised as Settlement Loss in P&L

  P&L A/c

  To Bank A/c

* If Acquirer Co. has already recognised some amount as Provision for this Liability in its Books, then only remaining amount is debited to P&L

Provision for Liability A/c

P&L A/c

To Bank A/c

If there is Contractual Pre Existing Relationship

[Eg:- Licence / Francise provided by Acquirer Co. to Acquiree Co.]

⇓

- Settlement Amount for this Pre Existing Relationship

  =

  Lower of

  Fair Value of such Licence − Carrying Amount of such Licence in Acquiree's Books

  OR

  Penalty Amount to terminate the Contract

- This Amount is to be deducted from PC

  &

  Recognised as Settlement Loss in P&L

  P&L A/c

  To Bank A/c

Example:-

A Ltd. acquires B Ltd. by paying PC of ₹ 500 Lakhs. B Ltd. had already filed a case against A Ltd. before this Business Combination. A Ltd. had already booked a liability against this of ₹ 10 Lakh. Fair Value of Litigation Liability is ₹ 25 Lakh.

Solution:-

Settlement Amount for Liability = ₹ 25 Lakh

∴ P.C. = 500 Lakh − 25 Lakh = ₹ 475 Lakh

Journal Entry:

Provision for Liability A/c	10 Lakh	
P&L A/c (B/F)	15 Lakh	
To Bank A/c		25 Lakh

- Also Fair Value of such Licence is also recognised by Acquirer Co. in Business Combination Entry as Asset (Reacquired Right) taken over from Acquiree Co.
  [We will read this concept in Step 4]

Example:-

A Ltd. acquires B Ltd. by paying PC of ₹ 1 Crore. A Ltd. had provided a licence 4 Years ago to B Ltd. for 10 Years at ₹ 2,50,000

This Licence can be terminated anytime by paying Amount equals to Unexpired Initial fee plus 20%.

Fair Value of Licence on Acquisition Date is ₹ 4,50,000

Solution:-

Carrying Amt. of Licence

$\Rightarrow 2,50,000 - \left(2,50,000 \times \frac{4}{10}\right) \Rightarrow 1,50,000$

Settlement Amount for Licence

$4,50,000 - 1,50,000 = 3,00,000$ $1,50,000 + 20\% = 1,80,000$

Lower is ₹ 1,80,000

PC = 1 Crore − 1,80,000 = 98,20,000 ₹

Journal Entry:

P&L A/c	1,80,000	
To Bank A/c		1,80,000

Step 4: Identifying the Net Assets taken over of Acquiree Company by Acquirer Company :-

- All Assets & Liabilities of Acquiree Company are taken over at Fair Value on Date of Acquisition
- Non-Current Assets Held For Sale of Acquiree Company is taken over at its Fair Value Less Costs to disposal as per Ind AS 105
- Intangible Assets that meet the recognition criteria as per Ind AS 38 but are not recorded in Acquiree's Books are also taken over & recognised at Fair Value on Date of Acquisition
  [Eg:- Internally Generated Customer Relationships of Acquiree Company, Internally developed Patent, Non-Compete fee, etc.]
- Contingent Liability of Acquiree Company is also taken over & recognised as a Liability at Fair Value on Date of Acquisition

- Indemnification Asset promised by Acquiree Company is also taken over
  [Maximum Amount at which this Indemnification Asset to be recognised is upto the Amount of Contingent Liability taken over]
- Reacquired Rights (Eg. Pre Existing Contractual Relationship Licence appearing in Books of Acquiree Co.) are also taken over & recognised at Fair Value on Date of Acquisition
- Calculate & Recognise DTA | DTL arising due to Net Assets taken over of Acquiree Company in Business Combination [As discussed in Ind AS 12]

If Fair Value of Net Assets taken [Treated as Carrying Amount as per Books] > Carrying Amount of Net Assets taken [Treated as Tax Base]
⇓
DTL is Created

If Fair Value of Net Assets taken [Treated as Carrying Amount as per Books] < Carrying Amount of Net Assets taken [Treated as Tax Base]
⇓
DTA is Created

* DTA | DTL already appearing in Acquiree's Books is also taken over

Note:- Fair Value should be determined by Registered Valuer

Step 5 : Calculation of Non-Controlling Interest (NCI) :-

- It is portion of Acquiree Company not owned by Acquirer Company
- Calculation of NCI on Acquisition Date :-

1st Preference
⇓
Fair Value Method
⇓
NCI =
→ Fair Value of NCI given in question
OTHERWISE
→ Fair Value per share of Acquiree Company × No. of Shares held by NCI

2nd Preference
⇓
Proportionate Share of Net Assets (PSNA) Method
⇓
NCI =
Net Assets taken over of Acquiree Company [As calculated in Step 4] × NCI Stake in Acquiree Company

- NCI is shown as a separate Line item in Equity head of Balance Sheet in CFS of Acquirer Company
- NCI is Not Applicable (does not arise) in case of Business Combination where Acquirer Company obtains control by Acquiring Net Assets of Acquiree Company OR by Acquiring 100% Equity Stake of Acquiree Company

Step 6 : Calculation of Goodwill or Capital Reserve (Gain on Bargain Purchase) on Acquisition Date :-

Purchase Consideration [Step 3]	xxx

Add: Non-Controlling Interest [Step 5] xxx

xxx

Less: Net Assets taken over of Acquiree Company (100%) [Step 4] (xxx)

xxx

If it is Positive ⇓ Goodwill

If it is Negative ⇓ Gain on Bargain Purchase which is recognised in OCI but accumulated as Capital Reserve in 'Other Equity' Head in B/S

Notes:-

(i) Goodwill calculated as above is known as Acquired Goodwill as per Ind AS 103

⇓

It cannot be Amortised like Other Intangible Assets but it is Tested for Impairment Annually

(ii) If in calculation of Goodwill ⇒ NCI used is calculated as per

Fair Value Method ⇓ then Goodwill is named as Full Goodwill

PSNA Method ⇓ then Goodwill is named as Partial Goodwill

Example 1:-

A Ltd. acquires 100% shares of B Ltd. for ₹ 10 Crore. Fair Value of Net Assets of B Ltd. is ₹ 8 Crore

Solution:-

Calculation of Goodwill:

PC	10 Crore
(-) Net Assets taken over	(8 Crore)
Goodwill	2 Crore

Example 2:-

A Ltd. acquires 70% shares of B Ltd. for ₹ 10 Crore. Fair Value of Net Assets of B Ltd. is ₹ 8 Crore. Calculate Goodwill if NCI is measured as per PSNA Method.

Solution:-

NCI at PSNA = 8 crore × 30% = 2.4 Crore

Goodwill:

PC	10 Crore
(+) NCI	2.4 Crore
	12.4 Crore
(-) Net Assets taken over	(8 Crore)
Partial Goodwill	4.4 Crore

Example 3:-

A Ltd. acquires 70% shares of B Ltd. for ₹ 10 Crore. Fair Value of Net Assets of B Ltd. is ₹ 8 Crore. Fair Value of NCI is ₹ 2.6 Crore. Calculate Goodwill if NCI is measured as per Fair Value Method.

Solution:-

Goodwill :

PC	10 Crore
(+) NCI	2.6 Crore
	12.6 Crore
(-) Net Assets taken over	(8 Crore)
Full Goodwill	4.6 Crore

Step 7: Journal Entry for Business Combination on Acquisition Date by Acquirer Company [In CFS]:-

Assets taken over of Acquiree Company A/c Dr. [As per Step 4]
Goodwill A/c (if any) Dr. [Balancing figure]
To Liabilities taken over of Acquiree Company A/c [As per Step 4]
To NCI A/c [As per Step 5]
To Gain on Bargain Purchase A/c (if any) [Balancing figure]
To Purchase Consideration (PC) :
- Cash / Bank A/c
- Equity Share Capital A/c
- Debentures A/c
- Provision for Deferred Consideration A/c
- Provision for Contingent Consideration A/c
- SBP Reserve A/c [Pre Combination Period Replacement Award]

[PC As per Step 3]

Note:- In above Journal Entry, we can also credit 'Investment in Acquiree A/c' instead of PC as that is already recorded in Separate financial Statements of Acquirer

Step 8: Prepare Consolidated Balance Sheet of Acquirer after Business Combination on Acquisition Date:-

Take All Items (Assets, Liabilities, Share Capital, Reserves) at Carrying Amount of Acquirer Company's Balance Sheet on Acquisition Date

and

Give Effect of Business Combination Entry [As per Step 7]

Note: Measurement Period:-

Where Any New Information is received after Acquisition Date regarding Fair Value of Assets & Liabilities taken over of Acquiree Company, then

↓ If New Information received, regarding Fair Value of Assets & Liabilities taken

↓ Otherwise
↓

over, reflects the facts & circumstances existing on Acquisition Date

AND

Such Information is Received within 1 Year of Acquisition Date

⇓

Required Changes will be done in :
→ Net Asset taken over value, &
→ NCI (if it is as per PSNA Method)

↓

Difference in Journal Entry will be adjusted in Goodwill or Capital Reserve

Normal Accounting as per applicable Ind AS on that Asset or Liability

Accounting for Business Combination in case of Step-up Acquisition

- Acquirer Company can obtain control in Acquiree Company Step by Step through Series of Purchase of Stake / Share in Acquiree Company
- In this Case, Acquirer Company obtains control in Acquiree Company on the date when Total Equity Stake Purchased in Acquiree Company crosses 50%
- Accounting for Business Combination in case of Step-up Acquisition :-

Same as discussed in Above Topic [Accounting for Bus. Comb.] Except for following points :

(1) Date of crossing 50% stake in Acquiree Company will be considered as Acquisition Date

Example :- Stake Acquired as follows :

1/4/22 → 18%
1/4/23 → 22%
1/4/24 → 30% ⇒ Acquisition Date
1/4/25 → 20%

(2) Calculation of Purchase Consideration (PC) :

PC as calculated in Step 3 of Above Topic	xxx
Add: Fair Value of Previously held Investment in Acquiree before Acquisition Date	xxx
	xxx

(3) In Journal Entry for Business Combination on Acquisition Date by Acquirer Company [In CFS] :

→ Credit Previously held Investment in Acquiree Company at its Carrying Amount [Since It is Part of PC]

→ Recognise Gain / Loss due to Remeasurement of Previously held Investment in Acquiree at Fair Value in P&L
[i.e. Difference between Fair Value & Carrying Amount of Previously held Investment on Acquisition Date]

→ If Previously held Investment in Acquiree is 20% or More (i.e. Our Associate Co.), then Share of Acquirer Co. (Ours) in OCI Reserves of Acquiree Co. (Associate till date) will also be derecognised by transferring it to P&L or Retained Earnings according to the Nature of OCI Reserve

[Eg.:- Share in Revaluation Reserve (PPE) of Acquiree (Associate) → T/f to R/E
Share in FCTR of Acquiree (Associate) → T/f to P&L]

Note:- Step-up Acquisition is not possible in case where Business Combination is done by obtaining control through Acquiring Net Assets of Acquiree Company

Business Combination without Transfer of Consideration (PC)

- It can happen when two companies decide to combine together through an agreement in which Newly formed Company will comprise of Board Members of Both Companies
- In this Case, the Company whose Board Members are in majority in Newly formed Company will be considered as Acquirer Company & Other Company becomes its Acquiree Company
- Accounting for Business Combination in case of Business Combination without transfer of PC :-

Same as discussed in Above Topic [Accounting for Bus. Comb.] Except for following points :

(1) PC is Nil

(2) NCI is 100% i.e. Equals to the Total Fair Value of Acquiree Company

(3) Goodwill or Capital Reserve is calculated as follows:

PC	Nil
Add: NCI	xxx
Less: Net Assets of Acquiree Company	(xxx)
	xxx

Example:-

A Ltd. & B Ltd. decides to combine together through a Shareholder's Agreement. In Newly Formed Company, Board Members are 10 out of which 6 are of A Ltd. & 4 are of B Ltd. Fair Value of B Ltd. is ₹ 10 Lakhs. Fair Value of Net Assets of B Ltd. is ₹ 9 Lakhs. Calculate Goodwill on acquisition.

Solution:-

Acquirer Co. → A Ltd.

NCI = ₹ 10 Lakhs

∴ Goodwill :

PC	Nil
(+) NCI	10 Lakhs
(−) Net Assets of B Ltd. (Acquiree)	(9 Lakhs)
Goodwill	1 Lakh

Accounting for Business Combination in case of Reverse Acquisition

- It happens when Company who Actually pays the PC is not the Acquirer Company for Accounting Purpose as per Ind AS 103
- Steps to be followed for Accounting of Business Combination in case of Reverse Acquisition :-

Step 1: Identifying the Acquirer Company

Company who actually pays the PC [Legal Acquirer]	Company to whom PC is Paid [Legal Acquiree]
⇓	⇓
Accounting Acquiree	Accounting Acquirer [Since it obtains the Control (> 50% Stake) in Combined Entity after Business Combination]

Example :-

A Ltd.	
ESC ↓ 100 Shares	

B Ltd.	
ESC ↓ 60 Shares	

A Ltd. acquires B Ltd. by issuing 2.5 shares in exchange of 1 share of B Ltd. as PC.
So, After Business Combination, Total Shares in combined entity will be
⇒ 100 shares [A Ltd.] + 150 Shares [Issued to B Ltd. as PC (60 shares × 2.5)]
⇒ 250 shares
Now, Check control in combined entity

$$\text{A Ltd.} = \frac{100}{250} = 40\% \qquad \text{B Ltd.} = \frac{150}{250} = 60\%$$

Hence, In this Case → B Ltd. is Accounting Acquirer [Legal Acquiree]
↳ A Ltd. is Accounting Acquiree [Legal Acquirer]

So, this is a case of Reverse Acquisition & Hence, we have to do Business Combination Accounting assuming 'B Ltd. as Acquirer Company' & A Ltd. as Acquiree Company

Step 2: Determining the Date of Acquisition :- Same as Above Topic Along for Bus. Comb.

Step 3: Calculation of Deemed | Notional PC :-

→ It is the Amount of PC on the assumption that if Accounting Acquirer (Eg. B Ltd.) had paid to the Accounting Acquiree (Eg. A Ltd.)

→ It is calculated as follows -

$$\left[\frac{\text{Actual No. of Shares in Equity Share Capital of Accounting Acquirer before Business Combination}}{\text{Stake of Accounting Acquirer in Combined Entity (\%)}} - \text{Actual No. of Shares in Equity Share Capital of Accounting Acquirer before Business Combination}\right] \times \text{Fair Value Per Share of Accounting Acquirer}$$

→ This Deemed PC is assumed as given by issuing Equity Shares to Accounting Acquiree

In Continuation of Above Example, Suppose fair Value per share of B Ltd. is ₹ 40

∴ Deemed PC given by B Ltd. (Accounting Acquirer) is

$$\Rightarrow \left[\frac{60 \text{ shares}}{60\%} - 60 \text{ shares}\right] \times ₹\,40 \Rightarrow [100 \text{ shares} - 60 \text{ shares}] \times ₹\,40$$

$$\Rightarrow 40 \text{ shares} \times ₹\,40 \Rightarrow ₹\,1{,}600$$

Step 4: All Net Assets of Accounting Acquiree (Eg. A Ltd.) are taken over at Fair Value [Same As Above Topic Along for Bus. Comb.]

Step 5: NCI is Not Applicable (does not arise) in case of Reverse Acquisition

Step 6: Calculation of Goodwill or Capital Reserve :

Deemed / Notional PC	xxx
Less: Net Assets taken over of Accounting Acquiree (Eg. A Ltd.)	(xxx)
	xxx

Step 7: Journal Entry for Business Combination by Accounting Acquirer (Eg. B Ltd.) on Date of Acquisition [Same As Above Topic Along for Bus. Comb.]

Step 8: Consolidated Balance Sheet will be prepared by Accounting Acquirer (Eg. B Ltd.) after Business Combination on Acquisition Date :

⇓

Take All Items (Assets, Liabilities, Share Capital, Reserves) at Carrying Amount of Accounting Acquirer's (Eg. B Ltd.) Balance Sheet on Acquisition Date

and

Give Effect of Business Combination Entry [As per Step 7]

Note:- In Consolidated Balance Sheet :

→ Name will be written of Legal Acquirer (Eg. A Ltd.)

Example :- Consolidated Balance Sheet of A Ltd.

→ No. of Shares issued in Equity Share Capital of Combined Entity will be written as Original Legal Shares

Example :- 100 shares of A Ltd. + 150 shares issued to B Ltd. ⇒ Total 250 Shares

Accounting for Business Combination in case of Common Control Transactions

- It happens when the Acquiree Company is ultimately controlled by the Same Company Both Before & After the Business Combination

Example :-

Existing Scenario ⇒ A Ltd. $\xrightarrow{100\%}$ B Ltd.

A Ltd. $\xrightarrow{100\%}$ C Ltd.

B Ltd. acquires C Ltd.

$\therefore$ A Ltd. $\xrightarrow{100\%}$ B Ltd. $\xrightarrow{100\%}$ C Ltd.

ultimately controlled by A Ltd.

- It is merely a Corporate Restructuring [Not a Business Acquisition in Substance]
- Here, Acquirer Company is known as Transferee Company & Acquiree Company is known as Transferor Company
- For Accounting of Common Control Transactions, Pooling of Interest Method is used
- Steps to be followed for Accounting of Business Combination in case of Common Control Transactions :-

Step 1 : Identifying the Transferee [Acquirer] Company

Step 2 : Determining the Date of Acquisition

Step 3 : Determining the Purchase Consideration [PC]

SAME AS IN TOPIC ACCOUNTING FOR BUSINESS COMBINATION

Step 4 : All Assets & Liabilities of Transferor [Acquiree] Company are taken over at Book Value

AND

All Reserves of Transferor [Acquiree] Company are also taken over at Book Value

Step 5 : NCI is Not Applicable (does not arise) in case of Common Control Transactions

Step 6 : Calculation of Capital Reserve [Gain / Loss on Restructuring] :

Purchase Consideration [PC]	xxx
Less : Net Assets including Reserves taken over of Transferee [Acquiree]	(xxx)
	xxx

If it is Positive ⇓ Loss on Restructuring [Capital Reserve (Dr.)]

If it is Negative ⇓ Gain on Restructuring [Capital Reserve (Cr.)]

Step 7 : Journal Entry on Acquisition Date by Transferee (Acquirer) Company [In CFS] :-

Assets taken over of Transferor Company A/c Dr.	[As per Step 4]	
Loss on Restructuring [Capital Reserve] A/c (if any) Dr.	[Balancing figure]	
To Liabilities taken over of Transferor Company A/c		[As per Step 4]
To Reserves taken over of Transferor Company A/c		[As per Step 4]
To Gain on Restructuring [Capital Reserve] A/c (if any)		[Balancing figure]
To Purchase Consideration (PC)		[As per Step 3]

Step 8 : Prepare Consolidated Balance Sheet of Transferee [Acquirer] on Acquisition Date :-

Take All Items (Assets, Liabilities, Share Capital, Reserves) at Carrying Amount of Transferee [Acquirer] Company's Balance Sheet on Acquisition Date

and

Give Effect of Above Journal Entry [As per Step 7]

Accounting for Mergers

(1) Meaning of Merger :-

It is a process by which 2 or More Companies joins together to form a New Company [Existing Companies बन्द हो जाती हैं]

(2) Types of Mergers & their Accounting :-

(i) Merger in Nature of Common Control :

Mr. X Owner ← A Ltd. B Ltd. → Mr. X Owner

↓ Merge

AB Ltd. → Mr. X Owner

- In this Case, Transferee Company (Eg. AB Ltd.) will apply Pooling of Interest Method for Accounting of Merger [Same As Accounting for Business Combination in case of Common Control Transactions]
- If In this Case, PC is not given in question [i.e. Question is asking to issue requisite No. of Shares to discharge claims of Both Transferor Companies], then PC is calculated as follows :

Total PC = Net Assets including Reserves taken over of Transferor Companies

⇓

Distribute this Total PC to both Transferor Companies in Ratio of their Net Assets

(ii) Merger in Nature of Business Acquisition :

Mr. A Owner ← A Ltd. B Ltd. → Mr. B Owner

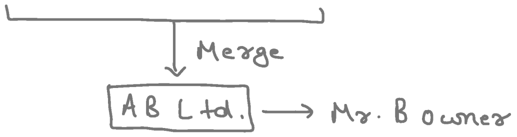
↓ Merge

AB Ltd. → Mr. X Owner

- In this Case, Acquirer Company (Eg. AB Ltd.) will apply Acquisition Method for Accounting of Merger [Same As Accounting for Business Combination]

(iii) Merger in Nature of Reverse Acquisition :

Mr. A Owner ← A Ltd. B Ltd. → Mr. B Owner



Here, B Ltd. → Accounting Acquirer [Legal Acquiree]
A Ltd. → Accounting Acquiree [Legal Acquiree]
AB Ltd. → Accounting Acquiree [Legal Acquirer]

- In this Case, Accounting Acquirer (Eg. B Ltd.) will apply Accounting Same as given for Business Combination in case of Reverse Acquisition
- If In this Case, Actual Legal PC is not given in question [i.e. Question is asking to issue requisite No. of Shares to discharge claims of Both Legal Acquiree Companies], then Actual PC will equals to the Fair Value of Business of Legal Acquiree Companies

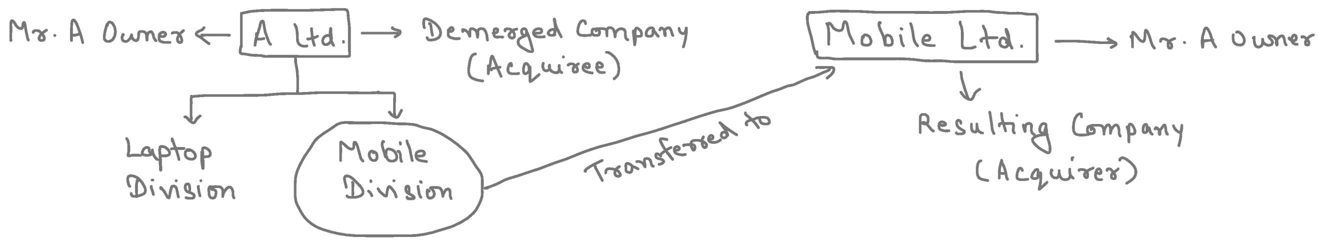
Accounting For Demergers

(1) **Meaning of Demerger :-**

It is an arrangement where some part (division) of a Company [Demerged Company] is transferred to Another Company [Resulting Company]

(2) **Types of Demergers & their Accounting :-**

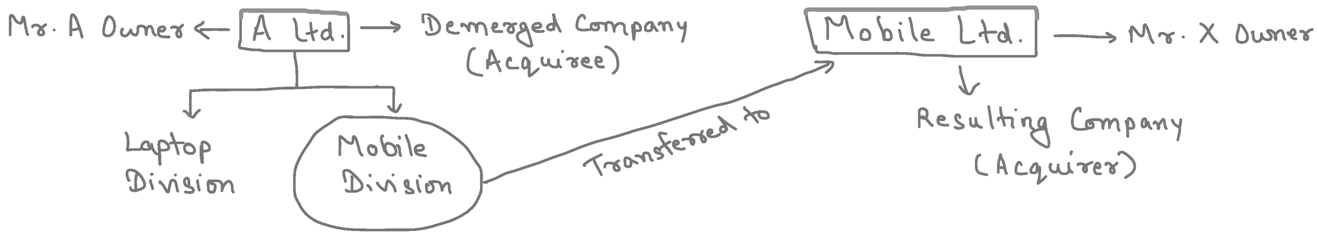
(i) **Demerger in Nature of Common Control :**



- In this Case, Resulting Company [Acquirer] (Eg. Mobile Ltd.) will apply Pooling of Interest Method for Accounting of Demerger [Same As Accounting for Business Combination in case of Common Control Transactions] with an EXCEPTION that Reserves of Demerged Company [Acquiree] will not be taken over.
- Accounting in Books of Demerged Company [Journal Entry] -

Liabilities transferred to Resulting Company A/c Dr.		[Book Value]	
Loss on Restructuring A/c [Capital Reserve] (if any) Dr.		[B/F]	
To Assets transferred to Resulting Company A/c			[Book Value]
To Gain on Restructuring A/c [Capital Reserve] (if any)			[B/F]

(ii) **Demerger in Nature of Business Acquisition :**



- In this Case, Resulting Company [Acquirer] (Eg. Mobile Ltd.) will apply Acquisition Method for Accounting of Demerger [Same As Accounting for Business Combination]

Accounting For Acquisition of Some Interest / Stake in a Joint Operation

Apply Business Combination Accounting [Acquisition Method] for Acquisition of Some Stake/ Interest in a Joint Operation from a Company

Example:-

Company Z has 10% Stake in a Joint Operation named 'XYZ Block'

Company X is acquiring 33.33% Share of Company Z Stake in such Joint Operation

So, Business Combination Accounting will be done by Company X for Acquiring 33.33% share of Company Z

Concentration Test

- It is an Optional Test to determine whether Acquired set of Activities & Assets is an Asset Acquisition or Business Acquisition

When Fair Value of Gross Assets Acquired is substantially concentrated in a Single Asset
⇓
Test is Met
↓
It is an Asset Acquisition

Otherwise
⇓
Test is Not Met
↓
Entity needs to do further Assessment to determine whether it is Asset Acquisition or Business Acquisition
[By considering definition of Business as per Ind AS 103]

- Concentration Test is done by following 3 Steps :-

Step 1: Calculate Fair Value of Gross Assets Acquired :

Fair Value of Consideration Transferred (PC)	xxx
(+) Fair Value of Previously Held Interest	xxx
(+) Fair Value of NCI	xxx
	xxx
(+) Fair Value of Liabilities taken over [Other than DTL]	xxx
	xxx
(-) Cash & Cash Equivalents	(xxx)
(-) DTA	(xxx)
	xxx

Step 2: Identify a Single Asset taken over [of which Fair Value is Higher amongst All Other Assets]

Step 3: Calculate % of Concentration :

$$\Rightarrow \frac{\text{Step 2 Amount}}{\text{Step 1 Amount}} \times 100$$

If it is Substantial (Own Judgement), then it means Concentration Test is Met

⇓

Hence, It is an Asset Acquisition

Asset Acquisition

- If Acquired Set of Activities & Assets is an Asset Acquisition, then We have to apply Accounting for Acquisition of those Assets as per their applicable Ind AS.
- In this Case, if we acquire More than 1 Asset, then Consideration paid is allocated to those Assets in Ratio of Fair Value of Assets Acquired.

Introduction to Ind AS 105

(1) This Ind AS is applicable to following Non Current Assets [Scoped in Assets] :-

- PPE [As per Ind AS 16]
- Intangible Assets [As per Ind AS 38]
- Investment Property [As per Ind AS 40]
- Goodwill Acquired in Business Combination [As per Ind AS 103]

(2) This Ind AS prescribes :-

- Accounting for
  - Non Current Asset Held for Sale
    ⇓
    It means Scoped-in Non Current Asset whose value will be recovered through Sale rather than Use
  - Disposal Group Held for Sale
    ⇓
    It means group of Assets [Both Scoped-in & Scoped-Out] & Liabilities to be disposed of.
    Example of Scoped-out assets are Current Assets, Financial Assets, DTA, etc.
- Disclosure for
  - Discontinued Operations
    ⇓
    It means a division of entity which is classified as held for sale
    [i.e. A Disposal Group which represents major business line, major geographical area of operation or a Subsidiary]

Classification of Non Current Assets [or Disposal Groups] as Held for Sale

Non Current Asset [or Disposal Group] is classified as held for sale only if

- It is available for immediate sale in its present condition
  [Note:
  If Regulatory Approval is pending for sale of an asset, then that asset is still considered as available for immediate sale]

and

- Sale is Highly Probable
  [i.e. Sale is expected within 1 Year from date of Classification]

Measurement of Non Current Assets [or Disposal Groups] as Held for Sale

(1) Initial Measurement on date of classification as held for sale :-

At Lower of
- Carrying Amount
- Fair Value Less Cost to Sell [FVLCTS]

⇓

If FVLCTS is lower, then difference amount is recognised as Impairment Loss as per Ind AS 105.

Example 1 :

A ltd. has classified a PPE as held for sale on 31.3.20X1. On this date, Carrying Amount of PPE is ₹ 1,00,000 and its FVLCTS is ₹ 80,000.

So, it will be measured at ₹ 80,000 [Lower of Carrying Amount & FVLCTS] on date of classification as held for sale.

Hence, there is Impairment Loss as per Ind AS 105 of ₹ 20,000 [1,00,000 - 80,000]

Note :-

(i) Depreciation or Amortisation shall be immediately stopped on such assets from the date of classification as held for sale.

(ii) Disposal Group is measured at Lower of < Carrying Amount of Disposal Group / FVLCTS of Disposal Group

⇓

Any Impairment Loss on Disposal Group as per Ind AS 105 will be borne by Scoped-in Non Current Assets only as follows :

→ Firstly, By Goodwill [Upto Carrying Amount of Goodwill]

→ Then, Remaining Impairment Loss of Disposal Group will be borne by all other scoped-in non current assets in Disposal Group in ratio of their Carrying Amounts.

(iii) If Non Current Asset held for sale is acquired in Business Combination, then it is measured at FVLCTS.

(2) Subsequent Measurement at each Balance Sheet date :-

At Lower of < Carrying Amount / Fair Value Less Cost to Sell [FVLCTS]

If FVLCTS is lower, then difference amount is recognised as Impairment Loss as per Ind AS 105.	If FVLCTS is higher, then difference amount is recognised as Reversal of Impairment Loss [Maximum Reversal of Impairment Loss can be upto the Amount of Total Impairment Loss recognised earlier as per Ind AS 36 & 105]

Note: In Case of Disposal Group, Reversal of Impairment Loss of Disposal Group will be done in All Scoped-in Non Current Assets in Disposal Group (excluding Goodwill) in ratio of their Carrying Amounts.

Example 2 :

In Continuation to Example 1; On 31.3.20X2, FVLCTS of PPE becomes ₹ 75,000.

So, On 31.3.20X2, it will be measured at ₹ 75,000 [Lower of ₹ 80,000 (Carrying Amount) & ₹ 75,000 (FVLCTS)]

Hence, there is Impairment Loss as per Ind AS 105 of ₹ 5,000 [80,000 - 75,000]

Example 3 :

In Continuation to Example 1 ; On 31.3.20x2 , FVLCTS of PPE becomes ₹ 1,10,000. Suppose an Impairment Loss as per Ind AS 36 of ₹ 3,000 is also recognised earlier on this PPE.

Since, On 31.3.20x2, FVLCTS [1,10,000] is higher than Carrying Amount [80,000]. There is Reversal of Impairment Loss of ₹ 30,000 [1,10,000 − 80,000].

Maximum Reversal of Impairment Loss

⇒ IL recognised as per Ind AS 36 + IL recognised as per Ind AS 105

⇒ 3,000 + 20,000 ⇒ ₹ 23,000

Hence Impairment Loss of ₹ 23,000 will be reversed.

New Carrying Amount of PPE = 80,000 + 23,000 ⇒ ₹ 1,03,000

Changes to a Plan of Sale

- If Non Current Asset [or Disposal Group] classified as held for sale no longer meet the criteria, then Entity should cease to classify Non Current Asset [or Disposal Group] as held for sale.
- On this date, it should be measured at the Carrying Amount on date of change of plan if the asset were never classified as held for sale. [i.e. Carrying Amount of Asset just before classification as held for sale adjusted for Depreciation or Amortisation till date]

⇓

Any difference amount will be recognised as Gain or Loss in P&L

Presentation & Disclosure of Non Current Assets [or Disposal Groups] classified as held for sale and Discontinued Operations

(1.) For Non Current Assets Held for Sale :-

Present such asset as a Separate Line Item in Balance Sheet.

(2.) For Disposal Group :-

- Present Assets of Disposal Group separately from Other Assets in Balance Sheet.
- Present Liabilities of Disposal Group separately from Other Liabilities in Balance Sheet.
- Assets & Liabilities of Disposal Group should not be offset in Balance Sheet.

(3.) For Discontinued Operations :-

- Present Assets of Discontinued Operation separately from Other Assets in Balance Sheet.
- Present Liabilities of Discontinued Operation separately from Other Liabilities in Balance Sheet.
- Assets & Liabilities of Discontinued Operation should not be offset in Balance Sheet.

- Post Tax Profit / Loss of Discontinued Operation should be disclosed separately as a Single Amount from Profit / Loss of Continuing Operation in P&L.
- EPS will be disclosed separately for Discontinued Operation.

Operating Segments

(1) Meaning of Operating Segments :-

It is Component of the Entity :

→ Engaged in Business Activity from which it earn revenues & incur expenses,

→ Regularly reviewed by the Chief Operating Decision Maker [CODM], and

→ Discrete Financial Information is available [i.e. Asset, Liability, Income, Expenses].

Note :- CODM can be a single person or group of person responsible for decision making.

(2) Aggregation of Multiple Operating Segments :-

Two or More Operating Segments of a Entity can be aggregated & treated as a Single Operating Segment if they have Similar :

- Economic Characteristics [i.e. Gross Margin]
- Nature of Products or Services
- Nature of Production Process
- Type of Customers
- Method to distribute Products or Services
- Nature of Regulatory Environment

Reportable Segments

- It is an Operating Segment of the Entity for which Segment Information is separately disclosed in Financial Statements.

- An Operating Segment of the Entity will be considered as Reportable Segment if it meets any one of the following criteria :-

(i) If Revenue (Sales) of that Segment is ≥ 10% of Combined Revenue (Sales) of All Segments.

* Revenue of Segment means Both External Revenue & Internal Revenue
  - External Revenue → Sales to Outsiders
  - Internal Revenue → Inter Segment Sales

(ii) If Profit or Loss of that Segment is ≥ 10% of Combined Result of All Segments.

* Combined Result of All Segment means Higher of
  - Combined Profit of All Segments which are in Profit
  - Combined Loss of All Segments which are in Loss

(iii) If Assets of that Segment are ≥ 10% of Combined Assets of All Segments.

Notes :-

→ If External Revenue of above identified All Reportable Segments is less than 75% of Total External Revenue of the Entity, then Additional Segments should be identified as Reportable.

→ If Entity wants to consider any Segment (which does not meet the above criteria) as Reportable, then it can do so.

- All Remaining Segments that are not reportable as above should be Combined & disclosed as "Other Segments" in Segment Information.

Disclosure of Segment Information in Financial Statements

Particulars	Segment A [Reportable Segment]	Segment B [Reportable Segment]	Other Segments	Total
1. Segment Profit or Loss :				
Segment Revenue / Sales [Gross]	xx	xx	xx	xx
(-) GST	(xx)	(xx)	(xx)	(xx)
Segment Revenue / Sales [Net]	xx	xx	xx	xx
(+) Other Operating Income	xx	xx	xx	xx
Total Revenue	xx	xx	xx	xx
(-) Segment Expenses	(xx)	(xx)	(xx)	(xx)
Segment Profit / (Loss)	xx	xx	xx	xx
(+) Unallocated Income Net of Unallocated Expenses				xx
PBIT				xx
(-) Interest & Other Finance Cost				(xx)
PBT				xx
(-) Tax Expense [Current Tax & Deferred Tax]				(xx)
PAT [Whole Entity]				xx
2. Segment Assets & Liabilities :				
(i) Assets				
Segment Assets	xx	xx	xx	xx
Unallocated Investments				xx
Other Unallocated Assets				xx
Total Assets [Whole Entity]				xx
(ii) Equity & Liabilities				
Segment Liabilities	xx	xx	xx	xx
Unallocated Liabilities				xx
Share Capital				xx
Reserves & Surplus				xx
Total Equity & Liabilities [Whole Entity]				xx
3. Other Information :				
Capital Expenditure	xx	xx	xx	xx
Depreciation & Amortization	xx	xx	xx	xx
4. Geographical Information :		Home Country	Foreign Country	Total
Total Revenue		xx	xx	xx
Total Assets		xx	xx	xx
Total Capital Expenditure		xx	xx	xx

Financial Instrument

Any contract which creates in Books of

- 1 Entity ⇓ Financial Asset [FA]
- Another Entity ⇓ Financial Liability [FL] **OR** Equity Instrument [Equity]

(1.) **Financial Assets** :-

- Cash & Bank Balance
- Equity Instruments of Any Other Entity [Eg. Investment in Equity Shares of Any Entity]
- Contractual Right to Receive Cash [Eg. Debtors, B/R, Investment in Debentures of Any Entity, Investment in Preference Shares of Any Entity, Loan given, etc.]
- Contractual Right to Receive Equity Instruments of Any Other Entity [Eg. Investment in Convertible Debentures / Preference Shares of Any Entity etc.]
- Derivative Contracts which are potentially favourable to the Entity

(2.) **Financial Liabilities** :-

- Contractual Obligation to deliver Cash [Eg. Creditors, B/P, Redeemable Debentures Issued by Entity, Redeemable Preference Shares Issued by Entity, Loan Taken, etc.]
- Contractual Obligation to deliver Other Financial Asset
- Derivative Contracts which are potentially unfavourable to the Entity
- Contract to issue Variable No. of Own Equity Shares

(3.) **Equity Instruments** :-

- Which has Residual Interest in Net Assets of the Entity [Eg. Entity's own Equity Shares]
- Contract to issue fixed No. of Own Equity Shares

Note :-

(i.) If there is Any Statutory Right to Receive Cash or Statutory Obligation to deliver Cash, then it will not be classified as Financial Asset or Financial Liability [Eg. Income Tax Payable]

(ii.) If an Entity issues Preference Shares or Debentures or takes a Loan [i.e. in case of Any Borrowing by the Entity]

⇓

It needs to classify that Borrowing as Financial Liability or Equity Instrument on the basis of following features :-

- If Interest / Dividend Payable on such Borrowing is
- If such Borrowing is
- If such Borrowing is Convertible in

- Mandatory → F.L.
- Discretionary → Equity

- Redeemable → F.L.
- Irredeemable/Perpetual → Equity

- Variable No. of Equity Shares of Entity → F.L.
- Fixed No. of Equity Shares of Entity
  - If it is Compulsorily Convertible → Equity
  - If it is Convertible At Option of
    - Issuer (Entity) → Equity
    - Holder → CFI

* If Any Borrowing by the Entity has Mix features of financial liability & Equity Instrument, then it is known as Compound Financial Instrument (CFI)

* Also for clarification purpose, Please Note that CFI can be possible only from view point of Entity taking money on Borrowing [ie. Issuer]

↓

from View Point of Investor who is Investing in Preference Shares / Debentures / Equity Shares of Any Entity [ie. Holder], it will be financial Asset only

(iii.) Interest / Dividend Income on financial Assets is recognised in P&L

(iv.) Interest / Dividend Expense on financial liability is recognised in P&L

(v.) Interest / Dividend Expense on Equity Instruments is recognised in Retained Earnings

Examples :-

Particulars	FA	FL	Equity	Not a financial Instrument As per Ind AS 109 [i.e. Other Asset / Liability]
Cash / Bank	✓			
T/R, B/R	✓			
Loan Given	✓			
Investment in Equity Shares / Preference Shares / Debentures, etc.	✓			
Investment in Convertible or Irredeemable Preference Shares / Debentures, etc.	✓			
Security Deposit Given	✓			
PPE				✓
Inventory				✓
Intangible Asset				✓
Prepaid Expenses				✓
Advance given for Goods & Services				✓
Investment Property				✓

T/P, B/P		✓		
Redeemable Preference Shares / Debentures with Mandatory Interest		✓		
Loan Payable in Cash with Interest		✓		
Security Deposit Taken		✓		
Income Received in Advance / Unearned Income				✓
Tax Liability or Tax Refundable				✓
Irredeemable Preference Shares / Debentures with Discretionary Interest			✓	
Compulsorily Convertible Preference Shares / Debentures with Discretionary Interest			✓	
Redeemable Preference Shares / Debentures with Discretionary Interest [CFI]		✓	✓	
Irredeemable Preference Shares / Debentures with Mandatory Interest [CFI]		✓	✓	
Compulsorily Convertible Preference Shares / Debentures with Mandatory Interest [CFI]		✓	✓	
Preference Shares / Debentures Convertible At Option of Holder [CFI]		✓	✓	

Methods for Measurement & Recognition of Financial Assets & Financial Liabilities

(1.) Financial Assets are measured at

Amortised Cost Method [ACM]

⇓

If Intention is to hold the Asset till Maturity

[i.e. Intention to collect only Contractual Cash flows of the Asset (Interest or Principal)]

Fair Value Through Other Comprehensive Income (FVTOCI)

⇓

If Intention is to hold the Asset for some time & sell it Before Maturity

[i.e. Intention to collect Contractual Cash flows & Cash flow from Sale of Asset (taking benefit of Market Prices)]

Fair Value Through Profit or Loss (FVTPL)

⇓

If Intention is to Hold the Asset for Trading Purpose Only

[i.e. Intention to collect Cash flow from Sale of Asset Only (taking Benefit of Market Prices)]

⇓

So, Only following 2 Financial Assets are shown at FVTPL:

→ Investment in Equity Shares of Any Other Entity

→ Derivative Financial Asset

Note :- Investment in Equity Shares of Any Other Entity can be shown At FVTOCI also. In that case, it will be an Irrevocable Choice [i.e. Entity has to follow it forever & it cannot show this Investment in Equity Shares at FVTPL again in future]

(2) Financial Liabilities are generally measured At Amortised Cost Method (ACM) only

Note :- Only following 2 Financial Liabilities should be measured at FVTPL :

→ Derivative Financial Liability

→ Financial Guarantee

Amortised Cost Method (ACM)

Under this Method, Entity shall do Accounting as follows :

- Entity shall initially recognise F.A. or F.L. at Fair Value [Adjusted with Transaction Cost]

Fair Value :-

If Transaction is done At Market Terms
[i.e. Only Effective Interest Rate (EIR) is given in question]
⇓
Amount received or given is considered as fair value

If Transaction is done At Off Market Terms
[i.e. Market Interest Rate on Similar Instrument is given in Question]
⇓
Calculate fair Value by discounting the future Cash flows using Market Interest Rate on similar Instruments (i.e. P.V. of future Cash flow)

- Entity shall charge Interest Expense (on F.L.) or Interest Income (on F.A.) at Discounting Rate over the period to unwind the discount

Calculation of Finance Cost or Finance Income [F.A. / F.L. A/c] using Amortisation Table :

Year (1)	Opening Balance of F.A. or F.L. (2)	Interest @ Discounting Rate (3) = (2) X Discounting Rate	Actual Payment of Interest & Principal Amount (4)	Closing Balance of F.A. or F.L. (5) = (2) + (3) - (4)
✓	✓	✓	✓	✓

Discounting Rate to charge Interest over the period :

If Transaction is done At Market Terms
⇓
EIR

If Transaction is done At Off Market Terms
⇓
Market Interest Rate on Similar Instrument

* In this case, If Transaction Cost is given in question, then EIR will also be given. Hence, Use EIR to unwind the discount in such case

- Journal Entries :-

For Financial Asset

→ At Beginning :

Financial Asset
  To Bank

→ At Each Year End :

Financial Asset
  To Finance Income [P&L]   [For Unwinding of Discount]

Bank
  To Financial Asset   [For Actual Interest or Principal Installment Received (if any)]

For Financial Liability

→ At Beginning :

Bank
  To Financial Liability

→ At Each Year End :

Finance Cost [P&L]
  To Financial Liability   [For Unwinding of Discount]

Financial Liability
  To Bank   [For Actual Interest or Principal Installment Received (if any)]

Note :-

(i) EIR is the Rate at which PV of Future Cash flows from the Instrument become equals to the Net Cash flow at the beginning
 → It will be given in question generally
 → Otherwise Calculated using Trial & Error Method

(ii.) Transaction Cost includes Regulatory fee, Charges for Document Preparation & Processing, Brokers fee, Upfront fee, etc.
 → It is Added to Fair Value of Financial Asset at Initial Recognition
 → It is Subtracted from Fair Value of Financial Liability at Initial Recognition

(iii) If Transaction is done At Off Market Terms, then there will be difference between Amount received or paid at beginning & Fair Value calculated at beginning
⇓
This difference will be recognised in Journal Entry on Initial Recognition as follows :

- If there is Any Special Relationship between the parties in the transaction
  - Employer - Employee
    ↓
    Loan At Concessional Rate is given to Employee
    ↓
    Employer : Prepaid Staff Cost
    Employee : Advance Salary Income
    ↓
    Write it off over the Period of Loan in P&L [As per Ind AS 19]
  - Lessor - Lessee
    ↓
    Security Deposit given to Lessor
    ↓
    Lessee : ROU Asset [Prepaid Lease Rent]
    Lessor : Advance Lease Income
    ↓
    Write it off by charging Depreciation in P&L over period of Loan [As per Ind AS 116]
  - Parent - Subsidiary
    - Parent Company is providing Loan to Subsidiary Co.
      ↓
      Parent : Investment in Subsidiary
      Subsidiary : Equity [Capital Contribution from Parent]
      ↓
      Treatment As per Ind AS 27 & 110
    - Subsidiary Co. is providing Loan to Parent Co.
      ↓
      Sub : Dividend Distribution
      Parent : Dividend Income
      ↓
      Recorded in Retained Earnings
- Otherwise
  ⇓
  P&L

Example :- Transaction At Market Terms

A ltd. issued 10% Debentures [Face Value ₹ 1,00,000] at ₹ 94,000. Interest is paid Annually & It will be redeemed at End of 3rd Year at Face Value. Pass Journal Entries for 1st Year. Given PV Factors

	Year 1	Year 2	Year 3
@ 12%	0.893	0.797	0.712
@ 13%	0.885	0.783	0.693

Solution :-

Calculation of EIR (By Using Trial & Error Method) :

Year	Cash flow	PVF @ 12%	P.V.	PVF @ 13%	P.V.
1	10,000	0.893	8,930	0.885	8,850
2	10,000	0.797	7,970	0.783	7,830
3	10,000	0.712	7,120	0.693	6,930
3	1,00,000	0.712	71,200	0.693	69,300
			95,220		92,910

∴ Now, Do Interpolation to find the EIR at which PV of future Cash flow is ₹ 94,000

$$EIR = 12\% + \frac{95,220 - 94,000}{95,220 - 92,910} \times (13 - 12) = 12 + 0.53 = 12.53\%$$

Calculation of Interest Expense (Finance Cost) on Financial Liability [F.L. A/c] :-

Year	Opening Balance of Debenture A/c	Interest @ 12.53%	Actual Payment of Coupon/ Principal	Closing Balance of Debenture A/c
1	94,000	11,778	10,000	95,778
2	95,778	12,001	10,000	97,779
3	97,779	12,221	1,10,000	—
		36,000		

Journal Entries :- 1st Year

	Particulars	Dr.	Cr.
At Beginning :	Bank	94,000	
	To 10% Debentures [F.L.]		94,000
At Year End :	Interest Expense [P&L]	11,778	
	To 10% Debentures [F.L.]		11,778
	10% Debentures [F.L.]	10,000	
	To Bank		10,000
	OR		
	Interest Expense [P&L]	11,778	
	To Bank		10,000
	To 10% Debentures [F.L.]		1,778

Example :- Transaction At Off Market Terms

A Ltd. provides concessional Loan of ₹ 1 Lakh to its Employee at Interest Rate of 6% p.a. for 3 years. Employee will pay Interest Annually & Principal Amount At End of 3rd Year. Market Rate of Interest is 10% p.a. Pass Journal Entries for 1st Year

Solution :-

Fair Value :

Year	Cash flow	PVF @ 10%	P.V.
1	6,000	0.909	5,454
2	6,000	0.826	4,956
3	6,000	0.751	4,506
3	1,00,000	0.751	75,100
			90,016

Calculation of Interest Income on Loan to Employee [F.A. AC] :

Year	Op. Bal. of F.A.	Interest @ 10%	Actual Payment of Interest / Principal	Cl. Bal. of F.A.
1	90,016	9,002	6,000	93,018
2	93,018	9,302	6000	96,320
3	96,320	9,680	1,06,000	–
		27,984		

Journal Entries :- 1st Year

		Dr.	Cr.
At Beginning :	Loan to Staff [F A]	90,016	
	Prepaid Staff Cost	9,984	
	To Bank		1,00,000
At Year End :	Loan to Staff [F A]	9,002	
	To Interest Income [P&L]		9,002
	Bank	6,000	
	To Loan to Staff [F A]		6,000
	Staff Cost [P&L]	3,328	
	To Prepaid Staff Cost		3,328

* Prepaid Staff Cost of ₹ 9,984 will be charged to P&L each year by ₹ 3,328 $\left[\frac{9,984}{3 \text{ Years}}\right]$

· Steps to Solve the Practical Questions :-

Step 1 : Calculate Fair Value of F.A. or F.L.

Step 2 : Adjust Transaction Cost from Fair Value (if any) to find the Amount to be recognised initially

Step 3 : Prepare Amortisation Table

Step 4 : Pass Journal Entries if required in question

Fair Value Through Other Comprehensive Income [FVTOCI]

Under this Method, Entity shall do Accounting As follows :

- Same as ACM But on Each Balance Sheet Date, Financial Asset is shown At Fair Value
  ⇓
  Hence, Difference between Carrying Amount as per ACM & Fair Value is recognised as Fair Value Gain | Loss in OCI

- Balance in Fair Value Reserve [OCI] A/c will be Reclassified to P&L on Sale of such Financial Asset But In case of Investment in Equity Shares shown at FVTOCI under irrevocable option, Fair Value Reserve [OCI] on sale of such Investment will be transferred to Retained Earnings directly (i.e. It is an item of OCI which is Not Reclassifiable to P&L)

Fair Value Through Profit or Loss [FVTPL]

Under this Method, Entity shall do Accounting as follows :

- Entity shall initially recognise the Financial Asset or Financial Liability At Fair Value
- Dividend will be recognised At Coupon Rate directly in P&L
- At Each Year end, Difference between Fair Value At Balance Sheet Date & At which it was previously recorded is recognised as Fair Value Gain | Loss in P&L

Note :- Transaction Cost is not added | deducted from Fair Value on Initial Recognition of Financial Asset or Financial Liability at FVTPL
⇓
It will be recognised as an Expense in P&L

Compound Financial Instruments [CFI]

- It is an Instrument issued by an Entity which has Mix Features of Financial Liability and Equity Instrument

- Steps to be followed to Solve the Practical Questions :-

  Step 1 : Allocate Total Proceeds of the Instrument (Issue Price) at Initial Recognition into following 2 Components :

Financial Liability (F.L.) Component	Equity Instruments (Equity) Component
⇓	⇓
P.V. of Future Cash flows in the "Nature of Financial Liability (F.L.)" discounted using the Market Interest Rate on Similar Instruments	Balancing Figure ⇓ Total Proceeds (Issue Price) − Financial Liability (F.L.) Component

Note :- Cash Flows in the Nature of financial Liability means :
→ Interest / Dividend Payment in Cash [If Mandatory]
→ Redemption Amount [If Redeemable in Cash or Convertible At Option of Holder]

Step 2 : Allocate Transaction Cost (if Any) on Compound financial Instrument to Financial Liability (F.L.) Component & Equity Component in ratio of their Amounts as calculated in Above Step 1

⇓

Then Initially Recognise financial Liability Component & Equity Component after deducting such transaction Cost

Journal Entry at Initial Recognition :

Bank A/c	Total Proceeds (Net of transaction Cost)
To Debentures (Financial Liability)	F.L. Component (Net of transaction Cost)
To Debentures (Equity)	Equity Component (Net of transaction Cost)

Step 3 : Financial Liability (F.L.) Component is measured At Amortised Cost Method [ACM] on each Balance Sheet Date [Prepare Amortisation Schedule]

Equity Component is carried at Initially Recognised Value Only

Step 4 : On Maturity Date

If It is Converted in Equity Shares

⇓

Debentures (financial Liability)	Carrying Amt.
Debentures (Equity)	Carrying Amt.
To Equity Share Capital	Face Value
To Securities Premium	B/f

If it is Redeemed in Cash

⇓

Debentures (Financial Liability)	Carrying Amount
To Bank	
Debentures (Equity)	Carrying Amount
To Retained Earnings	

Example :-

A Ltd. issued 10% Debentures of ₹ 1,00,000. Interest is paid Annually. It is convertible at option of holder at end of 3rd Year in Equity Shares of Company or will be redeemed at par. Market Interest Rate on Similar Non-Convertible Instrument is 12%. Pass Journal Entries.

Solution :-

Calculation of Amount of Financial Liability & Equity Component at Initial Recognition :

→ Calculation of Financial Liability Component ⇒

Year	Cash Flow	PVF @ 12%	P.V.
1	10,000	0.893	8,930
2	10,000	0.797	7,970
3	10,000	0.712	7,120
3	1,00,000	0.712	71,200
			95,220

→ Calculation of Equity Component ⇒ 1,00,000 − 95,220 = ₹ 4,780

Calculation of Interest Expense on Financial Liability Component [Amortisation Schedule]:

Year	Op. Bal. of F.L.	Interest @ 12%	Actual Payment of Installment	Cl. Bal. of F.L.
1	95,220	11,426	10,000	96,646
2	96,646	11,598	10,000	98,244
3	98,244	11,756	10,000	1,00,000

Journal Entries:

		Dr.	Cr.
1st Year Beginning	Bank	1,00,000	
	To 10% Debentures (F.L.)		95,220
	To 10% Debentures (Equity)		4,780
End	Int. Exp. (P&L)	11,426	
	To 10% Deb. (F.L.)		11,426
	10% Deb. (F.L.)	10,000	
	To Bank		10,000
2nd Year End	Int. Exp. (P&L)	11,598	
	To 10% Deb. (F.L.)		11,598
	10% Deb. (F.L.)	10,000	
	To Bank		10,000
3rd Year End	Int. Exp. (P&L)	11,756	
	To 10% Deb. (F.L.)		11,756
	10% Deb. (F.L.)	10,000	
	To Bank		10,000

Settlement:

→ Redeemed in Cash:

	Dr.	Cr.
10% Deb. (F.L.)	1,00,000	
To Cash		1,00,000
10% Deb. (Equity)	4780	
To R/E		4780

→ Convert in Equity Shares:

	Dr.	Cr.
10% Deb (F.L.)	1,00,000	
10% Deb. (Equity)	4,780	
To Equity Share Capital		1,04,780

<u>Note</u>:- <u>If there is Early Redemption/Repurchase of Instrument (Before Maturity) in Cash</u>:

Step 1 : Calculate Carrying Amount of Financial Liability Component [Using Amortisation Table] & Equity Component on Early Redemption / Repurchase Date

Step 2 : Assume Consideration paid on Early Redemption / Repurchase is for Both Financial Liability Component & Equity Component

⇓

So, Now find Out Consideration Paid for Financial Liability Component and Equity Component Separately as follows :

- Consideration Paid for Financial Liability Component
  ⇓
  P.V. of Remaining future Cash flows on Early Redemption / Repurchase Date discounted using the Market Interest Rate on Similar Instrument on Early Redemption / Repurchase Date

- Consideration Paid for Equity Component
  ⇓
  Total Consideration Paid for Early Redemption / Repurchase
  − Consideration Paid for Financial Liability Component

Step 3 : Journal Entry for Settlement :

→ Settlement of Financial Liability Component

Debentures (Financial Liability)	Carrying Amt. on Early Redemption Date
P&L	B/f
To Bank	Consideration calculated in Step 2 for F.L.
To P&L	B/f

→ Settlement of Equity Component

Debentures (Equity)	Carrying Amt. on Early Redemption Date
Retained Earnings	B/f
To Bank	Consideration calculated in Step 2 for Equity
To Retained Earnings	B/f

Modification in Terms of Financial Asset

Steps to be followed to Solve the Practical Question :

Step 1 : Calculate Carrying Amount of Financial Asset on Modification Date [Using Amortisation Table]

Step 2 : Calculate Revised Amount of Financial Asset by discounting the Revised Remaining future Cash flows using Original EIR

Step 3 : Difference between Amount in Step 1 & 2 will be recorded in P&L as Gain / Loss due to Modification

Journal Entry for Modification :

- If Amount of F.A. Increases due to Modification
  ⇓
- If Amount of F.A. Decreases due to Modification
  ⇓

Financial Asset To P&L	[Diff. b/w Amt. in Step 1 & 2]	P&L To Financial Asset	[Diff. b/w Amt. in Step 1 & 2]

Note :-

(i) If there is Any Special Relationship between Parties (Eg. Employer - Employee), then the Difference between Amount in Step 1 & 2 will be recorded in Special A/c initially created (Eg. Prepaid Staff Cost)

(ii) If on a Loan given (F.A), the Other Party Prepays an Installment, then It will also be considered as a Modification in Financial Asset.

In this Case, Journal Entry for Modification will be as follows :

Bank	Prepayment Amount
P&L / Special A/c	B/f
To Financial Asset	Decrease in F.A. as calculated by Diff. b/w Amt. in Step 1 & 2
To P&L / Special A/c	B/f

Modification in Terms of Financial Liability / Derecognition of Financial Liability

Steps to be followed to Solve the Practical Question :

Step 1 : Calculate Modification % :-

$$\Rightarrow \frac{\left[\text{P.V. of Revised Remaining Future Cash flows on Modification Date using Original EIR} + \text{Fees Paid on Modification}\right] - \text{Carrying Amount of Financial Liability on Modification Date}}{\text{Carrying Amount of Financial Liability on Modification Date}} \times 100$$

Step 2 : If Modification % is

- 10% or More
  - ⇓ Apply Extinguishment Accounting
    - Derecognise Existing Financial Liability on Modification Date at its Carrying Amount
    - Recognise New Financial Liability at P.V. of Revised Remaining Future Cash Flows on Modification Date discounted using the Market Interest Rate on Modification Date
      - [If Market Interest Rate on Modification Date is not given in question, then Assume New Interest Rate of Financial Liability as Market Interest Rate]
    - Pay fees Incurred on Modification through Bank
    - Difference in All these 3 Items in Journal Entry will be Gain/Loss due to Modification in P&L [B/F]
- Less than 10%
  - ⇓ Apply Modification Accounting
  - ⇓ Pay fees Incurred on Modification by Debiting Financial Liability :

    Financial Liability
    To Bank

    and

    Then Calculate New EIR on Modification Date At which P.V. of Revised Remaining Future Cash flows become equals to Carrying Amount of Financial Liability (after payment of Modification fee) on Modification Date

Journal Entry on Extinguishment Accounting

Financial Liability (Existing)	Carrying Amt.	
P&L	B/F	
To Financial Liability (New)		P.V.
To Bank		Fees Paid
To P&L		B/F

Note:- Debt for Equity Swap :-

- If Entity Extinguish / Settle its Financial Liability by issuing its Equity Instrument
- In this case, Accounting will be done as follows:

Derecognise Carrying Amount of Financial Liability extinguished/ settled by issuing Equity Instruments

Recognise Equity Instrument issued At Fair Value

[Fair Value ⇒ Fair Value of Net Assets of Entity × % of Equity Stake given]

Difference in these 2 Items in Journal Entry will be Gain / Loss in P&L

Journal Entry :

Financial Liability	Carrying Amount	
P&L	B/F	
To Equity		Fair Value of Equity Stake
To P&L		B/F

Derecognition of Financial Asset

Accounting for Derecognition of Financial Asset in following Specific Cases:

(1.) Securitisation of Loan :-

- In this, Entity transfers the Right to Receive the Cash flows on a Secured Loan to a SPV
- Steps to be followed to Solve the Practical Questions :

Step 1: Calculate Fair Value of Securitised Component (i.e. Transferred Component) of Loan :-

Fair Value of Total Loan	xxx
(-) Fair Value of Principal Retained [Principal Strip]	(xxx)
(-) Fair Value of Interest Retained [Interest Strip]	(xxx)
(-) Fair Value of Service fee for Collection of Amount [Service Asset]	(xxx)
Fair Value of Securitised Component of Loan	xxx

Step 2 : Allocate Carrying Amount of Loan to each component in Ratio of their Fair Value :-

→ Carrying Amount of Securitised Component = Carrying Amount of Total Loan × $\frac{\text{Fair Value of Securitised Component}}{\text{Fair Value of Total Loan}}$

→ Carrying Amount of Principal Strip = Carrying Amount of Total Loan × $\frac{\text{Fair Value of Principal Strip}}{\text{Fair Value of Total Loan}}$

→ Carrying Amount of Interest Strip = Carrying Amount of Total Loan × $\frac{\text{Fair Value of Interest Strip}}{\text{Fair Value of Total Loan}}$

→ Carrying Amount of Service Asset = Carrying Amount of Total Loan × $\frac{\text{Fair Value of Service Asset}}{\text{Fair Value of Total Loan}}$

Step 3 : Journal Entry for Securitisation of Loan

→ For Derecognition of Securitised Component of Loan

	Dr.	Cr.
Bank	Consideration Received	
P&L	B/f	
To Loan [Financial Asset]		Allocated Carrying Amt. of Securitised Component
To P&L		B/f

→ Recognising Retained Portion of Each Component Separately

	Dr.	Cr.
Principal Strip Receivable	Allocated Carrying Amount	
Interest Strip Receivable	Allocated Carrying Amount	
Service Asset	Allocated Carrying Amount	
To Loan [Financial Asset]		xxx

(2) Factoring of Debtors / Receivables :-

- Recognise Cash / Bank for Consideration Received from factoring Company
- Derecognise Receivables at its Carrying Amount
- Recognise Continuing Involvement Asset At Lower of
  ⇓
  Amount of Receivables
  $\boxed{\text{OR}}$
  Guarantee Amount to be Reimbursed to factoring Company in case of Any Loss
- Recognise Associated Liability equals to
  ⇓
  Guarantee Amount to be Reimbursed to factoring Company in case of Any Loss
  +
  Fair Value of Guarantee
- Difference in All these 4 Items in Journal Entry will be Gain / Loss on Derecognition [B/f]
  ⇓
  It is recognised in P&L

Journal Entry for Factoring of Receivables

	Dr.	Cr.
Bank	Consideration Received	
Continuing Involvement Asset	✓	
Loss on Derecognition [P&L]	B/f	
To Receivables		Carrying Amount
To Associated Liability		✓
To Gain on Derecognition [P&L]		B/f

Note:- Fair Value of Guarantee means Consideration received for giving Guarantee to Factoring Company
⇓
It is like Unearned Income. Hence, Recorded as Associated Liability and Amortised in P&L over the period of factoring.

Impairment of Financial Asset

- It is a Loss Allowance for Expected Credit Losses on Financial Asset [Eg. Provision for Doubtful Debts]
- It applies to Financial Assets measured At ACM or FVTOCI
- Impairment on a Financial Asset is recognised in P&L as follows:
  → If Credit Risk is Low, then 12 Months Expected Credit Loss (ECL) is recognised
  → If Credit Risk is High, then Lifetime Expected Credit Loss (ECL) is recognised
- Calculation of Impairment (Loss Allowance / Expected Credit Loss) Amount:

(i.) Method for Calculation of Impairment Loss For Single Financial Asset [PoD Approach]

⇒ Gross Carrying Amount of F.A. × Loss Given Default (LGD) × Probability of Default (PoD)

(ii.) Method for Calculation of Impairment Loss For Portfolio of Financial Asset [Provision Matrix Approach]

Category of Financial Asset on the basis of their Risk (1)	Gross Carrying Amount of Financial Asset (2)	Expected Credit Loss [(2) × Default/Loss Rate]
Current	xxx	xxx
1 - 30 Days Past Due	xxx	xxx
31 - 60 Days Past Due	xxx	xxx
More than 60 Days	xxx	xxx
		xxx

Note:- Default Rate | Loss Rate:

$$\Rightarrow \frac{\text{P.V. of Expected Loss (on the basis of Observed Historical Sample Data)}}{\text{Gross Carrying Amount of Financial Asset}} \times 100$$

Note:- In Case of Financial Assets measured at FVTOCI, Fair Value Change at each Balance Sheet Date contains ECL (Impairment) portion also. Hence, Decrease in Fair Value to the extent of Impairment will be recognised in P&L

Accounting for Financial Guarantee

- It is an Agreement in which Entity provides Guarantee to the Lender to repay the debt if the Borrower defaults
⇓
Due to this Financial Guarantee by the Entity, Lender agrees to provide the Loan to the Borrower at Normal Interest Rate (instead of Higher Interest Rate)

· Steps to be followed to solve the Practical Question :-

Step 1 : Entity shall Initially Recognise Financial Guarantee (It is a Financial Liability) at Present Value (P.V.) of Interest Savings to Borrower over the period discounted using the 'Interest Rate without Guarantee'

&

Debit the Same Amount as Receivable from Borrower or Special A/c (if any Special Relationship exists b/w Parties)

* Journal Entry at Initial Recognition :

Receivable / Special A/c Like Investment in Subsidiary
    To Financial Guarantee

* P.V. of Interest Savings is calculated as follows :

Year	Interest Payable by Borrower @ Rate Without Guarantee	Interest Payable by Borrower @ Rate With Guarantee	Interest Savings to Borrower	P.V.F. @ Rate Without Guarantee	P.V. of Interest Savings to Borrower
(1)	(2)	(3)	(4) = (2) - (3)	(5)	(6) = (4) × (5)

Step 2 : At Each Year End, We have to show Financial Guarantee at Fair Value (Since it is a Financial Liability measured at FVTPL)

Fair Value of Financial Guarantee At Each Year End is Higher of

P.V. of Remaining future Interest Savings to Borrower $\boxed{OR}$ Expected Loss due to Default by Borrower [Loan Amount taken by Borrower × Probability of Default by Borrower]

Step 3 : Difference in Amount in Step 2 & Previously recorded amount of Financial Guarantee will be recognised as Fair Value Gain / Loss in P&L

Journal Entry :

If Fair Value of Financial Guarantee Increases

P & L
    To Financial Guarantee

If Fair Value of Financial Guarantee Decreases

Financial Guarantee
    To P & L

Step 4 : On Maturity of Borrowing for which Guarantee is given

If Borrower does not defaults
⇓
Financial Guarantee   Carrying Amount
    To P & L

If Borrower defaults in Repayment of Borrowing
⇓
Financial Guarantee   Carrying Amt. B/F
P & L
    To Bank   Amt. Paid due to default
    To P & L   B/F

Example :

A Ltd. has taken a Loan of ₹ 1,00,000 for 3 years. Interest Rate is 8% since Loan is guaranteed by B Ltd. (Holding Co. of A Ltd.). Otherwise Interest Rate without guarantee for A Ltd. will be 11%. Interest is to be payable annually & Principal of ₹ 1,00,000 at end of 3rd year.

Pass Journal Entries if PoD by A Ltd. is 2% at end of 1st Year & 6% at end of 2nd Year.

Solution:

Calculation of Fair Value of financial Guarantee at Initial Recognition:

Year	Interest @ 11%	Interest @ 8%	Interest Savings	PVF @ 11%	P.V. of Interest Savings
1	11,000	8,000	3,000	0.901	2,703
2	11,000	8,000	3,000	0.812	2,436
3	11,000	8,000	3,000	0.731	2,193
					7,332

Journal Entry at Initial Recognition

	Dr	Cr
Investment in Subsidiary	7,332	
To financial Guarantee		7,332

Fair Value of financial Guarantee At 1st Year End

→ P.V. of Remaining Interest Savings

Year	Interest Savings	PVF @ 11%	P.V.
1 [2nd Year End]	3,000	0.901	2,703
2 [3rd Year End]	3,000	0.812	2,436
			5,139

→ Expected Loss ⇒ 1,00,000 x 2% = 2,000

∴ Higher is ₹ 5,139 [Fair Value At 1st Year End]

Now, Decrease in Fair Value of financial Guarantee At 1st Year End ⇒ 7332 − 5139 = 2193

Journal Entry At 1st Year End

	Dr	Cr
Financial Guarantee	2,193	
To P&L		2,193

Fair Value of financial Guarantee At 2nd Year End

→ P.V. of Remaining Interest Savings

Year	Interest Savings	PVF @ 11%	P.V.
1 [3rd Year End]	3,000	0.901	2,703
			2,703

→ Expected Loss ⇒ 1,00,000 x 6% = 6,000

∴ Higher is ₹ 6,000 [Fair Value At 2nd Year End]

Now, Increase in Fair Value of financial Guarantee At 2nd Year End ⇒ 6000 − 5139 = 861

Journal Entry At 2nd Year End

	Dr	Cr
P&L	861	
To Financial Guarantee		861

Journal Entry At 3rd Year End

If Borrower [A Ltd.] does not defaults

↓

	Dr	Cr
Financial Guarantee	6,000	
To P&L		6,000

If Borrower [A Ltd.] defaults in payment of Borrowing [Eg. 10% Default, i.e. 1,00,000 x 10% = 10,000]

↓

	Dr	Cr
Financial Guarantee	6,000	
P&L (B/F)	4,000	
To Bank		10,000

Accounting for Derivative Contracts

(1.) Meaning & Features of Derivative Contracts :-

- It is a Contract between 2 parties for Purchase or Sale of an Underlying Asset on a Certain future date for a certain price
- Underlying Asset can be Shares, Currency, etc.
- Examples of Derivative Contracts are Forward Contracts, Option Contracts, Future Contracts, etc.
- Derivative Contract does not have Any Value of its own but it derives its value from the underlying Asset
- Derivative Contracts require No or Little Initial Investment [Eg. Cost / Premium Paid for Purchase of an Option Contract]
- Derivative Contracts are Settled as follows :
  - → Forward & Option Contracts ⇒ By Physical Delivery ☑ OR Can Also be Settled in Net Cash
  - → Future Contracts ⇒ Settled in Net Cash Only

(2.) Accounting for Derivative Contracts :-

- If it is Potentially favourable for the Entity ⇒ Recognise Derivative Financial Asset [DFA]
- If it is Potentially unfavourable for the Entity ⇒ Recognise Derivative Financial Liability [DFL]
- It is measured at FVTPL

Fair Value of a Derivative Contract

At Initial Recognition [Contract Date]	At Each Balance Sheet Date
⇓	⇓
It is generally considered as 'Zero' But if there is Some Cost / Premium is paid to enter into Derivative Contract, then that Amount will be considered as Fair Value (Potentially Favourable)	Difference between Price of Underlying Asset on Contract Date & Balance Sheet Date [If Yield Rate is also given in question, then Consider P.V. of Above Amount as Fair Value]

- Journal Entries :-
  - (i) On Contract Date :
    - → Generally, No Entry as Fair Value is Zero
    - → But If Some Cost / Premium is Paid

	Dr	Cr
Derivative Financial Asset [DFA]	Amount Paid	
To Bank		Amount Paid

  - (ii) On Each Balance Sheet Date :
    - → DFA or DFL is to be shown At Fair Value. So, Difference between Fair Value of DFA or DFL on Balance Sheet Date & Previously Recorded Amount will be recognised as Fair Value Gain / Loss in P&L
    - → Journal Entry if Derivative Contract is

Potentially favourable	Potentially Unfavourable
⇓	⇓

DFA	P&L
To P&L	To DFL

(iii) On Settlement Date :

→ If Derivative Contract is Settled by Physical Delivery [Forward / Option Contract]

If Contract is for Purchase of Underlying Asset

Underlying Asset	Fair Value of UA on Settlement Date
DFL (if any)	Carrying Amount
To Bank	Payment of Initially Contracted Amount
To DFL (if any)	Carrying Amount

If Contract is for Sale of Underlying Asset

Bank	Payment of Initially Contracted Amount
DFL (if any)	Carrying Amount
To Underlying Asset	Fair Value of UA on Settlement Date
To DFL (if any)	Carrying Amount

* Difference in Journal Entry will be recognised in P&L as fair value Gain | Loss

→ If Derivative Contract is Settled by Net Cash [Future Contract]

If Gain on Settlement

Bank	Carrying Amount of DFA
To DFA	i.e. Its fair Value

If Loss on Settlement

DFL	Carrying Amount of DFL
To Bank	i.e. Its fair Value

Hedge Accounting

- When a Derivative Contract is entered for Hedging Purpose, Entity has a choice to Apply Hedge Accounting
- Accounting for Different Types of Hedge :

(1.) Cash flow Hedge :-

→ In this, Hedging is done to Protect the future Cash flows

Eg.: Hedging through future Contract for Receipt in foreign Currency of Sale of Goods in future

→ Hedged Item [Eg. Sale of Goods] is accounted as per respective Ind AS [Eg. Ind AS 115]

→ Hedging Instrument [Eg. Future Contract] is accounted as per Derivative Contract Accounting but the fair Value Gain | Loss at Each Balance Sheet Date will be recorded through 'Cash flow Hedge Reserve [OCI]' instead of P&L

↓

And It will be Reclassified to P&L when Hedged Item is recorded in Books

(2.) Fair Value Hedge :-

→ In this, Hedging is done to protect the Fair Value of an Item

Eg: Hedging through forward Contract for Fair Value After 1 Year of Investment in Debentures

→ Hedged Item is accounted as per respective Ind AS But Any Fair Value Gain | Loss on such Hedged Item will be recorded through P&L

→ Hedging Instrument is accounted as per Derivative Contract Accounting

(3) Hedge of Net Investment in Foreign Operation :-

→ In this, Hedging is done to Protect Receipt in Foreign Currency of Sale of Foreign Operation by Entity

→ Accounting similar to Cash Flow Hedge

Embedded Derivatives

- In this, A derivative is embedded in a Normal Host Contract
- Host Contract can be
  - → Financial Liability [Eg. Loan Taken from a Bank]
  - → Non-Financial Item [Purchase / Sale of Goods, PPE etc.]
- When Host Contract & Derivative Embedded in it are 'Not Closely Related', then We need to Separate Host Contract & Embedded Derivative to do their Accounting Separately.

[ie. When Host Contract & Derivative Embedded in it are 'Closely Related', then there is No need to separate them & Hence, Do Accounting only for Host Contract Normally]

* Closely Related means It is a general practice in Market

* When Host Contract & Embedded Derivative is Separated

Host Contract is Accounted as per respective Ind AS

Derivative Contract is Accounted as per Derivative Contract Accounting

- Following are the 2 Cases of a Derivative Embedded in a Normal Host Contract :-

(1.) Prepayment Option in a Loan Taken from a Bank :-

→ Host Contract : Loan Taken from a Bank (Financial Liability)

→ Embedded Derivative : Prepayment Option

→ These are Not Closely Related if Prepayment Amount is Not Approximately equals to the Carrying Amount of Loan taken from Bank (Financial Liability) Prepayment Option Exercise Date

(2.) Purchase / Sale of Goods, PPE etc. in Foreign Currency :-

→ Host Contract : Purchase / Sale of Goods, PPE etc. (Non-Financial Item)

→ Embedded Derivative : Contract in Foreign Currency

→ These are Not Closely Related if Transaction is entered in a Currency which is Foreign Currency for Both Parties of the Transaction

→ Accounting if these are Not Closely Related

Host Contract [Purchase / Sale of Goods, PPE etc.]

↓

Recognise Purchase / Sale of Goods, PPE etc. on Purchase / Sale / Delivery Date as per Respective Ind AS at Amount equivalent in Company's

Embedded Derivative [Foreign Currency]

⇓

Apply Accounting of Derivative Contracts

→ No Entry on Contract Date

→ Recognise DFA or DFL at Fair Value on Each Balance Sheet Date by Comparing Currency Forward Rate of Purchase / Sale / Delivery Date

Currency using Currency forward Rate of Purchase / Sale / Delivery Date on Contract Date

⇓

Journal Entry on Purchase / Sale / Delivery Date :

→ For Purchase of Goods, PPE etc.

Purchase / PPE
  To Creditors

→ For Sale of Goods, PPE etc.

Debtors
  To Sale / PPE

→ Recognise Fair Value Gain / Loss on DFA or DFL on Purchase / Sale / Delivery Date Also

→ Finally, Transfer DFA or DFL Balance to Debtors / Creditors A/c on Purchase / Sale / Delivery Date

Regular Way Purchase of Financial Asset

- This Concept applies where a Financial Asset is purchased on a Date (i.e. Trade Date) But its Settlement will be done on a Future Date (i.e. Settlement Date)
- Two Approaches for Accounting of Purchase of Financial Asset is available in this case :

(1.) Trade Date Accounting :-

→ Recognise Financial Asset on Trade Date itself At its Fair Value

→ Journal Entry on Trade Date

Financial Asset
  To Payables

→ On Settlement Date, Financial Asset is recognised as per ACM, FVTOCI, FVTPL Method

→ On Settlement Date, Payables is settled by paying Cash

Payables
  To Cash

(2.) Settlement Date Accounting :-

→ Recognise Financial Asset on Settlement Date Only. [No Accounting is done on Trade Date]

→ Journal Entry :

(i.) If ACM is followed

Financial Asset	Trade Date Fair Value	
To Bank		Trade Date Fair Value

(ii.) If FVTOCI is followed

Financial Asset	Settlement Date Fair Value	
To Bank		Trade Date Fair Value

* Difference in Journal Entry will be Fair Value Gain / Loss recognised in OCI

(iii.) If FVTPL is followed

Financial Asset	Settlement Date Fair Value	
To Bank		Trade Date Fair Value

* Difference in Journal Entry will be Fair Value Gain / Loss recognised in P&L

Reclassification of financial Asset

- Financial Assets are reclassified from a method to another method on change of Intention of Entity regarding the financial Asset holding
- Reclassification of financial Asset is done as follows :

	To ACM	To FVTOCI	To FVTPL
From ACM	–	Measured at Fair Value on Reclassification Date and Fair Value Gain | Loss is recognised in OCI	Measured at Fair Value on Reclassification Date and Fair Value Gain | Loss is recognised in P&L
From FVTPL	Measured at Fair Value on Reclassification Date and Fair Value Gain | Loss is recognised in P&L	Measured at Fair Value on Reclassification Date and Fair Value Gain | Loss is recognised in P&L	–
From FVTOCI	Measured at Original Amount of financial Asset ⇓ For this, Also Reverse Any Balance in Fair Value Reserve [OCI] A/c to financial Asset A/c	–	Measured at Fair Value on Reclassification Date and Fair Value Gain | Loss is recognised in P&L ⇓ And Also Transfer Any Balance existing in Fair Value Reserve [OCI] A/c to P&L A/c

Ind AS 110 : Consolidated Financial Statements

This Ind AS provides Accounting for Subsidiaries (Acquiree Co.) by Parent Co. (Acquirer Co) in CFS on Subsequent dates (at each year end) after Acquisition Date

Consolidation Procedure At Each Year End for Subsidiaries

Parent Co. should apply following Steps for Preparing CFS :-

Step 1 : Share of Parent Co. (%) in Subsidiary Co. on Consolidation Date :-

- Specially Given
- $\frac{\text{No. of Shares of Subsidiary Co. held by Parent Co.}}{\text{Total No. of Shares issued by Subsidiary Co.}} \times 100$

Step 2 : Share of NCI (%) in Subsidiary Co. on Consolidation Date :-

- Specially Given
- 100% – Share of Parent Co. (%)

Step 3 : Date of Acquisition

Step 4 : Date of Consolidation

Step 5 : Analysis of Reserves of Subsidiary Company :-

- Statement of Analysis of Reserves of Subsidiary Company :-

Particulars	Pre Acquisition Reserves of Subsidiary Company	Post Acquisition Reserves of Subsidiary Company		
		Retained Earnings	General Reserves	Other Reserves
Balance of R/E	xxx	xxx		
Balance of G/R	xxx		xxx	
Other Adjustments	xxx	xxx		
Total	xxx	xxx	xxx	xxx
Share of Parent Co. (%) in Post Acquisition Reserves of Subsidiary Co.		✓	✓	✓
Share of NCI (%) in Post Acquisition Reserves of Subsidiary Co.		✓	✓	✓

Example :-

Acquisition Date : 31.3.2023 ; Consolidation Date : 31.3.2024

Retained Earnings (R/E) of Subsidiary Co. on
- 31.3.23 ⇒ ₹ 6 Lakh
- 31.3.24 ⇒ ₹ 8 Lakh

Other Reserves of Subsidiary Co. on
- 31.3.23 ⇒ ₹ 1.5 Lakh
- 31.3.24 ⇒ ₹ 1.5 Lakh

Share of Parent Co. is 80% & NCI is 20% in Subsidiary Co.

Solution :-

Analysis of Reserves of Subsidiary Co. :-

Particulars	Pre Acquisition Reserves	Post Acquisition Reserves	
		Retained Earnings	Other Reserves
R/E Balance on 31.3.2023	6 Lakh	-	-
Increase in R/E [8 Lakh - 6 Lakh]	-	2 Lakh	-
Other Reserves Balance on 31.3.23	1.5 Lakh	-	-
Inc. in O/R [1.5 Lakh - 1.5 Lakh]	-	-	0
Total	7.5 Lakh	2 Lakh	-
Share of Parent Co. @ 80%		1.6 Lakh	-
Share of NCI @ 20%		0.4 Lakh	-

- Some Special Adjustments :-

(1) If Subsidiary Co. is acquired in between of a year, then Profit earned by Subsidiary Co. in that year will be allocated in Pre & Post Period on Time Basis

Example :-

Acquisition Date : 30.6.2023 ; Consolidation Date : 31.3.2024

Retained Earnings (R/E) of Subsidiary Co. on
- 31.3.23 ⇒ ₹ 6 Lakh
- 31.3.24 ⇒ ₹ 8 Lakh

Share of Parent Co. is 80% & NCI is 20% in Subsidiary Co.

Solution :-

Analysis of Reserves of Subsidiary Co. :-

Particulars	Pre Acquisition Reserves	Post Acquisition Reserves (Retained Earnings)
R/E Balance on 31.3.2023	6 Lakh	-
Increase in R/E [8 Lakh - 6 Lakh] = 2 Lakh is allocated in Pre & Post Period on Time Basis Ratio (3 months & 9 months) i.e. 3:9	0.5 Lakh	1.5 Lakh
Total	6.5 Lakh	1.5 Lakh
Share of Parent Co. @ 80%		1.2 Lakh
Share of NCI @ 20%		0.3 Lakh

(2) Treatment of Dividend paid by Subsidiary Co. in Current Year After Acquisition Date but before Consolidation Date:-

It is treated as Intra Group Item & Hence Eliminated in CFS as follows:

- Added Back to Reserves of Subsidiary Co. [In Analysis of Reserves of Subsidiary Co.]
  - If Subsidiary Co. is acquired on or before beginning of Current Year, then Dividend paid by Subsidiary Co. in Current Year is Added to the Post Acquisition R/E of Subsidiary Company
  - OR
  - If Subsidiary Co. is acquired in between of Current Year, then Dividend Paid by Subsidiary Co. in Current Year will be Added to Pre Acquisition Reserves & Post Acquisition R/E on Time Basis
- Share of Parent Co. in dividend paid by Subsidiary Co. is deducted from Group R/E [in Step 9]
- Share of NCI in Dividend paid by Subsidiary Co. is deducted from NCI [in Step 7]

Example 1:

Acquisition Date: 31.3.2023 ; Consolidation Date: 31.3.2024

Retained Earnings (R/E) of Subsidiary Co. on
- 31.3.23 ⇒ ₹ 3 Lakh
- 31.3.24 ⇒ ₹ 8 Lakh

Dividend paid by Subsidiary Co. on 1st November 2023 = ₹ 40,000

Share of Parent Co. is 80% & NCI is 20% in Subsidiary Co.

Solution:-

Analysis of Reserves of Subsidiary Co.:-

Particulars	Pre Acq. Reserves	Post Acq. R/E
Bal. of R/E on 31.3.23	3 Lakh	-
Inc. in R/E [8 Lakh - 3 Lakh]	-	5 Lakh
Dividend paid by Subsidiary Co. [Add Back]	-	40,000
Total	3 Lakh	5.4 Lakh
Sh. of Parent @ 80%		4.32 Lakh
Sh. of NCI @ 20%		1.08 Lakh

Share of Parent Co. & NCI in dividend paid by Subsidiary Co. of ₹ 40,000

Parent Co.'s Share @ 80% ⇓ 32,000 [Deducted from Group R/E]

NCI Share @ 20% ⇓ 8,000 [Deducted from NCI]

Example 2 :

Acquisition Date : 30.6.2023 ; Consolidation Date : 31.3.2024

Retained Earnings (R/E) of Subsidiary Co. on
- 31.3.23 ⇒ ₹ 3 Lakh
- 31.3.24 ⇒ ₹ 8 Lakh

Dividend paid by Subsidiary Co. on 1st November 2023 = ₹ 40,000

Share of Parent Co. is 80% & NCI is 20% in Subsidiary Co.

Solution :-

Analysis of Reserves of Subsidiary Co. :-

Particulars	Pre Acq. Reserves	Post Acq. R/E
Bal. of R/E on 31.3.23	3 Lakh	-
Inc. in R/E [8 Lakh - 3 Lakh] in 3:9 Ratio	1.25 Lakh	3.75 Lakh
Dividend paid by Subsidiary Co. [Add Back] in 3:9 Ratio	0.10 Lakh	0.30 Lakh
Total	4.35 Lakh	4.05 Lakh
Sh. of Parent @ 80%		3.24 Lakh
Sh. of NCI @ 20%		0.81 Lakh

Share of Parent Co. & NCI in dividend paid by Subsidiary Co. of ₹ 40000

Parent Co.'s Share @ 80% ⇓ 32,000 [Deducted from Group R/E]

NCI Share @ 20% ⇓ 8,000 [Deducted from NCI]

(3) Impact of Fair Value (on Acquisition Date) of Assets & Liabilities of Subsidiary Company :-

While doing Consolidation as per Ind AS 110, We calculate Net Assets of Subsidiary Co. by Analysis of Reserves of Subsidiary Co., hence those will be at Carrying Amount but on Acquisition Date we take over Net Assets of Subsidiary Co. at fair Value

⇓

So, we need to give impact of Fair Value of Assets & Liabilities of Subsidiary Company as follows :-

(A) For Liabilities of Subsidiary Company [Eg. Trade Payables] :

Increase in Fair Value, i.e.
Fair Value > Carrying Amount on Acquisition Date [Loss]

⇓

→ Deduct Fair Value Increase Amount from Pre Acquisition Reserves of Subsidiary Company

&

→ Add Fair Value Increase Amount to respective Liability in Consolidated Balance Sheet

Decrease in Fair Value, i.e.
Fair Value < Carrying Amount on Acquisition Date [Gain]

⇓

→ Add Fair Value Decrease Amount to Pre Acquisition Reserves of Subsidiary Company

&

→ Deduct Fair Value Decrease Amount from respective Liability in Consolidated Balance Sheet

* Fair Value Increase / Decrease Amount in Liability of Subsidiary Company will be given in question

(B) For Assets of Subsidiary Company [Eg. Land, Inventories, P&M, etc.] :

Increase in Fair Value, i.e.
Fair Value > Carrying Amount on Acquisition Date [Gain]

⇓

→ Add Fair Value Increase Amount to Pre Acquisition Reserves of Subsidiary Company

&

→ Add Fair Value Increase Amount to respective Asset in Consolidated Balance Sheet

Decrease in Fair Value, i.e.
Fair Value < Carrying Amount on Acquisition Date [Loss]

⇓

→ Deduct Fair Value Decrease Amount from Pre Acquisition Reserves of Subsidiary Company

&

→ Deduct Fair Value Decrease Amount from respective Asset in Consolidated Balance Sheet

Note:-

(i) Amount of Fair Value Increase / Decrease in Assets of Subsidiary Company will be given in question

⇓

But In Case of Depreciable Assets [Eg. P&M], We may have to calculate Amount of Fair Value Increase / Decrease as follows :

Fair Value of Asset on Acquisition Date	xxx
(-) Carrying Amount of Asset on Acquisition Date	(xxx)
Fair Value Increase / (Decrease)	xxx / (xxx)

Example :-

Financial Year ⇒ 1.4.23 to 31.3.24

Acquisition Date ⇒ 1.10.23 ; Consolidation Date ⇒ 31.3.24

Carrying Amount (Book Value) of P&M of Subsidiary Co. on 31.3.24 is ₹ 13,50,000

Depreciation Rate is 10%.
Fair Value of P&M of Subsidiary Co. on 1.10.23 is ₹ 20,00,000

Solution:-

Carrying Amount of P&M on 1.4.23 ⇒ $\frac{13,50,000}{90\%}$ ⇒ ₹ 15,00,000

Carrying Amount of P&M on 1.10.23 ⇒ 15,00,000 − [15,00,000 × 10% × $\frac{6}{12}$]

⇒ 14,25,000

∴ Fair Value Increase in P&M on Acquisition Date (1.10.23) ⇒
20,00,000 − 14,25,000 ⇒ ₹ 5,75,000

(ii) In Case of Depreciable Assets, Additional Effect for Depreciation due to Increase/Decrease in Fair Value of Asset of Subsidiary Co. is also given as follows:

Depreciation on Fair Value of Asset [From Acq. Date to Consolidation Date]	xxx
(−) Depreciation on Original Amount of Asset [From Acq. Date to Consolidation Date]	(xxx)
Additional Depreciation to be Charged / (Depreciation to be Reversed)	xxx/(xxx)

Additional Depreciation to be Charged
⇓
→ Deduct from Post Acquisition R/E of Subsidiary Company
&
→ Deduct from respective Asset in Consolidated Balance Sheet

Depreciation to be Reversed
⇓
→ Add to Post Acquisition R/E of Subsidiary Company
&
→ Add to respective Asset in Consolidated Balance Sheet

As per Above Example:-

Depreciation on Fair Value (from 1.10.23 to 31.3.24) [20,00,000 × 10% × $\frac{6}{12}$]	1,00,000
(−) Depreciation on Original Amt. (from 1.10.23 to 31.3.24) [15,00,000 × 10% × $\frac{6}{12}$]	(75,000)
Additional Depreciation to be Charged	25,000

(iii) Final Amount of Depreciable Asset of Subsidiary Company to be taken for Consolidation:

Carrying Amount of Asset as on Consolidation Date in B/s of Subsidiary Co.	xxx
Add/(Less): Fair Value Increase / (Decrease)	xxx/(xxx)
	xxx
Add/(Less): Dep. to be Reversed / (Additional Dep. to be Charged)	xxx/(xxx)
	xxx

As per Above Example:-

Carrying Amount of P&M as on 31.3.24	13,50,000
(+) Fair Value Increase	5,75,000
	19,25,000
(−) Additional Depreciation to be charged	(25,000)
	19,00,000

(iv.) If there is Increase / Decrease in Fair Value of Inventory of Subsidiary Co. on Acquisition Date & that Inventory get sold after Acquisition Date but before Consolidation Date

⇓

In this Case, Effect of Previously Recognised Fair Value Increase / Decrease on such Inventory is Reversed as follows

If there was Increase in Fair Value of Inventory on Acquisition Date

⇓

→ Deduct such Fair Value Increase Amount from Post Acquisition R/E of Subsidiary Company

&

→ Deduct from Inventory in Consolidated Balance Sheet

If there was Decrease in Fair Value of Inventory on Acquisition Date

⇓

→ Add such Fair Value Decrease Amount to Post Acquisition R/E of Subsidiary Company

&

→ Add to Inventory in Consolidated Balance Sheet

(4) <u>Treatment of Unrealised Gain on Inventory</u> :-

It happens when Sale / Purchase of Inventory takes place between Parent Company & Subsidiary Company during Parent - Subsidiary Relationship and that Inventory is lying in Stock (i.e. Remained Unsold) on Consolidation Date

Down Stream Transaction [P ↓ S]

⇓

Parent Co. sold goods (Inventory) to Subsidiary Co.

⇓

Unrealised Gain on Inventory [Sales Amount − Cost of Such Goods]

⇓

→ Deduct from Group R/E

&

→ Deduct from Inventory in Consolidated Balance Sheet

Up Stream Transaction [P ↑ S]

⇓

Subsidiary Co. sold goods (Inventory) to Parent Co.

⇓

Unrealised Gain on Inventory [Sales Amount − Cost of Such Goods]

⇓

→ Deduct from Post Acquisition R/E of Subsidiary Company

&

→ Deduct from Inventory in Consolidated Balance Sheet

(5) Treatment of Unrealised Gain on PPE :-

It happens when Sale | Purchase of PPE takes place between Parent Company & Subsidiary Company during Parent - Subsidiary Relationship and that PPE is lying (i.e. Remained unsold) on Consolidation Date

Down Stream Transaction [P ↓ S]

⇓

Parent Co. sold PPE to Subsidiary Co.

⇓

Unrealised Gain on PPE

[Sales Amount - Carrying Amount of such PPE on Sale Date]

⇓

→ Deduct from Group R/E

&

→ Deduct from PPE in Consolidated Balance Sheet

⇓

In this Case, Subsidiary Co. would have charged Depreciation on Total Value of PPE (Purchased Amount from Parent Co.); So Additional Depreciation Charged by Subsidiary Co. on Unrealised Gain Portion of PPE is to be Reversed as follows:

→ Add to Post Acquisition R/E of Subsidiary Company

&

→ Add to PPE in Consolidated Balance Sheet

Up Stream Transaction [P ↑ S]

⇓

Subsidiary Co. sold PPE to Parent Co.

⇓

Unrealised Gain on PPE

[Sales Amount - Carrying Amount of such PPE on Sale Date]

⇓

→ Deduct from Post Acquisition R/E of Subsidiary Company

&

→ Deduct from PPE in Consolidated Balance Sheet

⇓

In this Case, Parent Co. would have charged Depreciation on Total Value of PPE (Purchased Amount from Subsidiary Co.); So Additional Depreciation Charged by Parent Co. on Unrealised Gain Portion of PPE is to be Reversed as follows:

→ Add to Group R/E

&

→ Add to PPE in Consolidated Balance Sheet

Note :- Additional Depreciation charged on Unrealised Gain Portion of PPE is calculated as follows:

Depreciation on Sale / Purchase Amount within the Group	xxx
(-) Depreciation on Original Cost (Carrying Amount)	(xxx)
	xxx

Step 6 : Calculation of Net Assets taken over of Subsidiary Company on Acquisition Date :-

Share Capital of Subsidiary Company	xxx

(+) Pre Acquisition Reserves of Subsidiary Company [As Calculated in Step 5]	xxx
	xxx

Step 7: Calculation of Non-Controlling Interest (NCI) on Consolidation Date :-

NCI on Acquisition Date [Fair Value Method OR PSNA Method] PSNA Method ⇓ Share of NCI (%) × Net Assets taken over of Subsidiary Co. [Step 6]	xxx
(+) Share of NCI in Post Acquisition Reserves of Subsidiary Company [Step 5]	xxx
(−) Share of NCI in Dividend Paid by Subsidiary Company (if any) [Step 5]	(xxx)
(−) Share of NCI in Impairment of Full Goodwill (if any)	(xxx)
	xxx

Note :- NCI amount can be Negative also.

Step 8: Calculation of Goodwill OR Capital Reserve on Consolidation Date :-

- It will be same as of Acquisition Date unless there is Impairment in Goodwill
- It is calculated as follows :

PC paid to Subsidiary Company on Acquisition Date [i.e. Investment Amount by Parent Co. in Subsidiary Company]	xxx
(+) NCI on Acquisition Date	xxx
	xxx
(−) Net Assets taken over of Subsidiary Company on Acquisition Date [Step 6]	(xxx)
Goodwill / (Capital Reserve) on Acquisition Date	xxx / (xxx)
Less: Impairment in Goodwill (if any)	(xxx)
Goodwill on Consolidation Date	xxx

Note :- Impairment of Goodwill :-

Partial Goodwill (when NCI is as per PSNA Method)

[i.e. Goodwill belongs to Parent Co. Only]

⇓

Impairment Loss on Goodwill will be borne by Parent Company Only i.e. Deduct Total Impairment Loss on Goodwill from Group R/E [in Step 9]

⇓

Journal Entry for Goodwill Impairment:

Full Goodwill (when NCI is as per Fair Value Method)

[i.e. Goodwill belongs to Both Parent Co. & NCI]

⇓

Impairment Loss on Goodwill will be borne by Both Parent Company & NCI, i.e.

→ Deduct Share of Parent Co. in Impairment Loss of Goodwill from Group R/E [in Step 9]

&

Group R/E A/c Dr.
    To Goodwill A/c

→ Deduct Share of NCI in Impairment Loss of Goodwill from NCI [in Step 7]
↓
Journal Entry for Goodwill Impairment:
Group R/E A/c Dr.
NCI A/c Dr.
    To Goodwill A/c

Step 9: Calculation of Group Reserves / Consolidated Reserves [Consolidated Other Equity] Final Balance on Consolidation Date:

Particulars	Retained Earnings	General Reserves	Other Reserves	Total
Parent Company's own Reserve Balance as on Consolidation Date	✓	✓	✓	✓
(+) Share of Parent Co. in Post Acquisition Reserves of Subsidiary Co.	✓	✓	✓	✓
(−) Share of Parent Co. in Dividend Paid by Subsidiary Co. (if any)	(✓)	–	–	(✓)
(−) Share of Parent Co. in Impairment of Goodwill (if any)	(✓)	–	–	(✓)
(−) Unrealised Gain on Inventory / PPE in Down Stream transaction (if any)	(✓)	–	–	(✓)
(+) Additional Depreciation on Unrealised gain portion of PPE in Upstream transaction (if any)	✓	–	–	✓
(±) Any Other Adjustment (if any specifically given in question)	✓	✓	✓	✓
	xxx	xxx	xxx	xxx

Step 10: Preparation of Consolidated Balance Sheet :-

- Add Line by Line All Items of Assets & Liabilities of Parent Company & Subsidiary Company at Full Amount as appearing in their Separate Balance Sheets of Consolidation Date EXCEPT
  - → Investment Amount by Parent Company in Subsidiary Company
  - → Share Capital of Subsidiary Company
  - → Reserves of Subsidiary Company
- Recognise Goodwill / Capital Reserve & NCI of Consolidation Date [As Calculated in Step 7 & 8]
- Give Impact of Fair Value Increase / Decrease in Assets & Liabilities of Subsidiary Company [As discussed in Step 5]
- Give Impact of Unrealised Gain on Inventory / PPE [As discussed in Step 5]
- Eliminate Intra Group Transactions [i.e. Trade Receivables & Trade Payables between Parent Co. & Subsidiary Co., Loan given & Loan taken between Parent Co. & Subsidiary Co.]

Step 11: Preparation of Consolidated Statement of P&L :-

- Add Line by Line All Items of Incomes & Expenses of Parent Company & Subsidiary Company at Full Amount as appearing in their Separate P&L of Consolidation Date

- Give Impact of Items affecting P&L A/c of which Adjustments are appearing in Post Acquisition R/E of Subsidiary Company [Step 5] & Group R/E [Step 9]
- Eliminate Intra Group Transactions [i.e. Sale & Purchase of goods between Parent Co. & Subsidiary Co.]
- Finally, Present Total Profit / Loss attributable to Parent Co. & NCI

Step 12: Preparation of Consolidated Statement of Cash Flow :-

- Add Line by Line All Items of Cash flow Statement of Parent Company & Subsidiary Company at full Amount as appearing in their Separate Cash flow Statement of Consolidation Date
- Eliminate Intra Group Cash Transactions, i.e. Transactions between Parent Company & Subsidiary Company in Cash

  [In Case of Dividend paid by Subsidiary Co., Only Parent Co's Share is Eliminated]

Consolidation Procedure in Case of Chain Holding

$P \xrightarrow[80\%]{} S_1 \xrightarrow[60\%]{} S_2$

- Concepts for Preparing CFS at each year end will remain same as discussed in above Topic
- Parent Company should apply following steps for Preparing CFS :-

Step 1: Share (%) of Parent Co. (P) in Subsidiary Co. (S_1 & S_2) on Consolidation Date :-

In S_1 ⇒ Directly Given [Eg.: 80%]

In S_2 ⇒ Share of P in S_1 × Share of S_1 in S_2 [Eg.: 80% × 60% = 48%]

Step 2: Share (%) of NCI in Subsidiary Co. (S_1 & S_2) on Consolidation Date :-

In S_1 ⇒ 100% − 80% = 20%

In S_2 ⇒ 100% − 48% = 52%

Step 3: Date of Acquisition of Subsidiary Co. (S_1 & S_2) by Parent Co. (P) :-

For S_1 ⇒ Given Date in Question (Normally as discussed in Step 3 of Above Topic)

For S_2 ⇒ Date of Acquisition will be considered as Later of following Dates

Acquisition Date of S_1 by P **OR** Acquisition Date of S_2 by S_1

Example 1 :- $P \xrightarrow[1/4/23]{80\%} S_1 \xrightarrow[1/4/24]{60\%} S_2$

DOA → S_1 = 1/4/23
→ S_2 = 1/4/24

Example 2 :- $P \xrightarrow[1/4/24]{80\%} S_1 \xrightarrow[1/4/23]{60\%} S_2$

DOA → S_1 = 1/4/24
→ S_2 = 1/4/24

Step 4 : Date of Consolidation

Step 5 : Analysis of Reserves of Subsidiary Co. (S_1 & S_2) :-

It will be done Separately for each Subsidiary in same way as discussed in Step 5 of above Topic

Step 6 : Calculation of Net Assets taken over of Subsidiary Co. (S_1 & S_2) on Acquisition Date :-

	S_1	S_2
Share Capital of Subsidiary Company	xxx	xxx
(+) Pre Acquisition Reserves of Subsidiary Company [As Calculated in Step 5]	xxx	xxx
	xxx	xxx

Step 7 : Calculation of NCI in Subsidiary Co. (S_1 & S_2) on Consolidation Date :-

	S_1	S_2
NCI on Acquisition Date	xxx	xxx
(+) Share of NCI in Post Acquisition Reserves of Subsidiary [S_1]	xxx	–
(+) Share of NCI in Post Acquisition Reserves of Subsidiary [S_2]	–	xxx
(–) Share of NCI in Dividend Paid by Subsidiary Company (if any)	(xxx)	(xxx)
(–) Share of NCI in Impairment of Full Goodwill (if any)	(xxx)	(xxx)
(–) Share of NCI in S_1 on Investment Amount in S_2 [Investment Amount in S_2 x Share (%) of NCI in S_1]	(xxx)	–
	xxx	xxx

xxx

Step 8 : Calculation of Goodwill OR Capital Reserve on Consolidation Date :-

	S_1	S_2
PC paid to Subsidiary Company on Acquisition Date, i.e.		
PC to S_1 ⇒ Investment Amount in S_1 by P	xxx	–
PC to S_2 ⇒ Share of P in S_1 on Investment Amount in S_2 [Investment Amount in S_2 x Share (%) of P in S_1]	–	xxx
(+) NCI on Acquisition Date	xxx	xxx
	xxx	xxx
(–) Net Assets taken over of Subsidiary Company on Acquisition Date [Step 6]	(xxx)	(xxx)
Goodwill / (Capital Reserve)	xxx	xxx

xxx

Step 9 : Calculation of Consolidated Other Equity Final Balance on Consolidation Date :-

Particulars	Retained Earnings	General Reserves	Other Reserves	Total
Parent Company's [P] own Reserve Balance as on Consolidation Date	✓	✓	✓	✓
(+) Share of Parent [P] in Post Acquisition Reserves of Subsidiary [S_1]	✓	✓	✓	✓
(+) Share of Parent [P] in Post Acquisition Reserves of Subsidiary [S_2]	✓	✓	✓	✓
(–) Share of Parent Co. in Dividend Paid by Subsidiary Co. (if any)	(✓)	–	–	(✓)
(–) Share of Parent Co. in Impairment of Goodwill (if any)	(✓)	–	–	(✓)

(-) Unrealised Gain on Inventory / PPE in Down Stream transaction (if any)	(✓)	-	-	(✓)
(+) Additional Depreciation on Unrealised gain portion of PPE in Upstream transaction from Subsidiary Co. to Parent Co. (if any)	✓	-	-	✓
(±) Any Other Adjustment (if any specifically given in question)	✓	✓	✓	✓
	xxx	xxx	xxx	xxx

Step 10: Preparation of Consolidated Balance Sheet :- Same as discussed in Step 10 of above Topic

Purchase of Additional Stake in Subsidiary Co. after acquisition of Control by Parent Co.

- **Journal Entry in SFS by Parent Co. for Acquisition of Additional Stake in Subsidiary Co.** :-

Investment in Subsidiary Company A/c	Dr.	[Amount Paid to Acquire Additional Stake in Subsidiary Company]
To Cash / Bank A/c		

- **Accounting in CFS by Parent Co. for Acquisition of Additional Stake in Subsidiary Co.** :-

→ Share of NCI will decrease & Hence we have to Reduce NCI to the extent of Additional Stake purchased by Parent Company

→ Journal Entry in CFS :

NCI A/c	Dr.	Proportionate Carrying Amount of NCI	
Loss on Acquisition of Addl. Stake in Subs. [Consolidated Other Equity]	Dr.	B/F	
To Cash / Bank A/c			Amount Paid to Acquire Addl. Stake
To Gain on Acquisition of Addl. Stake in Subs. [Consolidated Other Equity]			B/F

* Consolidated Other Equity means Group R/E

Example :-

On 1.4.22, A Ltd. acquired 70% stake in B Ltd.

On 31.3.24, A Ltd. acquired another 10% Stake in B Ltd. by paying Cash of ₹ 2,600. Carrying Amount of NCI (30%) on this date is ₹ 6,600

Solution :-

Journal Entry in CFS :

NCI A/c $\left[6{,}600 \times \frac{10}{30}\right]$	Dr.	2,200	
Other Equity A/c [Loss] (B/F)	Dr.	400	
To Cash A/c			2,600

Sale of Stake in Subsidiary Company by Parent Company

- **Journal Entry in SFS by Parent Company for Sale of Stake in Subsidiary Company** :-

Cash / Bank A/c	Dr.	Amount Received on Sale of Stake
Loss on Sale of Stake in Subsidiary Co. [P&L]	Dr.	B/F

To Investment in Subsidiary Company A/c — Proportionate Carrying Amt. of Investment Sold

To Gain on Sale of Stake in Subsidiary Co. [P&L] — B/F

• **Accounting in CFS by Parent Company for Sale of Stake in Subsidiary Company :-**

If Sale of Stake Results in :-

(1.) No Loss of Control in Subsidiary Company : Journal Entry

Cash / Bank A/c Dr.	Amount Received on Sale of Stake	
Loss on Sale of Stake in Subsidiary Co. [Consolidated O/E] Dr.	B/F	
To NCI A/c		[Carrying Amount of Net Assets of Subsidiary & Goodwill on Sale Date × % Stake sold by Parent Company]
To Gain on Sale of Stake in Subsidiary Co. [Consolidated O/E]		B/F

* Consolidated Other Equity means Group R/E

Example :-

A Ltd. purchased 80% Stake in B Ltd. in 2021 for ₹ 1,040.
On 1.4.23, A ltd. sells 25% stake in B ltd. for ₹ 500.
Carrying Amount of Net Assets of Subsidiary is ₹ 1,300 & Goodwill is ₹ 200 on this date.

Solution :-

A ltd. sold 25% Stake in B ltd., thereafter its Stake in B ltd. will be = 80% - 25% = 55%
Hence, there is No Loss of Control of A ltd. in B ltd.

Journal Entry for Sale of Stake :

In SFS :-

Cash A/c	500	
To Investment in B ltd. $\left[1040 \times \frac{25}{80}\right]$		325
To Gain on Sale of Stake (P&L) [B/F]		175

In CFS :-

Cash A/c	500	
To NCI A/c [(1,300 + 200) × 25%]		375
To Gain on Sale of Stake (Consolidated O/E) [B/F]		125

(2.) Loss of Control in Subsidiary Company :

- Recognise Amount Received for Sale of Stake in Subsidiary
- Derecognise Carrying Amount of Net Assets of Subsidiary & Goodwill on Sale Date
- Derecognise Carrying Amount of NCI on Sale Date ⇓
  → It will be given in question
  → Otherwise calculate it -
- Recognise Stake Retained (if any) in Subsidiary Co. by Parent Co. as Investment at Fair Value ⇓
- Difference in All these 4 Items in Journal Entry will be recognised in P&L A/c

[i.e. Cash | Bank A/c]

If NCI is as per PSNA
↓
Carrying Amt. of Net Assets of Subsidiary on Sale Date
×
Share of NCI (%) before Sale of Stake

If NCI is at Fair Value
↓
Carrying Amt. of Net Assets of Subsidiary & Goodwill on Sale Date
×
Share of NCI (%) before Sale of Stake

→ Fair Value of Investment Retained will be given in question
→ Otherwise Calculate it -
Carrying Amt. of Net Assets of Subsidiary & Goodwill on Sale Date
×
% Stake retained by Parent Co. in Subsidiary Co.

as Gain or Loss on Sale of Stake in Subsidiary Co. [B/F]

Journal Entry:

Cash / Bank A/c	Amount Received	
NCI A/c	Carrying Amount	
Investment A/c [Retained Portion, if any]	Fair Value	
Loss on Sale of Stake in Subsidiary (P&L)	B/F	
To Net Assets of Subsidiary		Carrying Amount
To Goodwill		Carrying Amount
To Gain on Sale of Stake in Subsidiary (P&L)		B/F

Example :-

A ltd. purchased 80% Stake in B Ltd. in 2021 for ₹ 1,040. NCI is calculated as per PSNA.
On 1.4.23, A ltd. sells 35% stake in B ltd. for ₹ 600
Carrying Amount of Net Assets of Subsidiary is ₹ 1,300 & Goodwill is ₹ 200 on this date.

Solution :-

A ltd. sold 35% Stake in B ltd., thereafter its Stake in B ltd. will be = 80% - 35% = 45%
Hence, there is Loss of Control of A ltd. in B ltd.

Journal Entry for Sale of Stake :

In SFS :-

Cash A/c	600	
To Investment in B ltd. $\left[1040 \times \frac{35}{80}\right]$		455
To Gain on Sale of Stake (P&L) [B/F]		145

In CFS :-

Cash A/c	600	
NCI A/c [1,300 × 20%]	260	
Investment A/c [Retained Portion ⇒ (1,300 + 200) × 45%]	675	
To Net Assets of Subsidiary A/c		1,300
To Goodwill A/c		200

To Gain on Sale of Stake (P&L) [B|F]

Notes :-

(i.) Deemed Loss of Control in Subsidiary Company :-

→ It could happen when Subsidiary Company further issue Equity Shares to NCI shareholders.

→ Same Accounting will be done as of Sale of Stake in Subsidiary Company except No Amount/ Consideration is received by Parent Company in this case

Example:-

Current Shareholding Structure [On 1.4.22] of B Ltd.:	No. of Shares	%
Shares held by A Ltd. [Parent Co.]	30,000	60%
Shares held by NCI	20,000	40%
	50,000	100%

On 1.4.24, B Ltd. further issue 25,000 shares to NCI Shareholders at ₹ 10 per share.

So, New Shareholding Structure [On 1.4.24] of B Ltd.:	No. of Shares	%
Shares held by A Ltd.	30,000	40%
Shares held by NCI	45,000	60%
	75,000	100%

Hence, A Ltd. loses control over B Ltd. on 1.4.24 as its Stake remains only 40%
[Deemed Loss of Control]

(ii.) Parent Company may lose control in Subsidiary by Sale of Stake in 2 or More transactions on different dates

↓

In this Case, Parent Co. can account for Sale of Stake as a Single transaction if these transactions are dependent on each other as per Ind AS 110

Example:-

A Ltd. has 80% Stake in B Ltd. which it dispose in following 2 transactions:

On 1/4/24 → Sale 25% Stake for ₹ 2.5 Lakh
On 30/4/24 → Sale 55% Stake for ₹ 5.5 Lakh
→ Alcing for Sale of Stake will be done by assuming these as a Single transaction

(iii.) In Case of Loss of Control in Subsidiary Co., Parent Co. is also required to Reclassify its Share in OCI Reserves of Subsidiary Company by transferring it to P&L or Retained Earnings according to the Nature of OCI Reserve

Eg:- Share in Revaluation Reserve (PPE) of Subsidiary → T/f to R/E
Share in FCTR of Subsidiary → T/f to P&L
Share in Fair Value Reserve relating to Debt Investments at FVTOCI of Subsidiary → T/f to P&L
Share in Fair Value Reserve relating to Equity Investments at FVTOCI of Subsidiary → T/f to R/E
Share in Actuarial Gain/Loss of Subsidiary → T/f to R/E

Accounting for Change in Investment Entity Status

- Investment Entity means a Company that invests funds obtained from Various Investors into multiple companies to provide return to its Investors.

Eg. Mutual fund Company is an Investment Entity

- So, If an Investment Entity has any Subsidiary Company (by Investing funds in it), It shall not consolidate its subsidiaries (i.e. It will not prepare CFS)

⇓

It should record its Investment in Subsidiary as an Asset at FVTPL

- Accounting when a Company ceases to be an Investment Entity :-

→ It shall apply Ind AS 103 (Business Combination) Accounting to its subsidiaries assuming Date of Change in Status as Deemed Acquisition Date

→ Carrying Amount of Investment in Subsidiary on Deemed Acquisition Date is considered as Deemed Purchase Consideration (P.C.)

- Accounting when a Company becomes an Investment Entity :-

→ If a Company having Subsidiaries becomes an Investment Entity, It shall stop consolidating its Subsidiaries (i.e. Stop Preparing CFS) from Date of Change in Status.

→ In this Case, Apply Same Accounting in CFS as for Sale of Stake resulting in Loss of Control in Subsidiary as follows :

Derecognise Carrying Amount of Net Assets of Subsidiary and Goodwill on change in Status Date	Derecognise Carrying Amount of NCI on Change in Status Date	Recognise Investment in Subsidiary at FVTPL on change in Status Date	Difference in All these 3 Items in Journal Entry will be recognised in P&L as Gain or Loss on Change in Status of Entity

[B|F]

Ind AS 111 : Joint Arrangements

Meaning & Types of Joint Arrangements

- It is an arrangement of 2 or More Parties to have Joint Control over a Business
- Joint Arrangements can be of 2 types :

Joint Operation

⇓

→ If Parties in the Joint Arrangement have Right to Individual Assets & Obligations for Liabilities of the business

[It generally happens when Joint Arrangement is not Structured through a Separate Legal Entity]

→ In this Case, Parties in Joint Arrangement are called Joint Operators

Joint Venture

⇓

→ If Parties in the Joint Arrangement have Right to the Net Assets of the business

[It generally happens when Joint Arrangement is Structured through a Separate Legal Entity]

→ In this Case, Parties in Joint Arrangement are called Joint Venturers

Accounting of Joint Arrangements

Joint Operation

⇓

Proportionate Consolidation Method

⇓

Joint Operation shall recognise its Share in Assets, Liabilities, Income & Expenses of Joint Operation in respective heads in its Separate Financial Statements [SFS]

[CFS is not prepared separately]

Joint Venture

⇓

Investor Company has to prepare 2 types of FS, i.e. SFS & CFS

In SFS

⇓

Investor Company will account it as per Ind AS 27

In CFS

⇓

Investor Company will account it as per Ind AS 28

[Equity Method]

Accounting of Special Transactions in case of Joint Operation

1. **Accounting for Sale of Asset to Joint Operation by Joint Operator :-**

- Recognise Sale only to the extent of Share of Other Parties in Joint Operation
- Journal Entry :

Cash / Bank A/c	Dr.	Amount Received on Sale x Share of Other Parties in Joint Operation
Loss on Sale of Asset A/c [P&L]	Dr.	Balancing figure
To Asset A/c		Carrying Amount of Asset Sold x Share of Other Parties in Joint Operation
To Gain on Sale of Asset A/c [P&L]		Balancing figure

2. **Accounting for Purchase of Asset from Joint Operation by Joint Operator :-**

- Recognise Purchase only to the extent of Share of Other Parties in Joint Operation
- Journal Entry :

Asset A/c	Dr.	[Amount Paid to Purchase the Asset x Share of Other Parties in Joint Operation]
To Cash / Bank A/c		

Ind AS 28 : Investments in Associates and Joint Ventures

Meaning of Associate Company

If a Company [Investor] invests in 20% or More but less than equals to 50% Equity Shares of Another Company [Investee], then it is considered as Investor has Significant Influence over Investee & Hence, Investee Company becomes our Associate Company

Accounting for Investments in Associates and Joint Ventures

- Investor Company has to prepare 2 types of FS, i.e. SFS & CFS
  - In SFS → Investor Company will account it as per Ind AS 27
  - In CFS → Investor Company will account it as per Ind AS 28 [Equity Method]

- Accounting by Investor Co. for Investments in Associates and Joint Ventures in CFS [Equity Method] :-

(1) Initially Recognise Investment done in Associate OR Joint Venture at its Cost

Investment in Associate OR Joint Venture A/c Dr. [Cost of Investment / Consideration paid to Investee]
  To Cash | Bank A/c

(2) Calculate Goodwill / Capital Reserve arising from Investment in Associate OR Joint Venture :

Consideration paid to Investee [Cost of Investment in Associate OR Joint Venture]		xxx
Less:- Investor's Share in Fair Value of Net Assets of Associate OR Joint Venture	[Fair Value of Net Assets of Associate OR Joint Venture × Investor's Share]	(xxx)
		xxx

- If Positive → Goodwill → It is already included in Carrying Amount of Investment [No Separate Treatment, Just disclose it in Notes in Balance Sheet]
- If Negative → Capital Reserve → It is to be recognised as follows :

  Investment in Associate OR J.V. A/c Dr.
    To Capital Reserve A/c

(3) Recognise our Share in Profit | Loss of Associate OR Joint Venture after Investment Date :

→ For Share in Profit

Investment in Associate OR J.V. A/c [Profit earned by Associate OR Joint Venture × Investor's Share]
  To Share in Profit of Associate OR J.V. A/c [P&L]

→ For Share in Loss

Share in Loss of Associate OR J.V. A/c [P&L] To Investment in Associate OR J.V. A/c	[Loss arised in Associate OR Joint Venture	× Investor's Share]

(4) Recognise our Share in OCI of Associate OR Joint Venture after Investment Date:

→ For Share in Profit

Investment in Associate OR J.V. A/c To Share in OCI Profit of Associate OR J.V. A/c [OCI]	[OCI Profit of Associate OR Joint Venture	× Investor's Share]

→ For Share in Loss

Share in OCI Loss of Associate OR J.V. A/c [OCI] To Investment in Associate OR J.V. A/c	[OCI Loss of Associate OR Joint Venture	× Investor's Share]

(5) Recognise our Share in Dividend declared | paid by Associate OR Joint Venture:

Dividend Receivable A/c | Bank A/c To Investment in Associate OR J.V. A/c	[Dividend declared/paid by Associate OR J.V.	× Investor's Share]

(6) Depreciation Adjustment due to Fair Value Impact on Acquisition Date on Depreciable Assets of Associate OR Joint Venture:

→ If Fair Value of Asset is higher than Carrying Amount on Acquisition Date, then Recognise our Share in Additional Depreciation to be charged:

Share in Profit of Associate OR J.V. A/c [P&L] To Investment in Associate OR J.V. A/c	[Depreciation on difference Amount b/w Fair Value & Carrying Amount of Asset	× Investor's Share]

→ If Fair Value of Asset is Lower than Carrying Amount on Acquisition Date, then Recognise our Share in Depreciation to be reversed:

Investment in Associate OR J.V. A/c To Share in Profit of Associate OR J.V. A/c [P&L]	[Depreciation on difference Amount b/w Fair Value & Carrying Amount of Asset	× Investor's Share]

(7) Eliminate Unrealised Gain on Inventory | PPE:

→ For Upstream Transaction [Associate OR Joint Venture sold goods | PPE to Investor Co.]

Share in Profit of Associate OR J.V. A/c [P&L] To Inventory A/c	[Unrealised Gain on Inventory | PPE	× Investor's Share]

→ For Downstream Transaction [Investor Co. sold goods | PPE to Associate OR Joint Venture]

P&L A/c To Investment in Associate OR J.V. A/c	[Unrealised Gain on Inventory | PPE	× Investor's Share]

Notes:-

(i) Assets & Liabilities of Associate OR Joint Venture are not taken over in CFS

(ii) Inter Company transactions are not eliminated since Net Assets are not taken over

(iii) Calculation of Closing Balance of Investment in Associate OR Joint Venture A/c after considering above Journal Entries:

→ By Preparing Ledger A/c of Investment in Associate OR Joint Venture

→ By Preparing Statement as follows –

Cost of Investment [Consideration Paid]		xxx
(±) Share in Profit / (Loss) of Associate OR Joint Venture	xxx / (xxx)	
Add/(Less): Share in Dep. to be Reversed / (Additional Dep.)	xxx / (xxx)	xxx / (xxx)
(±) Share in OCI Profit / (Loss) of Associate OR Joint Venture		xxx / (xxx)
(–) Share in Dividend declared / paid by Associate OR Joint Venture		(xxx)
(–) Share in Unrealised Gain on Inventory / PPE in Downstream Transaction		(xxx)
(+) Capital Reserve [if any]		xxx
		xxx

Reduction of Interest in Associate OR Joint Venture

(1) If it happens due to issue of New Equity Shares to some other Investors by Associate OR J.V. :-

- Recognise Investor's Share in Consideration received by Associate OR Joint Venture for Issue of New Equity Shares [As per New Share of Investor]
- Derecognise Proportionate Carrying Amount of Investment in Associate OR Joint Venture to the extent of Reduction of Interest
- Difference between these 2 items in Journal Entry will be recognised in P&L as Gain/Loss on Reduction of Interest in Associate OR J.V. [B/f]

Journal Entry :

Investment in Associate OR J.V. A/c	[Consideration Received by Associate OR J.V. × Investor's New Share]	
Loss on Reduction of Interest A/c [P&L]	Balancing figure	
To Investment in Associate OR J.V. A/c		Proportionate Carrying Amount
To Gain on Reduction of Interest A/c [P&L]		Balancing figure

(2) If it happens due to Stake sold by Investor Company in Associate OR Joint Venture :-

- Recognise Amount received for Sale of Stake in Associate OR Joint Venture [i.e. Cash/Bank A/c]
- Derecognise full Carrying Amount of Investment in Associate OR Joint Venture
- Recognise Stake Retained (if any) in Associate OR Joint Venture by Investor Company as an Investment at Fair Value
- Difference in All these 3 items in Journal Entry will be recognised in P&L as Gain/Loss on Sale of Stake in Associate OR J.V. [B/f]

Journal Entry :

Cash / Bank A/c	Amount Received	
Investment in Associate OR J.V. A/c (Retained Portion)	Fair Value	
Loss on Sale of Stake A/c [P&L]	B/f	
To Investment in Associate OR J.V. A/c		Carrying Amount
To Gain on Sale of Stake A/c [P&L]		B/f

Loss making Associate OR Joint Venture

- If Associate OR Joint Venture is continuously making Losses, then Investor Company should recognise its Share in Loss of Associate OR Joint Venture till the time Carrying Amount of Investment in Equity Shares of Associate OR Joint Venture becomes NIL

  ⇓

  After that Any Unrecognised Share in Loss of Associate OR Joint Venture will be borne by following Long Term Investments in Associate OR Joint Venture in order of their Seniority:-

  → 1st ⇒ Investment in Preference Shares of Associate OR Joint Venture [By Investor]

  → 2nd ⇒ Investment in Long Term Loans of Associate OR Joint Venture [By Investor]

  Note:- Investor Company shall apply first Ind AS 109 on such Long Term Investments in Preference Shares / Loans of Associate OR Joint Venture and then adjust the Unrecognised Share in Loss to these Investments as mentioned above till the time their Carrying Amount becomes NIL

- If the Associate OR Joint Venture subsequently earns profits, then Investor Company should recognise its Share in Profit of Associate OR Joint Venture in following accounts as mentioned below:-

  → 1st ⇒ Investment in Long Term Loans of Associate OR Joint Venture [Upto Share of Loss Allocated to it]

  → 2nd ⇒ Investment in Preference Shares of Associate OR Joint Venture [Upto Share of Loss Allocated to it]

  → 3rd ⇒ Investment in Equity Shares of Associate OR Joint Venture [Remaining All Share in Profit of Associate OR Joint Venture]

This Ind AS determines the Calculation of fair Value of Assets or Liabilities required by many Ind AS.

Fair Value

- Fair Value is the Price
  → That would be Received to Sell an Asset OR Paid to transfer a Liability (ie. Exit Price)
  → In an orderly transaction (i.e. Transaction is not forced)
  → Between Market Participants (ie. Independent Buyer & Seller)

- While measuring fair Value, It is assumed that Transaction to Sell the Asset or Transfer the Liability takes place in

1st Preference
⇓
Principal Market
⇓
It is the Market in which the particular Asset or Liability is transacted in Highest Volume
⇓
Fair Value :-

Price of Asset or Liability	xx
(-) Transportation Cost [To transport the Asset from its Current Location to the Market]	(xx)
	xx

2nd Preference
[If there is No Principal Market]
⇓
Most Advantageous Market
⇓
It is the Market in which Net Amount received on Sale of Asset is Maximum OR Net Amount paid on transfer of Liability is Minimum

Net Amount Received / Paid :-

Price of Asset or Liability	xx
(-) Transportation Cost	(xx)
(-) Transaction Cost [i.e. Cost to Sell]	(xx)
	xx

⇓
Fair Value :-

Price of Asset or Liability	xx
(-) Transportation Cost	(xx)
	xx

Determining Price of Asset or Liability for Fair Value Measurement

(1) Price of Asset or Liability should be determined using following Inputs in priority [Fair Value Hierarchy] :-

- Level 1 Inputs [Observable Inputs] ⇒ Quoted Market Price of Asset or Liability
- Level 2 Inputs [Observable Inputs] ⇒ Market Price of similar Asset or Liability with adjustments
- Level 3 Inputs [Unobservable Inputs] ⇒ Price based on assumptions & forecasts of the entity [Example : PV of forecasted future cash flows]

(2) If Quoted Market Price of the Asset or Liability is not available, then Entity should apply following Valuation Techniques to determine the Price of Asset or Liability :-

- Market Approach [Level 2 Input] :

(i) Comparable Companies Method [EV | EBITDA Multiple]:

Enterprise Value [EBITDA × EV/EBITDA Multiple]	xx
(-) Market Value of Debt	(xx)
(+) Cash & Cash Equivalents	xx
(+) Fair Value of Surplus Assets	xx
	xx
(-) Adjustments [Liquidity Discount %, Lack of Marketability %, Non Controlling Stake Discount %]	(xx)
Equity Value of Company	xx

$$\therefore \text{Value Per Equity Share} = \frac{\text{Equity Value of Company}}{\text{Total Shares issued by the Company}}$$

(ii) P/E Ratio:

Price [Earnings × P/E Ratio]	xx
(-) Adjustments [Liquidity Discount %, Lack of Marketability %, Non Controlling Stake Discount %]	(xx)
Equity Value of Company	xx

$$\therefore \text{Value Per Equity Share} = \frac{\text{Equity Value of Company}}{\text{Total Shares issued by the Company}}$$

- **Net Asset Valuation Approach**:

Equity Value of Company = Fair Value of Net Assets of the Company

$$\therefore \text{Value Per Equity Share} = \frac{\text{Equity Value of Company}}{\text{Total Shares issued by the Company}}$$

- **Income Approach [Level 3 Input]**:

Value per Equity Share is determined by P.V. of Projected free Cash flows using appropriate discounting rate as follows:

PV of Projected Free Cash Flows using WACC	xx
(-) Market Value of Debt	(xx)
(+) Surplus Cash & Cash Equivalents	xx
(+) Fair Value of Surplus Assets	xx
Equity Value of Company	xx

$$\therefore \text{Value Per Equity Share} = \frac{\text{Equity Value of Company}}{\text{Total Shares issued by the Company}}$$

- **Cost Approach [Level 2 Input]**:

This Approach uses Replacement Cost of the particular Asset or Liability to find its Fair Value.

Notes:-

(i) Combination of More than 1 Valuation Technique is also allowed to measure Fair Value.

(ii) Fair Value of Decomissioning Liability [Asset Retirement Obligation] is determined by using Income Approach as follows:

Expected Labour Cost + Overheads + Profit Markup for transferring the Liability	xx
(+) Premium % for Risk in Expected Cash flows	xx
Real Cash Flows	xx

$\therefore$ Inflated Cash flows = Real Cash flows × $(1 + \text{Inflation Rate})^{\text{No. of Years}}$

⇓

Discount it by [Risk Free Rate + Company's Non Performance Risk]

(iii) While determining Fair Value of Non financial Assets [Example: PPE, Intangible Assets, etc.]:

→ Entity should consider the Highest & Best Use of the particular Non financial Asset to determine its Price for Fair Value Measurement.

→ Highest & Best Use of a Non financial Asset must be Physically Possible, Legally Permissible & Financially feasible.

Example :-

A Ltd. has a Land (PPE) which is currently used by it as a Warehouse. This Land could also be used for Commercial Purpose which could be of More Value.

Hence, Commercial Purpose would be considered as its Highest & Best Use if it is Physically, Legally & Financially feasible.

Introduction to Ind AS 115

- It deals with
  - → Accounting of Revenue
  - → from Contracts with Customers to provide Goods or Services
  - → in Entity's Ordinary course of Business

- Entity shall recognise Revenue when it satisfies a Performance Obligation (P.O.) in the Contract with the Customer (i.e. When the Control of Goods or Services promised in the Contract is transferred to the Customer)

⇓

For this purpose, Ind AS 115 prescribes 5 Step Model as follows:

Step 1:	Step 2:	Step 3:	Step 4:	Step 5:
Identify the Contract With Customer	Identify Performance Obligations (P.O.) in the Contract	Determine the Transaction Price	Allocate the Transaction Price in Performance Obligations in the Contract	Recognise Revenue when the Entity Satisfies a Performance obligation

Identifying the Contract with Customer

An Agreement done by the Entity with a Customer will be considered as Contract with Customer under Ind AS 115 if it fulfills ALL of the following Conditions :-

(i) It should be for providing Goods or Services to Customer in Entity's ordinary course of business

(ii) It is approved by the Entity & Customer both (Either in Writing or Orally)

(iii) Rights of Entity & Customer are identified

(iv) Payment Terms are identified

(v) It is probable that Entity will collect the consideration from the Customer [For this, Check Customer's Ability & Intention to pay]

(vi) Both Entity & Customer have Enforceable Rights & Obligations in the Contract (i.e. Parties can terminate the contract on payment of Penalty only)

Note :-

(i) If Any Consideration is received from the Customer in an Agreement which is Not a Contract under Ind AS 115 (i.e. Not Fulfilling Any of the Above Conditions)

⇓

In this Case, Consideration received will be recognised as Deposit Liability

↓

It can be recognised as Revenue Only When

Entity has transferred All Promised Goods or Services to the Customer
and
Full Consideration is Received & it is Non-Refundable

OR

Contract is Terminated
and
Consideration Received is Non-Refundable

(ii) Contract Term :-

Period over which Parties in the Contract have Enforceable Rights & Obligations (including Expected Renewal Period)

Example :-

A gym enters into a Contract with Customer to provide Access to Services for 12 Months. Customer can cancel the Membership anytime after 3 Months without Any Penalty.

Hence, Contract Term is 3 Months.

Identifying Performance Obligations (P.O.) in the Contract

Performance Obligation means promise to customer of transferring

Distinct Good or Service
⇓
Each Distinct Good or Service in a Contract is treated as Separate Performance Obligation (P.O.)
⇓
In this Case, Revenue for each distinct Good or Service is recognised by the Entity when its control is transferred to the Customer

OR

Series of Goods or Services that are Substantially the Same & have Same Pattern of transfer to Customer
[i.e. Customer receives the Benefit as it is Provided]
⇓
It is treated as Single Performance Obligation (P.O.)
⇓
In this Case, Revenue is generally recognised on SLM Basis over a period of time

Examples of Series of Goods or Services :-

- Cable Service, Accounting Service, Security Service, Hotel Management Service, Payroll Processing Service, etc.
- Supply of Daily Newspaper, Magazine, etc.

Note :- Meaning of Distinct Good or Service :-

If Customer can take Benefit from that Good or Service

On Alone Basis

OR

With Other Readily Available Resources

[Readily Available Resource means item that Can be purchased separately in the Market]

Example :-

An Entity enters into a Contract to provide Water Purifier and 1 Year Maintenance Service to the Customer. Customer can also take Water Purifier & Maintenance Service from Any Vendor in the Market.

Hence, There is 2 Separate P.O. in the Contract < Water Purifier / Maintenance Service

* In following Cases, Goods or Services are Not Treated as Distinct even if it fulfills the above mentioned condition :-

(i) Entity has done 'Significant Integration' (i.e. Entity is Using Multiple Goods or Services) to provide the Customer a final product he has asked for

Eg:- Entity is entering into a contract with Customer to build a Power Plant. For this, Entity has to do Engineering, Construction, Wiring, Installation, etc. Since here Integration is done for providing power plant asked by Customer. Hence, there is only Single P.O., i.e. to Build Power Plant

(ii) If Good or Service 'Significantly Modifies or Customizes' other Good or Service

Eg:- Entity is entering into a contract with Customer to provide Software Licence & installation. Installation will significantly customizes the software. Hence, there is only Single P.O., i.e. to provide Customised Software

(iii) If Good or Service are Highly Dependent or Interrelated

Eg:- Entity is entering into a contract with Customer to provide designing Services & construction services of a Building. These services can be taken separately from any vendor in the Market. Customer requires the Entity to continually alter the design & therefore construction will change.

Since Design & Construction Services are Highly Interrelated in this case due to customer requirement of continually alteration in design & construction

Hence, there is only Single P.O.

Determining the Transaction Price

- Transaction Price means consideration that Entity expects for transferring promised goods or services to Customer

  [It excludes Amount collected on behalf of 3rd Party. Eg. GST]

- Transaction Price may include :-

(1) Fixed Consideration :-

→ It is the fixed Amount mentioned in the Contract

→ It is always included in Transaction Price

(2) Variable Consideration :-

→ It is the Amount of Consideration dependent on future events.

Eg.:- Performance Bonus, Penalty, etc.

→ It is included in Transaction Price on the Basis of Entity's Estimation of receiving that consideration

→ Methods for Estimating Variable Consideration :-

(i) Expected Value Method :

- It is generally used if there are More than 2 possible outcomes
- In this Method, Expected Value (i.e. Probability Weighted Amount from a Range of Consideration) is taken as Variable Consideration
- Calculation will be done as follows :

Estimated Consideration Amount	Probability	Probability × Estimated Consideration
C_1	P_1	$C_1 \times P_1$
C_2	P_2	$C_2 \times P_2$
C_3	P_3	$C_3 \times P_3$
⋮	⋮	⋮
C_n	P_n	$C_n \times P_n$

Total Variable Consideration (Probability Weighted) = Sum

Now, Variable Consideration per Unit (Weighted Average Price per Unit)

$$\Rightarrow \frac{\text{Total Variable Consideration (Probability Weighted)}}{\text{Weighted Average No. of Units}}$$

Example :-

Sales Volume	Price p.u.	Total Consideration	Probability	Prob. × Consideration
9000	90	8,10,000	15%	1,21,500
28,000	80	22,40,000	75%	16,80,000
36,000	70	25,20,000	10%	2,52,000

Total Variable Consideration (Probability Weighted) 20,53,500

Weighted Average No. of Units Sold ⇒

Sales Volume	Probability	Probability × Sales Volume
9,000	15%	1,350
28,000	75%	21,000
36,000	10%	3,600
		25,950

$$\text{Variable Consideration p.u.} = \frac{20,53,500}{25,950} = ₹\ 79.13$$

(ii) Most Likely Amount Method :-

- It is generally used if there are only 2 possible outcomes
- In this Method, Single Most Likely Amount (i.e. Consideration of which Probability is Higher) is taken as Variable Consideration

Example :-

Sales Volume	Price p.u.	Total Consideration	Probability	
9000	90	8,10,000	15%	
28,000	80	22,40,000	75%	⇒ Single Most Likely Amount
36,000	70	25,20,000	10%	

∴ Total Variable Consideration = 22,40,000

Variable Consideration per unit = ₹ 80

→ Entity shall include Variable Consideration only to the extent that it is highly probable that Significant Reversal of Revenue Recognised will not occur in future
↓
In following Cases, Variable Consideration will not be included in Transaction Price [i.e. Cases which indicate Significant Reversal of Revenue in future]

If Consideration is dependent on factors outside the entity's influence like Market Volatility

Eg.:- Fee from Client is based on % of Return from Stock Market

OR

Amount of Price Concession in Consideration which Entity generally provides in Similar Contracts to Customers

Eg.:- Contracted Price is ₹ 2 million. Price Concession on same product to other customers is ₹ 0.25 million.
So, Transaction Price will be only ₹ 1.75 million [2 - 0.25]

→ Entity shall Reestimate the Variable Consideration at end of each Reporting Period
↓
If there is Any Change in Variable Consideration on Reestimation, then Such Change should be Accounted for on Cumulative Catchup Basis

Note:- Cumulative Catchup Basis :-

Amount of Revenue TO BE Recognised till date	xxx
Less:- Amount of Revenue Already Recognised till date	(xxx)
Adjustment in Revenue	xxx

(3) Non Cash Consideration :-

→ It means consideration in form other than Cash

→ Example :- Shares of Customer Co., Advertising by Customer, Equipment, etc.

→ Entity shall include Non Cash Consideration in Transaction Price At Fair Value of Non Cash Consideration received from the Customer

⇓

If it cannot be reliably estimated, then Assume Complete Transaction Price as equals to Standalone Selling Price of Goods or Services promised to the Customer

Note :- If Customer provides Any Goods to Entity to facilitate the Entity in fulfillment of his contract, then Such Goods will be treated as Non-Cash Consideration if Entity obtains control over those goods

• Transaction Price need to be Adjusted due to following components :-

(1.) Consideration Payable to Customer by the Entity

If Payment is for Distinct Goods or Services received from the Customer

⇓

→ Do not Adjust the Transaction Price

→ Recognise Purchase of Goods or Services from the Customer Separately

Note :-

If Consideration Payable to Customer

>

Fair Value of Goods or Services received from the Customer

⇓

then Such Excess Amount shall be reduced from Transaction Price

Otherwise

⇓

Eg :- Cash Back, Rebate Coupon on the Basis of expected Redemption %, Reimbursement for Price Protection, One-Time Post in Credit, Payment to make shelves to accomodate entity's Products, etc.

⇓

Reduce this Amount from the Transaction Price

(2.) Effect of Significant Financing Component :-

If there is Time Gap between Satisfaction of P.O. by the Entity & Payment of Consideration by the Customer, then there is Some financing Component in the Contract

⇓

In this Case, Such Significant Financing Component is Adjusted from the Transaction Price

(i.) If Entity satisfies its P.O. but Customer makes the Payment on a Later Date (i.e. Loan by Entity to Customer)

⇓

then Entity shall recognise Revenue at Normal Selling Price (i.e. Cash Selling Price)
Extra Amount received over Cash Selling Price will be treated as Interest Income (finance Income) over the credit period in P&L at Discounting Rate

Note :-

→ If Cash Selling Price is not given in question, then

- Cash Selling Price = Cost of Good or Service + Margin %
- Cash Selling Price = P.V. of future Cash Inflows at Discounting Rate

→ Discounting Rate :-

- Incremental Borrowing Rate [i.e. Actual Interest Rate in Separate financing transaction]
- Otherwise Consider Implicit Interest Rate in the Contract with Customer [i.e. Contractual Discount Rate]

→ Accounting Entries :-

- At the time when P.O. is satisfied

Debtor (Contract Asset)	At Cash Selling Price	
To Sales (Revenue)		At Cash Selling Price

- At Each Balance Sheet Date

For Unwinding of Discount on Debtor (Contract Asset)

Debtor	xxx	
To Interest / finance Income [Opening Balance of Debtor × Discounting Rate]		xxx

For transferring finance Income to P&L

Finance Income	xxx	
To P&L		xxx

- At the time when Payment is received from Customer (i.e. Debtor)

Bank	xxx	
To Debtor		xxx

Example :-

A Ltd. sells a product of which control has been given instantly to Customer but customer will make the payment after 2 years of ₹ 1,21,000. Discounting Rate is 10%. Use PV factor for 2 years = 0.82645

Pass Journal Entries

Solution :-

Calculate Normal Selling Price (Cash Selling Price) :-

⇒ P.V. of future Inflow

⇒ 1,21,000 × 0.82645

⇒ ₹ 1,00,000

Calculation of finance Income on Debtor [Debtor A/c]

Year	Op. Bal.	Interest @ Disc. Rate	Actual Payment	Cl. Bal.
1	1,00,000	10,000	–	1,10,000
2	1,10,000	11,000	1,21,000	–

Journal Entries :-

		Dr.	Cr.
1st Year Beginning (For Sale)	Debtor	1,00,000	
	To Sales		1,00,000
1st Year End	Debtor	10,000	
	To finance Income [P&L]		10,000
2nd Year End	Debtor	11,000	
	To finance Income [P&L]		11,000
	Bank	1,21,000	
	To Debtors		1,21,000

(ii) If Customer makes the Payment in Advance but Entity satisfies its P.O. on a Later Date [i.e. Loan to Entity by Customer]

⇓

then Entity shall recognise Advance Received from Customer as a Contract Liability (Unearned Income)

and

Charge Interest Expense (finance Cost) on such Contract Liability over the period in P&L at Discounting Rate

and

On date when Entity satisfies its P.O., Transfer Amount of Contract Liability (Unearned Income) to Sales A/c (Revenue)

Accounting Entries in this case :-

- At beginning when Advance is Received

  Bank

  To Contract Liability (Unearned Income)

- At Each Balance Sheet Date

  For Unwinding of Discount on Contract Liability (Unearned Income)

  Interest Expense / Finance Cost [Opening Balance of Contract Liability × Discounting Rate]

  To Contract Liability

For transferring finance Cost to P&L

P&L

To Interest Expense

· At the time when Entity satisfies its P.O.

Contract Liability

To Sales (Revenue)

Example :-

A Ltd. sells a product of which control will be transferred after 2 Years to Customer but Customer has made the payment in Advance of ₹ 50,000. Discounting Rate is 10%.

Pass Journal Entries.

Solution :-

Calculation of Interest Expense on Unearned Income [Contract Liability A/c]

Year	Op. Bal.	Interest @ Disc. Rate	Actual Payment	Cl. Bal.
1	50,000	5,000	-	55,000
2	55,000	5,500	-	60,500

Journal Entries :-

1st Year Beginning (For Advance Received)	Bank	50,000	
	To Unearned Income		50,000
1st Year End	Interest Expense [P&L]	5,000	
	To Unearned Income		5,000
2nd Year End	Interest Expense [P&L]	5,500	
	To Unearned Income		5,500
When P.O. is Satisfied ⇒	Unearned Income	60,500	
	To Sales		60,500

Note :- In following Cases, financing Component is Not Significant ; Hence, such Insignificant financing Component will Not be Adjusted from Transaction Price :-

→ If Amount of Interest is Insignificant (i.e. < 5%)

→ If Customer makes the Payment in Advance but P.O. is satisfied by the Entity on a Later Date due to request of Customer

→ If Consideration is based on future events [Eg.:- Sales Based Royalty]

→ If Time Gap between satisfaction of P.O. & Payment of Consideration is due to reasons other than financing
[Eg.:- Withholding Money by Customer for Quality Checks, Advance Payment from Customer for protection against Non-Payment]

→ If Time Gap is 1 Year or Less, then Entity may choose to not adjust Financing Component from Transaction Price as Practical Expedient

Allocating the Transaction Price in Performance Obligations (P.O.)

· Allocate the Transaction Price to each Performance Obligation (P.O.) in the Contract in Ratio of Standalone Selling Price (SSP) of each P.O.

Note:- Standalone Selling Price (SSP) is determined using following in Priority:

(i) Observable Price of Goods/Services:-

Price at which it is sold separately by the Entity

(ii) Estimated Price of Goods/Services:-

→ Adjusted Market Assessment Approach [i.e. Adjusting Competitor's Price]

→ Cost Plus Margin Approach

→ Residual Approach [Total Transaction Price of Contract − Standalone Selling Price of Other Goods or Services in the Contract]

Example:- Entity is Selling 3 Distinct Product A, B & C at ₹ 10,000 to Customer

Product	Standalone Selling Price (SSP)
A	5,000
B	2,500
C	7,500

Solution:- Allocation of Transaction Price

$A = 10{,}000 \times \frac{5{,}000}{15{,}000} = 3{,}333$

$B = 10{,}000 \times \frac{2{,}500}{15{,}000} = 1{,}667$

$C = 10{,}000 \times \frac{7{,}500}{15{,}000} = 5{,}000$

· If Discount in Contract is not proportionately related to All P.O.

Example:- Entity is Selling 3 Distinct Product A, B & C at ₹ 10000 to Customer

Product	Standalone Selling Price (SSP)
A	5,000
B	2,500
C	7,500

Also Entity regularly sells B & C together at ₹ 8,000 then, In this Case Use following Steps to Allocate Transaction Price in P.O. :-

Step 1: Calculate Revised SSP for Products which Entity already sells in Combo

Eg:- $B = 8{,}000 \times \frac{2{,}500}{10{,}000} = 2{,}000$

$C = 8{,}000 \times \frac{7{,}500}{10{,}000} = 6{,}000$

Step 2: Now, Allocate Transaction Price in all P.O. in Ratio of Revised SSP

Eg:-

Product	Revised SSP
A	5000
B	2000
C	6000

Allocation of Transaction Price

$A = 10{,}000 \times \frac{5{,}000}{13{,}000}$ $= 3{,}846$

$B = 10{,}000 \times \frac{2{,}000}{13{,}000}$ $= 1{,}539$

$C = 10{,}000 \times \frac{6{,}000}{13{,}000}$ $= 4{,}615$

- If there is Variable Consideration in Transaction Price, then Allocate it to that P.O. only to which it relates

Example:- Entity is Selling 3 Distinct Product A, B & C at ₹ 10,000 to Customer

Product	Standalone Selling Price (SSP)
A	9,000
B	2,000
C	1,000

Also, there is Variable Consideration of ₹ 500 on Product C

Solution:- Allocation of Transaction Price

$A = 10{,}000 \times \frac{9{,}000}{12{,}000}$ $= 7{,}500$

$B = 10{,}000 \times \frac{2{,}000}{12{,}000}$ $= 1{,}667$

$C = \left[10{,}000 \times \frac{1{,}000}{12{,}000}\right] + 500$ $= 833 + 500$ $= 1{,}333$

- If Consideration in a Contract with Customer is shown separately for different products but it is not representing Standalone Selling Price of those Products

Example:- Entity is selling Licence A & B to the Customer. Price stated in Contract is fixed ₹ 5,50,000 for Licence A and Price for Licence B is in % based on Sales-based Royalties (Variable Consideration) i.e. expected to be ₹ 30,00,000

Product	SSP
Licence A	16,00,000
Licence B	20,00,000

then, In this Case Allocate Total Transaction Price in Contract in Ratio of SSP of each P.O. (whether Transaction Price includes fixed Consideration or Variable Consideration)

Solution: Allocation of Transaction Price

$A = 35,50,000 \times \frac{16,00,000}{36,00,000}$

$= 15,77,778$

$B = 35,50,000 \times \frac{20,00,000}{36,00,000}$

$= 19,72,222$

Recognition of Revenue

- Entity shall recognise Revenue when it satisfies a P.O. in Contract with Customer, i.e. When the Control of Goods or Services promised in the Contract is transferred to the Customer

If Control is transferred Over a Period of Time
⇓
Recognise Revenue (Calculated as per Input or Output Method) over a Period of Time

If Control is transferred At a Point in Time
⇓
Recognise Full Revenue relating to that P.O. At A Point in Time

Note:-

(i) Transfer of Control of Good or Service

Over a Period of Time
⇓
If Any of the following Criteria is Met

Criteria A: Customer simultaneously receives & consumes the benefits as the entity performs

Eg:- Cable Service, Security Service, Accounting Service, Payroll Processing Service

OR

Criteria B: Customer controls the Asset as Entity Creates or Enhances the Asset

Eg:- Building WIP

OR

Criteria C: Asset created does not have Any Alternative Use to the Entity

and

Entity has enforceable Right to Receive Payment equals to Cost incurred plus Margin of Performance till date in case of Termination of Contract before Maturity

At a Point in Time
⇓
Otherwise

(ii) In Case of Sales Based Royalty, Revenue is Recognised When

→ Subsequent Sale Occurs

OR

→ P.O. to which Sales Based Royalty has been Allocated is satisfied

→ Whichever is Later

(iii) Methods to Measure % of Progress to Recognise Revenue in case of P.O. satisfied over a Period of Time :-

(A) Output Method :

In this Method, % of Progress is calculated on the basis of Goods|Services transferred in relation to Total Goods|Services to be transferred.

Eg :-

→ Progress % Given by Independent Surveyors

→ SLM Basis in case of Series of Goods or Services that are Substantially the Same

(B) Input Method :

In this Method, % of Progress is calculated on the basis of Costs incurred till date to satisfy P.O. in the Contract

$$\% \text{ of Progress} = \frac{\text{Costs incurred till date}}{\text{Total Estimated Costs}} \times 100$$

* Exclude following Costs in Above formula from Both Numerator & Denominator

→ Abnormal Costs

→ Cost of Major Component which is purchased & delivered to Customer but not Installed yet [Eg. Elevators in construction of Building]

- **Accounting of Revenue :-**

(A) General Accounting Entries for Revenue Related Transactions

→ When Control of Goods is transferred to Customer but Payment Not Received

Debtor
    To Sales

→ When Payment is Received from Customer but Control of Goods is Not transferred to him

Bank
    To Unearned Income

→ When Control of Goods is transferred to Customer & Payment is Also Received

Bank
    To Sales

(B) Following Items can be recognised in Books for Revenue related transaction

- Revenue to be recognised in P&L in Current Period
- Contract Asset (Debtor)
- Contract Liability [Unearned Income]
- Cost (Expense) to be recognised in P&L in Current Period
- WIP Asset [Prepaid Expense]

Calculation of All these items :

(i.) Calculation of Revenue to be recognised in P&L in Current Period :

First Calculate Cumulative Revenue to be Recognised in P&L till date

[Total Transaction Price – Cost of Major Component] × % of Progress	xxx
Add:- Cost of Major Component as Revenue [Eg. Elevators]	xxx
	xxx

Now Calculate Revenue to be recognised in P&L in Current Period

Cumulative Revenue to be recognised in P&L till date	xxx
Less:- Revenue already recognised in P&L upto Previous Period	(xxx)
	xxx

(ii.) Calculation of Amount Due from / (To) Customer [Contract Asset or Contract Liability]:

Cumulative Revenue recognised in P&L till date	xxx
Less:- Payment Received from Customer till date	(xxx)
Amount Due from Customer / (Due to Customer)	xxx / (xxx)

Amount Due from Customer → Contract Asset (Debtor)

(Due to Customer) → Contract Liability (Unearned Income)

(iii.) Calculation of Cost to be recognised in P&L in Current Period :

first Calculate Cumulative Cost to be recognised in P&L till date

[Total Estimated Cost - Abnormal Cost - Cost of Major Component] × % of Progress	xxx
Add:- Abnormal Cost	xxx
Add:- Cost of Major Component	xxx
	xxx

Now Calculate Cost to be recognised in P&L in Current Period

Cumulative Cost to be recognised in P&L till date	xxx
Less:- Cost already recognised in P&L upto Previous Period	xxx
	xxx

(iv.) Calculation of Work in Progress (WIP Asset) :

Costs incurred till date	xxx
Less:- Cumulative Cost recognised in P&L till date	(xxx)
WIP Asset (Prepaid Expense)	xxx

Some Special Cases

(1.) Accounting in case of Sale with Right of Return :-

Entity shall recognise

- Revenue for the products which are not expected to be returned
- Refund Liability for the products which are expected to be returned
- Inventory Asset at Cost for its Right to Recover product which are expected to be returned

Journal Entry :-

- Bank
  To Sales
  To Refund Liability
- Inventory
  To P & L

Note :- Amount of Restocking fee (i.e. fee charged on Returned Products as a compensation for Packing & Shipping Cost) is recognised as Revenue

(2.) Accounting of Warranties :-

Assurance Warranties

⇓

It is inbuilt in a product due to requirement of Law

⇓

Treatment As per Ind AS 37 (i.e. Make Provision for Expected Warranty obligation)

Journal Entry :-

Warranty Expense [P&L]
To Provision for Warranty Cost

Service Warranties

⇓

It can be purchased separately by Customer [Eg. Extended Warranty]

⇓

Treat it as Separate Performance Obligation (P.O.) and

Hence, Transaction Price is allocated to it as per Step 4 of Ind AS 115

(3.) Accounting of Revenue in case of Contract Renewal Option at Low Price is given to Customer :-

For this, Following Steps are needed :-

Step 1 :- Calculate Total Estimated Number of Customers over the period on the basis of Expected Renewal Rate

Step 2 :- Calculate Total Estimated Consideration over the period using Total Estimated No. of Customers

Step 3 :- Calculate Amount of Revenue to be recognised per Customer

$$\Rightarrow \frac{\text{Total Estimated Consideration}}{\text{Total Estimated Customers}}$$

Step 4 :- Any Extra Amount received from Customer above the Amount calculated in Step 3 will be recognised as Contract Liability (Unearned Income)

(4.) Treatment of Discount Voucher :-

- Treat it As Separate Performance Obligation (P.O.)
- Allocate Transaction Price in Product & Discount Voucher in ratio of their Stand-alone Selling Price (SSP)
- SSP of Discount Voucher = Expected Amount of Next Purchase by Customer × Discount % solely due to Discount Voucher × Probability % of Customer applying Discount Voucher on Next Purchase
- Amount of Transaction Price Allocated to Product is recognised as Revenue
- Amount of Transaction Price Allocated to Discount Voucher is recognised as Contract Liability
  [This Amount will be transferred to Revenue when Customer uses this Voucher on Next Purchase or on expiry of Discount Voucher Period]

(5.) Treatment of Loyalty Points :-

- Treat it As Separate Performance Obligation (P.O.)
- Allocate Transaction Price in Product & Loyalty Points in ratio of their Stand-alone Selling Price (SSP)
- SSP of Loyalty Points = Sales Amount × Points for Each 1 ₹ Sale × Value of Each Point
- Amount of Transaction Price Allocated to Product is recognised as Revenue
- Amount of Transaction Price Allocated to Loyalty Points is recognised as Contract Liability
  [This Amount will be transferred to Revenue when Customer redeem these Points or on expiry of Loyalty Points Redemption Period]
- Also, At Year End if Entity estimates only some Loyalty Points will be redeemed, then Amount of Contract Liability initially Booked for Loyalty Points will be assumed for those estimated points

(6.) Modification in Contract with Customer :-

Case 1 :-

Modification results in Addition of Goods or Services in the Contract

and

Price in the Contract increases by SSP of Additional Goods or Services

Case 2 :-

Modification Results in Change in Price of Existing Goods or Services

OR

Modification Results in Addition of Goods or Services in the Contract But Price in Contract Not increases by SSP of Additional Goods or Services

Case 3 :-

Modification Results in Increase in Labour Hours in Construction Contract

OR

Any Other Case of Modification

⇓ Treat it As Separate Contract

⇓ Terminate Old Contract & Create New Contract i.e. Consideration for Remaining Goods or Services is recognised as Revenue over the remaining period

⇓ Treat it As Part of Existing Contract i.e. Adjust Revenue on Cumulative Catch up Basis

(7.) Combination of Contracts :-

Entity shall combine 2 or More Contracts entered with the same Customer At or Near the Same Time as Single Contract if

- Contracts are Negotiated as a Single Package
- OR
- Consideration of 1 Contract depends on Price or Performance in Other Contract
- OR
- Goods or Services Promised in Contracts is Single P.O.

(8.) Principal Vs Agent :-

If Entity is Performing As a Principal
⇓
Recognise Gross Amount as Revenue [i.e. Total Amount]

If Entity is Performing as an Agent
⇓
Recognise Only Net Amount as Revenue [i.e. Commission Amount]

Note :- If Any of the following condition is fulfilled, then Entity will be considered as Principal :-
→ Entity is Primarily Responsible for fulfilling the Contract
→ Entity has Inventory Risk
→ Entity has discretion in Setting Prices

(9.) Consignment Arrangement :-

- Entity (i.e. Consignor) shall recognise Revenue only when the Control of Goods is transferred to the Consignee or End Consumer
- If All of the following 3 Conditions are fulfilled, then It is considered that Control of Goods has not been transferred to the Consignee yet :-
  → Consignee don't have any obligation to pay to Consignor until goods are sold to a Customer
  → Consignor is able to ask for Return of the goods provided to Consignee
  → Consignor is able to require Consignee to transfer goods to Any Other Party

(10.) Bill and Hold Arrangement :-

- Entity Bills a Customer for a Product but delivery of Product has not been done yet
- As Revenue is recognised only when Control is transferred to the Customer
⇓

So, In this Case, if all the following 3 Conditions are fulfilled, then it will be considered as Control is transferred to the Customer :-

→ Customer requested Entity to Bill & Hold

→ Product is identified separately & ready for immediate delivery

→ Entity does not have Ability to Use that Product

- In Case of Bill & Hold Arrangement, there may arise a Separate P.O. on part of Entity [i.e. Custodial Services for Storing Goods]

(11.) Accounting in case of Service Concession Arrangements :-

- It is an arrangement in which an Entity (operator) enters into a Contract with Customer / Grantor (i.e. Government) for constructing & operating an infrastructure for Public Service. Eg. Toll Road

- That infrastructure constructed & operated by Entity for Government is Not a PPE of Entity

- Accounting of Revenue :-

If Entity has Right to Receive Fixed Amount of Cash from Government

⇓

Recognise Right to Receive fix Amount as Financial Asset as per Ind AS 109

⇓

Journal Entry in Construction Phase:

→ Financial Asset (Debtor)
  To Sales (Revenue)
[At Fair Value of Construction Service]

Journal Entry in Operation Phase:

→ Financial Asset (Debtor)
  To Finance Income (P&L)
[For Unwinding discount on Financial Asset]

→ Financial Asset (Debtor)
  To Sales (Revenue)
[Income relating to Services in Operation Phase At fair Value]

→ Bank
  To Financial Asset (Debtor)
[When Payment is received from Government]

If Entity has Right to Collect Toll from Users of public infrastructure

⇓

Recognise Right to Collect Toll as Intangible Asset as per Ind AS 38

⇓

Journal Entry in Construction Phase:

→ Intangible Asset
  To Sales (Revenue)
[At Fair Value of Construction Services]

Journal Entry in Operation Phase:

→ Amortisation
  To Intangible Asset
[Amortisation of Intangible Asset over Contract Period]

→ Bank
  To Sales (Revenue)
[Toll Income Received during Operation Phase]

(12.) Repurchase Agreements :-

Forward Agreement
⇓
Entity sells the goods but promise to repurchase at a fixed Price at a fixed date

Call Option
⇓
Entity sells the goods but have an option to repurchase at a fixed price at a fixed date

⇓ (Forward Agreement & Call Option)

Accounting

If Repurchase Price ≥ Original Selling Price
⇓
then, It is a financing Arrangement (i.e. Loan)
[Apply Ind AS 109]
⇓
- Recognise financial Liability of Consideration received at Beginning

  Bank
  To Financial Liability

- Recognise difference between Consideration Received At Beginning & Amount Payable at time of Repurchase as Finance Cost

  Finance Cost [P&L]
  To Financial Liability

- At time of Repurchase

  Financial Liability
  To Bank

If Repurchase Price < Original Selling Price
⇓
then, It is a Lease Agreement
[Apply Ind AS 116]
⇓
- Recognise Consideration Received at Beginning As Deposit Liability (to the extent of Amount of Repurchase) & Unearned Lease Income (for the Balance Amount)

  Bank
  To Deposit Liability
  To Unearned Lease Income

- Recognise Lease Income over the period

  Unearned Lease Income
  To Lease Income [P&L]

- At time of Repurchase

  Deposit Liability
  To Bank

Put Option
⇓
Entity sells the goods but the Customer has an Option to Sale back the goods to the Entity at a fixed price at a fixed date
⇓

Accounting

If it is likely that Customer will exercise the Put Option, i.e. If Repurchase Price ≥ Expected Market Price of Goods at Repurchase Date
⇓
Same Accounting As in Forward Agreement or Call Option

Otherwise
⇓
Same Accounting As in case of Sale with Right of Return

Note :- If Repurchase Option is Not Exercised on Repurchase Date, then the Balance in Financial Liability or Deposit Liability A/c will be transferred to Sales (Revenue)

(13.) Contract Costs :-

Contract Acquisition Costs

- Sunk Costs i.e. Costs incurred whether Contract is done or Not
  - Eg:- Salesperson Travelling Expenses
  - ⇓
  - Charge to P&L Immediately
- Incremental Costs to obtain the Contract i.e. Costs incurred only when Contract is done
  - Eg:- Sales Commission
  - ⇓
  - Recognise it as WIP Asset & Amortise over the Contract Term

Contract Fulfillment Costs

⇓

Costs incurred to fulfill the Contract

Eg: Material, Labour, etc. in Construction Contract of a Building

- If these Costs are Covered by Any Other Ind AS
  - ⇓
  - Account for As per those Ind AS
  - [Eg:- Ind AS 16, 38, 19]
- If these Costs are Not Covered by Any Other Ind AS
  - ⇓
  - Recognise it as WIP Asset & Amortise over the Contract Term

Introduction to Ind AS 116

(1.) **Meaning of Lease :-**

Lease is a Contract that provides Right to Control the Use of Identified Asset to Lessee for a period of time in exchange for consideration

(2.) **Dates of Lease :-**

Inception Date of Lease

⇓

Date of Lease Agreement / Commitment by Parties

⇓

This Date is used to Check Whether a Contract is Lease or Not

Commencement Date of Lease

⇓

Date on which Asset is provided to Lessee by the Lessor

⇓

Accounting of Lease is done from this Date

Accounting of Lease in the Books of Lessee

(1.) Lessee shall initially recognise a Lease Liability & related RoU Asset on Commencement Date as follows :-

(A.) **Lease Liability :-**

- At P.V. of Lease Payments to be made by Lessee over the Lease Term by using Discounting Rate

  Calculation of Lease Liability to be booked Initially :

Year	Lease Payments	P.V.F. @ Discounting Rate	P.V. of Lease Payments
(1)	(2)	(3)	(4) = (2) x (3)
✓	✓	✓	✓

- Charge Interest Expense (Finance Cost) over the Lease Term on this Lease Liability to Unwind the discount

  Calculation of Finance Cost on Lease Liability [Lease Liability A/c] using Amortisation Table :

Year (1)	Opening Balance of Lease Liability (2)	Interest @ Discounting Rate (3) = (2) X Discounting Rate	Actual Payment of Lease Installment (4)	Closing Balance of Lease Liability (5) = (2) + (3) - (4)
✓	✓	✓	✓	✓

(B.) **Right of Use [RoU] Asset :-**

- RoU Asset is Initially recognised At Cost
- Calculation of Cost of RoU Asset :

Lease Liability Amount as calculated above	xxx
(+) Lease Payments made before Commencement Date	xxx
(−) Lease Incentives received before Commencement Date	(xxx)
(+) Initial Direct Costs incurred by Lessee	xxx
(+) P.V. of Dismantling or Restoration Cost	xxx
	xxx

- Depreciation is charged on RoU Asset over the Lease Term using SLM Method
  But if Lessee is reasonably certain to Exercise the Purchase Option at End of Lease, then Depreciation on RoU Asset is charged over the Useful Life of the Asset
- Subsequently At Each Balance Sheet Date, RoU Asset can be shown At Cost Model or Revaluation Model [Same As per Ind AS 16]

Note :-

(i) Lease Payments :-

- It means payments made by Lessee over the Lease Term to Lessor
- It includes :

(a) Fixed Payments

Fixed Payments	xxx
Less :- Lease Incentive received from Lessor	(xxx)
	xxx

* Payments Linked to Interest Rates (such as LIBOR) or Index (such as CPI or Inflation Index) are included using the Interest Rate or Index prevailing on the Lease Commencement Date

Example 1 :

Lease Payment are ₹ 1,00,000 at beginning of Each Year for 3 Years. It will increase by LIBOR Rate of each year. At Commencement Date, LIBOR is 2%

∴ Lease Payments are

1^{st} Year Beginning → ₹ 1,00,000

2^{nd} Year Beginning → ₹ 1,00,000 + 2% → ₹ 1,02,000

3^{rd} Year Beginning → ₹ 1,02,000 + 2% → ₹ 1,04,040

Example 2 :

Lease Payment are ₹ 1,00,000 at end of each year for 3 Years. It will increase based on CPI of each year. At Commencement Date, CPI is 280

∴ Lease Payments are

1^{st} Year End → ₹ 1,00,000 × $\frac{280}{280}$ ⇒ ₹ 1,00,000

2^{nd} Year End → ₹ 1,00,000 × $\frac{280}{280}$ ⇒ ₹ 1,00,000

3^{rd} Year End → ₹ 1,00,000 × $\frac{280}{280}$ ⇒ ₹ 1,00,000 (b.) Exercise Price of Asset under Purchase Option if it is reasonably certain that Lessee will exercise this option

(c.) Guaranteed Residual Value (GRV) expected to be paid by Lessee at end of Lease

(ii.) Lease Term :-

Normal Mandatory Period of Lease + Expected Renewal Period

(iii.) Discounting Rate to be used for Calculating P.V. of Lease Payments :-

1st Priority : Implicit Interest Rate in the Lease Contract (i.e. Lessor's IRR)

It is the Rate at which ⇒

P.V. of Lease Payments made by Lessee + P.V. of Unguaranteed Residual Value [UGRV] = Fair Value of Asset Under Lease

2nd Priority : Incremental Borrowing Rate of Lessee

(2.) Journal Entries for Accounting by Lessee :-

(i.) At Commencement Date :

RoU Asset A/c

Bank A/c [For Lease Incentives received before Commencement Date] (if any)

To Lease Liability A/c

To Bank A/c [For Lease Payments before Commencement Date or Initial Direct Cost] (if any)

To Provision for Dismantling Cost (if Any)

(ii.) At End of Each Year :

- For Unwinding Discount on Lease Liability

  Finance Cost A/c [P&L]

  To Lease Liability A/c

- For Depreciation on RoU Asset

  Depreciation A/c [P&L]

  To RoU Asset A/c

(iii.) At the time of Payment of Lease Installment :

Lease Liability A/c

To Bank A/c

(3.) Steps to be followed to solve the Practical Question :-

Step 1 : Calculate Lease Liability to be booked Initially

Step 2 : Calculate Cost of RoU Asset

Step 3 : Calculate Depreciation on RoU Asset & its Closing Balance at end of each year as follows:

Year	Opening Balance of RoU Asset	Depreciation	Closing Balance of RoU Asset
(1)	(2)	(3)	(4) = (2)-(3)
✓	✓	✓	✓

Step 4: Calculate Finance Cost on Lease Liability & its Closing Balance at end of each year using Amortisation Table

Step 5: Pass Journal Entries (if required in question)

Example :-

A ltd. takes an Equipment on Lease for 3 years. Lease Payments are ₹ 1,00,000 to be made at End of Each Year. Discounting Rate is 10%.
Pass Journal Entries for 1st Year in A ltd.'s Books.

Solution :-

Step 1:- Calculation of Lease Liability to be booked Initially

Year	Lease Payments	P.V.F. @ 10%	P.V. of Lease Payments
1	1,00,000	0.909	90,900
2	1,00,000	0.826	82,600
3	1,00,000	0.751	75,100
			2,48,600

Step 2:- Calculation of Cost of RoU Asset

⇒ Lease Liability ⇒ ₹ 2,48,600

Step 3:- Calculation of Depreciation on RoU Asset & its Closing Balance at Each Year End

$$\text{Depreciation} = \frac{248600}{3} = 82,867$$

Year	Op. Bal. of RoU Asset	Depreciation	Cl. Bal. of RoU Asset
1	2,48600	82,867	165,733
2	165,733	82,867	82,866
3	82,866	82,866	–

Step 4:- Calculation of Finance Cost & Closing Balance of Lease Liability at Each Year End

Year	Op. Bal. of Lease Liability	Interest @ 10%	Actual Payment of Lease Installment	Cl. Bal. of Lease Liability
1	2,48,600	24,860	1,00,000	1,73,460
2	1,73,460	17,346	1,00,000	90,806
3	90,806	9,194	1,00,000	–

Step 5:- Journal Entries for 1st Year

		Dr.	Cr.
→ At Commencement Date :	RoU Asset	2,48,600	
	To Lease Liability		2,48,600
→ At Year End :	Finance Cost [P&L]	24,860	
	To Lease Liability		24,860

Depreciation [P&L]	82,867	
To RoU Asset		82,867
Lease Liability	100,000	
To Bank		100,000

Accounting of Lease Modification in the Books of Lessee

- Lease Modification means change in Terms of Lease Contract (i.e. Lease Term, Area, Lease Payments)
- If Modification in Lease Contract Results in

Increase in Area & Increase in Lease Payment with Stand-alone Selling Price of such increased Area
⇓
Treat it As Separate Lease Contract

Increase in Lease Term
OR
Increase in Area & Lease Payment
OR
Increase / Decrease in Lease Payment
⇓
Apply Case A

Decrease in Lease Term
OR
Decrease in Area & Lease Payment
⇓
Apply Case B

Mix of Case A & B
⇓
Increase in Area & Lease Payment
+
Decrease in Lease Term
⇓
Apply Case C

- Case A :- Steps to be followed to solve the Practical Question:

Step 1 : Calculate Lease Liability to be booked Initially on Commencement Date

Step 2 : Calculate Cost of RoU Asset recognised on Commencement Date

Step 3 : Calculate Closing Balance of RoU Asset on Modification Date [Using Depreciation Table]

Step 4 : Calculate Closing Balance of Lease Liability on Modification Date [Using Amortisation Table]

Step 5 : Calculate Revised Lease Liability on Modification Date using Discounting Rate of Modification Date

Step 6 : Difference between Amount of Lease Liability in Step 5 & Step 4 will be Adjusted in Lease Liability A/c & RoU Asset A/c

Example :-

Year	Lease Payments	P.V.F. @ 10%	P.V.
1	1,000	0.909	909
2	1,500	0.826	1,239
3	1,000	0.751	751
4	2,000	0.683	1,366
5	1,500	0.621	932
		Initial Lease Liability	5,197

After 3 Years, Lease has been modified to Increase Lease Term by 1 More Year (i.e. for 6th Year Lease Payment will be ₹ 1,000). Discounting Rate on Modification Date is 11%

Calculation of Closing Balance of Lease Liability on Modification Date (ie. After 3 Yrs):

Year	Op. Bal. of L.L.	Int. @ 10%	Actual Payment	Cl. Bal. of L.L.
1	5,197	520	1,000	4,717
2	4,717	472	1,500	3,689
3	3,689	369	1,000	3,058

It is representing P.V. of Remaining Original Lease Payments on Modification Date [ie. P.V. of ₹ 2000 & ₹ 1500 of 4th & 5th Year]

Now, Revised Lease Liability that should exist in Books on Modification Date as per Modified Terms :-

Year	Lease Payments	P.V.F. @ 11%	P.V.
1 (4th Year)	2,000	0.901	1,802
2 (5th Year)	1,500	0.812	1,218
3 (6th Year)	1,000	0.731	731
			3,751

∴ Adjustment to be made in Lease Liability Balance on Modification Date

⇒ 3,751 − 3,058 ⇒ ₹ 693 [Increase in Lease Liability]

Journal Entry for Modification :

	Dr	Cr
RoU Asset	693	
To Lease Liability		693

- Case B :- Steps to be followed to solve the Practical Question:

Step 1 : Calculate Lease Liability to be booked Initially on Commencement Date

Step 2 : Calculate Cost of RoU Asset recognised on Commencement Date

Step 3 : Calculate Closing Balance of RoU Asset on Modification Date [Using Depreciation Table]

Step 4 : Calculate Closing Balance of Lease Liability on Modification Date [Using Amortisation Table]

Step 5 : Calculate Gain / Loss due to Decrease in Lease Term or Area

→ Calculation of Gain or Loss if there is Decrease in Area

Reduction in RoU Asset Balance

⇓

$$\text{Closing Balance of RoU Asset on Modification Date} \times \frac{\text{Decrease in Area}}{\text{Original Area}}$$

Reduction in Lease Liability Balance

⇓

$$\text{Closing Balance of Lease Liability on Modification Date} \times \frac{\text{Decrease in Area}}{\text{Original Area}}$$

⇓

Difference between these 2 Amounts is Gain or Loss due to decrease in Area

→ Calculation of Gain or Loss if there is Decrease in Lease Term

Reduction in RoU Asset Balance

$$\text{Closing Balance of RoU Asset on Modification Date} \times \frac{\text{Decrease in Lease Term}}{\text{Remaining Lease Term as per Original Contract}}$$

Reduction in Lease Liability Balance

Closing Balance of Lease Liability on Modification Date

—

P.V. of Original Lease Payments in Remaining Revised Lease Term using Original Discounting Rate

Difference between these 2 Amounts is Gain or Loss due to decrease in Lease Term

→ Journal Entry :-

Lease Liability A/c
Loss on Reduction A/c [P&L]
    To RoU Asset A/c
    To Gain on Reduction A/c [P&L]

Step 6 : Calculate Closing Balance of RoU Asset on Modification Date After Above Reduction
⇒ Balance As per Step 3 — Reduction As per Step 5

Step 7 : Calculate Closing Balance of Lease Liability on Modification Date After Above Reduction
⇒ Balance As per Step 4 — Reduction As per Step 5

Step 8 : Calculate Revised Lease Liability on Modification Date using Discounting Rate of Modification Date

Step 9 : Difference between Amount of Lease Liability in Step 8 & Step 7 will be Adjusted in Lease Liability A/c & RoU Asset A/c

- Case C :- Steps to be followed to solve the Practical Question:

Step 1 : Do Accounting for Case B Type Modification ignoring Case A Modification

Step 2 : Calculate Closing Balance of RoU Asset after Case B Modification

Step 3 : Calculate Closing Balance of Lease Liability after Case B Modification

Step 4 : Calculate Revised Lease Liability on Modification Date using Discounting Rate of Modification Date [For Case A Modification]

Step 5 : Difference between Amount of Lease Liability in Step 4 & Step 3 will be Adjusted in Lease Liability A/c & RoU Asset A/c

Accounting of Remeasurement in the Books of Lessee

Lessee is required to Remeasure Lease Liability upon a Change in Lease Payments due to

- Reassessment of Lease Term due to Exercising or Not Exercising Renewal Option by Lessee
- Reassessment of Exercising or Not Exercising Purchase Option by Lessee
- Change in future Lease Payments because of Change in Interest Rate or Index
- Change in Expected Amount of GRV

Significant Remeasurement
[As it was Not known previously]
⇓
Apply Same Accounting As per Case A of Modification

Insignificant Remeasurement
[As this Fact was known Already]
⇓
Apply Same Accounting As per Case A of Modification BUT Use the ORIGINAL Discounting Rate Instead of Discounting Rate of Modification Date in Step 5 for Calculating Revised Lease Liability on Modification Date

Note:- If Reason of Remeasurement is Both Significant & Insignificant, then Apply Same Accounting As per Case A of Modification [i.e. Treating it As Significant Remeasurement]

Accounting of Lease in the Books of Lessor

(1.) Lessor shall classify Lease as following on Inception Date:

- Finance Lease ⇓ Substantially All Risks & Rewards are transferred to Lessee
- Operating Lease ⇓ Substantially All Risks & Rewards are not transferred to Lessee

Note:- If Any of the following condition is satisfied, Lessor shall classify Lease as Finance Lease [otherwise Operating Lease]:

- Ownership of Asset will be transferred to Lessee At End of Lease
- Lessee has Option to Purchase the Asset At Price Expected to be Lower than Fair Value of Asset on Exercise Date
- Lease Term Covers Major Part of Life of Asset [i.e. >50%]
- P.V. of Lease Payments by Lessee substantially (i.e. > 90%) covers the Fair Value of Asset on Inception Date
- Asset is of Specialised Nature that Can be used by Lessee Only

(2.) Accounting of Operating Lease by Lessor:-

- Lessor shall recognise Lease Income on SLM Basis over the Lease Term
- Lessor shall continue to recognise Respective Asset & Charge Depreciation on it
- Journal Entry [At Each Year End]

→ For Lease Income

Bank
    To Lease Income [P&L]

→ For Depreciation on Asset

Depreciation [P&L]
    To Asset

(3) Accounting of Finance Lease by Lessor :-

- Lessor shall initially do the following on Commencement Date
  - → Derecognise the Asset given to Lessee under Lease At Carrying Amount

    ⇓

    No Depreciation will be charged on this Asset by Lessor in future after giving it on finance lease
  - → Recognise Lease Receivable [Asset] At an amount equals to Net Investment in Lease

    ⇓

    Interest Income (finance Income) is booked over the Lease Term on this Lease Receivable to Unwind the Discount

    Calculation of Finance Income on Lease Receivable [Lease Receivable A/c]

Year (1)	Opening Balance of Lease Receivable (2)	Interest @ Discounting Rate (3) = (2) × Discounting Rate	Actual Payment Received Under Lease (4)	Closing Balance of Lease Receivable (5) = (2) + (3) − (4)
✓	✓	✓	✓	✓

  - → Difference between the Above 2 Amounts will be recorded as Gain or Loss in P&L
- Journal Entries :-

(i) At Commencement Date

Lease Receivable	NIIL	
Loss in Lease [P&L]	if any	
To Asset		Carrying Amt.
To Gain in Lease [P&L]		if any

(ii) At End of Each Year

→ For Unwinding Discount on Lease Receivable

Lease Receivable
    To Finance Income [P&L]

→ For Receipt of Lease Installment

Bank
    To Lease Receivable

Note :-

(i) Gross Investment in Lease [GIIL]

⇒ Total Lease Payments by Lessee + Unguaranteed Residual Value [UGRV]

(ii) Net Investment in Lease [NIIL]

⇒ P.V. of GIIL using Lessor's IRR (Implicit Interest Rate in the Lease), i.e.

P.V. of Lease Payments by Lessee + P.V. of UGRV (iii.) Unearned finance Income

→ GIIL - NIIL

(iv.) UGRV

→ Total Expected Residual Value by Lessor − GRV Amount Expected to be paid by Lessee

Example:-

A ltd. provides an Asset on finance Lease for 3 years on Annual Lease Rent of ₹ 100000 at End of Each Year. Expected GRV by Lessee is ₹ 20,000. Expected UGRV is ₹ 30,000. Discounting Rate is 10% (Lessor's IRR). Carrying Amout of Asset in A ltd.'s Books is ₹ 2,50,000. Pass Journal Entries for 1st Year.

Solution:-

Calculation of Net Investment in Lease [Lease Receivable] :-

P.V. of Lease Payments:

Year	Lease Payments	PVF @ 10%	P.V.
1	1,00,000	0.909	90,900
2	1,00,000	0.826	82,600
3	1,00,000	0.751	75,100
3	20,000 [GRV]	0.751	15,020
			2,63,620

P.V. of UGRV :-

Year	Amount	PVF @ 10%	P.V.
3	30000	0.751	22,530

∴ NIIL = 2,63,620 + 22,530 ⇒ 2,86,150 ₹

Calculation of Finance Income on Lease Receivable:

Year	Op. Bal. of L.R.	Int. @ 10%	Actual Payment	Cl. Bal. of L.R.
1	2,86,150	28,615	100000	2,14,765
2	2,14,765	21,477	1,00000	1,36,242
3	1,36,242	13,758	1,50000	−
		63,850		

Journal Entries:

→ At Commencement Date

Lease Receivable	2,86,150	
To Asset		2,50,000
To Gain in Lease [P&L]		36,150

→ At 1st Year End

Lease Receivable	28,615	
To Finance Income [P&L]		28,615
Bank	100000	
To Lease Receivable		100000

Calculation of Unearned Finance Income :

⇒ GIIL − NIIL

⇒ [(100000 × 3) + 20000 + 30000] − 286150

⇒ 350000 − 286,150

⇒ 63,850

(4) <u>Accounting of Finance Lease by Dealer Lessor</u> :-

- Do All things same as above in Finance Lease
- Dealer Lessor will also recognise following At Lease Commencement Date
  - → Sales ⇒ NIIL − P.V. of UGRV
  - → COGS ⇒ Carrying Amount of Asset − P.V. of UGRV
  - ∴ Journal Entry by Dealer Lessor on Lease Commencement Date will be as follows:

Lease Receivable	NIIL	
COGS	Carrying Amount − P.V. of UGRV	
To Asset		Carrying Amount
To Sales		NIIL − P.V. of UGRV

* In this case Gain | Loss in Lease = Sales − COGS

- Steps to be followed to solve the Practical Question in case of Dealer Lessor :-
  - Step 1 : Calculate NIIL [Lease Receivable]
  - Step 2 : Check Carrying Amount of Asset
  - Step 3 : Calculate Sales
  - Step 4 : Calculate COGS
  - Step 5 : Calculate Gain | Loss in Lease
  - Step 6 : Calculate Finance Income on Lease Receivable & its Closing Balance at Each Year End using Amortisation Table
  - Step 7 : Pass Journal Entries [if required in question]

Accounting of Lease Modification in the Books of Lessor

↓ Modification in Finance Lease
- ↓ If Modification Results in Increase
- ↓ If Modification Results in Change in classification of
- ↓ Otherwise ↓

↓ Modification in Operating Lease
- ⇓ Treat it As Termination of Old Contract & Creation of New Lease Contract

in Area & Price with SSP of such Increased Area
⇓
Treat it As Separate Lease Contract

finance Lease into Operating Lease
⇓
Derecognise Lease Receivable At its Carrying Amount & Recognise Asset given Under Lease At Carrying Amount of Lease Receivable
[i.e. Only Classification will Change]

Asset
    To Lease Receivable

Apply Modification Accounting of Financial Asset as per Ind AS 109

Some Special Cases

(1.) Separation of Lease & Non - Lease Component in a Contract :-

- Lessor is required to Separate the Consideration for Lease & Non-Lease Component in a Contract on the basis of their Standalone Selling Price
    - Apply Ind AS 116 for Accounting of Lease Component
    - Apply Ind AS 115 for Accounting of Non-Lease Component
- Lessee is also required to Separate the Consideration for Lease & Non-Lease Component in a Contract on the basis of their Standalone Selling Price
    - Apply Ind AS 116 for Accounting of Lease Component
    - Recognise Amount Paid for Non-Lease Component as Expense in P&L when incurred

Note :- Lessee has a Choice to Not Separate the Lease & Non-Lease Components in a Contract As Practical Expedient [i.e. Treat Complete Contract As Lease Component Only]

(2.) Sale & Lease Back :-

Seller - Lessee $\xrightarrow{\text{Sell the Asset to}}$ Buyer - Lessor

Buyer - Lessor $\xrightarrow{\text{Lease it Back to}}$ Seller - Lessee

Accounting for this type of transaction :

- If Control of Asset is Not Passed to Buyer-Lessor, then Accounting will be done as Financing (Loan) Arrangement as per Ind AS 109
- If Control of Asset is Passed to Buyer-Lessor, then Accounting for Sales & Lease back will be done as per Ind AS 116 as follows:

(i.) Accounting in Books of Seller - Lessee

→ Case 1 : If Selling Price of Asset = Fair Value of Asset

Seller - Lessee shall initially do the following on Commencement Date

- Recognise Cash / Bank for Sales Amount
- Derecognise the Asset sold At Carrying Amount
  ⇓
  Depreciation is not charged on this Asset in future After Sale
- Recognise Lease Liability At P.V. of Lease Payments
  ⇓
  Finance Cost is booked on it over the Lease Term to Unwind the discount
- Recognise RoU Asset [Only to the Extent of Rights Held under Leaseback]
  ⇓
  $\text{Lease Liability} \times \dfrac{\text{Carrying Amount of Asset}}{\text{Fair Value of Asset}}$
  ⇓
  Depreciation is charged on it over the Lease Term
- Difference in All these 4 items in Journal Entry will be Gain/Loss on Sales & Lease back [B/F]

Journal Entry at Commencement Date :

Bank	Amount Received	
RoU Asset	Proportionate Amt. of Lease Liability	
Loss on Sale & Leaseback (if any)	B/F	
To Asset		Carrying Amount
To Lease Liability		P.V. of Lease Payments
To Gain on Sale & Leaseback (if any)		B/F

→ Case 2 : If Selling Price of Asset > Fair Value of Asset

Seller - Lessee shall initially do the following on Commencement Date

- Recognise Cash/Bank for Sales Amount
- Derecognise the Asset sold At Carrying Amount
  ⇓
  Depreciation is not charged on this Asset in future After Sale
- Recognise Financial Liability [Loan] At Sales Value − Fair Value
  ⇓
  Finance Cost is booked on it over the Lease Term to Unwind the discount
- Recognise Lease Liability At P.V. of Annual Payments − Financial Liability
  ⇓
  Finance Cost is booked on it over the Lease Term to Unwind the discount
- Recognise RoU Asset [Only to the Extent of Rights Held under Leaseback]
  ⇓
  $\text{Lease Liability} \times \dfrac{\text{Carrying Amount of Asset}}{\text{Fair Value of Asset}}$
  ⇓
  Depreciation is charged on it over the Lease Term
- Difference in All these 5 items in Journal Entry will be Gain/Loss on Sales & Lease back [B/F]

Note :- There is also a need to appropriate the Annual Payments made by Lessee in following 2 parts :

- Payment for Lease Liability
  ⇓
  $\text{Annual Payment} \times \dfrac{\text{Lease Liability}}{\text{P.V. of Annual Payments}}$
- Payment for Financial (Loan) Liability
  ⇓
  $\text{Annual Payment} \times \dfrac{\text{Financial Liability}}{\text{P.V. of Annual Payments}}$

* It will be used respectively in Amortisation Table of Lease & Financial Liability

Journal Entry at Commencement Date :

Bank	Amount Received
RoU Asset	Proportionate Amt. of Lease Liability
Loss on Sale & Leaseback (if any)	B/f
To Asset	Carrying Amount
To Lease Liability	P.V. of Annual Payments − Financial Liability
To Financial Liability	Sales Value − Fair Value
To Gain on Sale & Leaseback (if any)	B/f

→ Case 3: If Selling Price of Asset < Fair Value of Asset

Seller - Lessee shall initially do the following on Commencement Date

- Recognise Cash / Bank for Sales Amount
- Derecognise the Asset sold At Carrying Amount
  ⇓
  Depreciation is not charged on this Asset in future After Sale
- Recognise Lease Liability At P.V. of Lease Payments
  ⇓
  Finance Cost is booked on it over the Lease Term to Unwind the discount
- Recognise RoU Asset [Only to the Extent of Rights Held under Leaseback]
  ⇓
  $\left[\text{Lease Liability} + \left(\text{Fair Value} - \text{Sales Value}\right)\right] \times \dfrac{\text{Carrying Amount of Asset}}{\text{Fair Value of Asset}}$
  ⇓
  Depreciation is charged on it over the Lease Term
- Difference in All these 4 items in Journal Entry will be Gain/Loss on Sales & Lease back [B/F]

Journal Entry at Commencement Date :

Bank	Amount Received
RoU Asset	Proportionate Amt. of Lease Liability
Loss on Sale & Leaseback (if any)	B/f
To Asset	Carrying Amount
To Lease Liability	P.V. of Lease Payments
To Gain on Sale & Leaseback (if any)	B/f

(ii) Accounting in Books of Buyer - Lessor

Buyer - Lessor shall initially do the following on Commencement Date

- Recognise Asset Received At its Fair Value
  ⇓
  Depreciation is charged on it by Buyer - Lessor over its Useful Life
- Recognise Amount Paid through Cash / Bank to Purchase the Asset
- If Sales Value of Asset > Fair Value of Asset
  ⇓
  then Also recognise Financial Asset At Sales Value − Fair Value
- If Sales Value of Asset < Fair Value of Asset
- Do Accounting for Asset Leased back to Seller as Finance Lease or Operating Lease as discussed previously in this Ind AS

⇓ Finance Income is booked on it over the Lease Term to Unwind the discount

⇓ then Also recognise Unearned Lease Income

(3) Sub-Lease :-

Normal Lessor A/cing [F.L./O.L.] ← ORIGINAL LESSOR

↓

ORIGINAL LESSEE / INTERMEDIATE LESSOR ⇒ Head Lease

→ RoU Asset A/cing for Head Lease

→ Normal Lessor A/cing [F.L./O.L.] for Sub-Lease

Sub-Lease ⇐

↓

SUB-LESSEE → RoU Asset A/cing

- Intermediate Lessor should decide whether Sub-Lease done by him is Operating Lease or Finance Lease by Comparing Sub-Lease Term with Remaing Lease Term of RoU Asset in Head Lease

Example :- A ltd. takes an Asset on Lease for 10 years. After 6 years, A ltd. gave this Asset on Sub-lease for 3 years.

Now, Remaining Lease Term in Head Lease ⇒ 10 − 6 = 4 years

Sub-Lease Term ⇒ 3 years

∴ Sub-Lease is for Major Part of Remaining Lease Term $\left[\frac{3}{4} \times 100\right]$ i.e. 75%

Hence, Sub-Lease by A ltd. is Finance Lease

(4.) Optional Exemptions to Lessee :-

- Ind AS 116 gives Lessee an option to Not Apply this Ind AS on
  - → Short Term Leases (≤ 12 Months)
  - → Leases of Low Value Assets
- If Lessee elects for this Exemption, then he shall recognise Lease Payments as Expense in P&L on SLM Basis

Lease Payments [P&L]

To Bank

Introduction

Following Topics are covered in this Chapter :-

- Characteristics of Good Financial Statements
- Best Practices to be followed in preparation of Financial Statements
- Questions based on various Ind AS
- Questions based on correction of mistakes in Financial Statements [As per Division II of Schedule III]

Characteristics of Good Financial Statements

- True & Fair View of the affairs of enterprise
- Relevance
- Understandability
- Consistency
- Regulatory Compliance
- Universality

Best Practices to be followed for Preparation of Financial Statements

- Compliance
- Complete
- Simple & Specific
- Transparency
- Materiality
- Integration of Notes
- Disclosure of Material Accounting Policies, Key Estimates & Judgements
- Integrated Approach

Introduction

A Chartered Accountant has a Duty to act in public interest [i.e. for stakeholders (shareholders, employees & any other 3rd Party) & Professional Body (ICAI)] not only to the employing organisation.

Hence, he has to comply fundamental principles of ethics set out by Code of Ethics of ICAI to achieve objectives of accountancy profession.

↓

While Complying with fundamental principles of ethics, a CA has to identify & address the threats to compliance.

↓

Otherwise, CA is subject to Misconduct under various clauses of Chartered Accountants Act, 1949.

Fundamental Principles of Ethics [Ethical Principles]

A CA has to comply with following 5 Fundamental Principles of Ethics :-

(i) Integrity : Straight forward & honest

(ii) Objectivity : Not allow bias, conflict of interest or undue influence of others to override professional judgements.

(iii) Professional Competence & Due Care : Maintain Professional knowledge & act diligently

(iv) Confidentiality : Maintain confidentiality of information

(v) Professional Behaviour : Comply with Laws & Regulations [i.e. Ind AS]

Threats to Compliance with Fundamental Principles of Ethics [Ethical Conflict or Dilemma]

(i) Intimidation Threats

Eg : Threat of dismissal by employing organisation, Pressure on CA of his personal circumstances that he cannot afford to lose his job, etc.

(ii) Advocacy Threats

Eg : Pressure to obtain finance in Company, etc.

Addressing the Threats to Compliance with Fundamental Principles of Ethics [Ethical Responsibilities or Duties]

(1) <u>If CA is an Advisor or Consultant of the Organisation [CA in Practice]</u> :-

- Inform / Guide those charged with governance [Directors or Management] about the correct treatment & get the financial statements rectified, or
- Report Non Compliance to appropriate authorities, or
- Withdraw from the engagement

(2) <u>If CA is an Employee of the Organisation [CA in Service]</u> :-

- Remind those charged with governance [Directors or Management] the Ethical Responsibilities & communicate them the necessary adjustments to prevent the incorrect treatment in financial statements, or
- Bring this fact to attention of appropriate Internal Authority or Auditors, or
- Resign from the employing organisation

Professional Misconduct under Chartered Accountants Act, 1949

(1) If CA in practice accepts the incorrect treatment [i.e. fails to comply his professional duties], then he will subject to professional misconduct under clauses 5, 6, 7 & 8 of Part I of Second Schedule of the Chartered <u>Accountants Act, 1949 as follows</u> :-

- Clause 5 states that a Chartered Accountant is guilty of professional misconduct when he fails to disclose a material fact known to him which is not disclosed in financial statements.
- Clause 6 states that a Chartered Accountant is guilty of professional misconduct when he fails to report a material misstatement known to him to appear in financial statements.
- Clause 7 states that a Chartered Accountant is guilty of professional misconduct when he does not exercise due diligence or is grossly negligent in conduct of his professional duties.
- Clause 8 states that a Chartered Accountant is guilty of professional misconduct when he fails to obtain sufficient information which is necessary for expression of an opinion.

(2) If CA in service accepts the incorrect treatment [i.e. fails to comply his professional duties], then he will subject to professional misconduct under clause 1 of Part II of Second Schedule of the Chartered Accountants Act, <u>1949 as follows</u> :-

Clause 1 states that a member of Institue, whether in practice or not, shall be deemed to be guilty of professional misconduct, if he contravenes any of the provisions of this Act or the regulations made thereunder or any guidelines issued by the council.

As per the guidelines issued by the council, a member of the Institute who is an employee shall exercise due diligence & shall not be grossly negligent in the conduct of his duties.

Answer framing for a Question

- Accounting Implications [i.e. Relevant Ind AS & Correct Treatment]
- Ethical Implications [i.e. Ethical Principles, Ethical Conflict, Ethical Responsibilities & Professional Misconduct]

Introduction

This Chapter discuss the uses & impact of technology on accounting profession as follows :-

- Current Technology in Accounting
  - Automation Process
  - Cloud Computing
  - Enterprise Resource Planning
- Cyber Security in Accounting
- Future of Technology in Accounting
- Ind AS & Information Technology

Automation Process

(1) Meaning :-

It is the use of software & other tools to automate manual processes, making them faster & accurate.

(2) Benefits :- SAFE SI

- Streamlining Data Entry
- Accelerating Data Processing
- Facilitating Compliance
- Enhancing Accuracy
- Saving Time & Money
- Improving Decision Making

(3) Challenges / Drawbacks :- PNR

- Potential Loss of Jobs
- Need for Ongoing Training and Education
- Risk of Data Breaches & Cyber Attacks

(4) Robotic Process Automation [RPA] :-

- It is an emerging technology that revolutionizes financial reporting process by utilizing software robots (bots) to automate manual & repititive tasks.
- Bots can extract data, perform calculations & generate reports by mimicking human intervention with digital systems.

[Example : Using RPA Bots to Prepare Consolidated financial Statements]

Cloud Computing

(1) Meaning :-

It refers to delivery of computing services over the Internet [i.e. Remote access to data & system].

(2) Applications / Cases of Cloud Computing :- CS IPCC Big

- Cloud Storage
- Software as a Service [SaaS]
- Infrastructure as a Service [IaaS]
- Platform as a Service [PaaS]
- Cloud Based Communication & Collaboration
- Cloud Based E-commerce
- Big Data Analytics

(3) Benefits :- ESIIIR

- Enhanced Security
- Streamlined Collaboration
- Improved Accessibility
- Increased Scalability
- Improved Reporting & Analytics
- Reduced Costs

(4) Challenges / Drawbacks :-

- Prone to hackers who could steal data or compromise the integrity of processed data
- Strong net connectivity is must for cloud computing

Enterprise Resource Planning [ERP]

(1) Meaning :-

- It is a software that organisations use for managing day to day business activities like accounting & supply chain operations.
- It connects multiple business processes & eliminates data duplication.
- It has single defined data structure with common database (schema).

(2) Benefits :- BC LIER

- Better Efficiency
- Consistent Infrastructure
- Less Operational Costs
- Improved Business Insights
- Enhanced Collaboration of Users
- Reduction in Risk

(3) How does an ERP System work? :-

- It uses a defined standard data structure where information of department is immediately available to authorised users.
- Realtime data is woven into business processes across departments
- It is of most value when company has modules for each major business function.

(4) Illustrative Steps for Integrating Internal Control Over Financial Reporting with ERP

OR

Illustrative Steps for Financial Closing & Reporting with ERP :-

- Verify that process includes identification of financial reporting requirements.
- Review documented process to ensure it aligns with financial reporting policies.
- Use Change Management functionality to track & validate changes.
- Verify that changes are authorised by designated individuals.
- Review Change requests to ensure proper authorization.
- Validate that Roles & Responsibilities in the process are clearly defined.
- Assess qualifications of individuals assigned to financial reporting roles.
- Validate that individuals responsible for financial reporting have appropriate knowledge.

(5) ERP System for Inventory Management :-

- Steps to be followed to enable ERP : MID Track DIPU
  - → Maintain Bill of Materials Management
  - → Implement Purchase Order Controls
  - → Define appropriate Costing Methods
  - → Track Labour Costs
  - → Define Overhead Absorption Rate
  - → Integrate ERP System with General Ledger Modules
  - → Perform Periodic Reconciliations
  - → Utilise the Reporting Capabilities

- Integration of Internal Control Over Financial Reporting with respect to Inventory in ERP System : Enforce IIIIP
  - Enforce Segregation of Duties
  - Implementing Access Controls
  - Include Workflow Approval Processes
  - Integrate Bar code Scanners or RFID Readers
  - Integrate Technology driven data analytics tools
  - Provide Management Dashboards or Customised Reports

Cyber Security in Accounting

(1) Cyber Security Threats :- D PM SIR

- Denial of Service (DOS) Attacks
- Phishing Attacks
- Malware Attacks
- Supply Chain Attacks
- Insider Threats
- Ransomware Attacks

(2) Measures to Mitigate Cyber Security Risks :- PAINEED

- Password Management
- Access Control
- Incident Response Planning
- Network Security
- Employee Training
- Encryption
- Data Backup

Future of Technology in Accounting

(1) Blockchain :-

- Meaning :
  - → It is a decentralized & transparent ledger that enables secure transactions.
  - → It offers a distributed network where information is shared & verified by multiple participants.

- Impacts of Blockchain on Financial Reporting :- CS RISEE
  - Cost Reduction
  - Streamlined Audit Processes
  - Real Time Financial Reporting
  - Improved Data Integrity
  - Simplified Reconciliation
  - Enhanced Audit Trail
  - Enhanced Transparency

(2) Artificial Intelligence [AI] :-

- Meaning :
  - → It refers to simulation of human intelligence in machines enabling them to perform tasks that would require human intervention.
  - → It can be used to analyze data & make predictions about future trends.
  - → AI & Machine Learning [ML] are technologies that enable computers to learn & perform tasks without being programmed to do so.

- Benefits / Advantages : AFFAT
  - Automated Data Entry
  - Fraud Detection
  - Financial Forecasting
  - Accounting Automation
  - Tax Compliance

- Challenges / Risks :
  - Data Privacy
  - Security Concerns
  - Technical Complexity
  - Need to Train Employees

Ind AS & Information Technology

(1) Role of Technology in Ind AS Implementation & Validation :-

- Ind AS is a principle based framework. Hence, Technology can automate the validation process for Ind AS implementation by configuration at the account level [Rule Based Validations].

- If Account level configuration is not done, then Use 'Microsoft Excel' [External Source of Technology] to perform such validations.

(2) Steps to automate the Ind AS Implementation process using technology :-

- Integrate the Accounting Software with Other Operational Systems.
- Extract relevant data from accounting package / contract documents.
- Use Custom queries or predefined templates to extract information.
- Clean the data by removing unnecessary information.
- Analyze the clauses in contract.
- Define the criteria or rules for categorizing contracts as per relevant Ind AS.
- Codify each clause by assigning appropriate parameters / tags / attributes / labels / values based on defined criteria.
- Assign Scores / Weights / Boolean Values ["0" or "1"] to parameters.
- Establish conditions using Excel formulas (logical functions)

  OR

  Develop Automated Algorithms / Scripts / Rules to evaluate data.
- Based on the analysis & findings [i.e. Utilize the Scores / Weights assigned to parameters], determine or evaluate the result.
- Document the rationale & result of the analysis.
- Advanced Technologies that may be adopted are :
  → Use tools such as Business Intelligence Software.
  → Utilize OCR technology to extract information automatically.
  → Apply Machine Learning & NLP Techniques to extract data automatically.
  → Utilize Workflow Automation tools to streamline the process.

Differences between AS and Ind AS

Major differences in accounting treatment between AS and Ind AS

Ind AS Vs AS	Difference
Ind AS 1: Presentation of Financial Statements Vs AS 1: Disclosure of Accounting Policies	Major difference ▪ Scope of Ind AS 1 is much wider.
Ind AS 2: Inventories Vs AS 2: Valuation of Inventories	No major difference
Ind AS 7: Statement of Cash Flows Vs AS 3: Cash Flow Statements	No major difference
Ind AS 8: Accounting Policies, Changes in Accounting Estimates and Errors Vs AS 5: Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies	Major difference ▪ AS 5 provides different treatment for changes in accounting policies and errors.
Ind AS 10: Events After the Reporting Period Vs AS 4: Contingencies and Events Occurring After the Balance Sheet Date	No major difference
Ind AS 12: Income Taxes Vs AS 22: Accounting for Taxes on Income	Major Difference ▪ AS 22 is based on income statement (P&L) approach [i.e., it requires recognition of deferred tax on timing differences between taxable income and accounting income]. ▪ AS 22 requires virtual certainty of sufficient future taxable income for recognising DTA.
Ind AS 16: Property, Plant and Equipment Vs AS 10: Property, Plant and Equipment	No major difference
Ind AS 19: Employee Benefits Vs AS 15: Employee Benefits	No major difference

Ind AS 20: Accounting for Government Grants and Disclosure of Government Assistance Vs AS 12: Accounting for Government Grants	Major difference ▪ AS 12 provides different treatment for grant in nature of promoter contribution & monetary grants related to non-depreciable assets.
Ind AS 21: The Effects of Changes in Foreign Exchange Rates Vs AS 11: The Effects of Changes in Foreign Exchange Rates	Major difference ▪ AS 11 provides different treatment for exchange differences arising on translation of long-term monetary items and approach for translation of foreign operations.
Ind AS 23: Borrowing Costs Vs AS 16: Borrowing Costs	No major difference
Ind AS 24: Related Party Disclosures Vs AS 18: Related Party Disclosures	No major difference
Ind AS 33: Earnings Per Share Vs AS 20: Earnings Per Share	No major difference
Ind AS 34: Interim Financial Reporting Vs AS 25: Interim Financial Reporting	No major difference
Ind AS 36: Impairment of Assets Vs AS 28: Impairment of Assets	No major difference ▪ AS 28 provides bottom-up and top-down approach for allocation of goodwill.
Ind AS 37: Provisions, Contingent Liabilities and Contingent Assets Vs AS 29: Provisions, Contingent Liabilities and Contingent Assets	No major difference ▪ AS 29 prohibits discounting the amounts of provisions and disclosure of contingent assets in financial statements.
Ind AS 38: Intangible Assets Vs AS 26: Intangible Assets	No major difference
Ind AS 40: Investment Property	No respective AS
Ind AS 41: Agriculture	No respective AS
Ind AS 101: First-Time Adoption of Ind AS	No respective AS
Ind AS 102: Share Based Payment	No respective AS

Ind AS 103: Business Combinations Vs AS 14: Accounting for Amalgamations	Major difference ▪ Scope of Ind AS 103 is much wider.
Ind AS 105: Non-current Assets Held for Sale and Discontinued Operations Vs AS 24: Discontinuing Operations	Major difference ▪ Scope of Ind AS 105 is much wider.
Ind AS 108: Operating Segments Vs AS 17: Segment Reporting	No major difference
Ind AS 32, 107, 109: Financial Instruments	No respective AS
Ind AS 27, 28, 110, 111, 112: CFS Vs AS 21, 23, 27: CFS	Major difference ▪ Scope of Ind AS is much wider.
Ind AS 113: Fair Value Measurement	No respective AS
Ind AS 115: Revenue from Contracts with Customers Vs AS 7: Construction Contract AS 9: Revenue Recognition	Major Difference ▪ Scope of Ind AS 115 is much wider. ▪ AS 7 & 9 do not require separation of financing component, service warranty component, etc. from transaction price [i.e., complete amount will be considered as Sales]. ▪ AS 7 & 9 require contract acquisition costs (example: sales commission) to be expensed off in P&L immediately.
Ind AS 116: Leases Vs AS 19: Leases	Major Difference ▪ Scope of Ind AS 116 is much wider. ▪ AS 19 requires lessee to classify lease as operating or finance lease. ▪ AS 19 does not require separation of lease and non-lease components in a contract [i.e., entire contract is accounted as a lease contract]. ▪ AS 19 provides different treatment for accounting of sale and leaseback transaction [i.e., seller-lessee has to amortise difference between the sale value and carrying amount over the lease term].

1. This Schedule sets out the minimum requirements for disclosure on face of Financial Statements, i.e. Balance Sheet, Statement of Changes in Equity for the period, the Statement of profit and Loss for the period and Notes. Cash flow statement shall be prepared in accordance with Ind AS 7.
2. Depending upon the Total Income of the company, the figures appearing in the Financial Statements shall be rounded off as below:

Total Income	Rounding off
(i) Less than ₹ 100 crore	To nearest hundreds, thousands, lakhs or millions
(ii) ₹ 100 crore or more	To nearest, lakhs, millions or crores

Once a unit of measurement is used, it should be used uniformly in Financial Statements.

PART I – BALANCE SHEET

Name of the Company…………..

Balance Sheet as at………………

(₹ in …..)

	Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of previous reporting period
	1	2	3	4
	ASSETS			
(1)	**Non-current Assets**			
	(a) Property, Plant and Equipment			
	(b) Capital work-in-progress			
	(c) Investment Property			
	(d) Goodwill			
	(e) Other Intangible assets			
	(f) Intangible assets under development			
	(g) Biological Assets other than bearer plants			
	(h) Financial Assets			
	(i) Investments			
	(ii) Trade receivables			
	(iii) Loans			
	(iv) Others (to be specified)			
	(i) Deferred tax assets (Net)			
	(j) Other non-current assets			
(2)	**Current Assets**			
	(a) Inventories			
	(b) Financial Assets			
	(i) Investments			
	(ii) Trade receivables			
	(iii) Cash and cash equivalents			
	(iv) Bank balances other than (iii) above			
	(v) Loans			
	(vi) Others (to be specified)			
	(c) Current Tax Assets (Net)			
	(d) Other current assets			

	Total Assets			
	EQUITY AND LIABILITIES			
	EQUITY (a) Equity Share capital (b) Other Equity			
(1)	**LIABILITIES** **Non-current liabilities** (a) Financial Liabilities (i) Borrowings (ii) Lease Liabilities (iii) Trade Payables: (A) total outstanding dues of micro enterprises and small enterprises; and (B) total outstanding dues of creditors other than micro enterprises and small enterprises (iii) Other financial liabilities (to be specified) (b) Provisions (c) Deferred tax liabilities (Net) (d) Other non-current liabilities			
(2)	**Current liabilities** (a) Financial Liabilities (i) Borrowings (ii) Lease Liabilities (iii) Trade Payables: (A) total outstanding dues of micro enterprises and small enterprises; and (B) total outstanding dues of creditors other than micro enterprises and small enterprises (iv) Other financial liabilities (to be specified) (b) Other current liabilities (c) Provisions (d) Current tax liabilities (Net)			
	Total Equity and Liabilities			

see accompanying notes to the financial statements

STATEMENT OF CHANGES IN EQUITY

Name of the Company.............

A. Equity Share Capital

(1) Current reporting period

Balance at the beginning of the current reporting period	Changes in Equity Share Capital due to prior period errors	Restated balance at the beginning of the current reporting period	Changes in equity share capital during the current year	Balance at the end of the current reporting period

(2) Previous reporting period

Balance at the beginning of the previous reporting period	Changes in Equity Share Capital due to prior period errors	Restated balance at the beginning of the previous reporting period	Changes in equity share capital during the previous year	Balance at the end of the previous reporting period

B. Other Equity

(1) Current reporting period

	Share application on money pending allotment	Equity component of compound financial instruments	Reserve and Surplus				Items of Other Comprehensive Income (OCI)						Money received against share warrants	Total
			Capital Reserve	Securities Premium	Other Reserves (Specify nature)	Retained Earnings	Debt Instrument through OCI	Equity Instrument through OCI	Effective portion of Cash Flow Hedges	Revaluation Surplus	Exchange difference on translating the financial statements of a foreign operation	Other items of OCI (Specify nature)		
Balance at beginning of the current reporting period														
Changes in accounting policy or prior period errors														
Restated balance at beginning of the current reporting period														
Total comprehensive Income for the current year														
Dividends														
Transfer to retained earnings														

Any other change (to be specified)														
Balance at end of the current reporting period														

(2) Previous reporting period

	Share application on money pending allotment	Equity component of compound financial instruments	Reserve and Surplus				Items of Other Comprehensive Income (OCI)						Money received against share warrants	Total
			Capital Reserve	Securities Premium	Other Reserves (Specify nature)	Retained Earnings	Debt Instrument through OCI	Equity Instrument through OCI	Effective portion of Cash Flow Hedges	Revaluation Surplus	Exchange difference on translating the financial statements of a foreign operation	Other items of OCI (Specify nature)		
Balance at beginning of the previous reporting period														
Changes in accounting policy or prior period errors														
Restated balance at beginning of the previous reporting period														
Total comprehensive Income for the previous year														
Dividends														
Transfer to retained earnings														
Any other change (to be specified)														
Balance at end of the previous reporting period														

General Instructions for Preparation of Balance Sheet

- Classify Assets and Liabilities as Current or Non-current as per Ind AS 1
- A company shall disclose the following in the Notes:

A. Non-Current Assets

I. Property, Plant and Equipment

(i) Classification shall be given as:

(a) Land

(b) Buildings

(c) Plant and Equipment

(d) Furniture and Fixtures

(e) Vehicles

(f) Office equipment

(g) Bearer Plants

(h) Others (specify nature)

(ii) Assets under lease shall be separately specified under each class of assets.

(iii) Reconciliation of gross and net carrying amounts of each class of assets at beginning and end of reporting period showing additions, disposals, revaluation, depreciation and impairment losses shall be disclosed separately.

II. Investment Property

Reconciliation of gross and net carrying amounts of each class of assets at beginning and end of reporting period showing additions, disposals, depreciation and impairment losses shall be disclosed separately.

III. Goodwill

Reconciliation of gross and net carrying amount of goodwill at beginning and end of reporting period showing additions, disposals depreciation and impairment losses shall be disclosed.

IV. Other Intangible assets

(i) Classification shall be given as:

(a) Brands or trademarks

(b) Computer software

(c) Mastheads and publishing titles

(d) Mining rights

(e) Copyright, patents, other intellectual property rights

(f) Recipes, formulae

(g) Licenses and franchises

(h) Others (specify nature)

(ii) Reconciliation of gross and net carrying amounts of each class of assets at beginning and end of reporting period showing additions, disposals, amortization and impairment losses shall be disclosed separately.

V. Biological Assets other than bearer plants

Reconciliation of carrying amounts of each class of assets at beginning and end of reporting period showing additions, disposals and other adjustments shall be disclosed separately.

VI. Investment

(i) Investments shall be classified as:

(a) Investments in Equity Instruments;

(b) Investments in Preference Shares;

(c) Investments in Government or trust securities;

(d) Investments in debentures or bonds;

(e) Investments in Mutual Funds;

(f) Investments in partnership firms; or

(g) Other investments (specify nature)

Under each classification, give details of names of bodies corporate that are-

(i) subsidiaries,

(ii) associates,

(iii) joint ventures

in whom investments have been made and nature and extent of investment so made in each such body corporate.

(ii) The following shall also be disclosed:

(a) Aggregate amount of quoted investment and market value thereof:

(b) Aggregate amount of unquoted investment: and

(c) Aggregate amount of impairment in value of investment.

VII. Trade Receivables

(i) Trade receivables shall be sub-classified as;

(a) Trade Receivables considered good - Secured;

(b) Trade Receivables considered good - Unsecured;

(ii) Allowance for bad and doubtful debts shall be disclosed separately.

(iii) Debts due by directors or other officers of company should be separately stated.

(iv) For trade receivables outstanding, ageing schedule shall be given as Outstanding for following periods from due date of payment, i.e. Less than 6 months, 6 months to 1 year, 1 to 2 years, 2 to 3 years and More than 3 years.

VIII.Loans

(i) Loans shall be classified as-

(a) Loans to related parties (giving details thereof); and

(b) Other loans (specify nature).

(ii) Loans Receivables shall be sub-classified as:

(a) Secured;

(b) Unsecured;

(c) Doubtful.

(iii) Allowance for bad and doubtful debts shall be disclosed separately.

(iv) Loans due by directors or other officers of company should be separately stated.

IX. Other financial assets

(i) Security Deposits

(ii) Bank deposits with more than 12 months maturity

(iii) Others (to be specified)

X. Other non-current asset:

Other non-current assets shall be classified as

(i) Capital Advances; and

(ii) Advances other than capital advances;

(1) Advances other than capital advances shall be classified as:

(a) Security Deposits;

(b) Advances to related parties (giving details thereof); and

(c) Other advances (specify nature).

(2) Advances to directors or other officers of company should be separately stated.

In case advances are of nature of financial asset as per relevant Ind AS, these are to be disclosed under other financial assets separately.

(iii) Others (specify nature).

B. Current Assets

I. Inventories

(i) Inventories shall be classified as-

(a) Raw materials;

(b) Work in-progress;

(c) Finished goods;

(d) Stock-in-trade (in respect of goods acquired for trading);

(e) stores and spares;

(f) Loose tools; and

(g) Others (specify nature).

(ii) Goods-in-transit shall be disclosed under relevant sub-head of inventories.

(iii) Mode of valuation shall be stated.

II. Investment

(i) Investments shall be classified as:

(a) Investments in Equity Instruments;

(b) Investments in Preference Shares;

(c) Investments in Government or trust securities;

(d) Investments in debentures or bonds;

(e) Investments in Mutual Funds;

(f) Investments in partnership firms; or

(g) Other investments (specify nature)

Under each classification, give details of names of bodies corporate that are-

(i) subsidiaries,

(ii) associates,

(iii) joint ventures, or

in whom investments have been made and nature and extent of investment so made in each such body corporate.

(ii) The following shall also be disclosed:

(d) Aggregate amount of quoted investment and market value thereof:

(e) Aggregate amount of unquoted investment: and

(f) Aggregate amount of impairment in value of investment.

III. Trade Receivables

(i) Trade receivables shall be sub-classified as;

(a) Trade Receivables considered good - Secured;

(b) Trade Receivables considered good - Unsecured;

(ii) Allowance for bad and doubtful debts shall be disclosed separately.

(iii) Debts due by directors or other officers of company should be separately stated.

(iv) For trade receivables outstanding, ageing schedule shall be given as Outstanding for following periods from due date of payment, i.e. Less than 6 months, 6 months to 1 year, 1 to 2 years, 2 to 3 years and More than 3 years.

IV. Cash and cash equivalents

Cash and cash equivalents shall be classified as-

(a) Balances with Banks (of the nature of cash and cash equivalents);

(b) Cheques, drafts on hand;

(c) Cash on hand; and

(d) Others (specify nature).

V. Loans

(i) Loans shall be classified as-

(a) Loans to related parties (giving details thereof); and

(b) Other loans (specify nature).

(ii) Loans Receivables shall be sub-classified as:

(a) Loans Receivables considered good - Secured;

(b) Loans Receivables considered good - Unsecured;

(c) Doubtful.

(iii) Allowance for bad and doubtful debts shall be disclosed separately.

(iv) Loans due by directors or other officers of company should be separately stated.

VI. Other current assets (specify nature)

This is an all-inclusive heading, which incorporates current assets that do not fit into any other asset categories.

Other current assets shall be classified as-

(i) Capital Advances; and

(ii) Advances other than capital advances;

(1) Advances other than capital advances shall be classified as:

(a) Security Deposits;

(b) Advances to related parties (giving details thereof; and

(c) Other advances (specify nature).

(2) Advances to directors or other officers of company should be separately stated.

(iii) Others (specify nature).

C. Equity

I. Equity Share Capital

For each class of equity share capital:

(a) number and amount of shares authorised;

(b) number of shares issued, subscribed and fully paid, and subscribed but not fully paid;

(c) par value per Share;

(d) reconciliation of number of shares outstanding at beginning and at end of period;

II. Other Equity

(i) Other Reserves shall be classified in the notes as-

(a) Capital Redemption Reserve;

(b) Debenture Redemption Reserve;

(c) Share Options Outstanding Account; and

(d) Others (specify nature and purpose of each reserve and amount in respect thereof);

(ii) Retained Earnings represents surplus i.e. balance of relevant column in Statement of Changes in Equity;

(iii) Debit balance of Statement of Profit and Loss shall be shown as negative figure under the head 'retained earnings'. Similarly, the balance of 'Other Equity', after adjusting negative balance of retained earnings shall be shown under the head 'Other Equity' even if resulting figure is in negative; and

D. Non-Current Liabilities

I. Borrowings

(i) Borrowings shall be classified as-

(a) Bonds or debentures

(b) Term loans

(I) from banks

(II) from other Parties

(c) Deferred payment liabilities

(d) Deposits

(e) Loans from related parties

(f) Liability component of compound financial instruments

(g) Other loans (specify nature);

(ii) Borrowings shall further be sub-classified as secured and unsecured.

II. Provisions

The amounts shall be classified as-

(a) Provision for employee benefits; and

(b) Others (specify nature).

III. Other non-current liabilities

(a) Advances; and

(b) Others (specify nature).

E. Current Liabilities

I. Borrowings

(i) Borrowings shall be classified as-

(a) Loans repayable on demand

(I) from banks

(II) from other parties

(b) Loans from related parties

(c) Deposits

(d) Other loans (specify nature);

(ii) Borrowings shall further be sub-classified as secured and unsecured.

(iii) Current maturities of long-term borrowings shall be disclosed separately.

II. Other Financial Liabilities

Other Financial liabilities shall be classified as-

(a) Interest accrued;

(b) Unpaid dividends;

(c) Application money received for allotment of securities to the extent refundable and interest accrued thereon;

(d) Unpaid matured deposits and interest accrued thereon;

(e) Unpaid matured debentures and interest accrued thereon; and

(f) Others (specify nature).

III. Other current liabilities

The amounts shall be classified as-

(a) revenue received in advance;

(b) other advances (specify nature); and

(c) others (specify nature);

IV. Provisions

The amounts shall be classified as-

(a) provision for employee benefits; and

(b) others (specify nature)

F. Trade Payables

(1) Following details relating to micro, small and medium enterprises shall be disclosed in notes:

(a) principal amount and interest due thereon (to be shown separately) remaining unpaid to any supplier at end of each accounting year;

(b) amount of interest paid by buyer in terms of section 16 of Micro, Small and Medium Enterprises Development Act, 2006 during each accounting year;

(c) amount of interest due and payable for period of delay in making payment (which has been paid beyond the appointed day during the year).

(2) For trade payables due for payment, ageing schedule shall be given as Outstanding for following periods from due date of payment, i.e. Less than 1 year, 1 to 2 years, 2 to 3 years and More than 3 years.

G. Contingent Liabilities and Commitments (to the extent not provided for)

(i) Contingent Liabilities shall be classified as-

(a) claims against the company not acknowledged as debt;

(b) guarantees excluding financial guarantees; and

(c) other money for which company is contingently liable.

(ii) Commitments shall be classified as-

(a) estimated amount of contracts remaining to be executed and not provided for;

(b) uncalled liability on shares and other investments partly paid; and

(c) other commitments (specify nature).

H. Proposed dividend amount per share to be distributed to equity and preference shareholders for the period shall be disclosed separately.

I. When company applies accounting policy retrospectively or makes restatement of items in financial statements or when it reclassifies items in its financial statements, the company shall attach to the Balance Sheet, a "Balance Sheet" as at the beginning of earliest comparative period presented.

J. Following Ratios to be disclosed:

(a) Current Ratio,

(b) Debt-Equity Ratio,

(c) Debt Service Coverage Ratio,

(d) Return on Equity Ratio,

(e) Inventory turnover ratio,

(f) Trade Receivables turnover ratio,

(g) Trade payables turnover ratio,

(h) Net capital turnover ratio,

(i) Net profit ratio,

(j) Return on Capital employed,

(k) Return on investment.

PART II - STATEMENT OF PROFIT AND LOSS

Name of the Company……………………

Statement of Profit and Loss for the period ended……………

	Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of previous reporting period
I II	Revenue from operations Other Income			
III	Total Income (l + Il)			
IV	EXPENSES Cost of materials consumed Purchases of Stock-in-Trade Changes in inventories of finished goods, Stock-in-Trade and work-in-progress Employee benefits expense Finance costs Depreciation and amortization expenses Other expenses			
	Total expenses (IV)			
V	Profit/(loss) before exceptional items and tax (III – IV)			
VI	Exceptional Items			
VII	Profit/(loss) before tax (V – VI)			
VIII	Tax expense: (1) Current tax (2) Deferred tax			
IX	Profit/(Loss) for the period from continuing operations (VII – VIII)			
X	Profit/(loss) from discontinued operations			
XI	Tax expenses of discontinued operations			
XII	Profit/(loss) from discontinued operations (after tax) (X – XI)			
XIII	Profit/(loss) for the period (IX + XII)			
XIV	Other Comprehensive Income A. (i) Items that will not be reclassified to profit or loss (ii) Income tax relating to items that will not be			

	reclassified to profit or loss B. (i) Items that will be reclassified to profit or loss (ii) Income tax relating to items that will be reclassified to profit or loss			
XV	Total Comprehensive Income for the period (XIII + XIV) [Comprising Profit/(Loss) and Other Comprehensive Income for the period]			
XVI	Earnings per equity share (for continuing operation): (1) Basic (2) Diluted			
XVII	Earnings per equity share (for discontinued operation): (1) Basic (2) Diluted			
XVIII	Earning per equity share (for discontinued & continuing operation): (1) Basic (2) Diluted			

General Instructions for Preparation of Statement of Profit and Loss

1. Revenue from operations shall disclose separately in the notes
   - (a) sale of products;
   - (b) sale of services; and
   - (c) other operating revenues.
2. Finance Costs: Finance costs shall be classified as-
   - (a) interest;
   - (b) dividend on redeemable preference shares;
   - (c) exchange differences regarded as an adjustment to borrowing costs; and
   - (d) other borrowing costs (specify nature).
3. Other income: other income shall be classified as-
   - (a) interest Income;
   - (b) dividend Income; and
   - (c) other non-operating income (net of expenses directly attributable to such income)
4. Other Comprehensive Income shall be classified into-
   - (A) Items that will not be reclassified to profit or loss
     - (i) Changes in revaluation surplus;
     - (ii) Re-measurements of the defined benefit plans;
     - (iii) Equity Instruments through Other Comprehensive Income;
     - (iv) Share of Other Comprehensive Income in Associates and Joint Ventures, to the extent not to be classified into profit or loss; and
     - (v) Others (specify nature).
   - (B) Items that will be reclassified to profit or loss;
     - (i) Exchange differences in translating the financial statements of a foreign operation;
     - (ii) Debt instruments through Other Comprehensive Income;
     - (iii) The effective portion of gains and loss on hedging instruments in a cash flow hedge;
     - (iv) Share of other comprehensive income in Associates and Joint Ventures, to the extent to be classified into profit or loss; and
     - (v) Others (specify nature)
5. Additional Information: Company shall disclose by notes, additional information regarding aggregate expenditure and income on the following items:
   - (a) employee Benefits expense [showing separately (i) salaries and wages, (ii) contribution to provident and other funds, (iii) share based payments to employees, (iv) staff welfare expenses].
   - (b) depreciation and amortisation expense;
   - (c) any item of income or expenditure which exceeds 1% of revenue from operations or ₹ 10,00,000, whichever is higher;

(d) interest Income;

(e) interest Expense

(f) dividend income;

(g) net gain or loss on sale of investments;

(h) net gain or loss on foreign currency transaction and translation;

(i) payments to auditor as (a) auditor, (b) for taxation matters, (c) for company law matters, (d) for other services, (e) for reimbursement of expenses;

(j) in case of companies covered under section 135, amount of expenditure incurred on corporate social responsibility activities; and

(k) details of items of exceptional nature.